



**HAWAII CONVENTION CENTER**

Special-Purpose Financial Statements  
and Supplementary Information

June 30, 2012 and 2011

(With Independent Auditors' Report Thereon)

Submitted by

**THE AUDITOR  
STATE OF HAWAII**

# HAWAII CONVENTION CENTER

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## Independent Auditors' Report

The Auditor  
State of Hawaii:

We have audited the accompanying special-purpose balance sheets of the Hawaii Convention Center as of June 30, 2012 and 2011, and the related special-purpose statements of revenues, expenses, and changes in net assets, and cash flows for the years then ended. These special-purpose financial statements are the responsibility of the Hawaii Convention Center's management. Our responsibility is to express an opinion on these special-purpose 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 special-purpose financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Hawaii Convention Center's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the special-purpose financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

The accompanying special-purpose financial statements were prepared for the purpose of complying with the management agreement between the Hawaii Tourism Authority and SMG as described in note 2 to special-purpose financial statements, and are not intended to be a presentation in conformity with U.S. generally accepted accounting principles.

In our opinion, the special-purpose financial statements referred to above present fairly, in all material respects, the financial position of the Hawaii Convention Center as of June 30, 2012 and 2011, and the changes in its net assets and its cash flows for the years then ended, on the basis of accounting described in note 2.

Management's discussion and analysis on pages 3 through 7 is not a required part of the special-purpose financial statements but is supplementary information required by U.S. generally accepted accounting principles. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audits were conducted for the purpose of forming an opinion on the special-purpose financial statements taken as a whole. The supplementary information included in schedules 1 and 2 is presented for purposes of additional analysis and is not a required part of the special-purpose financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the special-purpose financial statements. The supplementary information has been subjected to the auditing procedures applied in the audits of the special-purpose financial statements and certain additional procedures, including comparing and



reconciling such information directly to the underlying accounting and other records used to prepare the special-purpose financial statements or to the special-purpose financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America, in our opinion, the supplementary information is fairly stated in all material respects in relation to the special-purpose financial statements taken as a whole.

This report is intended solely for the information and use of the Auditor, State of Hawaii and the boards of directors, and managements of the Hawaii Tourism Authority and SMG, and is not intended to be and should not be used by anyone other than these specified parties.

KPMG LLP

November 29, 2012

## HAWAII CONVENTION CENTER

### Management's Discussion and Analysis

June 30, 2012 and 2011

As financial management of the Hawaii Convention Center (the Center), we offer readers of these special-purpose financial statements this narrative overview and analysis of the financial activities of the Center for the fiscal years ended June 30, 2012 and 2011. SMG, a private management company, is contracted by the State of Hawaii (the State) through the Hawaii Tourism Authority (the Authority) to operate the Center. This discussion and analysis is designed to assist readers in focusing on the significant financial activities and to identify any significant changes in financial position. We encourage readers to consider the information presented here in conjunction with the special-purpose financial statements as a whole.

#### **Overview of the Special-Purpose Financial Statements**

This discussion and analysis is intended to serve as an introduction to the Center's special-purpose financial statements, which comprise the special-purpose financial statements and the notes to special-purpose financial statements. This report also contains other supplementary information concerning the Center's revenues, expenses, and changes in net assets.

#### ***Special-Purpose Financial Statements***

The special-purpose financial statements are designed to provide readers with a broad overview of the Center's finances in a manner similar to a private-sector business. The special-purpose financial statements have been prepared pursuant to the provisions of the management agreement between the Authority and SMG, and are intended to present the financial position, changes in net assets, and cash flows of only that portion of the Authority that is attributable to the transactions of the Center based upon the accounting records maintained by SMG. The Center's operations are reported under a flow of economic resources measurement focus using the accrual basis of accounting. The accounting policies of the Center conform in all material respects with U.S. generally accepted accounting principles, except that the property, building, furniture, and equipment used in the Center's operations, and related depreciation expense, as well as debt and the related interest expense, are not reflected on the accompanying special-purpose financial statements. Those assets, liabilities, and related expenses are reflected on the special-purpose financial statements of the Authority.

The special-purpose balance sheets present information on the Center's assets and liabilities with the difference between the two reported as net assets. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the Center is improving or deteriorating. Net assets increase when revenues and contributions from the State exceed expenses and funds remitted to the State. Increases to assets without a corresponding increase to liabilities result in increased net assets, which indicate an improved financial position.

The special-purpose statements of revenues, expenses, and changes in net assets present information showing how an entity's net assets changed during the fiscal year. All changes in net assets are reported as soon as the underlying event occurs, regardless of timing of related cash flows. Thus, revenues and expenses are reported in these statements for some items that will result in cash flows in future fiscal periods.

