

# 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)**

**YEAR ENDED DECEMBER 31, 2016**

## **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 150 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 650 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)**

**Year Ended December 31, 2016**



**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)**

TABLE OF CONTENTS

	<u>Exhibit</u>	<u>Page</u>
<b>Introductory Section</b>		
Organization		1
<b>Financial Section</b>		
Independent Auditor's Report		2
Management's Discussion and Analysis		4
Basic Financial Statements		
Statement of Net Position	1	10
Statement of Revenues, Expenses, and Changes in Net Position	2	12
Statement of Cash Flows	3	13
Notes to the Financial Statements		15
Required Supplementary Information		
Schedule of Funding Progress - Other Postemployment Benefits Plan	A-1	37
PERA General Employees Retirement Plan		
Schedule of Proportionate Share of Net Pension Liability	A-2	38
Schedule of Contributions	A-3	39
Notes to the Required Supplementary Information - PERA		40
<b>Management and Compliance Section</b>		
Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance With <i>Government Auditing Standards</i>		41

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

ORGANIZATION  
DECEMBER 31, 2016

	<u>Term Expires</u>
<b>Directors</b>	
Mary Finnegan-Ongaro	January 7, 2019
Gregory Fox	January 7, 2019
Carrie Heffernan	June 30, 2018
Debra Messer	January 7, 2019
Don Ness	June 30, 2019
Crystal Pelkey	June 30, 2019
Karen Pionk	June 30, 2019
Yvonne Prettner Solon	January 7, 2019
Roger Reinert	June 30, 2020
David Ross	June 30, 2019
Jay Seiler	June 30, 2018
<b>Officers</b>	
<b>President</b>	
Jay Seiler	June 30, 2018
<b>Vice President</b>	
Yvonne Prettner Solon	January 7, 2019
<b>Auditor/Treasurer</b>	
Josh Bailey	Indefinite
<b>Executive Director</b>	
Daniel J. Russell	Indefinite

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REBECCA OTTO  
STATE AUDITOR

# STATE OF MINNESOTA OFFICE OF THE STATE AUDITOR

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## INDEPENDENT AUDITOR'S REPORT

Mayor and City Council  
City of Duluth, Minnesota

Board of Directors  
Duluth Entertainment and Convention Center  
Authority  
Duluth, Minnesota

### Report on the Financial Statements

We have audited the accompanying financial statements of the Duluth Entertainment and Convention Center Authority, a component unit of the City of Duluth, Minnesota, as of and for the year ended December 31, 2016, and the related notes to the financial statements, which collectively comprise the Authority's basic financial statements, as listed in the table of contents.

#### *Management's Responsibility for the Financial Statements*

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

#### *Auditor's Responsibility*

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Authority's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion

on the effectiveness of the Authority's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

***Opinion***

In our opinion, the 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, 2016, and the results of its operations and its cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

***Other Matters***

***Required Supplementary Information***

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis 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. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

***Other Reporting Required by Government Auditing Standards***

In accordance with *Government Auditing Standards*, we have also issued our report dated April 28, 2017, 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 the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Duluth Entertainment and Convention Center Authority's internal control over financial reporting and compliance.

*/s/Rebecca Otto*

REBECCA OTTO  
STATE AUDITOR

*/s/Greg Hierlinger*

GREG HIERLINGER, CPA  
DEPUTY STATE AUDITOR

April 28, 2017

## **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, 2016  
(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, 2016. This information should be read in conjunction with the financial statements.

**FINANCIAL HIGHLIGHTS**

- In 2016, total net position decreased \$3.0 million, or 3.3 percent, over the course of the year's operations.
- Total operating revenue increased \$0.1 million, or 1.4 percent, in 2016 compared to last year.
- Total operating expenses in 2016 increased by \$0.7 million, or 4.6 percent, compared to 2015.

**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 position; statement of revenues, expenses, and changes in net position; statement of cash flows; and notes to the financial statements. The statement of net position presents the financial position of the Authority on a full accrual, historical cost basis. The statement of net position provides information about the nature and amount of resources and obligations at year-end. The statement of revenues, expenses, and changes in net position presents the results of the business activities over the course of the fiscal year and information as to how the net position changed during the year. All changes in net position 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 Position (000s)

	2016	2015	Dollar Change Increase (Decrease) 2015 to 2016
<b>Assets</b>			
Current and other assets	\$ 4,749	\$ 3,649	\$ 1,100
Capital assets	89,776	92,625	(2,849)
<b>Total Assets</b>	<b>\$ 94,525</b>	<b>\$ 96,274</b>	<b>\$ (1,749)</b>
<b>Deferred outflows of resources</b>			
Deferred pension obligation outflows	\$ 1,985	\$ 432	\$ 1,553
<b>Liabilities</b>			
Current liabilities	\$ 2,513	\$ 1,704	\$ 809
Long-term liabilities	5,663	3,905	1,758
<b>Total Liabilities</b>	<b>\$ 8,176</b>	<b>\$ 5,609</b>	<b>\$ 2,567</b>
<b>Deferred outflows of resources</b>			
Deferred pension obligation outflows	\$ 390	\$ 154	\$ 236
<b>Net position</b>			
Net investment in capital assets	\$ 89,776	\$ 92,616	\$ (2,840)
Restricted	-	10	(10)
Unrestricted	(1,832)	(1,683)	(149)
<b>Total Net Position</b>	<b>\$ 87,944</b>	<b>\$ 90,943</b>	<b>\$ (2,999)</b>

In 2016, net position decreased \$3.0 million compared to 2015. Total assets decreased \$1.7 million mainly due to depreciation of \$3.8 million in 2016. Total liabilities increased \$2.6 million due to an increase in customer deposits, net postemployment benefits, and net pension liability compared to 2015.

