
Sufficiency Certification for the Washington Convention and Sports Authority (Trading as Events DC) Projected Revenues and Excess Reserve to Meet Projected Operating and Debt Service Expenditures and Reserve Requirements for Fiscal Year 2019

July 16, 2018



AUDIT TEAM:

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A Report by the Office of the District of Columbia Auditor
Kathleen Patterson, District of Columbia Auditor

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July 16, 2018

The Honorable Phil Mendelson, Chairman
Council of the District of Columbia
1350 Pennsylvania Avenue, N.W., Suite 504
Washington, DC 20004

Letter Report: Sufficiency Certification for the Washington Convention and Sports Authority (Trading as Events DC) Projected Revenues and Excess Reserve to Meet Projected Operating and Debt Service Expenditures and Reserve Requirements for Fiscal Year 2019

Dear Chairman Mendelson:

Included herein is the Office of the District of Columbia Auditor's report, entitled "Sufficiency Certification for the Washington Convention and Sports Authority (Trading as Events DC) Projected Revenues and Excess Reserve to Meet Projected Operating and Debt Service Expenditures and Reserve Requirements for Fiscal Year 2019." Pursuant to D.C. Code §10-1203.05 (b), the District of Columbia Auditor is required to prepare and deliver to the Mayor, Council of the District of Columbia, Chief Financial Officer of the District of Columbia, and the Chairman of the Washington Convention and Sports Authority (WCSA) a certification of the sufficiency of WCSA's projected revenues and excess reserve to meet its projected expenditures and reserve requirements for the upcoming fiscal year (FY).

This certification letter report sets forth the Auditor's determination that the WCSA's FY 2019 projected revenue and excess reserve are sufficient to meet the requirements of the upcoming fiscal year.

Objective, Scope and Methodology

The objective of this analysis was to determine whether WCSA's projected dedicated tax revenue, operating revenue, and excess reserve will be sufficient to meet its projected operating and debt service expenditures and reserve funding requirements for FY 2019.

The scope of this analysis included WCSA's financial records and data for FYs 2015 through 2017 and FY 2018, as of March 31, 2018. Our analysis also included a review of WCSA's FY 2019 projected revenues, expenditures and reserves.

To accomplish our objective, we conducted a detailed review of WCSA's FY 2019 projected and historical operating revenues and expenses for the Convention and Meetings and Sports and Entertainment divisions. This review included an analysis of financial information included in WCSA's audited financial statements for FY 2015 through FY 2017, WCSA's FY 2018 internal financial statements (variance reports) as of March 31, 2018, and WCSA's FY 2018

and FY 2019 budget, as approved by the WCSA Board of Directors. We also analyzed trends in events booked at WCSA, and interviewed WCSA personnel.

In addition, we conducted a review of WCSA's FY 2019 non-operating revenues, non-operating expenses, and excess reserves.

In compliance with the D.C. Official Code, Section §10-1203.05 (b)¹ the Auditor conducted a sufficiency review to determine if WCSA's FY 2019 projected revenues and excess reserve were sufficient to meet WCSA's projected expenditures and reserve requirements. This sufficiency review was not conducted as an audit.

To conduct the sufficiency review, the Auditor relied on representations and other financial information provided by WCSA officials and dedicated tax revenue information provided by the Office of the Chief Financial Officer (OCFO) to determine the reliability and sufficiency of WCSA's projected revenues for FY 2019.

The Auditor notes that revenue, reserve, and expense estimates are based on information that can change rapidly, thus resulting in revisions to estimates after the Auditor's certification. Consequently, the Auditor does not, and cannot, guarantee the validity of revenue, reserve, and expense estimates.

The Auditor only certifies that the revenue estimate, expense estimate, and excess reserve estimate at the time of certification, as presented in Figure 5, appeared sufficiently supported and achievable by WCSA. Additionally, the validity and accuracy of the Auditor's sufficiency analysis and calculations are predicated upon the extent to which: (a) WCSA officials fully disclosed and provided the Auditor with reliable and accurate information regarding WCSA's operating and non-operating revenue, operating and capital improvement expenses, debt service and marketing contract costs, and other expenses relevant to the Auditor's sufficiency certification, and (b) OCFO officials provided sound estimates of dedicated tax revenues for the upcoming fiscal year.