The special-purpose statements of cash flows present the inflows and outflows of cash for the year and are summarized by operating, financing, and investing activities. The statements are prepared using the direct method of cash flows and, therefore, present gross rather than net amounts for the year's operating activities.

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### Management's Discussion and Analysis

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#### *Notes to Special-Purpose Financial Statements*

The notes provide additional information that is essential to a full understanding of the data provided in the special-purpose financial statements.

#### *Supplementary Information*

In addition to the special-purpose financial statements and accompanying notes, this report also presents certain supplementary information concerning the Center's revenues, expenses, and changes in net assets.

#### *Financial Analysis*

Net assets may serve, over time, as a useful indicator of an entity's financial position. In the case of the Center, assets exceeded liabilities by \$13,710,070 at June 30, 2012, and assets exceeded liabilities by \$14,453,817 at June 30, 2011, and net assets decreased by \$743,747 or 5% from June 30, 2011 to June 30, 2012. The change in net assets is attributable to the Center's operations and sales and marketing activities and the funding of future sales and marketing efforts and capital improvements.

By far, the largest portion of the Center's current assets at June 30, 2012 was cash of \$2,764,003. The cash is to be utilized to pay for liabilities at June 30, 2012, including accounts payable of \$728,646, and amounts due to the Authority of \$876,533, and accumulation of advance deposits received from clients for future events in the amount of \$214,082. The cash will also be used for future sales and marketing efforts.

By far, the largest portion of the Center's current assets at June 30, 2011 was cash of \$4,400,944. The cash is to be utilized to pay for liabilities at June 30, 2011, including accounts payable of \$1,377,375, revenues collected for the Authority of \$1,193,203, and accumulation of advance deposits received from clients for future events in the amount of \$418,014. The cash will also be used for future sales and marketing efforts.

#### Hawaii Convention Center Net assets

	June 30			2012 – 2011		2011 – 2010	
	2012	2011	2010	Decrease	Percentage change	Increase	Percentage change
Total assets	\$ 15,961,596	18,084,034	14,366,945	(2,122,438)	(12)%	\$ 3,717,089	26%
Total liabilities	2,251,526	3,630,217	2,118,271	(1,378,691)	(38)	1,511,946	71
Net assets	\$ <u>13,710,070</u>	<u>14,453,817</u>	<u>12,248,674</u>	<u>(743,747)</u>	<u>(5)%</u>	<u>\$ 2,205,143</u>	<u>18%</u>

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**Hawaii Convention Center**  
Changes in Net assets

	June 30		2012 – 2011		2011 – 2010		
	2012	2011	2010	Increase (decrease)	Percentage change	Increase (decrease)	Percentage change
Operating revenues:							
Food and beverage	\$ 5,267,077	7,177,478	4,595,398	(1,910,401)	(27)%	\$ 2,582,080	56%
Rental income	2,188,557	3,840,679	2,478,592	(1,652,122)	(43)	1,362,087	55
Events and other	1,499,177	1,702,979	1,273,351	(203,802)	(12)	429,628	34
Total operating revenues	8,954,811	12,721,136	8,347,341	(3,766,325)	(30)	4,373,795	52
Cost of goods sold	2,795,837	3,400,129	2,848,928	(604,292)	(18)	551,201	19
Gross profit	6,158,974	9,321,007	5,498,413	(3,162,033)	(34)	3,822,594	70
Other operating expenses:							
Convention center operations	10,520,772	10,084,475	8,859,008	436,297	4	1,225,467	14
Sales and marketing	3,913,182	6,867,182	6,048,279	(2,954,000)	(43)	818,903	14
Total other operating expenses	14,433,954	16,951,657	14,907,287	(2,517,703)	(15)	2,044,370	14
Operating loss	(8,274,980)	(7,630,650)	(9,408,874)	(644,330)	8	1,778,224	(19)
Interest income	26,084	38,960	83,406	(12,876)	(33)	(44,446)	(53)
Loss before contributions and remittance	(8,248,896)	(7,591,690)	(9,325,468)	(657,206)	9	1,733,778	(19)
Contributions from							
Hawaii Tourism Authority	17,019,923	22,339,946	19,237,497	(5,320,023)	(24)	3,102,449	16
Remittance to Hawaii Tourism Authority for completed events revenue	(9,514,774)	(12,543,113)	(8,649,797)	3,028,339	(24)	(3,893,316)	45
Change in net assets	(743,747)	2,205,143	1,262,232	(2,948,890)	(134)%	\$ 942,911	75%
Net assets at beginning of year	14,453,817	12,248,674	10,986,442				
Net assets at end of year	\$ 13,710,070	14,453,817	12,248,674				

Operating revenues include rental income, food and beverage, events, and other revenues. Operating revenues decreased by \$3,766,325 or 30% to \$8,954,811 in fiscal year 2012. Operating revenues increased by \$4,373,795 or 52% to \$12,721,136 in fiscal year 2011.

