SAN DIEGO CONVENTION CENTER CORPORATION
(A Component Unit of the City of San Diego, California)

Annual Financial Report

For the Year Ended June 30, 2018

MGO Certified Public Accountants

SAN DIEGO CONVENTION CENTER CORPORATION
Annual Financial Report
For the Year Ended June 30, 2018

Table of Contents

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, 2018, 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.

Macias Gini & O'Connell LLP
12264 El Camino Real, Suite 402
San Diego, CA 92130

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, 2018, 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 3-8 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 29, 2018, 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 the effectiveness of the SDCCC's 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 29, 2018

MANAGEMENT'S DISCUSSION AND ANALYSIS

SAN DIEGO CONVENTION CENTER CORPORATION
Management's Discussion and Analysis
For the Year Ended June 30, 2018
(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, 2018. 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 and liabilities as of June 30, 2018, with the difference 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.

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.

SDCCC FINANCIAL STATEMENT ANALYSIS

The following is a summary of SDCCC's assets, liabilities and net position comparing FY 2018 with FY 2017.

	FY 2018	FY 2017	Percentage Increase (Decrease)
ASSETS:			
Cash and cash equivalents	$ 13,780,846	$ 10,951,043	26%
Investments	3,544,159	--	--
Accounts receivable	6,546,869	8,373,155	(22%)
Prepaid expenses	596,518	630,506	(5%)
Deposits with others	131,072	124,702	5%
Inventory	38,416	38,416	--
Restricted cash - I-Bank contingency	826,954	826,954	--
Restricted investment - I-Bank construction fund	2,384,060	19,128,822	(88%)
Note receivable	574,556	--	--
Capital assets, net	36,571,170	23,589,252	55%
Total assets	64,994,620	63,662,850	2%
LIABILITIES:			
Accounts payable	2,209,370	1,068,083	107%
Accrued liabilities and compensated absences	3,167,794	4,108,732	(23%)
Retention payable	883,250	--	--
Unearned income	5,327,048	5,741,756	(7%)
Current portion of long-term debt	2,197	2,197	--
Long-term portion of unearned income	4,404,764	4,874,725	(10%)
Long-term debt	25,508,240	25,510,437	0%
Total liabilities	41,502,663	41,305,930	0%
NET POSITION:			
Net investment in capital assets	13,647,288	16,898,738	(19%)
Restricted – I-Bank contingency	826,954	826,954	--
Unrestricted	9,017,715	4,631,228	95%
Total net position	$ 23,491,957	$ 22,356,920	5%

SDCCC FINANCIAL STATEMENT ANALYSIS (Continued)

Assets

Total Assets of $65.0 million at FY 2018 year-end increased by $1.3 million, or 2%, from the prior year-end balance of $63.7 million. The changes were primarily due to an increase in cash and cash equivalents and investments of $6.4 million, or 58%, as well as an increase in capital assets, net of depreciation of $13.0 million, or 55%, offset by a decrease in restricted investment of $16.7 million, or 88% related to capital infrastructure projects. The net increase in cash and equivalents and investments was primarily due to the timing of FY2017 year-end capital purchases of $3.6 million reimbursed from restricted cash from I-Bank loan proceeds during September 2017, as well as $1.8 million of payments received in July 2017 related to food and beverage and utility commissions invoiced for an event hosted in June 2017. An increase in capital assets, net of depreciation, for capital improvement projects purchases of $13.0 million, or 55%, was directly offset by a decrease in I-Bank restricted investment of $16.7 million related to earmarked capital infrastructure projects.

Liabilities

Total Liabilities of $41.5 million at FY 2018 year-end increased by $0.2 million from a balance of $41.3 million in FY 2017 with significant offsetting category fluctuations. The changes were due to a decrease in accrued liabilities of $0.9 million, or 23%, a decrease in unearned income of $0.9 million, or 8%, offset by an increase in accounts payable of $1.1 million, or 107% as well as $0.9 million related to retention payable. The decrease in accrued liabilities was substantially due to $0.9 million reclassification of retention payments to a separate reporting category as well as a reduction in accrued payroll related expenses and note payable interest due in August 2018 compared to prior year. The increase in accounts payable related to $0.5 million payroll taxes due in July 2018, as well as $0.7 million for large construction progress payments due.

