



Miller & Miller, P.S.

**Washington State Convention
Center Public Facilities District**

**Financial Statements and
Independent Auditor's Report**

**For The Years Ended December 31,
2012 and 2011**

**Washington State Convention Center Public Facilities District
Financial Statements and Independent Auditor's Report
December 31, 2012 and 2011
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Independent Auditor's Report

Washington State Convention Center Public Facilities District
800 Convention Place
Seattle WA 98101-2350

Report on the Financial Statements

We have audited the accompanying statements of net position of the Washington State Convention Center Public Facilities District (the District) as of December 31, 2012 and 2011, and the related statements of revenues, expenses and changes in net position, and cash flows for the years then ended, and the related notes to the financial statements, which collectively comprise the District'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 audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of 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 District'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 District'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 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.

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the District as of December 31, 2012 and 2011, and the changes in financial position and the cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Accounting principles generally accepted in the United States of America require that management's discussion and analysis on pages 3 through 7 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.



Certified Public Accountants

April 22, 2013

WASHINGTON STATE CONVENTION CENTER PUBLIC FACILITIES DISTRICT

MANAGEMENT'S DISCUSSION AND ANALYSIS For the Years Ending December 31, 2012 and 2011

OVERVIEW

The Washington State Convention Center Public Facilities District (District) presents the Management's Discussion and Analysis (MD&A) of its financial activities for the second full year of operations in 2012. The MD&A focuses on significant financial issues, provides an overview of the District's financial activity and highlights operation changes in the District's financial position.

The accompanying financial statements present the activities of the District. The District was created on July 19, 2010, by King County (Ordinance 16883), pursuant to Substitute Senate Bill 6889, which authorized the creation of the public facilities district by King County and the transfer of assets and liabilities from the nonprofit corporation, established by the Washington State Legislature in 1982, to design, construct, promote and operate the Washington State Convention Center. Prior to its formation, the District was an agency of the state of Washington, and its activities were reported in the Comprehensive Annual Financial Report (CAFR) of Washington State.

FINANCIAL HIGHLIGHTS

- A. Net position increased by approximately \$22 million from 2011 to 2012. The increase is due to the receipt of lodging tax revenues exceeding the District's interest costs and positive operating income before depreciation.
- B. The District issued revenue bonds (Series 2010A and 2010B) in the amount of \$313,575,000 million in November 2010, for the purpose of defeasance of state debt, to support capital improvements and to fund a common reserve.
- C. New accounting software system Ungerboeck was implemented January 1, 2012 replacing MAS 200. Ungerboeck is event software that integrates sales, operations and financial functions. Upon implementation of the new software, the District invoices all services provided by subcontractors and the District, and reimburses subcontractors their portion of the sales. Aramark, the food service provider, has a management contract with the District whereby all invoices are billed through the District. Aramark is reimbursed for expenses they incurred, plus a management fee.

OVERVIEW OF THE FINANCIAL STATEMENTS

The operations of the District are grouped into one business type for financial reporting purposes. The District accounting demonstrates legal compliance and financial management over transactions related to certain functions or activities.

USING THIS ANNUAL REPORT

This annual report consists of a series of financial statements. The Statement of Net Position, the Statement of Revenues, Expenses and Changes in Net Position, and Statement of Cash Flow (on pages 8 through 10) provide information about the activities and finances of the District as a whole.

The Statement of Net Position

The Statement of Net Position reports information about the District as a whole and about its activities in a way that helps communicate the financial condition of the District. This statement includes assets and liabilities using the accrual basis of accounting, which is similar to the

WASHINGTON STATE CONVENTION CENTER PUBLIC FACILITIES DISTRICT

MANAGEMENT'S DISCUSSION AND ANALYSIS
For the Years Ending December 31, 2012 and 2011

accounting used by most private sector companies. All of the current year revenues and expenses are taken into account regardless of when cash is received or paid.

The District's net position is the difference between assets and liabilities. It is one way to measure the District's financial position. Over time, increases or decreases in the District's net position are one indicator of whether its financial condition is improving or deteriorating. You will need to consider other non-financial factors, however, such as changes in the District's funding structures and the condition of the District's operating assets to assess the overall financial health of the District.

The Statement of Revenues, Expenses and Changes in Net Position

The Statements of Revenues, Expenses and Changes in Net Position show the District's income and expenses during the period. All operating revenues and expenses during the year ended December 31, 2012 were accounted for by the District.

The Statement of Cash Flows

The District categorizes cash inflows and outflows into four categories: 1) cash flows from operations, 2) cash flows from non-capital financing activities, 3) cash flows from capital and related financing activities and 4) cash flows from investments.

FINANCIAL ANALYSIS

CONDENSED STATEMENT OF NET POSITION

	2012	2011	Percentage Change	2010	Percentage Change
ASSETS					
Current and Other assets	\$169,559,915	\$139,256,531	22%	\$ 99,256,668	40%
Capital Assets	399,943,705	408,866,558	-2%	399,881,037	2%
Total Assets	569,503,620	548,123,088	4%	499,137,706	10%
LIABILITIES					
Current Liabilities	28,806,692	22,736,670	27%	10,524,973	116%
Noncurrent Liabilities	308,267,701	314,747,177	-2%	314,652,701	0%
Total Liabilities	337,074,393	337,483,847	0%	325,177,674	4%
NET POSITION					
Net invested in capital assets	114,908,901	131,065,755	-12%	126,158,136	4%
Restricted	10,987,507	8,273,832	33%	6,990,732	18%
Unrestricted	106,532,819	71,434,865	49%	40,811,164	75%
Total Net Position	\$232,429,227	\$210,774,452	10%	\$173,960,032	21%

Capital Assets decreased from 2011 to 2012 due to net of current year depreciation and capital asset additions. Capital Assets increased from 2010 to 2011 because capital asset additions exceeded depreciation expense. Current and other assets increased from 2011 to 2012 and from 2010 to 2011 due mainly to the excess of lodging tax revenues above interest expense.

Current liabilities increased mainly due to the current portion of long term debt. Since principal payments on the bonds do not begin until 2013 there was no current portion recognized as of December 31, 2011. Current liabilities increased from 2010 to 2011 due mainly to the accrual of

WASHINGTON STATE CONVENTION CENTER PUBLIC FACILITIES DISTRICT

MANAGEMENT'S DISCUSSION AND ANALYSIS
For the Years Ending December 31, 2012 and 2011

interest for a full six months at the end of 2011 as compared to only one month at the end of 2010.

Noncurrent liabilities decreased from 2011 to 2012 due solely to recognizing the current portion of long-term debt due in 2013. Noncurrent liabilities have remained substantially unchanged between 2010 and 2011 because debt service (principal payments) on the 2010 bonds does not begin until 2013.

Net invested in capital assets decreased from 2011 to 2012 due the combination of depreciation expense, no principal payment on the related bonds and spending of bond proceeds. This balance increased from 2010 to 2011 due to capital asset additions. Restricted net position reflects the required reserve funds that changed between 2010, 2011 and 2012.