- The majority of operating revenues are generated from food and beverage operations. Food and beverage revenues decreased by \$1,910,401 or 27% to \$5,267,077 in fiscal year 2012. The decrease in food and beverage revenues is directly related to the decrease in the number of convention-type events held in the Center. Rent decreased by \$1,652,122 or 43% in fiscal year 2012. Effective July 1, 2012, the Authority

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### Management's Discussion and Analysis

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ceased funding for the Center's Marketing Flexibility Fund to cover expenses related to rental incentives. Food and beverage revenues increased by \$2,582,080 or 56% to \$7,177,478 in fiscal year 2011.

Typically, larger offshore convention-type events generate more revenue for the Center as opposed to meetings and other smaller events. There were 151 events in the Center in the fiscal year 2012, of which 11 were U.S. convention-type events, as compared to 181 events in the Center in the fiscal year 2011, of which 14 were convention-type events, and 153 events in the fiscal year 2010, of which 8 were U.S. convention-type events.

#### *Convention Center Operations*

Total operating expenses (cost of goods sold and other operating expenses) for convention center operations were \$13,316,609 and \$13,484,604 in fiscal year 2012 and 2011, respectively. This represents a decrease of \$167,995 or 1%, and a decrease of \$1,776,668 or 15% from fiscal years 2011 and 2010, respectively. A breakdown of changes in individual expense categories is as follows:

	2012 – 2011		2011 – 2010	
	Increase (decrease)	Percentage change	Increase	Percentage change
Cost of goods sold	\$ (604,292)	(18)%	\$ 551,201	19%
Salaries, wages, payroll taxes, and benefits	164,061	3	297,410	6
Contract labor	85,495	9	343,433	59
Repairs and maintenance	10,255	2	77,615	17
Building operations	(148,112)	(26)	167,727	42
Utilities	444,237	23	277,287	17
Management fee	(138,297)	(30)	2,305	1
Other	18,658	4	59,690	13
	\$ (167,995)		\$ 1,776,668	

The decrease in the cost of goods sold of \$604,292 or 18% in fiscal year 2012 from fiscal year 2011 is directly related to the decrease in the number of convention-type events held in the Center as well as the decrease in the food and beverage revenues. There were three fewer convention-type events in fiscal year 2012 than in fiscal year 2011. The increase in salaries, wages, payroll taxes, and benefits of \$164,061 or 3% is primarily due to filling vacancies in certain positions during the fiscal year 2012. In addition, employer matching 401(k) contributions was in effect for the entire fiscal year 2012 after resuming in January 1, 2011. Overall contract labor increased by \$85,495 or 9%, in preparation for presenting a world class facility for the Asia Pacific Economic Cooperation 2011 Leaders Week as well as filling other vacant in-house positions. Larger events are typically more complex in their programs and needs. With the cost of electricity significantly exceeding budget, building operational expenses were cut and decreased by \$148,112. Utilities increased by \$444,237 or 23% as a result of the continued high cost of oil and electricity. Management fees decreased by \$138,297 or 30% due to new negotiated management fee terms in fiscal year 2012.



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The increase in the cost of goods sold of \$551,201 or 19% in fiscal year 2011 from fiscal year 2010 is directly related to the increase in the number of convention-type events held in the Center as well as the increase in the food and beverage revenues. There were six more convention-type events in fiscal year 2011 than in fiscal year 2010. The increase in salaries, wages, payroll taxes, and benefits of \$297,410 or 6% is primarily due to filling vacancies in certain positions during the fiscal year 2011. In addition, employer matching 401(k) contributions resumed effective January 1, 2011. Overall contract labor increased by \$343,433 or 59%, as a result of the increase in the number of convention-type events at the Center from fiscal year 2010. Larger events are typically more complex in their programs and needs. Utilities increased by \$277,287 or 17% as a result of the rising cost of oil as well as higher electricity usage related to the increase in convention-type events from fiscal year 2010. Other expenses increased by \$61,995 or 7% due to increased overall activity at the Center in comparison to fiscal year 2010.