1 D.C. Code § 10-1203.05 (b) states: "On or before July 15 of each year in which there is outstanding any indebtedness issued by the Authority pursuant to this chapter, the District of Columbia Auditor shall prepare and deliver to the Mayor, the Council, the Chief Financial Officer of the District of Columbia, and the Chairman of the Authority a certification relating to the upcoming fiscal year of the District as to the sufficiency of the sum of the projected revenues from the following:

(1) The taxes imposed pursuant to §§ 47-2002.02 and 47-2202.01 and transferred to the Authority by the Mayor pursuant to §§ 47-2002.03 and 47-2202.02, as such tax revenues are estimated by the Office of Tax and Revenue for such upcoming fiscal year, which estimates shall be delivered by the Office of Tax and Revenue to the Authority on or prior to July 1 of such year, excluding from such estimate any amounts relating to any surtax imposed pursuant to subsection (c) of this section;

(2) The projected operating revenues of the Authority for such upcoming fiscal year contained in the most recent multiyear financial plan of the Board submitted pursuant to § 10-1202.06(g); and

(3) Any amounts on deposit in any reserve fund or account (other than any debt service reserve fund or account for indebtedness of the Authority), which are in excess of the required minimum balance for such fund or account, as certified by the Authority, to meet the sum of (i) projected operating and debt service expenditures and reserve requirements (other than amounts included in clause (ii) below) of the Authority for the upcoming fiscal year contained in the most recent multiyear financial plan of the Board submitted pursuant to § 10-1202.06(g), and (ii) any amounts required, as certified by the Authority, to restore any reserves relating to indebtedness of the Authority to their required minimum balance.

Overview of the Components of the Sufficiency Review

WCSA's sufficiency calculation consists of WCSA's projected revenues, expenditures and excess reserves. An overview of each area reviewed is documented below.

Revenue

Operating Revenue

WCSA has two divisions that generate operating revenue: The Conventions and Meetings Division, which includes the Carnegie Library, and the Sports and Entertainment Division. WCSA's operating revenues include revenue generated from conventions and meetings, sports events, entertainment events, advertising and sponsorships, and office and retail space rentals. WCSA's FY 2019 operating revenue estimate is \$29.26 million and accounts for 13.6 percent of the total FY 2019 projected revenue.

Figure 1 presents WCSA's FY 2019 projected operating revenues per WCSA's FY 2019 budget.

FIGURE 1: WCSA's FY 2019 Projected Operating Revenues

Revenue Category	FY 2019 Projected Revenue
Walter E. Washington Convention Center	\$22,507,985
Sports and Entertainment Division	\$5,955,225
Carnegie Library	\$792,820
Total Operating Revenue	\$29,256,030

Non-Operating Revenue

WCSA receives non-operating revenue from dedicated taxes, Tax Increment Financing (TIF), an IRS subsidy, lease income, a District transfer to Destination DC, and interest income.

WCSA is projected to receive 69.4 percent of its FY 2019 projected revenue from dedicated taxes received from the District. WCSA receives 4.45 percent of the gross receipts for the sale or charges for any hotel room charges, and 1 percent of the gross receipts from the sale or charges on restaurant meals, alcoholic beverages consumed on the premises, and automobile rental or leasing charges.² The Chief Financial Officer (CFO) provides the dedicated tax revenue projection to WCSA. According to the CFO's quarterly revenue estimate, as of February 28, 2018,³ the FY

² See D.C. Code §§ 47-2002.02 and 47-2002.03.

³ The CFO quarterly estimate, provided on February 28, 2018, was used by WCSA to formulate the FY 2019 approved budget.

2019 dedicated tax revenue estimate is \$155.5 million, which includes an annual transfer from the District that is paid directly to Destination DC,⁴ a private non-profit that provides marketing services for the District. The transfer amount to Destination DC for FY 2019 is projected to be \$6.4 million.

WCSA receives TIF revenues, lease payments, and an IRS subsidy as a result of the Marriott Marquis hotel financing. TIF revenues are collected from a portion of the sales and use taxes and property taxes generated by the hotel. WCSA generates lease revenue from leasing the Plumber’s building⁵ to the owners of the Marriott Marquis hotel.

To finance the hotel project, one of the series of bonds issued was Build America Bonds. The bonds provide an IRS subsidy through a refundable tax credit paid in an amount equal to 35 percent of the total coupon interest payable to investors on these taxable bonds. During FY 2019 the projected non-operating revenue from the TIF revenues, lease payments, and IRS subsidy is projected to be \$28.7 million.

Figure 2 presents WCSA’s FY 2019 projected non-operating revenues per WCSA’s FY 2019 budget.

FIGURE 2: WCSA’s FY 2019 Projected Non-Operating Revenues

Revenue Category	FY 2019 Projected Revenue
Dedicated Taxes	\$149,109,981
Interest Income	\$1,500,000
TIF Revenue – Hotel	\$20,201,503
IRS Subsidy – Hotel bonds	\$2,479,408
District Transfer to DDC Marketing	\$6,433,064
District Ground Lease Payment – Hotel	\$3,415,469
Lease Income – Plumber’s Building	\$2,588,670
Total Non-Operating Revenue	\$185,728,095

4 Destination DC is designated as the WCSA’s primary contractor to: (i) market and sell meetings and conventions for the Walter E. Washington Convention Center and District hotels; (ii) market and promote the District as a destination; and, (iii) increase revenue to the District and WCSA by maximizing sales of hotel rooms and restaurant meals.