CHANGES IN NET POSITION

	<u>2012</u>	<u>2011</u>	Percentage Change	<u>2010</u>
OPERATING REVENUES				
Building rent	\$ 4,778,169	\$ 4,441,649	8%	\$ -
Food service	15,915,988	15,097,453	5%	-
Parking	3,901,212	3,794,496	3%	4,441
Facility services	2,061,014	1,874,392	10%	-
Retail leases	642,568	600,766	7%	-
Lodging tax for marketing	8,788,172	8,069,824	9%	-
Other	681,846	565,190	21%	-
Total Operating Revenues	<u>36,768,969</u>	<u>34,443,770</u>	7%	<u>4,441</u>
NONOPERATING REVENUES				
Lodging tax - regular	43,930,310	40,339,492	9%	-
Interest and investment income	737,967	528,074	40%	(21,217)
Other revenue	-	-		35
Total Revenues	<u>81,437,246</u>	<u>75,311,336</u>	8%	<u>(16,741)</u>
OPERATING EXPENSES				
Salaries and wages	7,499,885	7,213,930	4%	-
Employee benefits	4,648,918	4,465,262	4%	1,760
Marketing services	7,038,118	6,820,020	3%	-
Professional and other services	1,972,975	1,820,046	8%	6,525
Promotional hosting	-	-		-
Food service	9,388,942	9,450,160	-1%	-
Supplies	516,256	555,776	-7%	14,957
Utilities	2,334,856	2,177,575	7%	-
Repair and maintenance	1,453,768	1,140,926	27%	14,548
Depreciation and amortization	10,706,415	9,688,816	11%	-
Other administrative and contingency	231,765	49,263	370%	27,050
Total Operating Expenses	<u>45,791,898</u>	<u>43,381,774</u>	6%	<u>64,840</u>
NONOPERATING EXPENSES				
Interest expense (net of BABs subsidy)	13,144,823	13,135,154	0%	633,222
Other expense	845,750	47,957	1664%	-
Total Expenses	<u>59,782,471</u>	<u>56,564,885</u>	6%	<u>698,062</u>
Net Income (Loss) Before Contributions	21,654,775	18,746,450	16%	(714,803)
Contributions	-	18,203,179	-100%	177,523,036
Change in Net Position	<u>21,654,775</u>	<u>36,949,629</u>	-41%	<u>176,808,233</u>
Net Position - Beginning	210,774,452	173,960,032	21%	-
Effect of Change in Accounting Principle		(135,209)		(2,848,201)
Net Position - Ending	<u>\$ 232,429,227</u>	<u>\$ 210,774,452</u>	10%	<u>\$ 173,960,032</u>

WASHINGTON STATE CONVENTION CENTER PUBLIC FACILITIES DISTRICT

MANAGEMENT'S DISCUSSION AND ANALYSIS
For the Years Ending December 31, 2012 and 2011

Operations have improved from 2011 because of improved event bookings. The number of events was up in 2012 as compared to 2011 and the events in 2012 generally produced more revenue. Related operating expenses also increased but less than operating revenues due to cost control measures enacted by the District. Other nonoperating expenses increased from 2011 to 2012 due to recording a loss on disposal of assets in connection with capital improvement projects. Comparisons with 2010 are not meaningful as substantially all but a minor amount of operations were accounted for by the state of Washington prior to the transfer of assets to the District.

CAPITAL ASSETS

The following schedule is a summary of the District's investment in capital assets as of December 31, 2012, 2011 and 2010:

	12/31/2012	12/31/2011	12/31/2010
Capital assets, not being depreciated			
Land	\$ 77,355,416	\$ 77,355,416	\$ 77,355,416
Construction in progress	4,820,609	4,275,219	-
Total capital assets, not being depreciated	82,176,025	81,630,635	77,355,416
Capital assets, being depreciated			
Buildings and improvements	446,471,185	447,769,668	435,554,006
Other improvements and art collection	3,510,564	3,447,431	2,771,226
Machinery/equipment/furniture/fixtures	8,893,547	6,939,504	5,153,857
Total capital assets, being depreciated	458,875,296	458,156,603	443,479,089
Less accumulated depreciation for			
Buildings	(135,416,847)	(125,647,141)	(115,381,494)
Other improvements and art collection	(1,049,066)	(914,311)	(633,713)
Machinery/equipment/furniture/fixtures	(4,641,703)	(4,359,228)	(4,938,261)
Total accumulated depreciation	(141,107,616)	(130,920,680)	(120,953,468)
Total capital assets, being depreciated, net	317,767,680	327,235,923	322,525,621
Total capital assets	\$ 399,943,705	\$ 408,866,558	\$ 399,881,037

Capital Assets decreased from 2011 to 2012 due to net of current year depreciation and capital asset additions. Capital Assets increased from 2010 to 2011 because capital asset additions exceeded depreciation expense. Art collections of \$13,140 are included in depreciable assets, but they are not depreciated. Additional information regarding capital assets is provided in Note 5 to the financial statements.

DEBT ADMINISTRATION

The District's bond rating is Aa3 by Moody's and A+ by Standard and Poor's.

As of December 31, 2012, 2011 and 2010 the District had \$313,575,000 in outstanding debt. The debt issued by the District in November 2010, was used to defease the state's debt, to provide for

WASHINGTON STATE CONVENTION CENTER PUBLIC FACILITIES DISTRICT

MANAGEMENT'S DISCUSSION AND ANALYSIS For the Years Ending December 31, 2012 and 2011

capital funding for improvement of the Convention Center and to fund a common reserve. Additional information regarding long-term debt is provided in Note 8 to the financial statements.

The District carries property and casualty insurance, employee dishonesty and errors and omissions insurance through Philadelphia Insurance Companies. It participates in the state's Workers' Compensation Program.

ECONOMIC FACTORS

The District moved forward on capital improvement projects in order to ensure that its facility continues to attract profitable events and compete with the many newer and larger buildings in the western United States. The District's newest meeting and event space, The Conference Center, opened in summer 2010. It offers 71,000 square feet of high-end, configurable space, and connects seamlessly to the 344,000 square foot Washington State Convention Center. There are event bookings for the entire facility through 2015. There is a market for an even larger facility; however, significant due diligence must be conducted before further expansion occurs.

The more significant planned improvements through 2013 include renovations of the exhibit hall, 6th floor ballroom, 6th floor lobbies and meeting rooms, Galleria meeting and restrooms and updates of fire/life/safety systems.

The District Board of Director's authorized an operating budget of \$36,711,606 for fiscal 2013.

Financial Contact

The District's financial statements are designed to provide users with a general overview of the District's finances and to demonstrate accountability to the taxpayers, investors, creditors and customers of the District. If you have questions about the report, please contact the District's administrative offices at 206-694-5000. The District's financial statements can be accessed at its website: www.wsc.com.