Net Position

Total Net Position of $23.5 million at FY 2018 year-end increased by $1.1 million, or 5%, compared to the prior year balance of $22.4 million. Unrestricted net position increased by $4.4 million compared to the prior due to excess revenues over expenses of $1.1 million, as well as net I-Bank capital infrastructure projects reimbursements exceeding capital purchases of $3.3 million directly offset by a decrease in net investment in capital assets of $3.2 million compared to the prior year.

SDCCC FINANCIAL STATEMENT ANALYSIS (Continued)

The following table summarizes the changes in net position for SDCCC comparing FY 2018 with FY 2017.

	FY 2018	FY 2017	Percentage Increase (Decrease)
Operating Revenues:			
Rental	$ 9,150,619	$ 9,178,411	0%
Food and beverage	9,486,165	11,330,266	(16%)
Ancillary services	15,619,060	15,997,246	(2%)
Contributions from the City of San Diego	3,436,000	3,436,000	0%
Business development	204,382	--	--
Other revenue	30,175	83,445	(64%)
Total operating revenues	37,926,401	40,025,368	(5%)
Operating Expenses:			
Salaries and benefits	21,701,984	21,468,463	1%
Services and supplies	11,419,373	11,012,446	4%
Depreciation	2,315,400	1,778,470	30%
Marketing contract	1,971,000	1,931,000	2%
Total operating expenses	37,407,757	36,190,379	3%
Operating Income	518,644	3,834,989	
Nonoperating Revenues (Expenses):			
Interest income	165,690	77,791	113%
Interest expense	(572,190)	(151,469)	278%
Loan origination fee	--	(255,000)	--
Loss on disposal of capital assets	(6,276)	(418,255)	(98%)
Other income	811,113	791,631	2%
Total nonoperating revenues, net	398,337	44,698	791%
Income before capital contributions	916,980	3,879,687	
Capital Contributions	218,056	168,551	29%
Change in net position	1,135,037	4,048,238	
Net position - beginning of year	22,356,920	18,308,682	
Net position - end of year	$ 23,491,957	$ 22,356,920	5%

SDCCC FINANCIAL STATEMENT ANALYSIS (Continued)

Operating Revenues

Total operating revenues generated in FY 2018 amounted to $37.9 million, a $2.1 million, or 5% decrease compared to the prior year's total of $40.0 million. The change was primarily the result of overall less event activity, primarily in decreased food and beverage commissions of $1.8 million, or 16%, as well as decreased ancillary services of $0.4 million, or 2%, compared to prior year.

Operating Expenses

Total operating expenses incurred during FY 2018 amounted to $37.4 million, a $1.2 million, or 3% increase compared to the prior year's total of $36.2 million. Depreciation expense increased by $0.5 million, or 30%, compared to the prior year due to nearly $22 million of I-Bank funded capital infrastructure projects placed in service over the last eighteen months. Additionally, increased repair and maintenance projects of $0.4 million, or 4% as well as salary and fringe benefit expenses of $0.2 million, or 1% related to increased worker's compensation claims.

Nonoperating Revenues and Expenses

During FY 2018, nonoperating revenues and expenses produced $0.4 million with offsetting category fluctuations compared to virtually zero net revenues produced in the prior year. The change was due to $0.8 million in food and beverage incentives and procurement card and recycling rebate programs as well as $0.1 million increase in interest income, offset by $0.5 million increase in I-Bank loan interest expense related to earmarked capital infrastructure projects.

CAPITAL ASSET ANALYSIS

As of June 30, 2018, SDCCC had a capital asset book value of $36.6 million, net of accumulated depreciation of $28.0 million, or 55% more than the prior year figure of $23.6 million. Capital assets spread across a broad range of computer, office and operating equipment, telecommunications and leasehold improvements. The gross value of capital purchases in FY 2018 of $15.3 million increased compared to prior year additions of $13.9 million due to infrastructure capital improvements purchased of $13.3 million.