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

	2016	2015	Dollar Change Increase (Decrease) 2015 to 2016
Operating revenues	\$ 9,696	\$ 9,561	\$ 135
Nonoperating revenues	1,915	1,753	162
<b>Total Revenues</b>	<b>\$ 11,611</b>	<b>\$ 11,314</b>	<b>\$ 297</b>
Operating expenses	\$ 15,010	\$ 14,350	\$ 660
Interest expense	-	2	(2)
<b>Total Expenses</b>	<b>\$ 15,010</b>	<b>\$ 14,352</b>	<b>\$ 658</b>
Excess of Revenues Over (Under) Expenses	\$ (3,399)	\$ (3,038)	\$ (361)
Capital Contributions	400	-	400
Change in Net Assets	\$ (2,999)	\$ (3,038)	\$ 39
Net Position - January 1	90,943	93,981	(3,038)
Net Position - December 31	<u>\$ 87,944</u>	<u>\$ 90,943</u>	<u>\$ (2,999)</u>

**Comparison with Budget**  
(000s)

	2016 Actual	2016 Budget	Variance with Budget	Percent Change (%)
Operating revenues	\$ 9,696	\$ 8,855	\$ 841	9.5
Nonoperating revenues	1,915	1,612	303	18.8
<b>Total Revenues</b>	<b>\$ 11,611</b>	<b>\$ 10,467</b>	<b>\$ 1,144</b>	<b>10.9</b>
Operating expenses	15,010	14,092	918	6.5
Excess of Revenues Over (Under) Expenses	\$ (3,399)	\$ (3,625)	\$ 226	(6.2)
Capital Contributions	400	-	400	-
Change in Net Assets	\$ (2,999)	\$ (3,625)	\$ 626	(17.3)
Net Position - January 1, a restated	90,943	90,943	-	-
Net Position - December 31	<u>\$ 87,944</u>	<u>\$ 87,318</u>	<u>\$ 626</u>	<u>0.7</u>

(Unaudited)

Page 7

## Revenues

The Authority's operating revenues increased \$135,000 to \$9.7 million in 2016 due to an increase in concessions sales, liquor sales, and ticket office and Irvin revenues. Nonoperating revenues increased \$162,000 compared to last year mainly due to hotel/motel tax contributions.

## Expenses

The Authority's operating expenses increased \$660,000 to \$15.0 million in 2016 mainly due to an increase in labor, food and liquor cost, utilities, and advertising/promotion compared to 2015.

## Budgetary Highlights

Operating revenues were over budget by \$841,000 in 2016 due mainly to an increase in concessions, ticket office sales, and Irvin sales. Nonoperating revenues were over budget by \$303,000 due to larger hotel/motel tax revenue than projected. Operating expenses were \$918,000 over budget in 2016 mainly due to labor, promotion costs, net other postemployment benefits liability, and net Public Employees Retirement Association pension liability.

## CAPITAL ASSETS AND DEBT ADMINISTRATION

### Capital Assets

	Capital Assets (000s)			Percent Change (%)
	2016	2015	Dollar Change	
Land	\$ 906	\$ 906	\$ -	-
Land improvements	303	303	-	-
Buildings	136,921	136,252	669	0.5
Equipment	11,237	10,956	281	2.6
Construction in progress	42	37	5	13.5
Total	\$ 149,409	\$ 148,454	\$ 955	0.6
Less: accumulated depreciation	(59,631)	(55,829)	(3,802)	6.8
Net Capital Assets	\$ 89,778	\$ 92,625	\$ (2,847)	(3.1)

By the end of 2016, the Authority had invested \$149.4 million in capital assets. The increase in buildings and structures is mainly due to a new building-wide signage package, elevator upgrade, retrofit lighting, and computer network/backup system. For more information, see Note 2.C. to the financial statements.

**Debt Administration**

	<b>Debt (000s)</b>		Dollar Change	Percent Change (%)
	2016	2015		
Locker room lease	\$ -	\$ 10	\$ (10)	(100.0)

As of December 31, 2016, the Authority’s outstanding debt was paid off. No additional debt was incurred during the year. For additional information, see Notes 2.K. to the financial statements.

**ECONOMIC FACTORS AND NEXT YEAR’S BUDGET**

Many factors were considered when completing the budget for 2017. Convention business is projected to be down in 2017 compared to 2016. Overall, a slight decrease in revenue is projected for 2017 compared to 2016 mainly due to a decrease in catering and parking revenue. Rent and building services prices for 2017 were established in 2013 and included a minimal increase for some goods and services. New catering prices went into effect on April 2015, and most concessions prices are increased annually in October. Overall operating expenses in 2017 are projected to stay the same as 2016.

**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*

**STATEMENT OF NET POSITION  
DECEMBER 31, 2016**

**Assets**

**Current assets**

Cash and cash equivalents	\$ 2,602,558
Accounts receivable	333,747
Due from City of Duluth	678,806
Inventory	163,900
Prepaid items	16,184
	16,184

**Total current assets** **\$ 3,795,195**

**Restricted current assets**

Assets restricted for customer deposits	
Cash and cash equivalents	\$ 926,484
Accounts receivable	26,059
Assets restricted for employee flexible benefits plan	
Cash and cash equivalents	806
	806

**Total restricted current assets** **\$ 953,349**

**Total current assets** **\$ 4,748,544**

**Noncurrent assets**

Capital assets	
Not depreciated	\$ 947,179
Depreciated	148,460,640
Less: allowance for depreciation	(59,631,345)
	(59,631,345)