Washington State Convention Center Public Facility District
Statement of Net Position
As of December 31, 2012 and 2011

	2012	2011
ASSETS		
Current Assets		
Cash and cash equivalents	\$ 19,963,134	\$ 46,333,805
Restricted cash and cash equivalents	25,003,573	25,487,051
Investments	10,075,150	15,015,601
Restricted investments	10,009,250	24,535,788
Restricted investments interest receivable	34,099	-
Receivables (net)	850,138	577,601
Due from other governments	7,519,097	6,509,329
Prepayments and other current assets	751,556	656,657
Total Current Assets	74,205,997	119,115,832
Noncurrent Assets		
Restricted cash and cash equivalents	-	-
Investments	75,582,083	15,093,029
Restricted investments	19,608,647	5,048,709
Other noncurrent assets	163,188	(1,041)
Total Noncurrent Assets	95,353,918	20,140,697
Capital Assets		
Land	77,355,416	77,355,416
Buildings and improvements	446,471,185	447,769,668
Machinery/equipment/furniture/fixtures	8,893,547	6,939,504
Other improvements and art collection	3,510,564	3,447,431
Accumulated depreciation	(141,107,616)	(130,920,680)
Construction in progress	4,820,609	4,275,219
Total Capital Assets	399,943,705	408,866,558
Total Assets	569,503,620	548,123,087
LIABILITIES		
Current Liabilities		
Accounts payable	1,912,049	3,001,473
Salaries, benefits and taxes payable	1,075,992	838,283
Unearned revenue and deposits payable	2,042,230	1,945,851
Due to other governments	7,424,225	7,005,245
Interest payable	9,945,818	9,945,818
Current portion of long term debt	6,385,000	-
Other	21,378	-
Total Current Liabilities	28,806,692	22,736,670
Noncurrent Liabilities		
Bonds, notes and loans payable	308,267,701	314,652,701
Other	-	94,476
Total Noncurrent Liabilities	308,267,701	314,747,177
Total Liabilities	337,074,393	337,483,847
NET POSITION		
Net investment in capital assets	114,908,901	131,065,755
Restricted:		
Restricted for debt service	1,094,696	1,283,100
Restricted for capital improvements	-	-
Restricted for operating reserve	9,892,811	6,990,732
Unrestricted	106,532,819	71,434,865
Total Net Position	\$ 232,429,227	\$ 210,774,452

The accompanying notes are an integral part of these financial statements.

Washington State Convention Center Public Facilities District
Statement of Revenue, Expenses and Changes in Net Position
For the Years Ending December 31, 2012 and 2011

	2012	2011
OPERATING REVENUES		
Building rent	\$ 4,778,169	\$ 4,441,649
Food service	15,915,988	15,097,453
Parking	3,901,212	3,794,496
Facility services	2,061,014	1,874,392
Retail leases	642,568	600,766
Lodging tax for marketing	8,788,172	8,069,824
Other	681,846	565,190
Total Operating Revenues	36,768,969	34,443,770
OPERATING EXPENSES		
Salaries and wages	7,499,885	7,213,930
Employee benefits	4,648,918	4,465,262
Marketing services (SCVB)	7,038,118	6,820,020
Professional and other services	1,972,975	1,820,046
Promotional hosting	-	-
Food service	9,388,942	9,450,160
Supplies	516,256	555,776
Utilities	2,334,856	2,177,575
Repair and maintenance	1,453,768	1,140,926
Depreciation and amortization	10,706,415	9,688,816
Other administrative and contingency	231,765	49,263
Total Operating Expenses	45,791,898	43,381,774
OPERATING INCOME (LOSS)	(9,022,929)	(8,938,004)
NONOPERATING REVENUES (EXPENSES)		
Lodging tax - regular	43,930,310	40,339,492
Interest and investment income	737,967	528,074
Interest expense (net of BAB's subsidy)	(13,144,823)	(13,135,154)
Loss on disposal of assets	(818,226)	-
Other revenue (expense)	(27,524)	(47,957)
Total Nonoperating Revenue (Expense)	30,677,704	27,684,455
NET INCOME (LOSS) BEFORE CONTRIBUTIONS AND TRANSFERS	21,654,775	18,746,451
Capital Contributions (Net)	-	18,203,179
Change in net position	21,654,775	36,949,630
Net Position - Beginning, As Previously Reported		176,808,233
Effect of Change in Accounting Principle		(2,983,411)
Net Position - Beginning, As Restated	210,774,452	173,824,822
Net Position - Ending	\$ 232,429,227	\$ 210,774,452

The accompanying notes are an integral part of these financial statements.

Washington State Convention Center Public Facilities District
Statement of Cash Flows
For the Years Ended December 31, 2012 and 2011

	<u>2012</u>	<u>2011</u>
CASH FLOWS FROM OPERATING ACTIVITIES		
Receipts from customers	\$ 27,804,639	\$ 26,102,799
Receipts from governments	8,683,416	8,069,824
Payments to suppliers	(22,890,582)	(22,151,649)
Payments to employees	(11,911,094)	(11,632,886)
Payments to others	(73,099)	-
Net Cash Provided By Operating Activities	<u>1,613,281</u>	<u>388,088</u>
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES		
Transfer from Office of State Treasurer	-	53,287,323
Nonoperating Portion of Lodging Taxes received	55,232,949	50,324,056
Portion of Lodging Tax paid to state	(11,374,855)	(9,401,103)
Purchase of other noncurrent assets	(42,878)	(89,931)
Start-up costs	-	(13,107)
Net Cash Provided By Noncapital Financing Activities	<u>43,815,216</u>	<u>94,107,238</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Purchases of Capital Assets	(4,243,502)	(4,199,125)
Interest paid on capital debt, net of BABs subsidy	(13,144,823)	(3,822,557)
Other receipts (payments) - bond issue costs	-	(424,574)
Net Cash Used By Capital and Related Financing Activities	<u>(17,388,325)</u>	<u>(8,446,256)</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Interest and dividends	618,778	528,074
Investment fees	(27,534)	(49,067)
Investment purchases	(100,085,565)	(39,871,854)
Investment maturities	44,600,000	-
Net Cash Used By Investing Activities	<u>(54,894,321)</u>	<u>(39,392,847)</u>
Net Increase (Decrease) In Cash and Cash Equivalents	<u>(26,854,149)</u>	<u>46,656,223</u>
Cash and Cash Equivalents Balances - Beginning	<u>71,820,856</u>	<u>25,164,633</u>
Cash and Cash Equivalents Balances - Ending	<u>\$ 44,966,707</u>	<u>\$ 71,820,856</u>
Cash and Cash Equivalents as Reflected in the Statement of Net Position:		
Cash and cash equivalents	\$ 19,963,134	\$ 46,333,805
Restricted cash and cash equivalents	25,003,573	25,487,051
Total Ending Cash and Cash Equivalents in the Statement of Net Position	<u>\$ 44,966,707</u>	<u>\$ 71,820,856</u>
RECONCILIATION OF OPERATING INCOME (LOSS) TO NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES		
Operating income (loss)	\$ (9,022,929)	\$ (8,938,004)
Adjustments to reconcile operating income (loss) to net cash provided (used) by operating activities		
Depreciation and amortization	10,706,415	9,688,816
Changes in operating assets and liabilities:		
Accounts Receivable	(272,537)	38,439
Due from Other Governments	(486,119)	
Operating Accounts Payable	522,360	414,228
Prepayments	(94,899)	(408,764)
Salaries, benefits and taxes payable	237,709	(46,306)
Unearned revenue and deposits payable	96,379	(309,587)
Other	(73,098)	(50,733)
Net Cash Provided By Operating Activities	<u>\$ 1,613,281</u>	<u>\$ 388,088</u>
SCHEDULE OF NON-CASH INVESTING, CAPITAL, NON CAPITAL AND RELATED FINANCING ACTIVITY		
Capital Assets acquired by capital contributions	\$ -	\$ 12,736,232
Capital Assets acquired by increases in accounts payable	-	1,611,785
Change in fair value of investments	234,898	-