#### ***Sales and Marketing***

Sales and marketing expenses decreased by \$2,954,000 or 43% to \$3,913,182 in fiscal year 2012. The sales and marketing expenses increased by \$818,903 or 14% to \$6,867,182 from fiscal year 2010 to 2011.

The major expenses for the fiscal year 2012 are in salaries and wages and advertising and promotion with \$1,283,670 and \$1,370,600, respectively. The Center continues to position itself in the market with a sales force locally as well as a sales team on the mainland in major markets, the Midwest and East coasts. Of the \$1,370,600 used for advertising and promotion, \$443,728 was used from the Marketing Flexibility Fund. The uses of the fund were for destination support for groups whose events were held in fiscal year 2012, including the Asia Pacific Economic Cooperation, American Phytopathological Society, Society of American Foresters, American College of Chest Physicians, Association of Legal Administrators, American Institute of Aeronautics and Astronautics, American Farm Bureau, and American Association of Orthodontics to name a few. The decrease in sales and marketing expenses from fiscal year 2011 to fiscal year 2012 of \$2,954,000 is primarily due to decreases in the use of the Marketing Flexibility Fund for site visits, attendance promotions, and global outreach. Effective July 1, 2012, the Authority ceased funding for the Center's Marketing Flexibility Fund to cover expenses related to rental incentives.

The major expenses for the fiscal year 2011 are in salaries and wages and advertising and promotion with \$1,462,817 and \$3,870,055, respectively. The Center continues to position itself in the market with a sales force locally as well as a sales team on the mainland in major markets, the Midwest and East coasts. Of the \$3,870,055 used for advertising and promotion, \$2,829,781 was used from the Marketing Flexibility Fund. The uses of the fund were for rent incentives and destination support for groups whose events were held in fiscal year 2011, including Alzheimer's Association, American Academy of Periodontology, International Federation of Employee Benefit Plans, Association for Asian Studies, National Veteran Golden Age Games, American Association of Orthodontists, and American Psychiatric Association. Other uses of the fund were for promotional support for groups whose events will be held at the Center in the future such as the American Phytopathological Society, Society of American Foresters, American Academy of Periodontology, Asia Pacific Economic Cooperation, American Farm Bureau Federation, Association of Legal Administrators, American Association of Orthodontists, and American Pain Society. The increase in sales and marketing expenses from fiscal year 2010 to fiscal year 2011 of \$818,903 is primarily due to increases in the use of the Marketing Flexibility Fund.

## HAWAII CONVENTION CENTER

### Special-Purpose Balance Sheets

June 30, 2012 and 2011

<b>Assets</b>	<b>2012</b>	<b>2011</b>
Current assets:		
Cash and cash equivalents	\$ 2,764,003	4,400,944
Accounts receivable	163,738	395,425
Inventories	152,330	193,110
Prepaid expenses	380,578	636,137
Deposits and other assets	1,667,099	721,758
Total current assets	5,127,748	6,347,374
Restricted cash	10,833,848	11,736,660
Total assets	\$ 15,961,596	18,084,034
<b>Liabilities and Net Assets</b>		
Current liabilities:		
Accounts payable	\$ 728,646	1,377,375
Due to Hawaii Tourism Authority	876,533	1,193,203
Accrued compensation	430,535	635,353
Advance deposits	209,582	377,203
Other liabilities	1,730	6,272
Total current liabilities	2,247,026	3,589,406
Advance deposits	4,500	40,811
Total liabilities	2,251,526	3,630,217
Commitments and contingencies		
Unrestricted net assets	2,876,222	2,717,157
Restricted net assets	10,833,848	11,736,660
Total net assets	13,710,070	14,453,817
Total liabilities and net assets	\$ 15,961,596	18,084,034

See accompanying notes to special-purpose financial statements.