5 The Marriott Marquis hotel incorporates the site’s original historic Samuel Gompers AFL-CIO headquarters, known as the “Plumber’s Building”.

Expenses

Operating Expenses

WCSA's operating expenses include personal services, professional/contractual services, utility costs, subsidies and transfers, and the cost of equipment and supplies.

As provided in Figure 3, WCSA's FY 2019 operating expense projection is approximately \$70.74 million.

FIGURE 3: WCSA's FY 2019 Projected Operating Expenses

Expense Category	FY 2019 Projected Expenses
Walter E. Washington Convention Center	\$56,759,010
Sports and Entertainment Division	\$13,129,611
Carnegie Library	\$847,381
Total Operating Expenses	\$70,736,002

Non-Operating Expenses

Non-operating expenses include payments to marketing agencies to promote conventions and tourism, debt service payments and possessory interest tax.⁶

As provided in Figure 4, WCSA's FY 2019 non-operating expense projection is \$77.2 million.

FIGURE 4: WCSA's FY 2019 Projected Non-Operating Expenses

Expense Category	FY 2019 Projected Expenses
Marketing Fund	\$27,602,818
Debt Service	\$49,048,252
Possessory Interest Tax	\$500,000
Total Non-Operating Expenses	\$77,151,070

⁶ In the District, government-owned real property used for governmental purposes is exempt from taxation. See D.C. Code § 47-1002(2). The Entertainment and Sports Arena (ESA) is owned by the District and is exempt from real property taxes. Events DC leases the ESA in connection with a business, and the use is not for an exempt purpose. See D.C. Code § 47-1005.01(b). In FY 2019, Events DC anticipates that the ESA will be assessed a possessory interest tax by the District.

Excess Reserves

The Amended and Restated Master Trust Agreement requires WCSA to establish and maintain certain funds and sub-accounts, referred to as pledged funds, in connection with WCSA's issuance of bonds. The establishment and funding of the various required funds and sub-accounts ensures that WCSA will have funds available for the repayment of bond principal and interest. Balances remaining in the various required funds and sub-accounts, after deducting the minimum balance requirements, represent WCSA's "excess reserve." WCSA has the authority to use its excess reserve to cover projected operating and debt services expenditures and reserve requirements.

Results of the Auditor's Examination

We conducted detailed analysis over each component of WCSA's FY 2019 sufficiency calculation presented in Figure 5 (page 8). Noted below are key observations based on our review.

Convention and Meetings Division

For FYs 2015 through 2017, the Walter E. Washington Convention Center has consistently exceeded its operating revenue projections, which indicates that leadership is adept at creating a reasonable, attainable budget, and balancing the venue's revenues and expenses. As of March 31, 2018, the Walter E. Washington Convention Center collected 52 percent of its FY 2018 projected operating revenue, and is on pace to meet or exceed the annual budget projection.

Beginning in FY 2017, WCSA gave renewed emphasis to the development of retail options on the ground level of the Convention Center building around its perimeter. Lease agreements have been executed with seven retailers, all with either 5-year or 10-year terms, creating a strong revenue stream for the Division.

City-wide events are conventions, meetings and trade shows that are international, national or regional in nature, and have a significant economic impact on the hotel community, with a minimum of 2,500 room nights on peak.⁷ In FY 2018, 18 city-wide events had a marked impact on operating revenue, and the Division is looking forward to a projected 17 city-wide events in FY 2019. City-wide events increase the number of individuals visiting the District, ultimately increasing revenue for both WCSA and the District.

Given the trend of meeting or exceeding revenue projections over the past several fiscal years, it appears reasonable that the Division will meet its FY 2019 operating revenue projection.

Carnegie Library, a component of the Convention and Meetings division, has been challenged to meet their overall revenue projection in recent years. Although the building was well-suited for hosting events, and routinely used for that purpose, use of the facility as a special events venue ceased after its last event was held on July 29, 2017. Effective August 9, 2017, WCSA entered into an agreement with Apple, Inc. to lease the building. The FY 2019 rental revenue for the building is expected to be \$792,820. The Historical Society of Washington will continue tenancy of the building.

⁷ "Peak room nights" are referring to the night during an event when most rooms are occupied by those in attendance.