WASHINGTON STATE CONVENTION CENTER PUBLIC FACILITIES DISTRICT
NOTES TO FINANCIAL STATEMENTS
December 31, 2012 and 2011

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. Reporting Entity

The accompanying financial statements present the activities of the Washington State Convention Center Public Facilities District (District). The District was created on July 19, 2010, by King County Ordinance 16883, pursuant to Substitute Senate Bill 6889, which authorized the creation of the public facilities district by King County and the transfer of assets and liabilities from the nonprofit corporation, established by the Washington State Legislature in 1982, to design, construct, promote and operate the Washington State Convention Center. Heretofore, the District was an enterprise fund of the state of Washington, and its activities were reported in the Comprehensive Annual Financial Report (CAFR) of Washington State.

The District is an independent, governmental entity, and all of its activities are accounted for in the records of the District. All liabilities incurred by the District are required to be satisfied exclusively from the assets, credit and property of the District. The District's reporting cycle is the 12-month calendar period from January 1, through December 31. The District began start-up activities subsequent to July 19, 2010, upon authorization by the Board of Directors of a \$500,000 loan from the nonprofit corporation to the District, which allowed the District to incur certain start-up and organizational costs. The nonprofit corporation continued to earn the revenues from hotel/motel taxes, event rentals and tenant leases and to incur the associated operating expenses through December 31, 2010.

In November 2010, the District issued bonds in the amount of \$314,652,701. The proceeds were distributed on November 30, in accordance with the Official Statement for the bonds and the Transfer Agreement between the state and the District as follows: to the District for capital improvements (\$21.4 million), to the state to defease Convention Center debt (\$270.9 million), to an external fiscal agent to establish the common reserve (\$19.5 million) and to fund bond issue costs (\$2.7 million).

As of December 31, 2010, the District recorded the assets of the nonprofit corporation (including all capital assets) and a receivable from the state in the amount of \$53.2 million, which represents a cash transfer to the District on January 4, 2011. The District also recorded all of the liabilities of the nonprofit corporation, with the exception of the long-term debt, which was defeased with the bond issue discussed in the above paragraph.

B. Basis of Accounting and Presentation

The District uses the accrual basis of accounting and the economic resources measurement focus. Revenues are recorded when earned, and expenses are recorded when a liability is incurred, regardless of when the related cash is received or disbursed.

Amounts received but not earned at year-end are reported as unearned revenues. Earned but unbilled revenues are accrued. Amounts disbursed but not owed at year-end are reported as pre-paid expenses. Amounts owed but for which the District has not yet been invoiced are accrued.

C. Summary of Significant Accounting Policies

1. Policy for defining operating and non-operating revenues/expenses

WASHINGTON STATE CONVENTION CENTER PUBLIC FACILITIES DISTRICT
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Operating revenues/expenses are distinguished from non-operating revenues/expenses based on their relationship to the primary purpose of the District, which is operating a convention center. The operating revenues of the District result from event rentals, related event fees, food service, parking and retail leases and that portion of the hotel/motel taxes transferred to the Seattle Convention Visitors Bureau for advertising and marketing. The operating expenses relate directly or indirectly to the generation of the operating revenues and include salaries and benefits, professional services, depreciation, supplies, utilities, advertising, marketing and other administrative expenses.

The District relies on four contractors to provide specific event services for clients. Rates charged for all contractor services are approved by the District. ARAMARK has a management contract with the District and is the exclusive food and beverage provider within the center. The District recognizes in its financial statements gross food revenues and food expense. Revenues from the other three contractors are recorded as Facility Services under Operating Revenues. Edlen is the exclusive electrical and air/water/drain provider for the District. The District receives in the range of 28 to 35 percent of the revenue generated by Edlen. Edlen retains the remaining revenues and all expenses. Convention Communication Provisioners, Inc (CPPI) provides exclusive telecommunication, data & internet services. Generally the District receives 30 percent of the gross revenues, and CCPI retains the remaining revenue and covers all expenses. Presentation Services Audio Visual (PSAV) is the preferred audio visual provider for the District. Generally PSAV pays the District a 23 to 40 percent commission depending on the service or rented equipment provided.

The District receives non-operating revenues from lodging taxes, investment interest earnings, insurance recoveries and capital contributions. Its non-operating expenses are mainly debt service interest payments.

2. Policy for applying Financial Accounting Standards Board (FASB) pronouncements issued after November 30, 1989

The District adheres to Governmental Accounting Standards Board (GASB) Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*. The District applies all GASB pronouncements as well as all FASB Statements and Interpretations, Accounting Principles Board (APB) Opinions and Accounting Research Bulletins (ARBs) issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements.

As required by the Governmental Accounting Standards Board (GASB) the District adopted GASB Statement number 63 *Deferred Outflows and Inflows of Resources and Net Position* and implemented GASB Statement number 65 *Items Previously Reported as Assets and Liabilities*. The effect of adopting GASB Statement number 65 was to write-off certain bond issue and other organizational costs and is reflected as a restatement of beginning net position as of January 1, 2011.

3. Policy for defining cash equivalents

Cash includes the following:

- a. Cash on hand.

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- b. Cash on demand deposit with financial institutions that can be withdrawn without prior notice or penalty.
- c. Cash in management pools (e.g., the Local Government Investment Pool) that are similar to demand deposits.

Cash equivalents include highly liquid investments with the following characteristics:

- a. Readily convertible to known amounts of cash.
- b. Mature in such a short period of time that their values are effectively immune from changes in interest rates.

The District considers all investments of a three-month term or less to be cash equivalents.

4. Policy for application of restricted versus unrestricted resources

The District applies all restricted resources to eligible expenses prior to applying unrestricted resources. For example, the District's debt covenants restrict certain resources for debt service, and the District applies these restricted resources to debt service. Were there to be insufficient restricted resources for debt service, the District would first apply the restricted resources and compensate for any insufficiency with unrestricted resources.