Major capital asset additions during FY 2018 included:

- $9,314,866 for Sail Pavilion roof fabric replacement
- $1,571,591 for fire water cannon replacements
- $1,330,234 for escalator retrofit work
- $854,212 for fire alarm system replacement
- $435,105 for elevator modernization work

DEBT ANALYSIS

Effective December 6, 2016, SDCCC and the City of San Diego entered into a financing lease agreement with the California Infrastructure and Economic Development Bank to finance capital infrastructure improvement projects valued at $25,500,000. The agreement calls for the loan to be amortized after two years at a 3.59 percent interest rate. For the year ended June 30, 2018, SDCCC incurred $915,450 in interest expense, $381,438 due payable in August 2018.

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. SDCCC exercised an option to extend for an additional five years effective April 1, 2018. For the year ended June 30, 2018, SDCCC paid $2,197 in principal payments on the warehouse loan.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGET

FY 2018 operational contributions from the City remained at $3,436,000 compared to prior year contributions. As described in Note 6, contributions from the City funded marketing, promotion and capital projects for the Convention Center. During FY 2018, total expenses on marketing, promotion and 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)). Effective July 1, 2017, a marketing and sales contract between SDCCC and SDTA was renegotiated and approved by City Council detailing the terms set forth by the City. For the year ended June 30, 2018, SDCCC paid $1.9 million in marketing contract payments related to SDTA.

Management is anticipating an increase in financial performance during FY 2019 as compared to FY 2018 due to record breaking medical convention events contracted as compared to FY 2018. The City's operational contributions to SDCCC were reduced from $3,436,000 to $2,133,025 beginning in FY 2019.

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.

BASIC FINANCIAL STATEMENTS

SAN DIEGO CONVENTION CENTER CORPORATION

Statement of Net Position

June 30, 2018

ASSETS		
Current assets:		
Cash and cash equivalents	$	13,780,846
Investments		3,544,159
Accounts receivables		5,046,869
Prepaid expenses		596,518
Deposits with others		131,072
Inventory		38,416
Total current assets		23,137,880
Noncurrent assets:		
Restricted cash - I-Bank contingency reserve		826,954
Restricted investment - I-Bank construction loan proceeds		2,384,060
Accounts receivables		1,500,000
Note receivable		574,556
Capital assets:		
Construction in progress		2,971,303
Furniture, equipment and software		5,104,884
Leasehold improvements		56,557,789
Less accumulated depreciation		(28,062,806)
Total capital assets		36,571,170
Total noncurrent assets		41,856,740
TOTAL ASSETS		64,994,620
LIABILITIES		
Current liabilities:		
Accounts payable		2,209,370
Accrued liabilities		1,969,938
Retention payable		883,250
Unearned income		5,327,048
Compensated employee absences		1,197,856
Current portion of long-term debt		2,197
Total current liabilities		11,589,659
Noncurrent liabilities:		
Long-term debt		25,508,240
Long-term portion of unearned income		4,404,764
Total noncurrent liabilities		29,913,004
TOTAL LIABILITIES		41,502,663
NET POSITION		
Net investment in capital assets		13,647,288
Restricted - I-Bank contingency		826,954
Unrestricted		9,017,715
TOTAL NET POSITION	$	23,491,957