**Total capital assets - net of accumulated depreciation** **\$ 89,776,474**

**Total noncurrent assets - net** **\$ 89,776,474**

**Total Assets** **\$ 94,525,018**

**Deferred Outflows of Resources**

Deferred pension outflows **\$ 1,984,573**

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

**EXHIBIT 1  
(Continued)**

**STATEMENT OF NET POSITION  
DECEMBER 31, 2016**

**Liabilities**

**Current liabilities**

Accounts payable	\$	586,521
Salaries payable		65,328
Compensated absences payable - current		127,022
Unearned revenue		782,289
		782,289

**Total current liabilities** **\$ 1,561,160**

**Current liabilities payable from restricted assets**

Customer deposits	\$	951,337
Employee flexible benefits plan payable		660
		660

**Total current liabilities payable from restricted assets** **\$ 951,997**

**Total current liabilities** **\$ 2,513,157**

**Noncurrent liabilities**

Compensated absences payable - long-term	\$	81,505
Net pension liability		4,798,627
Net other postemployment benefits liability		783,098
		783,098

**Total noncurrent liabilities** **\$ 5,663,230**

**Total Liabilities** **\$ 8,176,387**

**Deferred Inflows of Resources**

Deferred pension inflows **\$ 389,643**

**Net Position**

Net investment in capital assets	\$	89,776,474
Unrestricted		(1,832,913)
		(1,832,913)

**Total Net Position** **\$ 87,943,561**

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

*EXHIBIT 2*

**STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION  
FOR THE YEAR ENDED DECEMBER 31, 2016**

<b>Operating Revenues</b>	
Sales	\$ 3,817,411
Charges for services	5,400,446
Miscellaneous	477,722
	<hr/>
<b>Total Operating Revenues</b>	<b>\$ 9,695,579</b>
<b>Operating Expenses</b>	
Personal services	\$ 5,706,694
Supplies and services	1,871,492
Utilities	1,399,781
Other services and charges	2,217,626
Depreciation	3,814,952
	<hr/>
<b>Total Operating Expenses</b>	<b>\$ 15,010,545</b>
<b>Operating Income (Loss)</b>	<b>\$ (5,314,966)</b>
<b>Nonoperating Revenues (Expenses)</b>	
Interest income	\$ 20,086
Hotel/motel tax revenue	1,683,274
Naming rights revenue	200,000
Interest expense	(82)
	<hr/>
<b>Total Nonoperating Revenues (Expenses)</b>	<b>\$ 1,915,778</b>
<b>Change in Net Position</b>	<b>\$ (2,999,188)</b>
<b>Net Position - January 1</b>	<b>90,942,749</b>
	<hr/>
<b>Net Position - December 31</b>	<b>\$ 87,943,561</b>
	<hr/> <hr/>

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

*EXHIBIT 3*

**STATEMENT OF CASH FLOWS  
FOR THE YEAR ENDED DECEMBER 31, 2016**

<b>Cash Flows from Operating Activities</b>	
Cash received from customers	\$ 9,717,918
Payments to suppliers	(5,294,502)
Payments to employees	(5,244,299)
Other operating revenues	<u>477,722</u>
<b>Net cash provided by (used in) operating activities</b>	<b><u>\$ (343,161)</u></b>
<b>Cash Flows from Noncapital Financing Activities</b>	
City of Duluth hotel/motel taxes	<b><u>\$ 1,557,804</u></b>
<b>Cash Flows from Capital and Related Financing Activities</b>	
Payment received for naming rights	200,000
Cash from lease escrow account	10,096
Principal paid on lease purchases	(9,939)
Interest paid on lease purchases	(239)
Acquisition or construction of capital assets	<u>(966,084)</u>
<b>Net cash provided by (used in) capital and related financing activities</b>	<b><u>\$ (353,666)</u></b>
<b>Cash Flows from Investing Activities</b>	
Interest on investments	<b><u>\$ 20,086</u></b>
<b>Net Increase (Decrease) in Cash and Cash Equivalents</b>	<b>\$ 881,063</b>
<b>Cash and Cash Equivalents - January 1</b>	<b><u>2,648,785</u></b>
<b>Cash and Cash Equivalents - December 31</b>	<b><u><u>\$ 3,529,848</u></u></b>

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

**EXHIBIT 3  
(Continued)**

**STATEMENT OF CASH FLOWS  
FOR THE YEAR ENDED DECEMBER 31, 2016**

<b>Reconciliation of Operating Income (Loss) to Net Cash Provided by (Used in) Operating Activities</b>	
Operating income (loss)	\$ (5,314,966)
 <b>Adjustments to reconcile operating income (loss) to net cash provided by (used in) operating activities</b>	
Depreciation	3,814,952
(Increase) decrease in accounts receivable	(87,494)
(Increase) decrease in inventory	(17,642)
(Increase) decrease in prepaid items	2,037
(Increase) decrease in deferred pension outflows	(1,552,457)
Increase (decrease) in accounts payable	210,002
Increase (decrease) in salaries payable	21,402
Increase (decrease) in unearned revenue	19,155
Increase (decrease) in customer deposits	568,400
Increase (decrease) in compensated absences payable	(414)
Increase (decrease) in net other postemployment benefits liability	17,439
Increase (decrease) in deferred pension inflows	235,484
Increase (decrease) in net pension liability	1,740,941
	1,740,941
 <b>Net Cash Provided by (Used in) Operating Activities</b>	 <b><u><u>\$ (343,161)</u></u></b>

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

**NOTES TO THE FINANCIAL STATEMENTS  
AS OF AND FOR THE YEAR ENDED DECEMBER 31, 2016**

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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 with 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 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.

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

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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 a full accrual, economic resource basis, under which revenues are recorded when earned and expenses are recorded when liabilities are incurred.

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.

