# STATE OF MINNESOTA

## Office of the State Auditor


**Rebecca Otto**
**State Auditor**


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**DULUTH ENTERTAINMENT AND**
**CONVENTION CENTER AUTHORITY**
**(A COMPONENT UNIT OF THE CITY OF DULUTH)**

YEARS ENDED DECEMBER 31, 2011 AND 2010

# Description of the Office of the State Auditor

The mission of the Office of the State Auditor is to oversee local government finances for Minnesota taxpayers by helping to ensure financial integrity and accountability in local governmental financial activities.

Through financial, compliance, and special audits, the State Auditor oversees and ensures that local government funds are used for the purposes intended by law and that local governments hold themselves to the highest standards of financial accountability.

The State Auditor performs approximately 160 financial and compliance audits per year and has oversight responsibilities for over 3,300 local units of government throughout the state. The office currently maintains five divisions:

**Audit Practice** - conducts financial and legal compliance audits of local governments;

**Government Information** - collects and analyzes financial information for cities, towns, counties, and special districts;

**Legal/Special Investigations** - provides legal analysis and counsel to the Office and responds to outside inquiries about Minnesota local government law; as well as investigates allegations of misfeasance, malfeasance, and nonfeasance in local government;

**Pension** - monitors investment, financial, and actuarial reporting for approximately 730 public pension funds; and

**Tax Increment Financing** - promotes compliance and accountability in local governments' use of tax increment financing through financial and compliance audits.

The State Auditor serves on the State Executive Council, State Board of Investment, Land Exchange Board, Public Employees Retirement Association Board, Minnesota Housing Finance Agency, and the Rural Finance Authority Board.

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# DULUTH ENTERTAINMENT AND CONVENTION CENTER AUTHORITY (A COMPONENT UNIT OF THE CITY OF DULUTH)

## Years Ended December 31, 2011 and 2010

# Audit Practice Division
# Office of the State Auditor
# State of Minnesota

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**DULUTH ENTERTAINMENT AND CONVENTION CENTER AUTHORITY**
**(A COMPONENT UNIT OF THE CITY OF DULUTH)**

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# Introductory Section

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**DULUTH ENTERTAINMENT AND CONVENTION CENTER AUTHORITY**
**(A COMPONENT UNIT OF THE CITY OF DULUTH)**

ORGANIZATION
DECEMBER 31, 2011

| | Term Expires |
|---|---|
| Directors | |
| John Arnold | June 30, 2012 |
| Mark Emmel | June 30, 2012 |
| Mary Finnegan-Ongaro | February 1, 2014 |
| Gregory Fox | February 1, 2014 |
| Jim Laumeyer | June 30, 2013 |
| Darlene Marshall | June 30, 2013 |
| Debra Messer | February 1, 2014 |
| Nick Patronas | June 30, 2012 |
| Roger Reinert | June 30, 2014 |
| David Ross | June 30, 2013 |
| Yvonne Prettner Solon | June 30, 2014 |
| Officers | |
| President | |
| Debra Messer | February 1, 2014 |
| Vice President | |
| David Ross | June 30, 2013 |
| Treasurer (Duluth City Treasurer) | |
| Brian Hansen | Indefinite |
| Executive Director | |
| Daniel J. Russell | Indefinite |

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# Financial Section

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REBECCA OTTO
STATE AUDITOR

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## INDEPENDENT AUDITOR'S REPORT

Mayor and City Council
City of Duluth

Duluth Entertainment and Convention Center
Authority Board

We have audited the accompanying basic financial statements of the Duluth Entertainment and Convention Center Authority, a component unit of the City of Duluth, as of and for the years ended December 31, 2011 and 2010, as listed in the table of contents. These financial statements are the responsibility of the Authority's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America 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 of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the 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.

In our opinion, the basic financial statements referred to above present fairly, in all material respects, the financial position of the Duluth Entertainment and Convention Center Authority as of December 31, 2011 and 2010, and the changes in its financial position and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

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Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis and Required Supplementary Information as listed in the table of contents be presented to supplement the basic financial statements. Such information, although not 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. In accordance with auditing standards generally accepted in the United States of America, we have applied certain limited procedures to the required supplementary information, 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.

In accordance with *Government Auditing Standards,* we have also issued our report dated May 31, 2012, on our consideration of the Duluth Entertainment and Convention Center Authority'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 to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

| | |
|---|---|
| */s/Rebecca Otto* | */s/Greg Hierlinger* |
| REBECCA OTTO<br>STATE AUDITOR | GREG HIERLINGER, CPA<br>DEPUTY STATE AUDITOR |

May 31, 2012

# MANAGEMENT’S DISCUSSION AND ANALYSIS

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**DULUTH ENTERTAINMENT AND CONVENTION CENTER AUTHORITY**
**(A COMPONENT UNIT OF THE CITY OF DULUTH)**

MANAGEMENT'S DISCUSSION AND ANALYSIS
DECEMBER 31, 2011
(Unaudited)

This section presents a narrative overview and analysis of the Duluth Entertainment and Convention Center Authority's financial condition and activities for the fiscal year ended December 31, 2011. This information should be read in conjunction with the financial statements.

## FINANCIAL HIGHLIGHTS

- In 2011, total net assets decreased slightly ($2,700, or 0.003 percent) over the course of the year's operations.
- Total operating revenue increased $0.4 million, or 5.9 percent, in 2011 compared to last year.
- Total operating expenses in 2011 increased by $2.3 million, or 23.3 percent, compared to 2010.

## OVERVIEW OF ANNUAL FINANCIAL REPORT

The Management's Discussion and Analysis (MD&A) serves as an introduction to the financial statements. The MD&A represents management's examination and analysis of the Authority's financial condition and performance. Summary financial statement data, key financial and operational indicators used in the Authority's strategic plan, budget, and other management tools were used for this analysis.

The financial statements report information about the Authority using full accrual accounting methods as utilized by similar business activities in the private sector.

The financial statements include a statement of net assets; statement of revenues, expenses, and changes in net assets; statement of cash flows; and notes to the financial statements. The statement of net assets presents the financial position of the Authority on a full accrual, historical cost basis. The statement of net assets provides information about the nature and amount of resources and obligations at year-end. The statement of revenues, expenses, and changes in net assets presents the results of the business activities over the course of the fiscal year and information as to how the net assets changed during the year. All changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of the related cash flows. This statement also provides certain information about the Authority's recovery of its costs.

The statement of cash flows presents changes in cash and cash equivalents resulting from operating, noncapital financing, capital and related financing, and investing activities. This statement presents cash receipt and cash disbursement information without consideration of the earnings event, when an obligation arises, or depreciation of capital assets.

The notes to the financial statements provide required disclosures and other information essential to a full understanding of material data provided in the statements. The notes present information on the Authority's accounting policies, significant account balances and activities, material risks, obligations, commitments, contingencies, and subsequent events, if any.

The financial statements were prepared by the Authority's staff from the detailed books and records of the Authority. The financial statements were audited and adjusted, if material, during the independent external audit process.

**SUMMARY OF ORGANIZATION AND BUSINESS**

On April 22, 1963, the Minnesota State Legislature approved the Laws, 1963, Chapter 305, creating the Duluth Arena-Auditorium Board (the "Board"). The Board consisted of seven Directors. The Board, according to Section 5, Subdivision 2, is conferred the power and duty to contract for and superintend the erection, construction, equipping, and furnishing of such arena-auditorium and to administer, promote, control, direct, manage, and operate such arena-auditorium as a municipal facility. Legislation in 1985 renamed the Board the Duluth State Convention Center Administrative Board. In addition, the legislation added four Board members to be appointed by the Governor. In 1998, legislation again changed the name to the Duluth Entertainment and Convention Center Authority (the Authority).