WCSA's Sports and Entertainment Division

The Sports and Entertainment Division has been challenged to meet their overall revenue projections in recent years, except for FY 2016, the division exceeded revenue projections by \$268 thousand, 4.8 percent. As of March 31, 2018, the Sports and Entertainment division had collected 33 percent of its FY 2018 projected operating revenue, and is not on pace to meet the annual budget projection.

WCSA and the District agreed to jointly finance a new, multipurpose entertainment and sports arena and practice/training facility, currently referred to as the Entertainment and Sports Arena (ESA).⁸ The original budget for the ESA was projected not to exceed \$55 million, with a financial contribution from WCSA of \$27.5 million. However, after finalizing the plans for the arena, the total cost increased to \$65.5 million – increasing WCSA's contribution to the project by approximately \$10.5 million, for a total of \$38 million. The increase in funding was approved by WCSA Board of Directors on August 11, 2016. As of March 31, 2018, WCSA had paid \$32.9 million. The projected completion date for the ESA is September 2018.

The Sports and Entertainment Division's FY 2019 operating revenue estimate is \$6.0 million, an increase of 20 percent from FY 2018 projections. Considering SED's historical revenue collections, the FY 2019 revenue estimate is aggressive, and will require significant and intentional efforts of the SED team to achieve the revenue estimate. With multiple properties at its disposal for use as event venues, the SED has the flexibility to offer a variety of options to potential customers looking to host events in DC. SED's arena and festival-style destinations such as the new ESA, Robert F. Kennedy Memorial Stadium (RFK), the Festival Grounds at RFK, the DC Armory, and Gateway DC, provide options for events that attract different sized audiences and utilize indoor or outdoor spaces.

The Division's ability to meet its FY 2019 revenue projections of \$6 million will be dependent on its ability to schedule events and generate revenue at a greater pace than it has in the past few years.

Conclusion

Based upon a comparative analysis of WCSA's projected revenues and excess reserve, the Auditor determined that WCSA's projected revenues and excess reserve should be sufficient to cover its expenditures and reserve requirements for FY 2019 barring any unforeseen events that would adversely impact revenues and expenditures.

The Auditor's analysis indicated that WCSA's projected FY 2019 revenues and excess reserve should exceed expenditures by approximately \$188.97 million. Figure 5 (next page) presents WCSA's FY 2019 sufficiency calculation.

⁸ The ESA is jointly financed by WCSA and the District, with WCSA the District and Monumental Sports and Entertainment contributing funds to the project. The District will contribute \$23 million and \$4.5 million from Monumental Sports and Entertainment.

FIGURE 5: Fiscal Year 2019 Sufficiency Calculation

CATEGORY	AMOUNT (IN MILLIONS)
Revenues (Estimate)	
Dedicated Tax (February 2018 estimate)	\$149.10
TIF Revenue	20.20
IRS Subsidy	2.48
0.3% Additional hotel tax	6.43
Operating Revenue	29.26
Lease Payments	6.00
Interest Income	1.50
Subtotal Revenues	\$214.97
Reserves (Estimate)	
Excess reserves	\$176.07
Sum of Projected FY 2019 Revenues and Excess Reserve Estimate	\$391.04
Expenditures (Estimate)	
Debt Service	\$49.05
Operating Expenditures	70.74
Marketing Agencies	27.60
Capital Improvement Expenditures	52.68
District Payment and Possessory Tax	2.00
Sum of Projected FY 2019 Expenditures	\$202.07
WCSA's Projected Revenue and Excess Reserve Estimate Over Projected Expenditures	\$188.97

Source: WCSA Cash and Investment Manager

Auditor's Certification

Based upon the Auditor's analysis of information provided by the Washington Convention and Sports Authority (WCSA) and the Office of the Chief Financial Officer (OCFO), as of the date of this certification, July 13, 2018, WCSA's total projected revenues and excess reserve estimate for FY 2019 are sufficient to cover its projected expenditures. WCSA's FY 2019 estimated revenues and excess reserve are expected to exceed its projected expenditures and reserve requirements by \$188.97 million. This, we believe, constitutes a reasonable basis for the Auditor's sufficiency certification.

Sincerely,

A handwritten signature in blue ink that reads "Kathleen Patterson". The signature is written in a cursive style.

Kathleen Patterson
District of Columbia Auditor

Cc: Betsy Cavendish, EOM
Gregory O'Dell, Events DC
Henry Mosely, Events DC

About ODCA

The mission of the Office of the District of Columbia Auditor (ODCA) is to support the Council of the District of Columbia by making sound recommendations that improve the effectiveness, efficiency, and accountability of the District government.

To fulfill our mission, we conduct performance audits, non-audit reviews, and revenue certifications. The residents of the District of Columbia are one of our primary customers and we strive to keep the residents of the District of Columbia informed on how their government is operating and how their tax money is being spent.

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