## HAWAII CONVENTION CENTER

### Special-Purpose Statements of Revenues, Expenses, and Changes in Net Assets

Years ended June 30, 2012 and 2011

	<b>2012</b>	<b>2011</b>
Operating revenues, net:		
Food and beverage	\$ 5,267,077	7,177,478
Rental income	2,188,557	3,840,679
Events	1,420,313	1,613,414
Other	78,864	89,565
Total operating revenues	8,954,811	12,721,136
Operating expenses:		
Cost of goods sold:		
Food and beverage	1,033,283	1,322,027
Direct	1,762,554	2,078,102
Total cost of goods sold	2,795,837	3,400,129
Other operating expenses:		
Salaries and wages	5,454,187	5,514,253
Utilities	2,419,429	1,979,127
Advertising and promotion	1,382,434	3,901,879
Payroll taxes and benefits	1,347,229	1,316,335
Contract labor	1,268,163	1,204,151
Travel and entertainment	583,538	762,706
Repairs and maintenance	574,131	561,874
Building operations	415,830	563,555
Management fee	325,000	463,297
Insurance	138,089	171,653
Community relations	105,822	105,612
Professional fees	51,855	79,478
Computer	32,715	30,952
Printing and stationery	27,362	30,373
Rent	25,136	62,402
Dues and subscriptions	21,500	37,678
Postage	20,322	19,954
General excise tax	19,695	25,787
Office supplies	15,638	23,259
Employee training	10,379	17,071
Miscellaneous	195,500	80,261
Total other operating expenses	14,433,954	16,951,657
Total operating expenses	17,229,791	20,351,786
Operating loss	(8,274,980)	(7,630,650)
Nonoperating revenues:		
Interest income	26,084	38,960
Loss before contributions and remittance	(8,248,896)	(7,591,690)
Contributions from Hawaii Tourism Authority	17,019,923	22,339,946
Remittance to Hawaii Tourism Authority for completed events revenue	(9,514,774)	(12,543,113)
Change in net assets	(743,747)	2,205,143
Net assets at beginning of year	14,453,817	12,248,674
Net assets at end of year	\$ 13,710,070	14,453,817

See accompanying notes to special-purpose financial statements.

**HAWAII CONVENTION CENTER**  
Special-Purpose Statements of Cash Flows  
Years ended June 30, 2012 and 2011

	<u>2012</u>	<u>2011</u>
Cash flows from operating activities:		
Cash received from customers	\$ 8,982,566	12,532,950
Cash payments to suppliers of goods and services	(11,730,648)	(13,873,852)
Cash payments to employees	(7,006,234)	(6,688,685)
Net cash used in operating activities	<u>(9,754,316)</u>	<u>(8,029,587)</u>
Cash flows from noncapital financing activities:		
Contributions received from Hawaii Tourism Authority	17,019,923	22,498,017
Funds remitted to Hawaii Tourism Authority	(9,831,444)	(11,883,907)
Net cash provided by noncapital financing activities	<u>7,188,479</u>	<u>10,614,110</u>
Cash flows from investing activity:		
Interest income	26,084	38,960
Net (decrease) increase in cash and cash equivalents	(2,539,753)	2,623,483
Cash and cash equivalents and restricted cash at beginning of year	<u>16,137,604</u>	<u>13,514,121</u>
Cash and cash equivalents and restricted cash at end of year	<u>\$ 13,597,851</u>	<u>16,137,604</u>
Reconciliation of operating loss to net cash used in operating activities:		
Operating loss	\$ (8,274,980)	(7,630,650)
Adjustments to reconcile operating loss to net cash used in operating activities:		
Decrease (increase) in assets:		
Accounts receivable	231,687	(249,914)
Inventories	40,780	(12,553)
Prepaid expenses	255,559	(277,243)
Deposits and other assets	(945,341)	(711,967)
Increase (decrease) in liabilities:		
Accounts payable	(648,729)	644,603
Accrued compensation	(204,818)	141,903
Advance deposits	(203,932)	61,728
Other liabilities	(4,542)	4,506
Total adjustments	<u>(1,479,336)</u>	<u>(398,937)</u>
Net cash used in operating activities	<u>\$ (9,754,316)</u>	<u>(8,029,587)</u>

See accompanying notes to special-purpose financial statements.

## HAWAII CONVENTION CENTER

### Notes to Special-Purpose Financial Statements

June 30, 2012 and 2011

#### (1) Organization

The Hawaii Convention Center (the Center), which opened to the general public in June 1998, is used for a variety of events, including conventions and trade shows, public shows, and spectator events. The Center offers approximately 350,000 square feet of rentable space, including 51 meeting rooms.

Effective July 1, 2000, the Hawaii Tourism Authority, State of Hawaii (the Authority), is responsible for the operation, management, and maintenance of the Center. The Authority is a discretely presented component unit of the State of Hawaii. The Center is reported as a special revenue fund of the Authority.

#### (2) Summary of Significant Accounting Policies

This summary of significant accounting policies is presented to assist readers in interpreting the special-purpose financial statements. These policies are considered essential and should be read in conjunction with the special-purpose financial statements.

##### (a) *Financial Statement Presentation and Basis of Accounting*

The special-purpose financial statements have been prepared pursuant to the provisions of the management agreement between the Authority and SMG (note 4) and are intended to present the financial position, changes in net assets, and cash flows of only that portion of the Authority that is attributable to the transactions of the Center based upon the accounting records maintained by SMG. The Center's operations are reported on a flow of economic resources measurement focus using the accrual basis of accounting. Under this method, revenues are recorded when earned and expenses are recorded at the time liabilities are incurred.

