



**CITY AUDITOR** 345 6<sup>th</sup> Street, Suite 100, Bremerton, WA 98337-1873 & Phone (360) 473-5369

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October 17, 2018

To Audit Committee Members:

Leslie Daus, Audit Committee Chair and Council Member  
Deborah McDaniel, Audit Committee Vice-Chair and Citizen Member  
Pat Sullivan, Council Member  
Darryl Riley, Citizen Member  
Dennis Treger, CPA

### **Re: Kitsap Conference Center Review**

Dear Audit Committee Members:

At your request and based on information reviewed to date, following are the results of my Kitsap Conference Center (“KCC”) Review.

The KCC is owned by the City of Bremerton (“City”) and is managed by Columbia Hospitality, Inc. (“CHI”) per the terms of an agreement that [expires December 31, 2019](#). I was asked to summarize certain financial information concerning KCC, compare KCC to other Washington government-owned conference or convention centers, and provide other relevant information to assist City Administration and Council in their decisions regarding the pending expiration of this contract.

My work included the consideration and/or analysis of certain records including:

1. KCC 2018 Business Plan prepared by CHI, dated September 1, 2017;
2. KCC “By the Numbers, Segmentation and Overall Pace”, as of June 1, 2018;
3. KCC year-end Consolidated Income Statements from 2005 through 2017;
4. Unifocus reports summarizing KCC performance metrics from 2015 through July 30, 2018;
5. FinancePlus Revenue and Expenditure Comparison Reports for Fund 105, Parking;
6. FinancePlus Revenue and Expenditure Comparison Reports for Fund 120, Conference Center;
7. Columbia Hospitality website;
8. 2016 condensed statements of revenue and expenses for the following convention centers: Bell Harbor (Seattle), Lynnwood, Kennewick, Ocean Shores, Wenatchee, and Yakima;
9. Lodging tax reports;
10. Management Agreements with CHI to manage the KCC;
11. Other government-owned convention center management agreements; and
12. Miscellaneous research.



Additionally, I discussed the KCC background or operations with the following individuals:

Lori Main, KCC General Manager

DeWayne Pitts, Bremerton Financial Services Director

### **CONFERENCE CENTER INITIAL PURPOSE**

In 1985, the Kitsap Mall opened in Silverdale, Washington, which shifted the retail core of Kitsap County from Bremerton to Silverdale. As a result, retailers including Sears, J.C. Penney, Montgomery Ward, Nordstrom Place Two, Woolworth's, and Rite Aid all closed their downtown Bremerton stores in the '80s and '90s. Downtown Bremerton was left with many large empty storefronts and a waterfront cluttered with parking lots.

Along with the construction of the Norm Dicks Government Center ("NDGC"), construction of the KCC was one of the first key revitalization projects<sup>1</sup> undertaken in downtown Bremerton in an effort to draw people and businesses to the area and restore economic development. Construction of NDGC, KCC, and the adjacent Hampton Inn was completed in 2004. Some other key revitalization projects that followed the construction of the KCC are summarized below:

- 2006: Anthony's restaurant opens
- 2006: Kitsap Credit Union building is complete
- 2007: The Harborside Fountain Park and Puget Sound Naval Museum open
- 2007: Harborside Condominiums are built
- 2008: A newly expanded marina with increased boat capacity is complete
- 2009: A tunnel traversing from the ferry terminal to Highway 304/Burwell opens
- 2010: Fairfield Inn and Suites by Marriott opens on the site of the old City Hall building
- 2011: Manette Bridge replacement opens
- 2016: 606 Apartments are built
- 2016: Voters approve new tax for fast ferry service between Bremerton and Seattle
- 2017: Spyglass Apartments are built
- 2017: Fast ferry service between Bremerton and Seattle begins
- 2018: Marvin Williams Teen & Recreation Center is complete
- 2018: Roxy Theatre is renovated
- 2018: Burwell Pedestrian Tunnel is completed

In addition to the completed projects noted above, there are multiple significant projects currently in various phases of development, including several housing/apartment projects, a planned waterfront hotel with retail, Quincy Square, and more.

The KCC was one of the early projects intended to spur development in Bremerton. Based on the extent of development completed and underway since the construction of the KCC, it seems reasonable to conclude that Bremerton is succeeding in accomplishing its goal of revitalizing downtown. Although the KCC isn't the only project or event that spurred development downtown, many would agree it is one of several projects that served as a catalyst for a renewed Bremerton.

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<sup>1</sup> Preceding the KCC construction was a waterfront multimodal bus/ferry terminal completed in 2000.



## KCC FUNDING

An Interlocal agreement [dated July 28, 2003](#) between Kitsap County (“County”), Kitsap Public Facilities District (“PFD”), and the City stipulates the terms for funding, developing, and operating the KCC. In summary, the funding was as follows:

The City owned the land upon which the KCC was constructed. The County issued bonds to make [\\$6.9 million available to the PFD](#) to be used by the City for construction of the KCC. The PFD pledged to pay sales tax revenue to the County in the amount needed to repay the Bonds. The PFD also contributed excess sales tax revenue of \$75,000.