The Authority's mission statement, as defined by the Board of Directors, is committed to provide a multi-dimensional entertainment and convention facility with high quality integrated support services that will maximize the economic and social benefit to our business community, our investors, our clients, and our customers. The method used to accomplish the mission will always revolve around: providing a consistently high level of customer service; operating in a fiscally responsible manner; always recognizing our obligations as a public entity; providing a well-maintained facility that is a source of pride for the community; insisting on excellence in all aspects of Duluth Entertainment and Convention Center operations, including safety of the public and employees; broad public access to facility and events; and partnership with community businesses.

The Authority does not have taxing power. Operations are funded from customer revenues. Customer revenues, together with City tourism taxes, City of Duluth contributions, and State of Minnesota grants, fund the acquisition and construction of capital assets.

## FINANCIAL ANALYSIS

The following comparative condensed financial statements and other selected information serve as the key financial data and indicators for management, monitoring, and planning. Comments regarding budget-to-actual variances and year-to-year variances are included in each section by the name of the statement or account.

**Condensed Statement of Net Assets**
**(000s)**

| | 2011 | 2010 | 2009 | Dollar Change Increase (Decrease) 2010 to 2011 | Dollar Change Increase (Decrease) 2009 to 2010 |
|---|---|---|---|---|---|
| Assets | | | | | |
| Current and other assets | $ 3,539 | $ 7,848 | $ 7,174 | $ (4,309) | $ 674 |
| Capital assets | 106,426 | 106,126 | 72,918 | 300 | 33,208 |
| Total Assets | $ 109,965 | $ 113,974 | $ 80,092 | $ (4,009) | $ 33,882 |
| Liabilities | | | | | |
| Current liabilities | $ 2,574 | $ 6,500 | $ 7,305 | $ (3,926) | $ (805) |
| Long-term liabilities | 1,108 | 1,188 | 1,865 | (80) | (677) |
| Total Liabilities | $ 3,682 | $ 7,688 | $ 9,170 | $ (4,006) | $ (1,482) |
| Net Assets | | | | | |
| Invested in capital assets | $ 105,361 | $ 104,654 | $ 70,759 | $ 707 | $ 33,895 |
| Restricted | 87 | 87 | 87 | - | - |
| Unrestricted | 835 | 1,545 | 76 | (710) | 1,469 |
| Total Net Assets | $ 106,283 | $ 106,286 | $ 70,922 | $ (3) | $ 35,364 |

In 2011, net assets decreased $3 thousand compared to 2010. Total assets decreased due to zero construction contribution receivables in 2011 compared to $4.2 million in 2010. However, this decrease was offset by a decrease in total liabilities. In 2011, total liabilities decreased $4.0 million due to a decrease in contracts payable and bonds payable. In 2010, net assets increased $35.4 million to $106.3 million, up from $70.9 million due to capital contributions.

## Condensed Statement of Revenues, Expenses, and Changes in Net Assets
**(000s)**

| | 2011 | 2010 | 2009 | Dollar Change Increase (Decrease) 2010 to 2011 | Dollar Change Increase (Decrease) 2009 to 2010 |
|---|---|---|---|---|---|
| Operating revenues | $ 7,672 | $ 7,242 | $ 6,684 | $ 430 | $ 558 |
| Nonoperating revenues | 1,361 | 3,070 | 975 | (1,709) | 2,095 |
| Total Revenues | $ 9,033 | $ 10,312 | $ 7,659 | $ (1,279) | $ 2,653 |
| Operating expenses | $ 12,144 | $ 9,847 | $ 9,070 | $ 2,297 | $ 777 |
| Interest expense | 142 | 187 | 222 | (45) | (35) |
| Amortization of bond issuance costs | 1 | 2 | 2 | (1) | - |
| Loss on sale of assets | - | - | 1,697 | - | (1,697) |
| Total Expenses | $ 12,287 | $ 10,036 | $ 10,991 | $ 2,251 | $ (955) |
| Excess of Revenues Over (Under) Expenses | $ (3,254) | $ 276 | $ (3,332) | $ (3,530) | $ 3,608 |
| Capital contributions | 3,251 | 35,088 | 34,431 | (31,837) | 657 |
| Change in Net Assets | $ (3) | $ 35,364 | $ 31,099 | $ (35,367) | $ 4,265 |
| Net Assets - January 1 | 106,286 | 70,922 | 39,823 | 35,364 | 31,099 |
| Net Assets - December 31 | $ 106,283 | $ 106,286 | $ 70,922 | $ (3) | $ 35,364 |

## Comparison with Budget
**(000s)**

| | 2011 Actual | 2011 Budget | Variance with Budget | Percent Change (%) |
|---|---|---|---|---|
| Operating revenues | $ 7,672 | $ 7,086 | $ 586 | 8.3 |
| Nonoperating revenues | 1,361 | 1,236 | 125 | 10.1 |
| Total Revenues | $ 9,033 | $ 8,322 | $ 711 | 8.5 |
| Operating expenses | $ 12,144 | $ 11,130 | $ 1,014 | 9.1 |
| Interest expense | 142 | 142 | - | - |
| Amortization of bond issuance costs | 1 | 1 | - | - |
| Total Expenses | $ 12,287 | $ 11,273 | $ 1,014 | 9.0 |
| Excess of Revenues Over (Under) Expenses | $ (3,254) | $ (2,951) | $ (303) | (10.3) |
| Capital contributions | 3,251 | - | 3,251 | 100.0 |
| Change in Net Assets | $ (3) | $ (2,951) | $ 2,948 | 99.9 |
| Net Assets - January 1 | 106,286 | 106,286 | - | - |
| Net Assets - December 31 | $ 106,283 | $ 103,335 | $ 2,948 | 2.9 |

### Revenues

The Authority's operating revenues increased $430,000 to $7.7 million in 2011 due to an increase in AMSOIL arena concessions revenue. In addition, daily parking revenues were up 16 percent over last year due to a mid-year daily parking price increase. Nonoperating revenues were down $1,709,000 compared to last year mainly due to naming rights revenue for AMSOIL arena going from $2 million in 2010 to $200,000 in 2011.

### Expenses

The Authority's operating expenses increased $2,297,000 to $12.1 million in 2011 mainly due to an increase in depreciation, which increased $1.8 million over last year. An increase in personal services, operating supplies, and utilities due to AMSOIL arena also contribute to the expense increase in 2011.

### Budgetary Highlights

Operating revenues were over budget by $586,000 in 2011 due mainly to increased AMSOIL concession sales and a number of large concerts increasing ticket office revenue. Nonoperating revenues were up $125,000 due to larger Hotel/Motel tax revenue than projected. Operating expenses were $1,014,000 over budget in 2011 mainly due to payments of UMD lease revenues to the City of Duluth pursuant to a pledge agreement. These payments were not included in the budget. In addition, labor and concessions food costs were over budget due to AMSOIL events busier than forecasted.

## CAPITAL ASSETS AND DEBT ADMINISTRATION

### Capital Assets

**Capital Assets**
**(000s)**

| | 2011 | 2010 | Dollar Change | Percent Change (%) |
|---|---|---|---|---|
| Land | $ 906 | $ 906 | $ - | - |
| Land improvements | 303 | 303 | - | - |
| Buildings and structures | 135,852 | 132,231 | 3,621 | 2.7 |
| Equipment | 9,917 | 9,498 | 419 | 4.4 |
| Work in progress | - | 23 | (23) | (100.0) |
| Subtotal | $ 146,978 | $ 142,961 | $ 4,017 | 2.8 |
| Less: accumulated depreciation | (40,552) | (36,835) | (3,717) | 10.1 |
| Net Capital Assets | $ 106,426 | $ 106,126 | $ 300 | 0.3 |

By the end of 2011, the Authority had invested $147.0 million in capital assets. The increase in buildings and structures is mainly due to facility roof repairs and business office upgrades. For more information, see Note 2.C. to the financial statements.