These special-purpose financial statements are prepared in conformity with U.S. generally accepted accounting principles for state and local governments as prescribed by the Governmental Accounting Standards Board, except that the property, building, furniture, and equipment used in the Center's operations, and related depreciation expense, as well as debt used to finance such capital assets and the related interest expense, are not reflected on the accompanying special-purpose financial statements. Those assets, liabilities, and related expenses are reflected on the financial statements of the Authority.

The Center has elected not to apply any Financial Accounting Standards Board pronouncements issued subsequent to November 30, 1989.

##### (b) *Operating Revenues and Expenses*

The Center distinguishes operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services in connection with the principal ongoing operations, management, and maintenance of the Center. Operating revenues include charges for services. Operating expenses include costs of services and administrative expenses. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

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### Notes to Special-Purpose Financial Statements

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(c) ***Classification of Current and Noncurrent Assets and Liabilities***

The Center considers assets to be current that can reasonably be expected, as part of its normal business operations, to be converted to cash and be available for liquidation of current liabilities within 12 months of the special-purpose balance sheet date. Liabilities that reasonably can be expected, as part of normal Center business operations, to be liquidated within 12 months of the special-purpose balance sheet date are considered to be current. All other assets and liabilities are considered to be noncurrent.

(d) ***Cash and Cash Equivalents***

For purposes of the special-purpose statements of cash flows, the Center considers currency on hand, savings, demand deposits, and certificates of deposits purchased with an original maturity of three months or less to be cash and cash equivalents.

(e) ***Due from/to the Hawaii Tourism Authority***

Due from the Authority represents expenses to be reimbursed by the Authority. Due to the Authority represents revenues on completed events and contributions that are required to be remitted to the Authority. These amounts are required to be accounted for separately and are not netted together for financial statement reporting purposes.

(f) ***Revenue Recognition***

Operating revenues include charges for services, which are recognized when services are provided. The Center's accounts receivable are due from companies in various industries. Credit is extended based on evaluation of the customer's financial condition and collateral is not required. Accounts receivable are due within 30 days and are at stated amounts due from customers. The allowance for doubtful accounts is the Center's best estimate of the amount of probable losses in the Center's existing accounts receivable. Management determines the allowance based on a review of each specific customer accounts receivable balance. Accounts outstanding longer than 90 days are considered past due, and delinquency letters are sent. The Center writes off accounts receivable when it determines they are uncollectible.

(g) ***Inventory***

Inventory held by the Center comprises food and beverage items. Inventory is valued at the lower of cost (first-in, first-out method) or market.

(h) ***Discounts***

Operating revenues are net of sales discounts amounting to \$1,441,411 and \$531,191 for the years ended June 30, 2012 and 2011, respectively.

(i) ***Advertising Expenses***

The Center expenses costs of advertising as incurred.

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### Notes to Special-Purpose Financial Statements

June 30, 2012 and 2011

*(j) Use of Estimates*

The preparation of the special-purpose financial statements, in accordance with the terms of the management agreement, requires management of the Center to make estimates and assumptions that affect the amounts reported in the special-purpose financial statements and accompanying notes. Actual results could differ from those estimates. Significant items subject to such estimates and assumptions include the valuation of accounts receivable.

**(3) Cash and Cash Equivalents**

The Center maintains cash at a financial institution located in Hawaii and in an investment sweep account with the same financial institution. At June 30, 2012 and 2011, the carrying amount of the Center's deposits was \$13,597,851 and \$16,137,604, including \$10,833,848 and \$11,736,660 of restricted cash, respectively, and the bank balance was \$13,800,335 and \$16,484,388, respectively. Of the bank balance at June 30, 2012 and 2011, \$1,105,009 and \$990,217, respectively, was insured by the Federal Deposit Insurance Corporation and \$12,695,326 and \$15,494,171, respectively, was uninsured and uncollateralized. Accordingly, these deposits were exposed to custodial credit risk. Custodial credit risk is the risk that in the event of a bank failure, the Center's deposits may not be returned to it.