D. Budgetary Information

1. Scope of Budget

The District adopts an annual operating budget by resolution no later than December 31. It adopts budgets for the debt service requirements of individual debt issues. It adopts capital projects' budgets for specific projects for a three-year period. Each year's annual operating budget is developed based on economic projections. The Board adopts a contingency amount, within which management can control spending variances.

Capital Bond budget funding carries forward until projects are completed and/or funding is exhausted.

The Board of Director's approved Resolution number 2012-6 a Capital Improvement Project Funding Program. Annually \$4 million will be dedicated to fund annually approved capital improvement projects. Unspent funds will carry forward but capital improvement projects must be approved annually.

The Board of Director's approved Resolution number 2010-16 that requires the establishment of an annual operating reserve based on 100 days of the budgeted expenses.

2. Amending the Budget

The District prepares a monthly comparison of budgeted amounts to actual amounts. It can amend its operating budget only by board resolution. Capital budgets are monitored

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throughout the length of the specific projects, and budgets are modified by board resolution.

D. Assets, Liabilities and Net Position

1. Cash and Cash Equivalents

It is the District's policy to invest all temporary cash surpluses. At December 31, 2012 and 2011, the District had \$20,041,259 and \$46,333,805, respectively in short-term residual investments of surplus cash. This amount is classified on the Statement of Net Position as cash and cash equivalents.

2. Investments (Note 4)

It is the policy of the District to invest all public funds in accordance with governing federal, state and local statutes. The District's objectives are to ensure safety of the principal, to maintain an investment portfolio that is sufficiently liquid to meet all operating requirements, debt payments and capital purchases and to achieve a market rate of return taking into account risk constraints.

Additionally, the District maintained restricted investments with external fiscal agents, which are presented on the Statement of Net Position as restricted investments in the amount of \$29,617,897 for 2012 and \$29,584,497 for 2011. Unrestricted investments are \$85,657,233 as of December 31, 2012 and \$30,108,630 as of December 31, 2011. All investments are reported at fair value as reported by the external fiscal agent.

3. Receivables

Receivables consist of the following components:

Taxes receivable consist of the Public Facilities Sales and Use Tax, the Lodging Taxes and Leasehold Excise Taxes.

Customer accounts receivable consist of amounts owed by private organizations for goods and services and leased retail space.

Interest receivable consists of amounts owed by financial institutions on the District's investments.

4. Due to/from Other Governments

As of December 31, 2012, the Due from other governments account is mainly composed of lodging tax collected by the hotels and earned in November and December 2012, but paid to District in January and February 2013.

5. Inventories

The District does not carry any significant inventories. It expenses operating supplies and small tools when purchased.

6. Restricted Assets and Liabilities

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The District restricts certain resources based on bond covenants, board requirements and contractual arrangements. The following restrictions pertain:

- Operating Reserve Account
- Additional Lodging Account
- Lodging Account
- Bond Interest Account
- Bond Principal Account
- Common Reserve Account
- Retainage Accounts

7. Capital Assets (Note 5)

Capital assets include land, buildings, building improvements, machinery and equipment, furniture and fixtures, art collections and construction in progress. Assets are capitalized if the initial investment is \$5,000 or greater and have an estimated useful life of more than one year. Capital assets are recorded at cost. Costs of additions or improvements to capital assets are capitalized if they increase the useful life of the asset. Routine repair and maintenance costs are expensed when incurred.

Costs for capital assets under construction are capitalized, as is the net interest expense related to the debt issue supporting the project. During 2012, net interest was not capitalized as most costs were incurred near year end. As such, all interest costs and interest income are reflected in the Statement of Revenue, Expenses and Changes in Net Position.

Capital assets in service are depreciated over their useful lives using the straight-line method. The following useful lives pertain:

Assets	Useful Lives (Years)
Buildings	50
Building Improvements	50
Equipment – Heating/Air Conditioning	13
Vehicular Equipment	13
Equipment – Furniture	10
Equipment – Communications	7
Equipment – Data Processing	6
Vehicles and All Other Equipment	5
Art Collections	Not depreciated

8. Compensated Absences

The District compensates employees for vacation and sick leave. All such leave is accrued when earned and reduced when used. Vacation leave for administrative staff may be accumulated to a maximum of 240 hours on the employee's anniversary date. Vacation leave for union staff may be accumulated to a maximum of 80 hours (1-8 years) and 120 hours (9 years and above). Sick leave for all staff may be accumulated to a maximum of 720 hours, with excess up to 96 hours payable at 25 percent annually. Part-time staff may accumulate vacation and sick leave, using a pro-rata formula based on 2080 hours annually. Upon retirement, termination or death, unused vacation leave is payable in full and unused sick leave is forfeited.

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9. Unearned Revenue and Deposits Payable

The District collects certain money in advance, primarily customer deposits for future events. Until earned, these collections are presented as unearned revenues or deposits payable.

10. Restricted and Unrestricted Net Position

The District's net position is presented as restricted and unrestricted. Restricted net position exclude capital assets, net of related debt, but include other assets on which there are externally imposed legal restrictions. Unrestricted net assets include all other net assets. Additional details regarding the classification of net position is provided in Note 14.

E. Prior-Year Comparative Data

The current period, January 1, 2012 through December 31, 2012, is the second year of operating revenues and expenses reported by the District. Comparative data for the period of January 1, 2011 through December 31, 2011 are reported in the financial statements. Certain reclassifications have been made to the 2011 presentation to conform to the presentation used in 2012.

NOTE 2 – STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY

There have been no material violations of finance-related or contractual provisions.

NOTE 3 - CASH DEPOSITS WITH FINANCIAL INSTITUTIONS

The District's cash and cash equivalents are held in multiple financial institutions and are covered by the Federal Deposit Insurance Corporation (FDIC) or by collateral held in a pool administered by the Washington State Public Deposit Protection Commission (PDPC).

As of December 31, 2012 and 2011, they include:

Financial Institution	2012	2011
US Bank	\$6,623,638	\$5,908,096
Local Government Investment Pool	22,256,539	55,837,782
Petty Cash/Change Funds	46,100	46,100
TOTAL	\$29,126,277	\$60,981,978

The District maintains a minimum compensating balance at US Bank of \$1,600,000.