### Debt Administration

**Debt**
**(000s)**

| | 2011 | 2010 | Dollar Change | Percent Change (%) |
|---|---|---|---|---|
| Locker room lease | $ 577 | $ 697 | $ (120) | (17.2) |
| Omnimax bonds | - | 775 | (775) | (100.0) |
| Total Debt | $ 577 | $ 1,472 | $ (895) | (60.8) |

As of December 31, 2011, the Authority's outstanding debt decreased $0.9 million, or 60.8 percent, compared to December 31, 2010. Omnimax bonds were paid off in 2011, and no additional debt was incurred during the year. For additional information, see Notes 2.K. and 2.L. to the financial statements.

## ECONOMIC FACTORS AND NEXT YEAR'S BUDGET

Many factors were considered when completing the budget for 2012. Convention business is projected to be slightly down in 2012 compared to 2011. Overall, a slight decrease in revenue is projected for 2012 compared to 2011 mainly due to a decrease in concessions and ticket office revenue due to slightly slower concert schedule. Rent and building services prices for 2012 were established in 2008 and included a minimal increase for some goods and services. New catering prices will be in effect in January 2012, and concessions prices are increased annually in October. Operating expenses for payroll and cost of sales in 2012 are projected to decrease due to slightly slower convention and concert schedule.

The Duluth Omnimax Theatre closed in March 2011.

## REQUESTS FOR INFORMATION

This financial report is designed to provide a general overview of the Authority's finances and to demonstrate the Authority's accountability for the money it receives. If you have any questions about this report, or need additional financial information, contact the Finance Director, Duluth Entertainment and Convention Center Authority, 350 Harbor Drive, Duluth, Minnesota 55802.

# BASIC FINANCIAL STATEMENTS

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## DULUTH ENTERTAINMENT AND CONVENTION CENTER AUTHORITY
## (A COMPONENT UNIT OF THE CITY OF DULUTH)

***EXHIBIT 1***

### COMPARATIVE STATEMENT OF NET ASSETS
### DECEMBER 31, 2011 AND 2010

| | 2011 | 2010 |
|---|---|---|
| **Assets** | | |
| **Current assets** | | |
| Cash and cash equivalents | $ 2,180,970 | $ 2,546,480 |
| Accounts receivable | 632,064 | 113,103 |
| Due from City of Duluth | 127,426 | 119,492 |
| Inventory | 120,768 | 158,121 |
| Prepaid items | 11,428 | 18,706 |
| **Total current assets** | **$ 3,072,656** | **$ 2,955,902** |
| **Restricted current assets** | | |
| Assets restricted for customers' deposits | | |
| Cash and cash equivalents | $ 349,373 | $ 609,039 |
| Accounts receivable | 28,088 | 31,648 |
| Assets restricted for employee flexible benefits | | |
| Cash and cash equivalents | 1,759 | 3,028 |
| Assets restricted for construction | | |
| Due from City of Duluth | - | 2,118,408 |
| Due from State of Minnesota | - | 2,042,675 |
| **Total restricted current assets** | **$ 379,220** | **$ 4,804,798** |
| **Total current assets** | **$ 3,451,876** | **$ 7,760,700** |
| **Noncurrent assets** | | |
| Restricted debt service - assets held by trustee | | |
| Lease financing escrow account | $ 86,835 | $ 86,681 |
| Bond issuance costs | - | 725 |
| **Total noncurrent assets, other than capital assets** | **$ 86,835** | **$ 87,406** |
| **Capital assets** | | |
| Not depreciated | $ 905,601 | $ 928,945 |
| Depreciated | 146,072,368 | 142,031,771 |
| Less: allowance for depreciation | (40,551,597) | (36,835,070) |
| **Total capital assets - net of accumulated depreciation** | **$ 106,426,372** | **$ 106,125,646** |
| **Total noncurrent assets** | **$ 106,513,207** | **$ 106,213,052** |
| **Total Assets** | **$ 109,965,083** | **$ 113,973,752** |

The notes to the financial statements are an integral part of this statement.

## DULUTH ENTERTAINMENT AND CONVENTION CENTER AUTHORITY
## (A COMPONENT UNIT OF THE CITY OF DULUTH)

***EXHIBIT 1***
***(Continued)***

**COMPARATIVE STATEMENT OF NET ASSETS**
**DECEMBER 31, 2011 AND 2010**

| | 2011 | | 2010 | |
|---|---|---|---|---|
| **Liabilities** | | | | |
| **Current liabilities** | | | | |
| Accounts payable | $ | 175,026 | $ | 471,995 |
| Salaries payable | | 91,562 | | 120,716 |
| Compensated absences payable - current | | 110,321 | | 115,611 |
| Contracts payable | | 488,213 | | - |
| Due to City of Duluth | | 455,146 | | - |
| Accrued interest payable | | 10,094 | | 14,906 |
| Deferred revenue | | 738,572 | | 298,491 |
| General obligation revenue bonds payable - current | | - | | 775,000 |
| Less: unamortized discount | | - | | (759) |
| Less: deferred amount on refunding | | - | | (78,557) |
| Capital leases payable - current | | 126,354 | | 119,972 |
| **Total current liabilities** | **$** | **2,195,288** | **$** | **1,837,375** |
| **Current liabilities payable from restricted assets** | | | | |
| Customer deposits | $ | 377,461 | $ | 640,687 |
| Employee flexible benefits plan payable | | 1,759 | | 3,028 |
| Contracts payable | | - | | 4,019,166 |
| **Total current liabilities payable from restricted assets** | **$** | **379,220** | **$** | **4,662,881** |
| **Total current liabilities** | **$** | **2,574,508** | **$** | **6,500,256** |
| **Noncurrent liabilities** | | | | |
| Compensated absences payable - long-term | $ | 79,511 | $ | 77,194 |
| Capital leases payable - long-term | | 450,469 | | 576,823 |
| Net other postemployment benefits liability | | 577,699 | | 533,889 |
| **Total noncurrent liabilities** | **$** | **1,107,679** | **$** | **1,187,906** |
| **Total Liabilities** | **$** | **3,682,187** | **$** | **7,688,162** |
| **Net Assets** | | | | |
| Invested in capital assets - net of related debt | $ | 105,361,336 | $ | 104,653,851 |
| Restricted for debt service | | 86,835 | | 86,681 |
| Unrestricted | | 834,725 | | 1,545,058 |
| **Total Net Assets** | **$** | **106,282,896** | **$** | **106,285,590** |

The notes to the financial statements are an integral part of this statement.