**(4) Management Agreement**

The Center is managed and operated by SMG under a management agreement dated June 28, 1996, as amended. The term of the original agreement was from June 28, 1996 to June 30, 2001 with two two-year option periods through June 30, 2005. In 2001, the first two-year option period was exercised by the Authority. Effective January 1, 2003, the Authority and SMG renegotiated the terms of the management agreement and extended the term of the agreement through June 30, 2006 with two five-year option periods through June 30, 2016. In June 2005, the Authority approved SMG's option to extend the term of the agreement through June 30, 2011. In July 2011, the Authority extended the term of the agreement through June 30, 2012. In July 2012, the Authority extended the term of the agreement through December 31, 2013.

The management fee for the years ended June 30, 2012 and 2011 amounted to \$325,000 and \$463,297, respectively. The management fee for the next term through December 31, 2013 is a base fee of \$350,000 plus up to \$75,000 if SMG exceeds certain performance measures.

SMG is on a cost-reimbursement contract whereby they are reimbursed by the Authority for costs incurred in operating the Center.

**(5) License and Food and Beverage Agreements**

At June 30, 2012 and 2011, various clients have contracts with the Center to reserve space for future conventions and events to be held at the Center. These clients signed license agreements with the Center, which require rental payments in advance. In addition, clients may be required to make payments for food and beverage in advance. At June 30, 2012 and 2011, the Center estimates approximately \$2,048,121 and \$2,749,044, respectively, in future revenues, of which \$214,082 and \$418,014, respectively, were collected in advance and recorded as advance deposits on the special-purpose balance sheets.

**HAWAII CONVENTION CENTER**

Notes to Special-Purpose Financial Statements

June 30, 2012 and 2011

**(6) Sales and Marketing**

In accordance with Act 253 of the 2002 Session Laws of Hawaii, the Center assumed responsibility for the advertisement and promotion of the Center effective January 1, 2003. In an effort to increase its sales and marketing efforts, the Center entered into an agreement with the Authority whereby the Authority agreed to provide additional funding to the Center. The term on the agreement is from January 1, 2003 through June 30, 2006 with two five-year option periods through June 30, 2016. In June 2005, the Authority approved the Center's option to extend the terms of the agreement through June 2011. In July 2011, the Authority extended the term of the agreement through June 2012. In July 2012, the Authority extended the term of the agreement through December 2013. During the year ended June 30, 2012, the Center received \$17,019,923 from the Authority, of which approximately \$3,570,000 was required to be spent on sales and marketing. During the year ended June 30, 2011, the Center received \$22,339,946 from the Authority, of which approximately \$6,000,000 was required to be spent on sales and marketing. During the years ended June 30, 2012 and 2011, the Center's sales and marketing expenses were \$3,913,182 and \$6,867,182, respectively. In accordance with the agreement between the Authority and the Center, the Center is not required to remit the unspent funds back to the Authority provided that the unspent funds be used for sales and marketing in subsequent years and approved by the Authority's board of directors. These sales and marketing costs are included as operating expenses in the Center's special-purpose statements of revenues, expenses, and changes in net assets for the years ended June 30, 2012 and 2011.

**(7) Capital Improvements**

Expenditures for property, building, and equipment are recorded as a reduction of contributions from the State since such capital assets are not recorded on the Center's special-purpose balance sheets (note 2). Expenditures for property, building, and equipment were \$1,277,187 and \$360,385 as of June 30, 2012 and 2011, respectively.

In 2012 and 2011, the Center received \$1,200,000 and \$3,000,000, respectively, from the Authority to be used for emergency capital improvements, repair or maintenance purchases, and on various capital improvement projects. The Center is not required to remit unspent funds back to the Authority provided that the unspent funds be used for capital improvements. The Center had \$10,833,848 in unspent funds at June 30, 2012. As of June 30, 2012, the Center had remaining commitments relating to the acquisition of capital assets of \$797,000.

**(8) Commitments**

The Center entered into various contractual agreements relating to public relations support, digital phone services, and the maintenance of the facility. As of June 30, 2012, the Center had remaining commitments under these contracts as follows:

Year ending December 31:	
2013	\$ <u>121,000</u>
Total remaining commitments under contractual agreements	\$ <u><u>121,000</u></u>



## HAWAII CONVENTION CENTER

### Notes to Special-Purpose Financial Statements

June 30, 2012 and 2011

The Center conducts a portion of its operations utilizing a leased facility for sales offices under a noncancelable operating lease expiring in 2012. Rent expense for all operating leases for the years ended June 30, 2012 and 2011 was \$25,136 and \$62,402, respectively. Future minimum rental payments required for the noncancelable operating lease at June 30, 2012 is as follows:

Year ending June 30:	
2013	\$ <u>2,460</u>
Total remaining lease commitments	\$ <u><u>2,460</u></u>

#### (9) Contingencies

The Center is involved in various other claims and legal actions arising in the ordinary course of business. In the opinion of management, the ultimate disposition of these matters will not have a material adverse effect on the Center's assets and liabilities, results of operations, or liquidity.