NOTE 4 – INVESTMENTS

As of December 31, 2012 and 2011, the District had the following investments (in thousands):

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Investments	Maturities	Moody, S&P Rating	Cost	Beginning Fair Value 12/31/2011	Purchases	Sales	Subtotal	Ending Fair Value 12/31/2012
Fed Home LN BK (1)	11/20/2015	AAA, AA+	\$19,590		\$ 19,590	\$ -	\$19,590	\$ 19,609
Fed Home LN BK	5/30/2014	AAA, AA+	9,992		9,992	-	9,992	10,019
Fed Home LN BK	12/27/2013	AAA, AA+	4,943	\$5,043		-	5,043	5,034
Fed Home LN BK	3/27/2013	AAA, AA+	5,000	5,042		-	5,042	5,010
Fed Home LN BK	6/21/2013	AAA, AA+	5,101	5,112		-	5,112	5,041
FFCB Bond	10/9/2015	AAA, AA+	4,994		4,994	-	4,994	4,999
FHLMC	11/25/2014	AAA, AA+	15,137		15,136	-	15,136	15,136
FHLMC	9/10/2015	AAA, AA+	10,386		10,386		10,386	10,366
FNMA MTN	6/5/2015	AAA, AA+	10,006		10,006	-	10,006	9,998
FNMA MTN	11/27/2015	AAA, AA+	10,000		10,000		10,000	10,010
FNMA MTN	5/27/2015	AAA, AA+	14,896		14,986	-	14,986	15,055
US Treas. Note	8/31/2013	AAA, NA	4,997		4,997		4,997	4,999
Total			\$115,042	\$ 15,197	\$100,087	\$ -	\$115,284	\$ 115,276

(1) These investments are restricted for debt service.

Interest Rate Risk is the risk that changes in interest rates will adversely affect the fair value of an investment. To mitigate this risk, the District limits the maturity of any single security to five years, in accordance with its investment policy. To achieve its financial objective of ensuring liquidity most investments have shorter maturities.

Credit Risk is the risk that an issuer or other counterparty of an investment will not fulfill its obligations. To mitigate this risk, the District ensures that it adheres to the credit standards as defined in its investment policy. The Moody and S&P rating (if available) are provided in the chart above.

Concentration of Credit Risk is the risk of loss attributed to the percentage of a government's investment in a single issuer. To mitigate this risk, the District ensures that it maintains portfolio diversification as defined in its investment policy.

Custodial Credit Risk is the risk that, in the event of failure of the counterparty, the District will not be able to recover the value of its investments that are in the possession of an outside counterparty. To mitigate this risk, the District ensures that investments are held in safekeeping at a qualified financial institution as defined in its investment policy.

NOTE 5 – CAPITAL ASSETS

The capital assets and related changes during the year ended December 31, 2012 and 2011 are reflected in the following chart.

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Asset Class	Beginning Balance			Ending Balance
	January 1, 2012	Increases	Decreases	December 31, 2012
Capital assets, not being depreciated				
Land	\$ 77,355,416	\$ -	\$ -	\$ 77,355,416
Construction in progress	4,275,219	2,632,358	(2,086,968)	4,820,609
Total capital assets, not being depreciated	81,630,635	2,632,358	(2,086,968)	82,176,025
Capital assets, being depreciated				
Buildings and improvements	447,769,668	6,452	(1,304,935)	446,471,185
Other improvements and art collection	3,447,431	90,453	(27,320)	3,510,564
Machinery/equipment/furniture/fixtures	6,939,504	1,980,974	(26,931)	8,893,547
Total capital assets, being depreciated	458,156,603	2,077,879	(1,359,186)	458,875,296
Less accumulated depreciation for				
Buildings	(125,647,141)	(10,256,415)	486,709	(135,416,847)
Other improvements and art collection	(914,311)	(134,755)		(1,049,066)
Machinery/equipment/furniture/fixtures	(4,359,228)	(301,384)	18,909	(4,641,703)
Total accumulated depreciation	(130,920,680)	(10,692,554)	505,618	(141,107,616)
Total capital assets, being depreciated, net	327,235,923	(8,614,675)	(853,568)	317,767,680
Total capital assets	\$ 408,866,558	\$ (5,982,317)	\$ (2,940,536)	\$ 399,943,705

Art collections of \$13,140 for 2012 are reflected in depreciable assets even though art is not depreciated. Art Collections were not recognized in 2011.

NOTE 6 – RETIREMENT PLANS

Before transition to a public facilities district, the agency of the state of Washington participated in a 401(k) retirement plan for its employees under the authority of Internal Revenue Code 457. It continued its Retirement Contribution Plan. In the transition to a public facilities district, Internal Revenue rules required the funds in 401(k) be transferred into the District's 401(a) and the 457 Plan rollover to the District's 457(b) Plan. All of the plans as agency to the state of Washington and the District under ERISA 404(c) transferred the responsibility for selecting among investment options from the plan fiduciaries to the plan participants.

401(a) – Compensation Deferral Plan

All full-time employees are eligible for this plan upon hire, with the exception of 1) leased employees, 2) union employees, 3) non-resident aliens with no US source income and 4) individuals not eligible based on written agreement. The entry date is the first day of any month. Each employee directs how contributions are to be invested and receives an individual monthly statement of activity.

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The District contributed \$189,181 and \$217,373 to the employee 401(a) in fiscal 2012 and 2011 respectively. The District's basic contribution is five percent based on employee's compensation; and it may match \$0.50 for each dollar an employee contributes to the employee retirement contribution plan up to 6 percent of the employee's wages. Vesting in the employer contributions occurs in accordance with the following schedule:

Years of Service	Vested Percentage
Less than 2	0%
2	20%
3	40%
4	60%
5	80%
6 or more	100%

457 (b) Employee Retirement Contribution Plan

All full-time employees are eligible for this plan upon hire, with the exception of 1) leased employees, 2) union employees, 3) non-resident aliens with no US source income and 4) individuals not eligible based on written agreement. The entry date is the first day of any month. Each eligible employee determines the pre-tax contribution to be withheld from gross wages, with a minimum participation of 1 percent of compensation and a maximum of \$16,500 or 100 percent of includible compensation, whichever is less. Employees age 50 or older, or those within three years of retirement, may contribute an additional \$5,500. Each employee directs how contributions are to be invested and receives an individual monthly statement of activity.

Employees vest in the program from inception, at which time they may receive contributions upon retirement, termination or death.

The employee may make a pre-tax contribution to the contribution plan. All full-time non-represented employees are eligible and 100 percent vested. Employees contributed \$179,204 and \$215,821 to their 457(b) plan in 2012 and 2011 respectively.

Retirement Savings Plan

The employee, employer and retirement savings plan contributions are held in trust by TD Ameritrade. The District receives a monthly accounting of all activity. The employee/employer and retirement savings plan contributions are not considered either assets or liabilities of the District.

NOTE 7 – RISK MANAGEMENT

A. General Liability Insurance

The District has property and casualty insurance through Factory Mutual Insurance Company of Rhode Island through November 30, 2013, as follows: \$426 million in total coverage for its facilities and operations including earthquake, flood and terrorism coverage. The total combined maximum deductible is \$250,000.