## DULUTH ENTERTAINMENT AND CONVENTION CENTER AUTHORITY
## (A COMPONENT UNIT OF THE CITY OF DULUTH)

***EXHIBIT 2***

### COMPARATIVE STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS
### FOR THE YEARS ENDED DECEMBER 31, 2011 AND 2010

| | 2011 | 2010 |
|---|---|---|
| **Operating Revenues** | | |
| Sales | $ 3,347,327 | $ 2,878,822 |
| Charges for services | 3,968,322 | 4,121,987 |
| Miscellaneous | 356,609 | 240,960 |
| **Total Operating Revenues** | **$ 7,672,258** | **$ 7,241,769** |
| **Operating Expenses** | | |
| Personal services | $ 4,388,588 | $ 4,170,630 |
| Supplies and services | 1,556,935 | 1,358,576 |
| Utilities | 992,478 | 896,855 |
| Other services and charges | 1,488,964 | 1,477,342 |
| Depreciation | 3,716,527 | 1,943,917 |
| **Total Operating Expenses** | **$ 12,143,492** | **$ 9,847,320** |
| **Operating Income (Loss)** | **$ (4,471,234)** | **$ (2,605,551)** |
| **Nonoperating Revenues (Expenses)** | | |
| Interest income | $ 39,917 | $ 20,063 |
| Hotel/motel tax revenue | 1,120,629 | 1,050,022 |
| Naming rights revenue | 200,000 | 2,000,000 |
| Interest expense | (142,082) | (186,919) |
| Amortization of bond issuance costs | (725) | (1,531) |
| **Total Nonoperating Revenues (Expenses)** | **$ 1,217,739** | **$ 2,881,635** |
| **Income (Loss) Before Contributions** | **$ (3,253,495)** | $ **276,084** |
| **Capital Contributions** | | |
| Capital contributions from City of Duluth | $ 1,703,131 | $ 17,863,184 |
| Capital contributions from State of Minnesota | 1,547,670 | 17,224,440 |
| **Total capital contributions** | **$ 3,250,801** | **$ 35,087,624** |
| **Change in Net Assets** | $ **(2,694)** | $ **35,363,708** |
| **Net Assets - January 1** | **106,285,590** | **70,921,882** |
| **Net Assets - December 31** | **$ 106,282,896** | **$ 106,285,590** |

The notes to the financial statements are an integral part of this statement.

**DULUTH ENTERTAINMENT AND CONVENTION CENTER AUTHORITY**
**(A COMPONENT UNIT OF THE CITY OF DULUTH)**

***EXHIBIT 3***

## COMPARATIVE STATEMENT OF CASH FLOWS
## YEARS ENDED DECEMBER 31, 2011 AND 2010

| | 2011 | 2010 |
|---|---|---|
| **Cash Flows from Operating Activities** | | |
| Cash received from customers | $ 6,977,103 | $ 7,486,325 |
| Payments to suppliers | (3,835,569) | (3,503,561) |
| Payments to employees | (4,378,174) | (4,062,373) |
| Other operating revenues | 356,609 | 240,960 |
| **Net cash provided by (used in) operating activities** | **$ (880,031)** | **$ 161,351** |
| **Cash Flows from Noncapital Financing Activities** | | |
| City of Duluth hotel/motel taxes | **$ 1,112,695** | **$ 1,031,507** |
| **Cash Flows from Capital and Related Financing Activities** | | |
| Cash received from City of Duluth for capital improvements | $ 3,821,539 | $ 18,565,997 |
| Cash received from State of Minnesota for capital improvements | 3,590,345 | 17,902,246 |
| Payment received for naming rights | 200,000 | 2,000,000 |
| Principal paid on lease purchases | (119,972) | (113,914) |
| Interest paid on lease purchases | (35,028) | (41,086) |
| Principal paid on bonds payable | (775,000) | (740,000) |
| Interest paid on bonds payable | (32,550) | (63,075) |
| Acquisition or construction of capital assets | (7,548,206) | (36,637,729) |
| **Net cash provided by (used in) capital and related financing activities** | **$ (898,872)** | **$ 872,439** |
| **Cash Flows from Investing Activities** | | |
| Interest on investments | **$ 39,763** | **$ 19,877** |
| **Net Increase (Decrease) in Cash and Cash Equivalents** | **$ (626,445)** | **$ 2,085,174** |
| **Cash and Cash Equivalents - January 1** | **3,158,547** | **1,073,373** |
| **Cash and Cash Equivalents - December 31** | **$ 2,532,102** | **$ 3,158,547** |

The notes to the financial statements are an integral part of this statement.

## DULUTH ENTERTAINMENT AND CONVENTION CENTER AUTHORITY
## (A COMPONENT UNIT OF THE CITY OF DULUTH)

***EXHIBIT 3***
***(Continued)***

### COMPARATIVE STATEMENT OF CASH FLOWS
### YEARS ENDED DECEMBER 31, 2011 AND 2010

| | 2011 | 2010 |
|---|---|---|
| **Reconciliation of Operating Income (Loss) to Net Cash Provided by (Used in) Operating Activities** | | |
| **Operating income (loss)** | **$ (4,471,234)** | **$ (2,605,551)** |
| **Adjustments to reconcile operating income (loss) to net cash provided by (used in) operating activities** | | |
| Depreciation | 3,716,527 | 1,943,917 |
| (Increase) decrease in accounts receivable | (515,401) | 78,532 |
| (Increase) decrease in inventories | 37,353 | (40,295) |
| (Increase) decrease in prepaid items | 7,278 | 9,249 |
| Increase (decrease) in payables | 169,860 | 367,195 |
| Increase (decrease) in deferred revenue | 440,081 | 113,988 |
| Increase (decrease) in employee flexible benefits plan deposits | (1,269) | 1,320 |
| Increase (decrease) in customer deposits | (263,226) | 292,996 |
| **Net Cash Provided by (Used in) Operating Activities** | **$ (880,031)** | **$ 161,351** |
| **Noncash Investing, Capital, and Financing Activities** | | |
| Interest earned on the debt service reserve account. | $ 154 | $ 186 |
| Capital assets acquired which had not been paid for at year-end. The unpaid amount is shown as contracts payable. | 488,213 | 4,019,166 |

The notes to the financial statements are an integral part of this statement.

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## 1. Summary of Significant Accounting Policies

The Duluth Entertainment and Convention Center Authority was created by Minn. Laws 1963, ch. 305; Minn. Laws 1985, 1st Spec. Sess., ch. 15, § 36, as amended; and by Minn. Laws 1998, ch. 404, § 61. The Authority has the power to contract, administer, promote, control, direct, manage, and operate the Duluth Entertainment and Convention Center for the City of Duluth and the State of Minnesota. The Authority consists of seven Directors appointed by the Mayor of the City of Duluth and approved by resolution of the City Council and four Directors appointed by the Governor of Minnesota.

The accounting policies of the Authority conform to generally accepted accounting principles.

### A. Financial Reporting Entity

For financial reporting purposes, a reporting entity includes all funds, organizations, agencies, boards, commissions, and authorities for which it is financially accountable and other organizations for which the nature and significance of their relationship with it are such that exclusion would cause its financial statements to be misleading or incomplete. The Governmental Accounting Standards Board (GASB) has set forth criteria to be considered in determining financial accountability. These criteria include appointing a voting majority of an organization's governing body and (1) the ability of the reporting entity to impose its will on that organization, or (2) the potential for the organization to provide specific financial benefits to, or impose specific financial burdens on, the reporting entity.

As required by generally accepted accounting principles, these financial statements present the Duluth Entertainment and Convention Center Authority, a component unit of the City of Duluth. The Authority is included in the City of Duluth's reporting entity because of the significance of its operational or financial relationships with the City.

1. Summary of Significant Accounting Policies (Continued)

B. Basis of Presentation

The accounts of the Duluth Entertainment and Convention Center Authority are presented as an enterprise fund. Enterprise funds are used to account for operations that are financed and operated in a manner similar to private business enterprises--where the intent of the governing body is that the costs (expenses, including depreciation) of providing goods or services to the general public on a continuing basis be financed or recovered primarily through user charges.

C. Basis of Accounting

Accounting records are maintained on the accrual basis, under which revenues are recorded when earned and expenses are recorded when liabilities are incurred.

Pursuant to GASB Statement 20, the Authority has elected not to apply accounting standards issued by the Financial Accounting Standards Board after November 30, 1989.