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, 2018

Operating Revenues	
Rental Revenue:	
Convention and trade shows	$ 6,629,702
Corporate/incentive events	269,228
Consumer shows	558,260
Meetings and seminars	368,392
Cancelled events	657,400
Community events	498,909
Local trade shows	168,728
Food and beverage revenue	9,486,165
Ancillary service revenue:	
Utilities	5,902,621
Telecommunications	4,444,169
Event and cleaning services	4,110,291
Audio visual	1,161,979
Contributions:	
City of San Diego	3,436,000
Business development	204,382
Other revenue	30,175
Total operating revenues	37,926,401
Operating Expenses	
Salaries and wages	16,675,829
Fringe benefits	5,026,155
Utilities	4,110,677
Repairs and maintenance	2,884,233
General	2,320,891
Depreciation	2,315,400
Contractual marketing and sales	1,971,000
Contracted services	874,749
Supplies	606,265
Insurance	347,613
Travel and transportation	123,718
Sales and marketing	111,600
Telecommunications	39,627
Total operating expenses	37,407,757
Operating income	518,644
Nonoperating Revenues (Expenses)	
Interest income	165,690
Interest expense	(572,190)
Loss on disposal of capital assets	(6,276)
Other income	811,113
Total nonoperating revenues, net	398,337
Income before capital contributions	916,981
Capital contributions	218,056
Change in net position	1,135,037
Net position - beginning of year	22,356,920
Net position - end of year	$ 23,491,957

See Accompanying Notes to the Basic Financial Statements.

SAN DIEGO CONVENTION CENTER CORPORATION
Statement of Cash Flows
For the Year Ended June 30, 2018

CASH FLOWS FROM OPERATING ACTIVITIES	
Receipts from customers	$ 36,243,131
Contributions received from City of San Diego	3,436,000
Payments to suppliers for goods and services	(12,715,696)
Payments to employees for services	(21,404,100)
Net cash provided by operating activities	5,559,335
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES	
Acquisition and construction of capital assets	(14,495,020)
Loan to Centerplate for equipment	(574,556)
Principal payments on note payable	(2,197)
Interest paid on long-term debt	(1,055,265)
Proceeds from the sale of capital assets	31,213
Net cash used by capital and related financing activities	(16,095,825)
CASH FLOWS FROM INVESTING ACTIVITIES	
Purchase of investments	(3,544,159)
Proceeds from restricted investment	16,744,762
Interest received	165,690
Net cash used in investing activities	13,366,293
INCREASE IN CASH AND CASH EQUIVALENTS	2,829,803
CASH AND CASH EQUIVALENTS - BEGINNING OF YEAR	11,777,997
CASH AND CASH EQUIVALENTS - END OF YEAR	$ 14,607,800

See Accompanying Notes to the Basic Financial Statements.

SAN DIEGO CONVENTION CENTER CORPORATION
Statement of Cash Flows (Continued)
For the Year Ended June 30, 2018

RECONCILIATION OF CASH AND CASH EQUIVALENTS TO THE STATEMENT OF NET POSITION		
Cash	$	13,780,846
Restricted cash - I-Bank contingency reserve		826,954
'Total cash and cash equivalents	$	14,607,800
RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES		
Operating income	$	518,644
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation		2,315,400
Other income		811,113
Changes in operating assets and liabilities:		
Decrease in receivables		1,826,286
Decrease in prepaid expenses		33,988
Increase in deposits with others		(6,370)
Increase in accounts payable		647,059
Decrease in compensated employee absences		(143,992)
Increase in accrued liabilities		441,876
Decrease in unearned income		(884,669)
Net cash provided by operating activities	$	5,559,335
NONCASH CAPITAL AND FINANCING ACTIVITIES		
Capital asset contributions	$	218,056
Acquisition of capital assets included in accounts payable and accrued liabilities		646,341
Capitalized interest		343,214
Carrying value of disposed capital assets		6,276

NOTES TO THE BASIC FINANCIAL STATEMENTS

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.

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 mutual fund restiricted investment is not considered to be a cash and cash equivalent.

NOTE 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

C. *Accounts Receivable*

Long-term receivables in the amount of $1,500,000 represent incentive payments to be received by SDCCC 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. *Note Receivable*

In January 2018, SDCCC entered into a non-interest bearing agreement with Centerplate for SDCCC to fund the purchase of food service equipment in the principal amount of $574,556. The principal amount is due and payable in full by Centerplate no later than June 30, 2023, unless the contract is terminated prior to the due date. Centerplate has the right to fully pay the principal amount owed to SDCCC prior to the due date with no prepayment penalty. If the contract is terminated prior to the due date, the remaining principal amount owed to SDCCC becomes due and payable within 30 days from the date of termination.