F. Inventories of Merchandise for Resale

Inventories are priced at the lower of cost or market value on a first-in, first-out basis and are recorded as expenses when consumed.

G. Capital Assets

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



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

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1. Summary of Significant Accounting Policies

G. Capital Assets (Continued)

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, 20 years for land improvements, and 3 to 20 years for equipment.

I. Deferred Outflows/Inflows of Resources

In addition to assets, the statement of financial position reports a separate section for deferred outflows of resources. This separate financial statement element, deferred outflows of resources, represents a consumption of net position that applies to a future period(s) and will not be recognized as an outflow of resources (expense) until then. Currently, the Authority has one item, deferred pension outflows, that qualifies for reporting in this category. Deferred pension outflows consist of changes in actuarial assumptions, the difference between projected and actual investment earnings, changes in proportion, and contributions paid to PERA subsequent to the measurement date.

In addition to liabilities, the statement of financial position reports a separate section for deferred inflows of resources. This separate financial statement element, deferred inflows of resources, represents an acquisition of net position that applies to a future period(s) and so will not be recognized as an inflow of resources (revenue) until that time. The Authority has only one type of item, deferred pension inflows, that qualifies for reporting in this category. This amount consists of the difference between expected and actual economic experience.

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

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1. Summary of Significant Accounting Policies (Continued)

J. Restricted Assets

Restricted assets consist of promoter-escrowed funds and the employee flexible benefits plan account. 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.

K. Unearned Revenue

Unearned 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.

L. Classification of Net Position

Net position is classified in the following categories:

Net investment in capital assets - the amount of net position representing capital assets, net of accumulated depreciation, and reduced by outstanding debt, if any, attributed to the acquisition, construction or improvement of the assets.

Restricted net position - the amount of net position for which external restrictions have been imposed by creditors, grantors, contributors, or laws, or constitutional provisions or enabling legislation.

Unrestricted net position - the amount of net position that does not meet the definition of restricted or net investment in capital assets.

When both restricted and unrestricted resources are available for use, it is the Authority's policy to use restricted resources first and then unrestricted resources as needed.

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

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1. Summary of Significant Accounting Policies (Continued)

M. 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.

N. Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make certain estimates and assumptions that affect the reported amounts of assets, deferred inflows of resources, liabilities, and deferred inflows or resources; 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.

O. 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 are debited to the appropriate expense accounts and credited to the appropriate revenue accounts.

P. Pension Plan

For purposes of measuring the net pension liability, deferred outflows/inflows of resources, and pension expense, information about the fiduciary net position of the Public Employees Retirement Association of Minnesota (PERA) and additions to/deductions from PERA's fiduciary net position have been determined on the same basis as they are reported by PERA, except that PERA's fiscal year-end is June 30. For this purpose, plan contributions are recognized as of employer payroll paid dates, and benefit payments and refunds are recognized when due and payable in accordance with the benefit terms. Plan investments are reported at fair value.

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

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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 Authority invests funds in the City of Duluth's investment pool. The fair value of the investment is the fair value per share of the underlying portfolio. The Authority invests in this pool for the purpose of joint investment with the City in order to enhance investment earnings. There are no redemption limitations. 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, 2016:

Current assets	
City of Duluth pooled cash account	\$ 522,186
Checking account - ticket office	7,000
Checking account - employee flexible benefits plan	7,372
Savings account - operating reserve	2,000,000
Petty cash and change funds	<u>66,000</u>
Total current assets	<u>\$ 2,602,558</u>
Restricted current assets	
Ticket office customer deposits - checking	\$ 909,284
Ticket office change fund	17,200
Employee flexible benefits plan - checking	<u>806</u>
Total restricted current assets	<u>\$ 927,290</u>
Total	<u>\$ 3,529,848</u>

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

2. Detailed Notes (Continued)

B. Due From City of Duluth

Amounts due from the City of Duluth at December 31, 2016, are as follows:

Current Hotel/motel tax	<u>\$ 678,806</u>
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C. Capital Assets

A summary of the changes in the capital asset accounts for the year ended December 31, 2016, follows:

	Balance January 1, 2016	Increase	Decrease	Reclassifications	Balance December 31, 2016
Capital assets not depreciated					
Land	\$ 905,601	\$ -	\$ -	\$ -	\$ 905,601
Construction in progress	37,388	228,376	-	(224,186)	41,578
Total capital assets not depreciated	\$ 942,989	\$ 228,376	\$ -	\$ (224,186)	\$ 947,179
Capital assets depreciated					
Land improvements	\$ 302,957	\$ -	\$ -	\$ -	\$ 302,957
Buildings	136,251,889	447,856	-	221,047	136,920,792
Equipment	10,956,400	289,852	12,500	3,139	11,236,891
Total capital assets depreciated	\$ 147,511,246	\$ 737,708	\$ 12,500	\$ 224,186	\$ 148,460,640
Less: accumulated depreciation for					
Land improvements	\$ 302,957	\$ -	\$ -	\$ -	\$ 302,957
Buildings	47,649,071	3,449,628	-	-	51,098,699
Equipment	7,876,865	365,324	12,500	-	8,229,689
Total accumulated depreciation	\$ 55,828,893	\$ 3,814,952	\$ 12,500	\$ -	\$ 59,631,345
Total capital assets depreciated, net	\$ 91,682,353	\$ (3,077,244)	\$ -	\$ 224,186	\$ 88,829,295
Total Capital Assets, Net	\$ 92,625,342	\$ (2,848,868)	\$ -	\$ -	\$ 89,776,474

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

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2. Detailed Notes (Continued)

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.