[The City was responsible for all funding necessary to construct, furnish and operate the KCC, other than the \\$6,975,000 contributed by the PFD.](#) In January 2002, the City Council unanimously approved an [\\$11.7 million revenue bond issue to help pay for the project](#). The City expected parking revenue from the KCC parking garage to cover the cost of the bond.

## CHI BACKGROUND

John Oppenheimer is the founder and CEO of CHI. [According to a February 2015 Seattle Business Magazine article, “When John Oppenheimer boldly put in his 1995 bid to operate the Port of Seattle’s new Bell Harbor International Conference Center, he did so despite never having run a facility before.”](#)

[On June 6, 2003](#), the City and CHI signed an agreement to have CHI manage the KCC. At that time, it appears the only properties CHI was managing were the Port of Seattle’s Bell Harbor International Conference Center, which they have managed since 1995, and (possibly) Friday Harbor House. CHI’s website indicates it now manages or is under contract to manage [40 properties](#)<sup>2</sup>, as summarized below:

- [21 hotels](#)
- [4 conference centers](#)
- [8 golf clubs](#)
- [4 distinctive venues](#)
- [3 residential properties](#)

It should be noted that the Bremerton Cambria Hotel, slated to open in 2020, is one of the hotel properties that CHI is under contract to manage. Please refer to Schedule 1 for additional details of the properties now managed or under contract to be managed by CHI.

[In 2016, CHI was ranked by Puget Sound Business Journals as the 77<sup>th</sup> largest private company in Washington based on 2015 revenue of \\$89.43 million.](#) The report indicates in 2015, CHI employed 717 people in Washington and 1,266 people globally. Since 2015, CHI has doubled the number of properties in its portfolio and was reported [in 2017 to be one of the largest hospitality management companies based in the Northwest.](#)

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<sup>2</sup> 33 of the properties are in Washington; the others are in Arizona, Montana, Idaho, California, and Hawaii.



**BREMERTON CONTRACTS WITH CHI TO OPERATE KCC**

The City did not select CHI through a competitive bid process. Although Sean Flannery of Municipal Research and Services Center (“MRSC”) stated MRSC recommends cities do a Request for Proposals (“RFP”), Washington state law does not require competitive bids for professional services.

The initial contract appointing CHI as manager of KCC was signed by City Mayor Cary Bozeman and Mr. Oppenheimer on June 6, 2003. The initial term was five years expiring May 31, 2008 with an automatic two-year renewal unless either party provided 90-day written notice. Contractor compensation for operating years one through six was \$6,000 per month plus 1.5 percent of gross revenue.

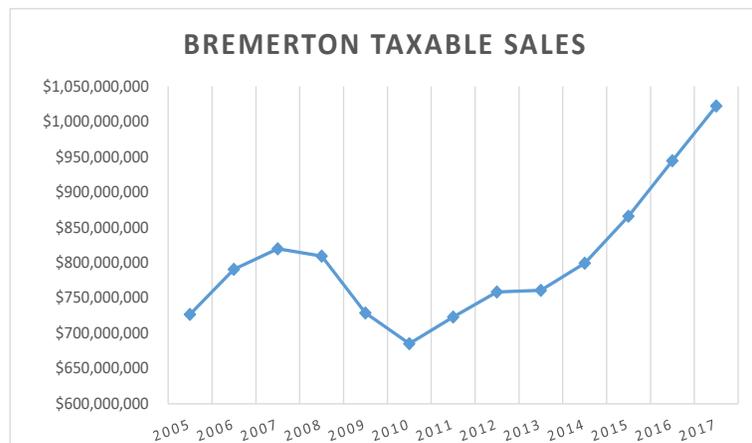
There were three amendments to the original contract. The first two amendments provided some changes regarding insurance and clarification regarding certain other contract terms. The third amendment was entered into on June 15, 2007 and added the Fountain Park Facilities to the list of facilities managed by CHI and included a \$1,000 increase to the monthly fixed fee paid to CHI.

A new agreement was entered on August 11, 2016 with a term from June 1, 2016 through December 31, 2019. This agreement provided that additional renewals, if any, require mutual agreement in writing prior to the expiration of the contract and City Council approval. The 2016 agreement increased CHI’s monthly fixed compensation from \$7,000 to \$7,500. CHI’s variable compensation remained at 1.5 percent of gross revenue. Annual compensation paid to CHI for managing the conference center in 2017 was approximately \$108,000.

**ECONOMY**

A good measure of economic activity is taxable sales, which is maintained in an online database by the Washington State Department of Revenue (“DOR”). The data below summarizes taxable sales in Bremerton from 2005 through 2017. The trend shows taxable sales (i.e. economic activity) in Bremerton declined considerably in 2009 and 2010, then began increasing in 2011, with substantial growth from 2013 through 2017.