E. *Prepaid Expenses*

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

F. *Inventory*

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

G. *Capital Assets*

Capital assets are reported at cost. Capital assets are defined as assets with an initial cost of more than $5,000 per item and a useful life of greater than one year. For assets acquired from the proceeds received from the I-Bank financing lease, SDCCC capitalizes a portion of the interest incurred in accordance with the provisions of GASB Statement No. 62. The amount of interest capitalized as part of the underlying assets historical cost is the amount of interest that would have been avoided during the assets acquisition period if the asset had not been acquired. The amount capitalized is determined by applying the interest rate on the financing lease to the average amount of accumulated capital outlays for the asset during the accounting period. Capital assets are depreciated using the straight-line method over the following estimated useful lives:

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

NOTE 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

H. *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.

I. *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 120 hours paid compensation in lieu of annual leave provided they maintain a minimum balance of 40 hours and have taken a minimum of 80 hours of paid leave during the prior twelve month period. Additionally, non-represented part-time employees who have PTO balances in excess of 40 hours at fiscal year-end as well as represented part-time employees full PTO balance at fiscal year-end, are paid their annual leave balance within 30 days of fiscal year-end and carry over any remaining balance each year.

J. *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, 2018 was $13,647,288.

Restricted – This amount consists of restricted assets which are reduced by liabilities related to those assets. As of June 30, 2018, the amount of restricted net position remained at $826,954 due to the required reserves associated with the I-Bank 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".

K. *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). However, the Corporation is subject to income taxes on any net income that is derived from a trade or business carried on, and not in furtherance of the purposes for which it was granted exemption. No income tax provision has been recorded as the net income, if any, from any unrelated trade or business, in the opinion of management, is not material to the accompanying financial statements.

L. *Use of Estimates*

The preparation of financial statements in conformity with accounting principles generally accepted in the Unites 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 AND INVESTMENTS, RESTRICTED CASH AND RESTRICTED INVESTMENTS

At June 30, 2018, the book balance of SDCCC's cash on hand, deposits, and bank money market account deposits was $9,113,759 and the bank balance was $9,154,666. 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 and amended in December 2017 by SDCCC's Board of Directors, which addresses custodial credit risk, interest rate risk, credit quality risk and allowable investments. SDCCC is provided a broad spectrum of eligible investments under California Government Code (CGC) 53600 which includes: obligations of the U.S. government, its agencies and instrumentalities; investment grade state and local government securities; certificates of deposit; bankers' acceptances; commercial paper: repurchase agreements; and money market mutual funds whose portfolios consist only of domestic securities.

The SDCCC's Investment Policy is governed by the California Government Code (CGC), 56000 et seq. The following table represents the authorized investments, requirements and restrictions per the CGC and the SDCCC investment policy:

	Maximum Maturity		Maximum % of Portfolio		Minimum Rating	
Investment Type	CGC	SDCCC Policy [1]	CGC	SDCCC Policy	CGC	SDCCC Policy
Local Agency Bonds	5 years	5 years	None	None	None	None
U.S. Treasury Obligations (bills, notes, or bonds)	5 years	5 years	None	None	None	None
State Obligations – CA and Others	5 years	5 years	None	None	None	None
CA Local Agency Obligations	5 years	5 years	None	None	None	None
U.S. Agency Obligations	5 years	5 years	None	None	None	None
Bankers' Acceptances	180 days	180 days	40%	40%	None	None
Commercial Paper – Non-Pooled Funds	270 days	270 days	25%	25%	Highest letter and number rating	Highest letter and number rating
Negotiable Certificates of Deposit	5 years	5 years	30%	30%	None	None
Non-Negotiable Certificates of Deposit	5 years	5 years	None	None	None	None
CD Placement Service	5 years	5 years	30%	30%	None	None
Repurchase Agreements	1 year	1 year	None	None	None	None
Reverse Repurchase Agreements	92 days	92 days	20%	20%	None	None
Medium-Term Notes	5 years	5 years	30%	30%	A	A
Money Market Mutual Funds	None	None	20%	20%	AAA	AAA
Collateralized Bank Deposits	5 years	5 years	None	None	None	None
Mortgage Pass-Through Securities	5 years	5 years	20%	20%	AA	AA
Local Agency Investment Fund	None	None	None	None	None	None
Supranational Obligations	5 years	5 years	30%	30%	AA	AA
Insured Savings & Bank Money Market Accounts	N/A	N/A	N/A	N/A	N/A	N/A

[1] In the absence of a specified maximum, the maximum is 5 years.