E. Defined Benefit Pension Plan

1. Plan Description

All full-time and certain part-time employees of the Duluth Entertainment and Convention Center Authority are covered by a defined benefit pension plan administered by the Public Employees Retirement Association of Minnesota (PERA). PERA administers the General Employees Retirement Plan, which is a cost-sharing, multiple-employer retirement plan. The plan is established and administered in accordance with Minn. Stat. chs. 353 and 356. PERA's defined benefit pension plan is a tax qualified plan under Section 401(a) of the Internal Revenue Code.

The General Employees Retirement Plan (accounted for in the General Employees Fund) has multiple benefit structures with members belonging to the Coordinated Plan, the Basic Plan, or the Minneapolis Employees Retirement Fund. Coordinated Plan members are covered by Social Security and Basic Plan and Minneapolis Employees Retirement Fund members are not. The Basic Plan was closed to new members in 1967. The Minneapolis Employees Retirement Fund was closed to new members during 1968 and merged with the General Employees Retirement Plan in 2015. All new members must participate in the Coordinated Plan, for which benefits vest after five years of credited service. No authority employees belong to the Basic Plan or the Minneapolis Employees Retirement Fund.

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

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2. Detailed Notes

E. Defined Benefit Pension Plan (Continued)

2. Benefits Provided

PERA provides retirement benefits as well as disability benefits to members and benefits to survivors upon death of eligible members. Benefit provisions are established by state statute and can be modified only by the state legislature. Benefit increases are provided to benefit recipients each January. Increases are related to the funding ratio of the plan. Benefit recipients receive a future annual 1.0 percent post-retirement benefit increase. If the funding ratio reaches 90 percent for two consecutive years, the benefit increase will revert to 2.5 percent. If, after reverting to a 2.5 percent benefit increase, the funding ratio declines to less than 80 percent for one year or less than 85 percent for two consecutive years, the benefit increase will decrease to 1.0 percent.

The benefit provisions stated in the following paragraph 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 their public service.

Benefits are based on a member's highest average salary for any five successive years of allowable service, age, and years of credit at termination of service. Two methods are used to compute benefits for General Employees Retirement Plan Coordinated Plan members. Members hired prior to July 1, 1989, receive 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 for a Coordinated Plan member is 1.2 percent of average salary for each of the first ten years of service and 1.7 percent for each remaining year. Under Method 2, the annuity accrual rate is 1.7 percent for Coordinated Plan members for each year of service.

For General Employees Retirement Plan members hired prior to July 1, 1989, a full annuity is available when age plus years of service equal 90, and normal retirement age is 65. For members hired on or after July 1, 1989, normal retirement age is the age for unreduced Social Security benefits capped at 66. Disability benefits are available for vested members and are based on years of service and average high-five salary.

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

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2. Detailed Notes

E. Defined Benefit Pension Plan (Continued)

3. Contributions

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. General Employees Retirement Plan Coordinated members were required to contribute 6.50 percent of their annual covered salary in 2016.

In 2016, the Authority was required to contribute the following percentages of annual covered salary:

General Employees Retirement Plan Coordinated Plan members	7.50%
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The employee and employer contribution rates did not change from the previous year.

The Authority's contribution for the General Employees Retirement Plan for the year ended December 31, 2016, were \$267,844. The contributions are equal to the contractually required contributions as set by state statute.

4. Pension Costs

At December 31, 2016, the Authority reported a liability of \$4,798,627 for its proportionate share of the General Employees Retirement Plan's net pension liability. The net pension liability was measured as of June 30, 2016, and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of that date. The Authority's proportion of the net pension liability was based on the Authority's contributions received by PERA during the measurement period for employer payroll paid dates from July 1, 2015, through June 30, 2016, relative to the total employer contributions received from all of PERA's participating employers. At June 30, 2016, the Authority's proportion was 0.0591 percent. It was 0.0590 percent measured as of June 30, 2015. The Authority recognized pension expense of \$442,664 for its proportionate share of the General Employees Retirement Plan's pension expense.



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

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2. Detailed Notes

E. Defined Benefit Pension Plan

4. Pension Costs (Continued)

The Authority also recognized \$18,696 as revenue, which results in a reduction of the net pension liability, for its proportionate share of the State of Minnesota's contribution to the General Employees Retirement Plan, which qualifies as a special funding situation. Legislation requires the State of Minnesota to contribute \$6 million to the General Employees Retirement Plan each year, starting September 15, 2015, through September 15, 2031.

Authority's proportionate share of the net pension liability	\$	4,798,627
State of Minnesota's proportionate share of the net pension liability associated with the Authority		62,701
Total	\$	4,861,328

The Authority reported its proportionate share of the General Employees Retirement Plan's deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

	Deferred Outflows of Resources	Deferred Inflows of Resources
Difference between expected and actual economic experience	\$ -	\$ 389,643
Changes in actuarial assumptions	939,575	
Difference between projected and actual investment earnings	910,432	-
Changes in proportion	13,282	-
Contributions paid to PERA subsequent to the measurement date	121,284	-
Total	\$ 1,984,573	\$ 389,643

The \$121,284 reported as deferred outflows of resources related to pensions resulting from contributions subsequent to the measurement date will be recognized as a reduction of the net pension liability in the year ended December 31, 2017.

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

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2. Detailed Notes

E. Defined Benefit Pension Plan

4. Pension Costs (Continued)

Other amounts reported as deferred outflows and inflows of resources related to pensions will be recognized in pension expense as follows:

<u>Year Ended December 31</u>	<u>Pension Expense Amount</u>
2017	\$ 417,874
2018	417,874
2019	464,563
2020	173,335

5. Actuarial Assumptions

The total pension liability in the June 30, 2016, actuarial valuation was determined using the individual entry age normal actuarial cost method and the following additional actuarial assumptions:

Inflation	2.50 percent per year
Active member payroll growth	3.25 percent per year
Investment rate of return	7.50 percent

Salary increases were based on a service-related table. Mortality rates for active members, retirees, survivors, and disabilitants in the General Employees Retirement Plan were based on RP-2014 tables. The cost of living benefit increases for retirees is assumed to be 1.0 percent.