B. Employee Dishonesty Insurance

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The District maintains a blanket bond for employee dishonesty, with a current coverage limit of \$1,000,000, with no deductible. There were no claims against this policy in 2012.
 Liability Insurance

C. Liability Insurance

The District maintains liability insurance through Philadelphia Indemnity Insurance Company for the following liability categories (aggregate limit): General (\$3,000,000), Employee Liability (\$2,000,000), Stop Gap (\$1,000,000), Auto (\$1,000,000); Umbrella (\$10,000,000), and Management (\$2,000,000). No deductibles apply to these coverages, with the exception of a retention amount of \$10,000 which is applicable to the Directors & Officers and Employment Practices portions of the Management Liability coverage.

NOTE 8 – LONG-TERM DEBT

A. Long-Term Debt

The District issued revenue bonds in November 2010. The debt service is supported by the Lodging Tax, pursuant to RCW 36.100.040(4). This debt issue had three purposes:

1. Finance the transfer of the Washington State Convention Center from the state to the District.
2. Provide capital funds for renovations of the Convention Center.
3. Provide funds for a Common Reserve.

Revenue bonds currently outstanding are as follows:

Description	Maturity	Interest Rates	Balance 12/31/2011	Additions	Reduction	Balance 12/31/2012	Amount Due Within One Year
Bonds 2010A	2013-2014	4.0%-5.5%	\$ 13,025,000	\$ -	\$ -	\$ 13,025,000	\$6,385,000
Bonds 2010B	2015-2040	3.53%-6.79%	300,550,000	-	-	300,550,000	-
Bond Premium			1,077,701			1,077,701	
Total Long Term Debt			314,652,701	-	-	314,652,701	
Less Current Portion			-			(6,385,000)	
Long Term Portion			<u>\$ 314,652,701</u>			<u>\$ 308,267,701</u>	

There were no changes in the bonds payable accounts during 2011 or 2012.

Revenue bond debt service requirements to maturity for the year ending December 31, 2012 are as follows:

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Year	2010A		2010B		Less BABs	Total
	Principal	Interest	Principal	Interest	Subsidy	
2013	\$ 6,385,000	\$ 587,400		\$ 19,304,237	\$ (6,756,483)	\$ 19,520,154
2014	6,640,000	332,000		19,304,237	(6,756,483)	19,519,754
2015			6,970,000	19,304,237	(6,756,483)	19,517,754
2016			7,130,000	19,058,196	(6,670,369)	19,517,827
2017			7,315,000	18,778,486	(6,572,470)	19,521,016
2018 - 2022			40,150,000	88,375,060	(30,931,271)	97,593,789
2023 - 2027			48,985,000	74,770,122	(26,169,543)	97,585,579
2028 - 2032			60,800,000	56,604,156	(19,811,455)	97,592,701
2033 - 2037			75,455,000	34,058,980	(11,920,643)	97,593,337
2038 - 2040			53,745,000	7,403,816	(2,591,336)	58,557,480
Total	\$ 13,025,000	\$ 919,400	\$ 300,550,000	\$ 356,961,526	\$ (124,936,535)	\$ 546,519,391

As discussed in NOTE 12, future BABs subsidies may be reduced. The effect would be to increase debt service to maturity on the bonds. Effects of future subsidy reductions have not been reflected in the debt service to maturity chart above.

NOTE 9 – LEASES

Operating Leases

The District leases office equipment under non-cancellable operating leases. The annual commitments under these leases are approximately \$117,865 until the end of the leases in 2016 as follows:

Year	Operating Leases
2013	\$41,225
2014	36,000
2015	27,789
2016	12,851
Total	\$117,865

Tenant Leasing Agreements

The District leases building space to various retail tenants. A total of 17 retail leases provided revenue of \$642,568 in fiscal 2012. Lease contract terms will expire within one to four years for many of the retail tenants. It is not known if options to extend terms will be exercised but, negotiations are ongoing at this time with some retail tenants. Based on enforceable contracts as of December 31, 2012 future minimum rental payments required for five succeeding years are as follows:

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Year	Lease Revenue
2013	\$515,267
2014	295,243
2015	235,406
2016	144,754
2017	55,357
Total	\$1,246,027

NOTE 10– CONTINGENCIES AND LITIGATION

The District has recorded in its financial statements all material liabilities, including an estimate for situations which are not yet resolved, but where based on available information, management believes it is probable that the District will be assessed a liability. In the opinion of management, the District’s insurance policies are adequate to pay all known or pending claims. However, as of December 31, 2011 and 2012 there are no known or pending claims.

NOTE 11 – COMMITMENTS

A. Capital Projects

The proceeds of \$21,435,000 from the November 2010 debt issue are restricted for capital improvements and must be expended within a 36-month period to avoid arbitrage requirements. As of December 31, 2012 \$7,364,668 was spent on capital improvements.

B. Freeway Park

In February 1997, the nonprofit corporation entered into a 30-year lease agreement with the city of Seattle for the 665-stall Freeway Park garage. Under this agreement, the nonprofit corporation paid debt service on the \$1.3 million of city bonds outstanding at the time, and the final debt service payment was made in June 2002. In accordance with the lease agreement, a capital reserve account, not to exceed \$500,000, with annual maximum payments of \$20,000, was set up. The Center is responsible for all repairs and maintenance. The city of Seattle has assigned the remainder of the lease from the nonprofit corporation to the District.

Future expected capital reserve account payments required for five succeeding fiscal years are:

2013	20,000
2014	20,000
2015	20,000
2016	20,000
2017	20,000
Total	\$100,000

C. Airspace Lease WSDOT

In February 4, 1986, the nonprofit corporation entered into a 66-year lease agreement with the Washington State Department of Transportation (WSDOT). The WSDOT has assigned the

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remainder of the lease from the nonprofit corporation to the District. Under this agreement, the nonprofit corporation leases airspace and other real property. In 1984, Shorett & Riely appraised the leased airspace and determined that its value was \$12,869,000. Additionally, it was determined that qualifying site penalties were valued at \$10,722,983 and qualifying rent credits were valued at \$5,631,358. The payment of rent by the District may be satisfied by payments in cash or by rental credits. After the first 15 years of the lease and every 10 years thereafter, the lease shall be reviewed. In fiscal 2013 the lease payments come up for review. For any review period the rent cannot increase by more than 30%. For the first 25 years the qualifying site penalties and the qualifying rent credits have offset annual rent.

NOTE 12 – INFREQUENT EVENTS

The Washington State Convention Center (Center) had been an agency of the state of Washington since 1982. For financial reporting purposes, it was presented in the state's Comprehensive Annual Financial Report (CAFR) as an enterprise fund. In 2009, the Tourism Alliance, a Washington nonprofit corporation, brought suit against the state of Washington, arguing that the taxes collected by the state on behalf of the Washington State Convention Center – a 7 percent tax on hotel rooms in Seattle and a 2.8 percent tax in the rest of King County – were supposed to be dedicated to the Center and marketing the venue. The lawsuit contended that during the 2007-09 biennium \$57 million was transferred from the Center to the state's General Fund. In exchange for not having to repay the \$57 million to the Center, the state introduced legislation (SB 6889) to authorize transfer of the assets and liabilities of the Center to a newly created public facilities district.