NOTE 3. CASH AND INVESTMENTS, RESTRICTED CASH AND RESTRICTED INVESTMENTS (Continued)

Cash/restricted cash and investments/restricted investments as reported in the statement of net position are categorized as follows at June 30, 2018:

	Cash and Cash Equivalents	Investments	Restricted Cash	Restricted Investments
Cash on hand	$ 6,135	$ -	$ -	$ -
Bank checking and savings deposits	3,499,918	-	826,954	-
Bank money market account deposits	4,780,752	-	-	-
Fixed income investments	5,494,041	1,893,436	-	-
Government money market mutual funds	-	1,650,723	-	2,384,060
Total	$ 13,780,846	$ 3,544,159	$ 826,954	$ 2,384,060

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. Fair value is defined as the quoted market value on the last trading day of the period, obtained from various pricing sources by our custodian bank. SDCCC does not value any of its investments using Level 1 and Level 3 inputs. Investment in repurchase agreements are valued at amortized cost and is exempt from the fair value hierarchy. Investments that are measured at fair value using the net asset value (NAV) per share (or its equivalent) are not classified in the fair value hierarchy. SDCCC's values investments in government money market mutual funds at NAV, and therefore are not subject to the fair value hierarchy.

The table below represents SDCCC's fair value hierarchy for reporting its investments as of June 30, 2018:

	Fair Value	Level 2
Investments at fair value level		
U.S.Treasury Bills	$ 299,211	$ 299,211
U.S. Agency Obligations	2,743,588	2,743,588
Commercial Paper	1,844,636	1,844,636
Negotiable Certificates of Deposit	1,300,042	1,300,042
Total investments at fair value	6,187,477	6,187,477
Investments measured at amortized cost:		
Repurchase Agreement	1,200,000	
Investments measured at the net asset value (NAV):		
Government Money Market Mutual Funds	4,034,783	
Total investments	$ 11,422,260	

NOTE 3. CASH AND INVESTMENTS, RESTRICTED CASH AND RESTRICTED INVESTMENTS (Continued)

GASB Statement No. 40 requires that risks for deposits and investments with fair values as it relates to credit risk, concentration of credit risk, and interest rate risk be disclosed. SDCCC minimizes exposure by limiting investments to short-term, safe securities such as mutual funds or similar investment pools to ensure preservation of capital as well as pre-qualifying brokers and diversification of the investment portfolio. In order to maintain proper cash flow requirements, funds are continuously invested in readily available securities to ensure appropriate liquidity is maintained.

Interest Rate Risk

Interest rate risk is the risk that the fair value of the securities may fall due to changes in interest rates. SDCCC mitigates this risk by investing in short-term securities of less than a year in order to meet operational cash requirements, structuring the investment portfolio to allow securities to mature to avoid selling on the open market. As of June 30, 2018, SDCCC's investment interest rate risk by maturity is as follows:

	Investment Maturity in Months			
	Under 1	1 - 6	6 - 12	Fair Value
U.S. Treasury bills	$ -	$ 299,211	$ -	$ 299,211
U.S. Agency obligation	499,350	2,244,238	-	2,743,588
Commercial Paper	499,517	1,345,119	-	1,844,636
Negotiable Certificats of Deposit	-	1,300,042	-	1,300,042
Government Money Market Mutual Funds	1,650,723	-	2,384,060	4,034,783
Repurchase Agreement	1,200,000	-	-	1,200,000
	$ 3,849,590	$ 5,188,610	$ 2,384,060	$ 11,422,260