Actuarial assumptions used in the June 30, 2016, valuation were based on the results of actuarial experience studies. The experience study in the General Employees Retirement Plan was for the period 2008 through 2015.

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

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2. Detailed Notes

E. Defined Benefit Pension Plan

5. Actuarial Assumptions (Continued)

The long-term expected rate of return on pension plan investments is 7.5 percent. The State Board of Investment, which manages the investments of PERA, prepares an analysis of the reasonableness of the long-term expected rate of return on a regular basis using a building-block method in which best-estimate ranges of expected future rates of return are developed for each major asset class. These ranges are combined to produce an expected long-term rate of return by weighting the expected future rates of return by the target asset allocation percentages. The target allocation and best estimates of arithmetic real rates of return for each major asset class are summarized in the following table:

<u>Asset Class</u>	<u>Target Allocation</u>	<u>Long-Term Expected Real Rate of Return</u>
Domestic stocks	45%	5.50%
International stocks	15	6.00
Bonds	18	1.45
Alternative assets	20	6.40
Cash	2	0.50

6. Discount Rate

The discount rate used to measure the total pension liability was 7.50 percent in 2016, a reduction of the 7.90 percent used in 2015. The projection of cash flows used to determine the discount rate assumed that employee and employer contributions will be made at the rate specified in statute. Based on that assumption, the fiduciary net position of the General Employees Retirement Plan was projected to be available to make all projected future benefit payments of current active and inactive employees. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the total pension liability.

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

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2. Detailed Notes

E. Defined Benefit Pension Plan (Continued)

7. Changes in Actuarial Assumptions

The following changes in actuarial assumptions occurred in 2016:

General Employees Retirement Plan

- The assumed post-retirement benefit increase rate was changed from 1.00 percent per year through 2035 and 2.50 percent per year thereafter, to 1.00 percent for all future years.
- The assumed investment rate was changed from 7.90 percent to 7.50 percent. The single discount rate was also changed from 7.90 percent to 7.50 percent.
- Other assumptions were changed pursuant to the experience study dated June 30, 2015. The assumed payroll growth and inflation were decreased by 0.25 percent. Payroll growth was reduced from 3.50 percent to 3.25 percent. Inflation was reduced from 2.75 percent to 2.50 percent.

8. Pension Liability Sensitivity

The following presents the Authority's share of the net pension liability calculated using the discount rate disclosed in the preceding paragraph, as well as what the Authority's proportionate share of the net pension liability would be if it were calculated using a discount rate 1.0 percentage point lower or 1.0 percentage point higher than the current discount rate:

	Proportionate Share of the General Employees Retirement Fund	
	Discount Rate	Net Pension Liability
1% Decrease	6.50%	\$ 6,815,472
Current	7.50	4,798,627
1% Increase	8.50	3,137,295

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

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2. Detailed Notes

E. Defined Benefit Pension Plan (Continued)

9. Pension Plan Fiduciary Net Position

Detailed information about the pension plan's fiduciary net position is available in a separately issued PERA financial report that includes financial statements and required supplementary information. That report may be obtained on the internet at [www.mnpera.org](http://www.mnpera.org); by writing to PERA at 60 Empire Drive, Suite 200, St. Paul, Minnesota 55103-2088; or by calling 651-296-7460 or 1-800-652-9026.

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 not 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, 2016, 15 retirees were receiving health benefits from the Authority's health plan.

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

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2. Detailed Notes

F. Postemployment Benefits

1. Plan Description and Funding Policy (Continued)

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. 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	\$	106,563
Interest on net OPEB obligation		24,884
Adjustment to ARC		(40,336)
		_____
Annual OPEB cost	\$	91,111
Contributions during the year		(73,672)
		_____
Increase in net OPEB obligation	\$	17,439
Net OPEB, Beginning of Year		765,659
		_____
Net OPEB, End of Year	\$	783,098

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

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2. Detailed Notes

F. Postemployment Benefits

2. Annual OPEB Cost and Net OPEB Obligation (Continued)

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, 2016, 2015, and 2014, were as follows:

	2016	2015	2014
Percentage of annual OPEB cost contributed	80.86%	56.09%	57.64%
Annual OPEB cost	\$ 91,111	\$ 133,042	\$ 133,821
Employer contributions	<u>(73,672)</u>	<u>(74,618)</u>	<u>(77,132)</u>
Net Increase in Net OPEB Obligation	\$ 17,439	\$ 58,424	\$ 56,689
Net OPEB Obligation, Beginning of Year	<u>765,659</u>	<u>707,235</u>	<u>650,546</u>
Net OPEB Obligation, End of Year	<u>\$ 783,098</u>	<u>\$ 765,659</u>	<u>\$ 707,235</u>

3. Funded Status and Funding Progress

The actuarial accrued liability for benefits at January 1, 2016, the most recent actuarial valuation date, is \$1,591,996. 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 \$1,712,423. The ratio of the unfunded actuarially accrued liabilities to covered payroll is 92.97 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.

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

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2. Detailed Notes

F. Postemployment Benefits

3. Funded Status and Funding Progress (Continued)

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 January 1, 2016, actuarial valuation, the projected unit credit actuarial cost method was used. The actuarial assumptions included a 3.25 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.

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, 2016, is estimated to be \$127,022 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 \$81,505 as of December 31, 2016. 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, 2016, was estimated to be \$681,014 and is not recognized as a liability in the financial statements.