D. Budget and Budgetary Accounting

Budgetary control is maintained through an annual budget adopted by the Duluth Entertainment and Convention Center Authority. The budget is prepared on the accrual basis of accounting.

E. Cash and Cash Equivalents

Cash and cash equivalents consist of cash and investments held by the Treasurer of the City of Duluth. Investments are stated at fair value, and investment revenue is recorded as it is earned. For purposes of the statement of cash flows, all highly liquid investments (including restricted assets) with a maturity of three months or less when purchased are considered to be cash equivalents. The lease financing escrow account is not considered to be a cash equivalent because the Authority cannot withdraw from this account at any time without penalty.

F. Inventories of Merchandise for Resale

Inventories are priced at the lower of cost or market value on a first-in, first-out basis.

1. Summary of Significant Accounting Policies (Continued)

G. Capital Assets

All capital assets are valued at historical or estimated historical cost. Donated capital assets are recorded at estimated fair value at the date of donation.

The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend assets' lives are not capitalized.

Net interest costs on funds borrowed to finance construction of capital assets in proprietary funds are capitalized during the construction period and amortized over the life of the related asset.

H. Depreciation

Depreciation of capital assets is determined using the straight-line method. The estimated useful lives of the assets are 40 years for buildings and structures, 20 years for improvements, and 3 to 20 years for equipment.

I. Restricted Assets

Restricted assets consist of promoter-escrowed funds, the employee flexible benefits plan account, construction funds, and assets held by a trustee. Promoter-escrowed funds consist of cash and receivables escrowed on behalf of various promoters related to advance ticket sales for upcoming events. The employee flexible spending plan account consists of amounts withheld from employees pursuant to Internal Revenue Service regulations designated for reimbursement to employees for specific plan expenses. Restricted construction funds consist of receivables from the State of Minnesota and the City of Duluth for construction of the new arena. Assets held by the trustee consist of cash held pursuant to a reserve requirement of a lease agreement as described in Note 2.K.

When an expense is incurred for purposes for which both restricted and unrestricted net assets are available, it is the Authority's policy to use restricted resources first.

1. Summary of Significant Accounting Policies (Continued)

J. Deferred Revenue

Deferred revenue represents advance deposits to reserve Authority facilities for future events, proceeds from the sale of gift certificates and gift cards that have not been redeemed as of year-end, and lease revenues that have not been earned as of year-end.

K. Operating Revenues

Operating revenues, such as sales and charges for services, result from exchange transactions associated with the principal activity of the fund. Exchange transactions are those in which each party receives and gives up essentially equal values. Nonoperating revenues, such as subsidies and investment earnings, result from nonexchange transactions or incidental activities.

L. Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

M. Trade-Offs

The Authority exchanges scoreboard advertising, attraction admissions, building rent, and other services for other non-monetary assets or services such as radio, television, or print advertising. The value of the services exchanged is debited to the appropriate expense accounts and credited to the appropriate revenue accounts.

## 2. Detailed Notes

### A. Deposits and Investments

The City of Duluth Treasurer is designated by Minn. Laws 1963, ch. 305, as the Treasurer of the Authority. The City Treasurer is authorized by Minn. Stat. §§ 118A.02 and 118A.04 to deposit the Authority's cash and to invest in certificates of deposit in financial institutions designated by the Duluth City Council. Minnesota statutes require that all of the Authority's deposits be covered by insurance, surety bond, or collateral.

The types of investment securities available to the City of Duluth Treasurer are authorized by Minn. Stat. §§ 118A.04 and 118A.05.

Additional disclosures required by GASB Statement No. 40, *Deposit and Investment Risk Disclosures,* are disclosed on an entity-wide basis in the City of Duluth's Comprehensive Annual Financial Report. The Authority is a component unit of the City of Duluth.

The following is a summary of the Authority's cash and investments at December 31, 2011 and 2010:

| | 2011 | 2010 |
|---|---|---|
| Current assets | | |
| City of Duluth pooled cash account | $ 331,598 | $ 191,608 |
| Checking account - ticket office | 7,000 | 7,000 |
| Checking account - employee flexible benefits plan | 7,372 | 7,372 |
| Savings account - operating reserve | 1,800,000 | 2,300,000 |
| Petty cash and change funds | 35,000 | 40,500 |
| Total current assets | $ 2,180,970 | $ 2,546,480 |
| Restricted current assets | | |
| Ticket office customer deposits - checking | $ 224,505 | $ 532,041 |
| Ticket office customer deposits - savings | 113,668 | 63,098 |
| Ticket office change fund | 11,200 | 13,900 |
| Employee flexible benefits plan - checking | 1,759 | 3,028 |
| Total restricted current assets | $ 351,132 | $ 612,067 |
| Restricted noncurrent assets | | |
| Lease reserve - savings escrow | $ 86,835 | $ 86,681 |
| Total | $ 2,618,937 | $ 3,245,228 |

2. Detailed Notes (Continued)

B. Due From City of Duluth

Amounts due from the City of Duluth at December 31, 2011 and 2010, are as follows:

| | 2011 | 2010 |
|---|---|---|
| Current | | |
| Hotel/motel tax | $ 127,426 | $ 119,492 |
| Restricted current | | |
| Construction | $ - | $ 2,118,408 |

C. Capital Assets

A summary of the changes in the capital asset accounts for the years ended December 31, 2011 and 2010, follows:

| | Balance January 1, 2011 | Increase | Decrease | Reclassification | Balance December 31, 2011 |
|---|---|---|---|---|---|
| Capital assets not depreciated | | | | | |
| Land | $ 905,601 | $ - | $ - | $ - | $ 905,601 |
| Construction in progress | 23,344 | - | - | (23,344) | - |
| Total capital assets not depreciated | $ 928,945 | $ - | $ - | $ (23,344) | $ 905,601 |
| Capital assets depreciated | | | | | |
| Land improvements | $ 302,957 | $ - | $ - | $ - | $ 302,957 |
| Buildings | 132,231,039 | 3,598,093 | - | 23,344 | 135,852,476 |
| Equipment | 9,497,775 | 419,160 | - | - | 9,916,935 |
| Total capital assets depreciated | $ 142,031,771 | $ 4,017,253 | $ - | $ 23,344 | $ 146,072,368 |
| Less: accumulated depreciation for | | | | | |
| Land improvements | $ 302,957 | $ - | $ - | $ - | $ 302,957 |
| Buildings | 30,403,259 | 3,378,941 | - | - | 33,782,200 |
| Equipment | 6,128,854 | 337,586 | - | - | 6,466,440 |
| Total accumulated depreciation | $ 36,835,070 | $ 3,716,527 | $ - | $ - | $ 40,551,597 |
| Total capital assets depreciated, net | $ 105,196,701 | $ 300,726 | $ - | $ 23,344 | $ 105,520,771 |
| Capital Assets, Net | $ 106,125,646 | $ 300,726 | $ - | $ - | $ 106,426,372 |