Credit Risk

Credit risk is the risk that an issuer of an investment will not fulfill their obligation to the holder of the investment. This is measured by the assignment of a rating by a nationally recognized statistical rating organization (NRSRO). The SDCCC mitigates credit risk through its Investment Policy. Section I of the Investment Policy outlines the authorized investments, requirements, and investment restrictions. As of June 30, 2018, SDCCC's investment and correspondieng credit ratinges are follows:

	Fair Value	Credit Rating
U.S. Treasury Bills	$ 299,211	Exempt
U.S. Agency Obligations	2,743,588	A-1+
Commercial Paper	796,192	A-1+
Commercial Paper	1,048,444	A-1
Negotiable Certificates of Deposit	600,028	A-1+
Negotiable Certificates of Deposit	700,414	A-1
Government Money Market Mutual Fund	1,650,723	AAA
Government Money Market Mutual Fund	2,384,060	Not Rated
Repurchase Agreement	1,200,000	AAA

NOTE 3. CASH AND INVESTMENTS, RESTRICTED CASH AND RESTRICTED INVESTMENTS (Continued)

Concentration of Credit Risk

GASB Statement No. 40 also requires disclosure of investments in any one issuer (other than U.S. Treasury securities, mutual funds, and external investment pools) that represent 5% or more of total investments. A summary of disclosures related to concentration of credit risk as of June 30, 2018 is as follows:

Issuer	Investment Type	Fair Value
Federal Home Loan Bank	U.S. Agency Securities	$ 1,950,702
INTL FCStone Financial Inc.	Repurchase Agreement	1,200,000

Custodial Credit Risk

Custodial credit risk for *deposits* is the risk that, in the event of the failure of a depository financial institution, a government will not be able to recover its deposits or will not be able to recover collateral securities that are in the possession of an outside party. The custodial credit risk for *investments* is the risk that, in the event of the failure of the counterparty (e.g., broker-dealer) to a transaction, a government will not be able to recover the value of its investment or collateral securities that are in the possession of another party. The California Government Code and SDCCC's investment policy do not contain legal or policy requirements that would limit the exposure to custodial credit risk for deposits or investments, other than the following provision for deposits: The California Government Code requires that a financial institution secure deposits made by state or local governmental units by pledging securities in an undivided collateral pool held by a depository regulated under state law (unless so waived by the governmental unit). The market value of the pledged securities in the collateral pool must equal at least 110% of the total amount deposited by the public agencies. California law also allows financial institutions to secure SDCCC deposits by pledging first trust deed mortgage notes having a value of 150% of the secured public deposits.

NOTE 4. CAPITAL ASSETS

A summary of changes in capital assets for the year ended June 30, 2018, is as follows:

	Beginning Balance June 30, 2017	Additions	Deletions	Transfers In/(Out)	Ending Balance June 30, 2018
Non-Depreciable Capital Assets:					
Construction in progress	$ 3,980,097	$ 15,062,112	$ -	$ (16,070,906)	$ 2,971,303
Depreciable Capital Assets:					
Furniture, equipment and software	5,349,561	495,211	(752,213)	12,325	5,104,884
Leasehold improvements	40,929,180	-	(176,243)	15,804,852	56,557,789
Total Depreciable Capital Assets	46,278,741	495,211	(928,456)	15,817,177	61,662,673
Less Accumulated Depreciation:					
Furniture, equipment and software	(3,871,318)	(369,735)	745,937	-	(3,495,116)
Leasehold improvements	(22,798,268)	(1,945,665)	176,243	-	(24,567,690)
Total Accumulated Depreciation	(26,669,586)	(2,315,400)	922,180	-	(28,062,806)
Total Depreciable Capital Assets - Net	19,609,155	(1,820,189)	(6,276)	15,817,177	33,599,867
Capital Assets, Net	$ 23,589,252	$ 13,241,923	$ (6,276)	$ (253,729)	$ 36,571,170

Depreciation expense for the year ended June 30, 2018 was $2,315,400. $343,214 of interest incurred during the year ended June 30, 2018 was capitalized.