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

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2. Detailed Notes (Continued)

H. Unearned Revenue

Unearned revenue as of December 31, 2016, consists of the following:

Advance deposits for future events	\$ 123,719
Gift certificates	15,279
Unearned lease revenue	<u>643,291</u>
Total	<u>\$ 782,289</u>

I. Minimum Future Rents Receivable

On January 1, 2012, the Authority entered into a lease agreement with Vistas Cruises, Inc., for ten years, with two five-year options to renew. This agreement is for the lease of space and facilities. Rent is adjusted by 3.0 percent annually. In 2016, rent was \$61,903.

On April 13, 2004, the Authority entered into a lease agreement with Cinema Entertainment Corporation (CEC) for 20 years, with two 5-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 2.0 percent each year in years 2 through 10 and 3.0 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 January 1, 2012, an amended lease agreement was signed with B & G Realty, LLC, to include the OMNIMAX Theatre space in the leased premises for an additional \$36,000 per year, with an annual Consumer Price Index increase beginning January 1, 2015. In addition, the Authority agreed to reimburse B & G Realty, through lease payment deductions, \$25,000 for expenses related to the conversion and remodeling of said space. On April 18 and August 1, 2012, the reimbursable amount to B & G Realty was increased \$10,000 and \$11,417, respectively, for a total of \$46,417 for conversion and remodeling.

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.

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

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2. Detailed Notes

I. Minimum Future Rents Receivable (Continued)

On October 1, 2015, the Authority entered into a 22-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 \$43,358, and the Pioneer Hall Annex Ice Arena for a rental rate of \$43,358 for pre-defined curling season dates. The rental rate increases annually by 2.0 percent.

Minimum future rents on non-cancellable leases are:

<u>Year</u>	
2017	\$ 980,648
2018	1,009,195
2019	1,038,580
2020	1,068,827
2021	1,099,966
After 2021	<u>12,000,968</u>
Total	<u>\$ 17,198,184</u>

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 through 2031.

Minimum future rents on this agreement are:

<u>Year</u>	
2017	\$ 200,000
2018	200,000
2019	200,000
2020	200,000
2021	200,000
After 2021	<u>1,800,000</u>
Total	<u>\$ 2,800,000</u>

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

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2. Detailed Notes (Continued)

K. Long-Term Liabilities

The following is a schedule of long-term liability activity of the Duluth Entertainment and Convention Center Authority for the year ended December 31, 2016.

	Balance January 1, 2016	Additions	Reductions	Balance December 31, 2016	Due Within One Year
Capital leases payable	\$ 9,939	\$ -	\$ 9,939	\$ -	\$ -
Compensated absences payable	208,941	141,550	141,964	208,527	127,022
Total	<u>\$ 218,880</u>	<u>\$ 141,550</u>	<u>\$ 151,903</u>	<u>\$ 208,527</u>	<u>\$ 127,022</u>

L. Pledge Agreement with City of Duluth

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

In March 2016, the City of Duluth issued \$33,440,000 in General Obligation Duluth Entertainment and Convention Center Authority Improvement Refunding Bonds, Series 2016A, to refund the City of Duluth's Series 2008A Duluth Entertainment and Convention Center Authority Improvement Bonds of \$40,285,000. The transaction resulted in a net present value savings of \$5,414,950.

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.

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

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2. Detailed Notes (Continued)

M. Budget to Actual for 2016

The Duluth Entertainment and Convention Center Authority adopts a budget to be approved by the Duluth City Council. A summary of the operating budget compared to actual for the year ended December 31, 2016, follows.

	<u>Budget</u>	<u>Actual</u>	<u>Favorable (Unfavorable)</u>
Operating Revenues	\$ 8,855,295	\$ 9,695,579	\$ 840,284
Operating Expenses	<u>14,091,993</u>	<u>15,010,545</u>	<u>(918,552)</u>
Operating Income (Loss)	\$ (5,236,698)	\$ (5,314,966)	\$ (78,268)
Nonoperating Revenues (Expenses)	<u>1,611,920</u>	<u>1,915,778</u>	<u>303,858</u>
Income (Loss) Before Contributions	\$ (3,624,778)	\$ (3,399,188)	\$ 225,590
Capital contributions	<u>-</u>	<u>400,000</u>	<u>400,000</u>
Change in Net Position	<u>\$ (3,624,778)</u>	<u>\$ (2,999,188)</u>	<u>\$ 625,590</u>

**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, 2016**

<u>Actuarial Valuation Date</u>	<u>Actuarial Value of Assets (a)</u>	<u>Actuarial Accrued Liability (b)</u>	<u>Unfunded Actuarial Accrued Liability (UAAL) (b - a)</u>	<u>Funded Ratio (a/b)</u>	<u>Covered Payroll (c)</u>	<u>UAAL as a Percentage of Covered Payroll ((b - a)/c)</u>
June 1, 2010	\$ -	\$ 2,298,091	\$ 2,298,091	0.00%	\$ 1,584,550	145.03%
January 1, 2013	-	1,853,643	1,853,643	0.00	1,603,586	115.59
January 1, 2016	-	1,591,996	1,591,996	0.00	1,712,423	92.97

Notes to Schedule of Funding Progress - Other Postemployment Benefits Plan

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 June 1, 2010, actuarial valuation, 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.

The January 1, 2016, actuarial valuation reflected a discount rate of 3.25 percent, a change of 1.25 percent from the previous actuarial valuation.