2. Detailed Notes

C. Capital Assets (Continued)

| | Balance January 1, 2010 | Increase | Decrease | Reclassification | Balance December 31, 2010 |
|---|---|---|---|---|---|
| Capital assets not depreciated | | | | | |
| Land | $ 905,601 | $ - | $ - | $ - | $ 905,601 |
| Construction in progress | 31,252,734 | 35,025,009 | - | (66,254,399) | 23,344 |
| Total capital assets not depreciated | $ 32,158,335 | $ 35,025,009 | $ - | $ (66,254,399) | $ 928,945 |
| Capital assets depreciated | | | | | |
| Land improvements | $ 302,957 | $ - | $ - | $ - | $ 302,957 |
| Buildings | 67,152,861 | 75,541 | - | 65,002,637 | 132,231,039 |
| Equipment | 8,289,517 | 50,646 | 94,150 | 1,251,762 | 9,497,775 |
| Total capital assets depreciated | $ 75,745,335 | $ 126,187 | $ 94,150 | $ 66,254,399 | $ 142,031,771 |
| Less: accumulated depreciation for | | | | | |
| Land improvements | $ 302,957 | $ - | $ - | $ - | $ 302,957 |
| Buildings | 28,713,961 | 1,689,298 | - | - | 30,403,259 |
| Equipment | 5,968,385 | 254,619 | 94,150 | - | 6,128,854 |
| Total accumulated depreciation | $ 34,985,303 | $ 1,943,917 | $ 94,150 | $ - | $ 36,835,070 |
| Total capital assets depreciated, net | $ 40,760,032 | $ (1,817,730) | $ - | $ 66,254,399 | $ 105,196,701 |
| Capital Assets, Net | $ 72,918,367 | $ 33,207,279 | $ - | $ - | $ 106,125,646 |

D. Risk Management

The Authority is exposed to various risks of loss related to torts; injuries to employees; theft of, damage to, and destruction of assets; errors and omissions; and natural disasters. These risks are covered by commercial insurance purchased from independent third parties. Settled claims from these risks have not exceeded commercial insurance coverage for the past three years. There were no significant reductions in insurance coverage from the previous year. The Authority retains the risk of loss for the first $10,000 per occurrence.

Permanent employees are eligible to participate in the City of Duluth Joint Powers Enterprise Trust for the benefit of governmental units of the City. The Authority pays an annual premium for health and dental insurance coverage.

2. Detailed Notes (Continued)

E. Pension Plans

1. Plan Description

All full-time and certain part-time employees of the Duluth Entertainment and Convention Center Authority are covered by defined benefit pension plans administered by the Public Employees Retirement Association of Minnesota (PERA). PERA administers the General Employees Retirement Fund, which is a cost-sharing, multiple-employer retirement plan. The plan is established and administered in accordance with Minn. Stat. chs. 353 and 356.

General Employees Retirement Fund members belong to either the Coordinated Plan or the Basic Plan. Coordinated Plan members are covered by Social Security, and Basic Plan members are not. All new members must participate in the Coordinated Plan. No Authority employees belong to the Basic Plan.

PERA provides retirement benefits as well as disability benefits to members and benefits to survivors upon death of eligible members. Benefits are established by state statute and vest after three years of credited service (five years for those first eligible for membership after June 30, 2010). Defined retirement benefits are based on a member's average yearly salary for the five highest-paid consecutive years of allowable service, age, and years of credit at termination of service.

Two methods are used to compute benefits for Coordinated Plan members. The retiring member receives the higher of a step-rate benefit accrual formula (Method 1) or a level accrual formula (Method 2). Under Method 1, the annuity accrual rate is 1.2 percent of average salary for each of the first ten years of service and 1.7 percent for each successive year. Using Method 2, the annuity accrual rate is 1.7 percent for Coordinated Plan members for each year of service.

For General Employees Retirement Fund members whose annuity is calculated using Method 1, a full annuity is available when age plus years of service equal 90. Normal retirement age is 65 for members hired prior to July 1, 1989, and is the age for unreduced Social Security benefits capped at age 66 for Coordinated Plan members hired on or after July 1, 1989. A reduced retirement annuity is also available to eligible members seeking early retirement.

2. Detailed Notes

E. Pension Plans

1. Plan Description (Continued)

The benefit provisions stated in the previous paragraphs of this section are current provisions and apply to active plan participants. Vested, terminated employees who are entitled to benefits but are not yet receiving them are bound by the provisions in effect at the time they last terminated public service.

PERA issues a publicly available financial report that includes financial statements and required supplementary information for the General Employees Retirement Fund. That report may be obtained on the internet at www.mnpera.org; by writing to PERA at 60 Empire Drive, Suite 200, Saint Paul, Minnesota 55103-2088; or by calling 651-296-7460 or 1-800-652-9026.

2. Funding Policy

Pension benefits are funded from member and employer contributions and income from the investment of fund assets. Rates for employer and employee contributions are set by Minn. Stat. ch. 353. These statutes are established and amended by the State Legislature. The Duluth Entertainment and Convention Center Authority makes annual contributions to the pension plans equal to the amount required by state statutes. General Employees Retirement Fund Coordinated Plan members are required to contribute 6.25 percent of their annual covered salary.

The Duluth Entertainment and Convention Center Authority is required to contribute the following percentage of annual covered payroll in 2011:

| | |
|---|---|
| General Employees Retirement Fund<br>Coordinated Plan members | 7.25% |

The Authority's contributions for the years ending December 31, 2011, 2010, and 2009, for the General Employees Retirement Fund were:

| 2011 | 2010 | 2009 |
|---|---|---|
| $ 208,874 | $ 190,626 | $ 174,749 |

These contributions are equal to the contractually required contribution rate for each year as set by state statute.

2. Detailed Notes (Continued)

F. Postemployment Benefits

1. Plan Description and Funding Policy

The Authority provides health insurance benefits for certain retired employees under a single-employer self-insured plan. Employees who retired between January 1, 1983, and January 1, 1995, and employees who were full-time employees prior to January 1, 1995, and retire from the Authority at or after age 62 with at least ten years of full-time service, are eligible to receive hospital/medical benefits to the same extent as active employees for the life of the retiree or surviving spouse. The Authority will pay 80 percent of the premium for these qualifying retirees. The benefits are provided through the City of Duluth's Joint Powers Enterprise Trust. A separate report is issued for the plan. The authority to provide this benefit is established in Minn. Stat. § 471.61, subd. 2a.

Active employees who retire from the Authority when eligible to receive a retirement benefit from PERA who do not qualify for the aforementioned benefits, and do not participate in any other health benefits program providing coverage similar to that herein described, will be eligible to continue coverage with respect to both themselves and their eligible dependents under the Authority's health benefits program. These retirees are required to pay 100 percent of the total premium cost. Since the premium is a blended rate determined on the entire active and retiree population, the retirees are receiving an implicit rate subsidy. As of December 31, 2011, 16 retirees were receiving health benefits from the Authority's health plan.

The Authority's employment contract with the Executive Director provides for continuing family health insurance coverage for a period of 24 months following the termination of his employment contract. The Authority will provide this benefit.

The cost of other postemployment benefits is funded on a "pay-as-you-go" method.