With passage of SB 6889, the lawsuit was dismissed. On July 19, 2010, King County passed Ordinance 16889, which created the Washington State Convention Center Public Facilities District. During the ensuing months, the nonprofit corporation, which managed the Washington State Convention Center, and the District began the process of transitioning ownership of the assets and liabilities from the Center to the District.

In November 2010, the District issued bonds, which defeased the state's Center debt, provided funding for future improvement and expansion of the Center and provided for a common reserve. As of December 31, 2010, the District assumed all remaining capital and other assets and liabilities of the nonprofit corporation.

BUILD AMERICA BONDS

The District made an irrevocable election to have Section 54AA of the Internal Revenue Code of 1986, apply to 2010B Bonds so that the 2010B Bonds are treated as "Build America Bonds" (BAB). Under this treatment the District has received an interest subsidy of 35% from the US Treasury. The District believed this subsidy would be intact for the life of the bonds outstanding. Pursuant to the requirements of the Balanced Budget and Emergency Deficit Control Act of 1985, as amended in 2012 certain automatic reductions will take place as of March 1, 2013. These required reductions include a reduction to refundable credits under section 6431 of the Internal Revenue Code applicable to certain qualified bonds. The sequester reduction is applied to section 6431 amounts claimed by an issuer on any Form 8038-CP filed with the Service which results in a payment to such issuer on or after March 1, 2013. The sequestration reduction rate will be applied until the end of the fiscal year (September 30, 2013) or intervening Congressional action, at which time the sequestration rate is subject to change.

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BAB subsidy request form is Form 8038-CP. It has been circulated that the District BAB subsidy will be reduced by 8.9 percent. The District will not know the reduction for certain until July 2013. The District has assumed the BAB reduction to be \$300,664. The normal semi-annual BAB subsidy is \$3,378,242, less the forecasted reduction \$300,664, equals a net semi-annual subsidy of \$3,077,578.

NOTE 13 – RELATED PARTY TRANSACTIONS

The Board members, managers and staff of the nonprofit corporation and the District are the same individuals, charged with governance and daily operations of the transition of the Washington State Convention Center (Center) from an enterprise fund of the state of Washington to an independent governmental public facilities district. The transition began in July 2010. All transactions between July and December 2010 were controlled by the common board, managers and staff of the Center, with oversight by the Office of State Treasurer and the Office of Financial Management.

NOTE 14 – RESTRICTED NET POSITION

In accordance with GASB 34, net assets are presented on the Statement of Net Position in three categories:

Net investment in capital assets
Restricted assets
Unrestricted assets

Capital assets consist of land, buildings, machinery and equipment, furniture and fixtures, art collections and construction in progress. The related debt is the debt issued to support acquisition and construction of capital assets, reduced for any unspent proceeds. *Restricted assets* are defined as assets that have been restricted by contractual agreement with external parties (e.g., debt covenants) or by law through enabling legislation. *Unrestricted assets* include assets that have no restrictions placed on them, as well as assets that have been internally restricted (e.g., imposed by the District's Board of Directors).

The following provides further detail:

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Category	Assets	Related Liability	Net Position
Capital assets, net of accumulated depreciation	\$ 399,943,705		
Less Bonds Payable		(314,652,701)	
Plus unspent proceeds reflected as restricted below		29,617,897	
Net position invested in capital assets			\$ 114,908,901
Restricted assets			
Restricted for debt service under bond covenants	30,649,161	(19,608,647)	
Interest payable to be paid from restricted assets		(9,945,818)	1,094,696
Restricted for capital improvements	10,009,250	(10,009,250)	-
Restricted for operating reserve	9,892,811		9,892,811
Restricted net assets			10,987,507
Unrestricted			106,532,819
Total Net Position			<u>\$ 232,429,227</u>

NOTE 15 – ARBITRAGE

Arbitrage is the ability to obtain tax-exempt bond proceeds and invest the funds in higher yielding taxable securities, resulting in a profit.

Abuses associated with tax-exempt financings led the federal government to issue regulations to restrict the use of tax-exempt bond proceeds. The two primary purposes for establishing the arbitrage laws were: 1) to minimize the benefits of investing tax-exempt bond proceeds and 2) to remove the incentive to issue more bonds, issue bonds earlier or to leave bonds outstanding longer than necessary to carry out the governmental purpose of the issue.

The arbitrage laws are issued by either the United States Congress or the United States Treasury Department. The hierarchy of these laws is:

- Internal Revenue Code (Section 148(f)(2) of 1986 as amended)
- Treasury Regulations
- Revenue Procedures
- Private Letter Rulings.

Generally, tax-exempt bond issues, which were issued on or after September 1, 1986, are subject to the arbitrage rebate requirements. The arbitrage rebate requirements require that any profit (i.e., arbitrage) be rebated to the federal government.

The rebate amount due to the federal government is equal to the excess of the amount earned on all non-purpose investments purchased with gross proceeds of the bonds over the amount which would have been earned if such non-purpose investments were invested at a rate equal to the yield on the bonds.

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The general steps to calculate the rebate liability are: 1) calculate the yield on the bonds, 2) calculate the actual earnings on all non-purpose investment activity purchased with gross proceeds of the bonds, 3) calculate the allowable earnings on the non-purpose investment activity assuming the investments were earning at a rate equal to the bond yield and 4) future value the difference from the actual payment or receipt date to the computation date at a rate equal to the yield on the bond issue.

A rebate computation and payment to the federal government, if applicable, is required to be made at least every five years or each "Rebate Installment Computation Date" and upon final redemption or maturity of the bonds, the "Final Rebate Computation Date." The payment is due to the federal government within 60 days from either each Rebate Installment Computation Date or Final Rebate Computation Date.

Failure to comply with these rebate requirements could lead to substantial late filing penalties and interest and or, potentially, the loss of tax-exempt status for the bonds.

The portion of the bonds held for capital projects are exempt from arbitrage rules, if expended within three years. The unexpended balance of the bond proceeds dedicated to a capital project can be invested at unrestricted yield during this three-year period.

Unrestricted investments also are allowed for bond proceeds held in a reasonably required reserve account, up to 10 percent of the proceeds, to ensure repayment of principal and interest should revenue sources not be sufficient at some future period.

In addition, a *de minimis* portion of the proceeds may be invested at unrestricted yield, defined as the lesser of \$100,000 or 5 percent of the proceeds.

The District has designated the 2010A Bonds as "qualified tax-exempt obligations" within the meaning of Section 265(b)(3)(B) of the Internal Revenue Code. The District monitors arbitrage rebate liability on its outstanding 2010A bonds. At December 31, 2010, the District had no arbitrage rebate liability, and does not anticipate that it will incur an arbitrage rebate liability on this bond issue.

The 2010B Bonds are not "qualified tax-exempt obligations," due to the Building America Bonds subsidy, which the District receives to offset interest expense. The proceeds of this bond issue must be expended within 36 months, to avoid arbitrage requirements.