NOTE 5. LONG-TERM LIABILITIES

A. *Compensated Employee Absences*

A summary of changes in accrued compensated employee absences for the year ended June 30, 2018 is as follows:

	Balance June 30, 2017	Additions	Retirements	Balance June 30, 2018	Current Portion
Compensated Employee Absences	$ 1,341,848	$ 1,478,776	$ (1,622,768)	$ 1,197,856	$ 1,197,856

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.

NOTE 5. LONG-TERM LIABILITIES (Continued)

On December 6, 2016, SDCCC (lessee) together with the City jointly entered into a financing lease agreement with the California Infrastructure and Economic Development Bank (I-Bank), as the lessor, in which the lessor financed facilities and building improvements anticipated to cost a total of approximately $25,300,000. 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, 2018, is as follows:

	Balance June 30, 2017	Additions	Retirements	Balance June 30, 2018	Current Portion
CG 7600 LP	$ 12,634	$ -	$ (2,197)	$ 10,437	$ 2,197
I-Bank financing lease	25,500,000	-	-	25,500,000	-
Total	$ 25,512,634	$ -	$ (2,197)	$ 25,510,437	$ 2,197

Annual requirements to amortize the notes payable as of June 30, 2018, including interest payments to maturity, are as follows:

Year Ending June 30,	Principal	Interest	Annual Fee	Total
2019	$ 2,197	$ 915,450	$ -	$ 917,647
2020	734,170	891,362	76,500	1,702,032
2021	760,448	864,219	74,304	1,698,971
2022	787,669	836,102	72,029	1,695,800
2023	815,318	806,976	69,673	1,691,967
2024 - 2028	4,528,058	3,560,044	309,949	8,398,051
2029 - 2033	5,401,336	2,658,029	236,973	8,296,338
2034 - 2038	6,443,033	1,582,051	149,923	8,175,007
2039 - 2042	6,038,208	352,776	46,085	6,437,069
Total	$ 25,510,437	$ 12,467,009	$ 1,035,436	$ 39,012,882

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, 2018, SDCCC received $3,436,000 from the City, of which $1,971,000 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 $1,465,000 was used to fund various capital projects.

Moving into FY 2019, SDCCC anticipates that contributions from the City will be reduced to $2,133,025, to be used to fund marketing contract expenses.

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.

Full time employees are eligible to participate in the plan on the first day of the month after completing 1,000 hours of service and receive contributions on a bi-weekly basis thereafter. Part-time employees are eligible to participate in the plan after completion of 1,000 hours and receive contributions annually once they meet the 1,000 hours threshold requirement each 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, 2018, pension expense amounted to $1,246,876 with no employee contributions made to the Plan. Included in pension expense were forfeitures in the amount of $19,105. SDCCC records pension expense during the fiscal year based upon employee compensation that is included in qualified gross compensation.

NOTE 8. 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 and exercised its option to extend for an additional five years effective April 1, 2018 – March 31, 2023. Future minimum annual rental lease revenues are as follows:

Year Ending June 30,	Amount
2019	$ 141,908
2020	145,980
2021	149,973
2022	153,905
2023	118,356
	$ 710,122

Rental income related to the sublease was $136,708 for the year ended June 30, 2018.

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:

Year Ending June 30,	Amount
2019	$ 241,384
2020	247,457
2021	251,106
2022	228,813
2023	175,307
Total	$ 1,144,067

Lease expense for the year ended June 30, 2018 was $233,984.

NOTE 8. COMMITMENTS (Continued)

Construction Commitments

SDCCC has material commitments under construction contracts as of June 30, 2018 as follows:

Construction Projects	Remaining Construction Value	Expected Completion Year
Rooftop HVAC Replacement	$ 906,453	FY 2021
Retrofit Elevators	725,783	FY 2019
Convert Pneumatic Controls	723,520	FY 2019
Proximity Lock Replacement	457,742	FY 2020
Cooling Actuators	309,579	FY 2019
Fire Alarm System Replacement	119,227	FY 2019
	$ 3,242,303	

NOTE 9. 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, 2018, 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 29, 2018.

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 29, 2018