2. Detailed Notes

F. Postemployment Benefits (Continued)

2. Annual OPEB Cost and Net OPEB Obligation

The Authority's annual other postemployment benefits (OPEB) cost is calculated based on the annual required contribution (ARC) of the employer, an amount actuarially determined in accordance with the parameters of GASB Statement 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and amortize any unfunded actuarial accrued liabilities (or funding excess) over a period not to exceed 30 years. The following table shows the components of the Authority's annual OPEB cost for the amount actually contributed to the plan and changes in the Authority's net OPEB obligation:

| | | |
|---|---|---|
| ARC | $ | 158,130 |
| Interest on net OPEB obligation | | 24,025 |
| Adjustment to ARC | | (31,365) |
| Annual OPEB cost | $ | 150,790 |
| Contributions during the year | | (106,980) |
| Increase in net OPEB obligation | $ | 43,810 |
| Net OPEB, Beginning of Year | | 533,889 |
| Net OPEB, End of Year | $ | 577,699 |

The Authority's annual OPEB cost, the percentage of annual OPEB cost contributed to the plan, and the net OPEB obligation as of and for the years ended December 31, 2011, 2010, and 2009, were as follows:

| | 2011 | | 2010 | | 2009 | |
|---|---|---|---|---|---|---|
| Percentage of annual OPEB cost contributed | | 70.95% | | 67.80% | | 45.49% |
| Annual OPEB cost | $ | 150,790 | $ | 151,461 | $ | 270,893 |
| Employer contributions | | (106,980) | | (102,684) | | (123,232) |
| Net Increase in Net OPEB Obligation | $ | 43,810 | $ | 48,777 | $ | 147,661 |
| Net OPEB Obligation, Beginning of Year | | 533,889 | | 485,112 | | 337,451 |
| Net OPEB Obligation, End of Year | $ | 577,699 | $ | 533,889 | $ | 485,112 |

2. Detailed Notes

F. Postemployment Benefits (Continued)

3. Funded Status and Funding Progress

The actuarial accrued liability for benefits at June 1, 2010, the most recent actuarial valuation date, is $2,298,091. The Authority currently has no assets that have been irrevocably deposited in a trust for future health benefits; thus, the entire amount is unfunded. The covered payroll (annual payroll of active employees covered by the plan) is $1,584,550. The ratio of the unfunded actuarially accrued liabilities to covered payroll is 145.03 percent.

Actuarial valuations involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and health care cost trends. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The Schedule of Funding Progress - Other Postemployment Benefits Plan, presented as required supplementary information following the notes to the financial statements, presents multi-year trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liabilities for benefits.

Projections of benefits for financial reporting purposes are based on the substantive plan (as understood by the employer and plan members) and include the types of benefits provided at the time of each valuation. The actuarial methods and assumptions used include techniques designed to reduce the effect of short-term volatility in actuarial accrued liabilities, consistent with the long-term perspective of the calculations.

In the June 1, 2010, actuarial valuation, the projected unit credit actuarial cost method was used. The actuarial assumptions included a 4.5 percent discount rate, which is based on the estimated long-term investment yield on the general assets of the Authority. The annual health care cost trend rate is 10.0 percent initially, reduced incrementally to an ultimate rate of 5.0 percent after ten years. The unfunded actuarial accrued liability is being amortized as a level dollar amount over 30 years.

2. Detailed Notes (Continued)

G. Compensated Absences

Full-time employees are granted from 10 to 25 days of vacation time per year depending on their years of service. Vacation earned during one year must be taken within the following year. The Executive Director is allowed to carry forward up to 50 days of vacation. Upon termination of employment, employees are compensated for the full value of all unused vacation pay. Part-time employees who work more than 1,000 hours in a calendar year will receive a personal day off (8 hours) for each 100 hours worked in excess of 1,000 hours. Unused vacation and personal leave earned as of December 31, 2011 and 2010, is estimated to be $110,321 and $115,611, respectively, and is recognized as a liability in the financial statements. The Executive Director's employment contract provides a benefit of six months of current salary upon termination. This has been accrued in the financial statements in the amount of $79,511 and $77,194 as of December 31, 2011 and 2010, respectively. Sick leave is earned at the rate of 1.5 days per month for full-time personnel. No more than 150 days may be carried at any time. Employees are not compensated for unused sick leave upon termination of employment.

The contingent liability for sick leave at December 31, 2011 and 2010, was estimated to be $582,836 and $591,146, respectively, and is not recognized as a liability in the financial statements.

H. Deferred Revenue

Deferred revenue consists of the following:

| | 2011 | 2010 |
|---|---|---|
| Advance deposits for future events | $ 139,770 | $ 130,874 |
| Gift certificates | 12,752 | 63,867 |
| Deferred lease revenue | 586,050 | 103,750 |
| Total | $ 738,572 | $ 298,491 |

2. Detailed Notes (Continued)

I. Minimum Future Rents Receivable

On January 9, 2001, the Authority entered into an amended lease agreement with Duluth Superior Excursions for six years with two five-year options to renew. This agreement is for the lease of space and facilities. Rent is adjusted annually based on the percentage increase in the Consumer Price Index. In 2011, rent was $55,185. This agreement terminated on December 31, 2011. A new agreement was entered into commencing on January 1, 2012, for a period of ten years with two five-year options to renew. Rent is adjusted by three percent annually.

On April 13, 2004, the Authority entered into a lease agreement with Cinema Entertainment Corporation (CEC) for 20 years with two five-year options to renew. This agreement is for the lease of property on which CEC constructed a theater. The annual rent of $175,000 will be increased by two percent each year in years 2 through 10 and three percent each year in years 11 through 20. In May 2007, Marcus Theatre Corporation purchased the Duluth 10 theater from CEC and is now responsible for the lease.

On November 18, 2010, the Authority entered into a lease agreement with the University of Minnesota for 25 years to rent space, facilities, and advertising for the men’s and women’s hockey programs in the new AMSOIL Arena. The annual rent ranges from $468,800 in 2011 to $898,270 in 2033. These lease revenues are dedicated to repay the City of Duluth bonds which were used to construct the new arena.

On October 15, 2011, the Authority entered into a 5-year lease agreement with the Duluth Curling Club, Inc., to occupy a portion of the Pioneer Hall Clubrooms for year-round rental at an annual rate of $39,074, and the Pioneer Hall Annex Ice Arena for a rental rate of $38,701 for pre-defined curling season dates. The rental rate increases annually by 2.25 percent.

Minimum future rents on non-cancelable leases are:

| Year | | |
|---|---|---|
| 2012 | $ | 930,812 |
| 2013 | | 951,371 |
| 2014 | | 860,061 |
| 2015 | | 885,248 |
| 2016 | | 878,631 |
| After 2016 | | 14,495,542 |
| Total | $ | 19,001,665 |

2. Detailed Notes (Continued)

J. Naming Rights Agreement

On June 29, 2010, the Authority entered into an agreement with AMSOIL, Inc., for naming rights to the new arena which was completed in 2010. The agreement grants AMSOIL, Inc., the rights to name the new arena in exchange for an initial payment of $2,000,000 in 2010 and payments of $200,000 per year for the years 2011 - 2031.

Minimum future rents on this agreement are:

| Year | |
|---|---|
| 2012 | $ 200,000 |
| 2013 | 200,000 |
| 2014 | 200,000 |
| 2015 | 200,000 |
| 2016 | 200,000 |
| After 2016 | 2,800,000 |
| Total | $ 3,800,000 |

K. Leases Payable

In May 2001, the Authority entered into a lease agreement to finance improvements to the locker rooms used by University of Minnesota Duluth hockey teams in the DECC arena. The lease agreement runs for 15 years, with interest at 5.25 percent and semi-annual payments of $77,500. At lease expiration, the locker room improvements will become the Authority's property and, as such, they have been recorded as capital assets. At December 31, 2011, the locker room improvements are valued at $1,534,313, with accumulated depreciation of $767,156.

The lease agreement for the locker room improvements required the Authority to deposit $77,500 into a reserve account to secure the lease purchase payments.