#### (10) Pension Plan

The Center has a defined-contribution pension plan for all employees meeting service, age, and employment status requirements. The Center contributes an amount equal to 40% on up to the first 5% of the employee's contributions to be determined annually based on a percentage of a participating employee's annual salary at the end of each calendar year. Contributions to the plan amounted to \$70,741 and \$35,543 during the years ended June 30, 2012 and 2011, respectively. Effective January 1, 2011, the employer matching contributions resumed.

**SUPPLEMENTARY INFORMATION**

## HAWAII CONVENTION CENTER

## Schedule of Changes in Net Assets

Years ended June 30, 2012 and 2011

	<b>Contributions from Hawaii Tourism Authority</b>	<b>Accumulated deficit</b>	<b>Total</b>
Balance at June 30, 2010	\$ 95,331,130	(83,082,456)	12,248,674
Loss before contributions and funds remitted	—	(7,591,690)	(7,591,690)
Contributions from Hawaii Tourism Authority	22,339,946	—	22,339,946
Remittance to Hawaii Tourism Authority for completed events revenue	(12,543,113)	—	(12,543,113)
Balance at June 30, 2011	105,127,963	(90,674,146)	14,453,817
Loss before contributions and funds remitted	—	(8,248,896)	(8,248,896)
Contributions from Hawaii Tourism Authority	17,019,923	—	17,019,923
Remittance to Hawaii Tourism Authority for completed events revenue	(9,514,774)	—	(9,514,774)
Balance at June 30, 2012	\$ <u>112,633,112</u>	<u>(98,923,042)</u>	<u>13,710,070</u>

See accompanying independent auditors' report.

## HAWAII CONVENTION CENTER

## Schedule of Revenues, Expenses, and Changes in Net Assets

Year ended June 30, 2012

	<b>Convention center operations</b>	<b>Sales and marketing</b>	<b>Total</b>
Operating revenues, net:			
Food and beverage	\$ 5,267,077	—	5,267,077
Rental income	2,188,557	—	2,188,557
Events	1,420,313	—	1,420,313
Other	78,864	—	78,864
Total operating revenues	<u>8,954,811</u>	<u>—</u>	<u>8,954,811</u>
Cost of goods sold:			
Food and beverage	1,033,283	—	1,033,283
Direct	1,762,554	—	1,762,554
Total cost of goods sold	<u>2,795,837</u>	<u>—</u>	<u>2,795,837</u>
Gross profit	<u>6,158,974</u>	<u>—</u>	<u>6,158,974</u>
Other operating expenses:			
Salaries and wages	4,170,517	1,283,670	5,454,187
Utilities	2,399,127	20,302	2,419,429
Advertising and promotion	11,834	1,370,600	1,382,434
Payroll taxes and benefits	1,104,906	242,323	1,347,229
Contract labor	1,006,868	261,295	1,268,163
Travel and entertainment	40,624	542,914	583,538
Repairs and maintenance	557,521	16,610	574,131
Building operations	415,443	387	415,830
Management fee	325,000	—	325,000
Insurance	138,089	—	138,089
Community relations	52,749	53,073	105,822
Professional fees	22,489	29,366	51,855
Computer	27,669	5,046	32,715
Printing and stationery	1,010	26,352	27,362
Rent	—	25,136	25,136
Dues and subscriptions	9,111	12,389	21,500
Postage	5,718	14,604	20,322
General excise tax	17,341	2,354	19,695
Office supplies	13,743	1,895	15,638
Employee training	10,079	300	10,379
Miscellaneous	190,934	4,566	195,500
Total other operating expenses	<u>10,520,772</u>	<u>3,913,182</u>	<u>14,433,954</u>
Operating loss	<u>(4,361,798)</u>	<u>(3,913,182)</u>	<u>(8,274,980)</u>
Nonoperating revenues:			
Interest income	23,870	2,214	26,084
Loss before contributions and remittance	<u>(4,337,928)</u>	<u>(3,910,968)</u>	<u>(8,248,896)</u>
Contributions from Hawaii Tourism Authority	13,449,923	3,570,000	17,019,923
Remittance to Hawaii Tourism Authority for completed events revenue	<u>(9,514,774)</u>	<u>—</u>	<u>(9,514,774)</u>
Change in net assets	<u>\$ (402,779)</u>	<u>(340,968)</u>	<u>(743,747)</u>

See accompanying independent auditors' report.