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

*EXHIBIT A-2*

**SCHEDULE OF PROPORTIONATE SHARE OF NET PENSION LIABILITY  
PERA GENERAL EMPLOYEES RETIREMENT PLAN  
DECEMBER 31, 2016**

<b>Measurement Date</b>	<b>Employer's Proportion of the Net Pension Liability (Asset)</b>	<b>Employer's Proportionate Share of the Net Pension Liability (Asset) (a)</b>	<b>State's Proportionate Share of the Net Pension Liability Associated with the Authority (b)</b>	<b>Employer's Proportionate Share of the Net Pension Liability and the State's Related Share of the Net Pension Liability (Asset) (a + b)</b>	<b>Covered Payroll (c)</b>	<b>Employer's Proportionate Share of the Net Pension Liability (Asset) as a Percentage of Covered Payroll (a/c)</b>	<b>Plan Fiduciary Net Position as a Percentage of the Total Pension Liability</b>
2016	0.0591%	\$ 4,798,627	\$ 62,701	\$ 4,861,328	\$ 3,620,162	132.55%	68.91%
2015	0.0590	3,057,686	N/A	3,057,686	3,463,401	88.29	78.19

This schedule is intended to show information for ten years. Additional years will be displayed as they become available.  
The measurement date for each year is June 30.  
N/A - Not Applicable



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

*EXHIBIT A-3*

**SCHEDULE OF CONTRIBUTIONS  
PERA GENERAL EMPLOYEES RETIREMENT PLAN  
DECEMBER 31, 2016**

<b>Year Ending</b>	<b>Statutorily Required Contributions (a)</b>	<b>Actual Contributions in Relation to Statutorily Required Contributions (b)</b>	<b>Contribution (Deficiency) Excess (b - a)</b>	<b>Covered Payroll (c)</b>	<b>Actual Contributions as a Percentage of Covered Payroll (b/c)</b>
2016	\$ 267,844	\$ 267,844	\$ -	\$ 3,715,149	7.21%
2015	277,570	264,824	(12,746)	3,700,932	7.16

This schedule is intended to show information for ten years. Additional years will be displayed as they become available. The Duluth Entertainment and Convention Center Authority's year-end is December 31.

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

**NOTES TO THE REQUIRED SUPPLEMENTARY INFORMATION - PERA  
FOR THE YEAR ENDED DECEMBER 31, 2016**

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Defined Benefit Pension Plans - Changes in Significant Plan Provisions, Actuarial Methods, and Assumptions

The following changes were reflected in the valuation performed on behalf of the Public Employees Retirement Association for the year ended June 30, 2016:

General Employees Retirement Plan

- The assumed post-retirement benefit increase rate was changed from 1.00 percent per year through 2035 and 2.50 percent per year thereafter, to 1.00 percent for all future years.
- The assumed investment rate was changed from 7.90 percent to 7.50 percent. The single discount rate was also changed from 7.90 percent to 7.50 percent.
- Other assumptions were changed pursuant to the experience study dated June 30, 2015. The assumed payroll growth and inflation were decreased by 0.25 percent. Payroll growth was reduced from 3.50 percent to 3.25 percent. Inflation was reduced from 2.75 percent to 2.50 percent.

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REBECCA OTTO  
STATE AUDITOR

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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***

### Independent Auditor's Report

Mayor and City Council  
City of Duluth, Minnesota

Board of Directors  
Duluth Entertainment and Convention Center  
Authority  
Duluth, Minnesota

We have audited, 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, the financial statements of the Duluth Entertainment and Convention Center Authority, a component unit of the City of Duluth, Minnesota, as of and for the year ended December 31, 2016, and the related notes to the financial statements, which collectively comprise the Authority's basic financial statements, and have issued our report thereon dated April 28, 2017.

### **Internal Control Over Financial Reporting**

In planning and performing our audit of the financial statements, we considered the Duluth Entertainment and Convention Center Authority's internal control over financial reporting to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the 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. A significant deficiency is a deficiency, or combination of deficiencies, in internal control over financial reporting that is less severe than a material weakness, yet important enough to merit the attention of those charged with governance.

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 material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses or significant deficiencies. However, material weaknesses or significant deficiencies may exist that have not been identified.

### **Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the Duluth Entertainment and Convention Center Authority's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

### **Minnesota Legal Compliance**

The *Minnesota Legal Compliance Audit Guide for Cities*, promulgated by the State Auditor pursuant to Minn. Stat. § 6.65, contains seven categories of compliance to be tested in connection with the audit of the Authority's financial statements: contracting and bidding, deposits and investments, conflicts of interest, public indebtedness, claims and disbursements, miscellaneous provisions, and tax increment financing. Our audit considered all of the listed categories, except that we did not test for compliance with the provisions for tax increment financing because the Authority did not administer any tax increment financing districts. The provisions for deposits and investments and public indebtedness were tested in conjunction with our audit of the City of Duluth, Minnesota, who holds the Authority's cash and investments and issues debt on behalf of the Authority.

In connection with our audit, nothing came to our attention that caused us to believe that the Duluth Entertainment and Convention Center Authority failed to comply with the provisions of the *Minnesota Legal Compliance Audit Guide for Cities*. However, our audit was not directed primarily toward obtaining knowledge of such noncompliance. Accordingly, had we performed additional procedures, other matters may have come to our attention regarding the Authority's noncompliance with the above referenced provisions.



## **Purpose of This Report**

The purpose of this report is solely to describe the scope of our testing of internal control over financial reporting, compliance, and the provisions of the *Minnesota Legal Compliance Audit Guide for Cities* and the results of that testing, and not to provide an opinion on the effectiveness of the Authority's internal control over financial reporting or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Authority's internal control over financial reporting and compliance. Accordingly, this communication is not suitable for any other purpose.

*/s/Rebecca Otto*

REBECCA OTTO  
STATE AUDITOR

*/s/Greg Hierlinger*

GREG HIERLINGER, CPA  
DEPUTY STATE AUDITOR

April 28, 2017