2. Detailed Notes

K. Leases Payable (Continued)

The present value of future minimum lease payments is shown below:

| Year | Interest | Principal |
|---|---|---|
| 2012 | $ 28,646 | $ 126,354 |
| 2013 | 21,926 | 133,074 |
| 2014 | 14,848 | 140,152 |
| 2015 | 7,393 | 147,607 |
| 2016 | 777 | 29,636 |
| Total | $ 73,590 | $ 576,823 |

L. Long-Term Debt

The following is a schedule of long-term liability activity of the Duluth Entertainment and Convention Center Authority for the years ended December 31, 2011 and 2010.

| | Balance January 1, 2011 | Additions | Reductions | Balance December 31, 2011 | Due Within One Year |
|---|---|---|---|---|---|
| General obligation refunding revenue bonds | $ 775,000 | $ - | $ 775,000 | $ - | $ - |
| Capital leases payable | 696,795 | - | 119,972 | 576,823 | 126,354 |
| Compensated absences payable | 192,805 | 129,070 | 132,043 | 189,832 | 110,321 |
| Total | $ 1,664,600 | $ 129,070 | $ 1,027,015 | $ 766,655 | $ 236,675 |

| | Balance January 1, 2010 | Additions | Reductions | Balance December 31, 2010 | Due Within One Year |
|---|---|---|---|---|---|
| General obligation refunding revenue bonds | $ 1,515,000 | $ - | $ 740,000 | $ 775,000 | $ 775,000 |
| Capital leases payable | 810,709 | - | 113,914 | 696,795 | 119,972 |
| Compensated absences payable | 184,991 | 142,486 | 134,672 | 192,805 | 115,611 |
| Total | $ 2,510,700 | $ 142,486 | $ 988,586 | $ 1,664,600 | $ 1,010,583 |

2. Detailed Notes (Continued)

M. Pledge Agreement with City of Duluth

In 2010, the Authority completed construction on a new arena and parking ramp. The total project of $78,285,000 was funded by a state grant of $38,000,000 and city general obligation bond proceeds of $40,285,000.

The Authority entered into a pledge agreement with the City of Duluth dated August 7, 2008, that requires the Authority to pledge $461,000 per year of Authority revenues beginning in 2012 through the life of the bonds ending in 2034. The pledged revenues will be used in combination with City of Duluth 0.75 percent food and beverage taxes and University of Minnesota Duluth lease revenues to repay the principal and interest on the bonds.

N. Budget to Actual for 2011 and 2010

The Duluth Entertainment and Convention Center Authority adopts a budget to be approved by the Duluth City Council. A summary of the operating budgets for the years ended December 31, 2011 and 2010, follows.

| | 2011 | | |
|---|---|---|---|
| | Budget | Actual | Favorable (Unfavorable) |
| Operating Revenues | $ 7,086,095 | $ 7,672,258 | $ 586,163 |
| Operating Expenses | 11,130,330 | 12,143,492 | (1,013,162) |
| Operating Income (Loss) | $ (4,044,235) | $ (4,471,234) | $ (426,999) |
| Nonoperating Revenues (Expenses) | 1,093,322 | 1,217,739 | 124,417 |
| Income (Loss) Before Contributions | $ (2,950,913) | $ (3,253,495) | $ (302,582) |
| Capital contributions | - | 3,250,801 | 3,250,801 |
| Change in Net Assets | $ (2,950,913) | $ (2,694) | $ 2,948,219 |

2. Detailed Notes

N. Budget to Actual for 2011 and 2010 (Continued)

| | 2010 | | |
|---|---|---|---|
| | Budget | Actual | Favorable (Unfavorable) |
| Operating Revenues | $ 6,978,370 | $ 7,241,769 | $ 263,399 |
| Operating Expenses | 10,339,485 | 9,847,320 | 492,165 |
| Operating Income (Loss) | $ (3,361,115) | $ (2,605,551) | $ 755,564 |
| Nonoperating Revenues (Expenses) | 731,839 | 2,881,635 | 2,149,796 |
| Income (Loss) Before Contributions | $ (2,629,276) | $ 276,084 | $ 2,905,360 |
| Capital contributions | - | 35,087,624 | 35,087,624 |
| Change in Net Assets | $ (2,629,276) | $ 35,363,708 | $ 37,992,984 |

O. Subsequent Event - OmniMax Theatre

In March 2011, the Duluth Omnimax Theatre operated by the Authority closed. In 2012, the Authority entered into a 20-year lease agreement with Marcus Theaters to rent the former Omnimax Theater and operate it as an UltraScreen movie theater.

# REQUIRED SUPPLEMENTARY INFORMATION

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**DULUTH ENTERTAINMENT AND CONVENTION CENTER AUTHORITY**
**(A COMPONENT UNIT OF THE CITY OF DULUTH)**

***EXHIBIT A-1***

SCHEDULE OF FUNDING PROGRESS - OTHER POSTEMPLOYMENT BENEFITS PLAN
DECEMBER 31, 2011

| Actuarial Valuation Date | Actuarial Value of Assets (a) | Actuarial Accrued Liability (b) | Unfunded Actuarial Accrued Liability (UAAL) (b - a) | Funded Ratio (a/b) | Covered Payroll (c) | UAAL as a Percentage of Covered Payroll ((b - a)/c) |
|---|---|---|---|---|---|---|
| June 1, 2007 | $ - | $ 3,709,014 | $ 3,709,014 | 0.00% | $ 1,456,880 | 254.58% |
| June 1, 2010 | - | 2,298,091 | 2,298,091 | 0.00 | 1,584,550 | 145.03 |

<u>Notes to Schedule of Funding Progress - Other Postemployment Benefits Plan</u>

The Duluth Entertainment and Convention Center Authority currently has no assets that have been irrevocably deposited in a trust for future health benefits. Therefore, the actuarial value of assets is zero.

The Authority implemented Governmental Accounting Standards Board Statement 45 in the fiscal year ended December 31, 2007. Information for prior years is not available.

The most recent actuarial valuation as of June 1, 2010, reflected changes in benefit provisions which resulted in a lower actuarial accrued liability. The primary change in benefit provisions was the transition of all retirees to Medical Plan 3 and Rx Plan 1, effective January 1, 2010. These are the same plans provided to active employees.

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**Management and Compliance Section**

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**STATE OF MINNESOTA**
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# 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*

Mayor and City Council
City of Duluth

Duluth Entertainment and Convention Center
 Authority Board

We have audited the basic financial statements of the Duluth Entertainment and Convention Center Authority, a component unit of the City of Duluth, as of and for the year ended December 31, 2011, and have issued our report thereon dated May 31, 2012. 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.

Internal Control Over Financial Reporting

Management of the Duluth Entertainment and Convention Center Authority is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered the Duluth Entertainment and Convention Center Authority's internal control over financial reporting as a basis for designing our auditing procedures 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 Authority's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Authority's internal control over financial reporting.

A deficiency in internal control over financial reporting 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 combination of deficiencies, in internal control over financial reporting such that there is a reasonable possibility that a material misstatement of the Authority's financial statements will not be prevented, or detected and corrected, on a timely basis.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Duluth Entertainment and Convention Center Authority's financial statements are free of 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*.

Minnesota Legal Compliance

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the provisions of the *Minnesota Legal Compliance Audit Guide for Political Subdivisions*, promulgated by the State Auditor pursuant to Minn. Stat. § 6.65. Accordingly, the audit included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

The *Minnesota Legal Compliance Audit Guide for Political Subdivisions* contains six categories of compliance to be tested: contracting and bidding, deposits and investments, conflicts of interest, public indebtedness, claims and disbursements, and miscellaneous provisions. Our study included all of the listed categories.

The results of our tests indicate that for the items tested, the Duluth Entertainment and Convention Center Authority complied with the material terms and conditions of applicable legal provisions.

This report is intended solely for the information and use of the Duluth Entertainment and Convention Center Authority Board, Mayor and City Council of Duluth, the Authority's management, and others within the Duluth Entertainment and Convention Center Authority and is not intended to be, and should not be, used by anyone other than those specified parties.

*/s/Rebecca Otto*

REBECCA OTTO
STATE AUDITOR

*/s/Greg Hierlinger*

GREG HIERLINGER, CPA
DEPUTY STATE AUDITOR

May 31, 2012