Year	Taxable Sales - Bremerton	Change	
		Amount	Percent
2005	\$ 726,937,605		
2006	790,717,478	\$ 63,779,873	8.8%
2007	819,771,680	29,054,202	3.7%
2008	809,372,462	(10,399,218)	-1.3%
2009	728,905,080	(80,467,382)	-9.9%
2010	685,256,563	(43,648,517)	-6.0%
2011	722,985,872	37,729,309	5.5%
2012	758,491,316	35,505,444	4.9%
2013	760,875,930	2,384,614	0.3%
2014	799,436,873	38,560,943	5.1%
2015	865,938,365	66,501,492	8.3%
2016	944,541,704	78,603,339	9.1%
2017	1,022,133,109	77,591,405	8.2%

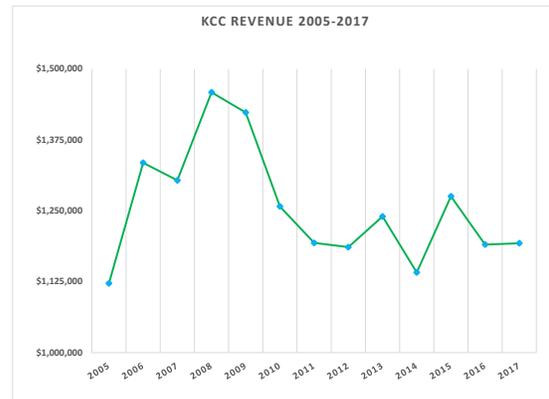




**KCC REVENUE**

The KCC revenue trend from 2005 through 2010 is similar to Bremerton’s economic activity/taxable sales trend during the same period as shown right: a period of growth followed by the recession in 2009/2010.

After 2010, the KCC revenue trend is relatively flat compared to Bremerton’s growing economy.



2005 was KCC’s first full year of operations. [Annual revenue from 2005 through 2017 averaged \\$1,255,290. Revenue was highest from 2006 through 2009 when it averaged close to \\$1.4 million. Since 2010, revenue has remained fairly consistent at about \\$1.2 million per year.](#)

CHI’s 2018 business plan for KCC identifies five primary market segments that it serves. [The table below shows the market segment and the percent of KCC’s revenue derived from that segment.](#) Assuming annual revenue of \$1.2 million, the column on the right estimates the amount of KCC revenue by market segment:

Market Segment	Percent of Business	Estimated Revenue
Association/Nonprofit Organization Meetings	34.58%	\$ 415,000
Corporate	29.71%	357,000
Weddings/Receptions	18.22%	219,000
Government	10.72%	129,000
Social events	6.77%	81,000
<b>Total</b>	<b>100.00%</b>	<b>\$ 1,201,000</b>

Prior to 2014, CHI stated stagnant revenue was largely due to lack of breakout rooms. Hence, [in October 2013](#), the City signed an agreement with Kitsap Transit to lease space for breakout rooms on the third floor of the Kitsap Transit Building that is adjacent to the KCC. It appears breakout room construction was completed early 2014. Although the [breakout rooms were available during most of 2014](#), revenue did not change significantly in 2014 or after.

In June 2015, sixteen months after the third floor was completed, the Clearwater Casino Resort (“CCR”) opened a new meeting and convention space and added 98 hotel rooms to its existing facility in Suquamish. The CCR and KCC reportedly compete for business on the Kitsap Peninsula. KCC annual revenue remained fairly unchanged following the 2015 opening of the CCR event space.

According to Ms. Main, KCC recently lost some significant business: two clients became too large to have certain events at KCC and moved these events to larger venues; and one client was sold to an entity that did not sponsor certain events previously hosted by its predecessor.



Ms. Main stated the KCC continues to lose business due to lack of hotel accommodations. The local hotels seek the best rate available and sometimes the event planners have a lower per diem than the hotel is willing to accept. As previously mentioned, another hotel (Hotel Cambria) is expected to open adjacent to the KCC in 2020 and CHI is under contract to manage it.

**KCC BOOKINGS**

When KCC obtains a signed contract for an event, the estimated revenue from the event is recorded as a booking. Tracking bookings is useful for managing business and forecasting. Bookings at the KCC increased 23 percent as of June 1, 2018 compared to June 1, 2017. Bookings at KCC can be for events scheduled out 18 months to two years. [The following booking amounts](#) include actual revenue through May of the corresponding year, plus bookings for future events.

Description	2015	2016	2017	2018
Bookings at June 1:				
Association	\$ 405,436	\$ 410,307	\$ 323,528	\$ 416,150
Corporate	310,557	182,298	224,512	227,064
Social (non-wedding)	78,507	103,176	56,868	81,263
Government	67,871	96,649	93,996	79,000
Wedding	97,774	121,733	163,630	258,715
<b>Total</b>	<b>\$ 960,145</b>	<b>\$ 914,163</b>	<b>\$ 862,534</b>	<b>\$ 1,062,192</b>
<b>Growth</b>		<b>-4.8%</b>	<b>-5.6%</b>	<b>23.1%</b>

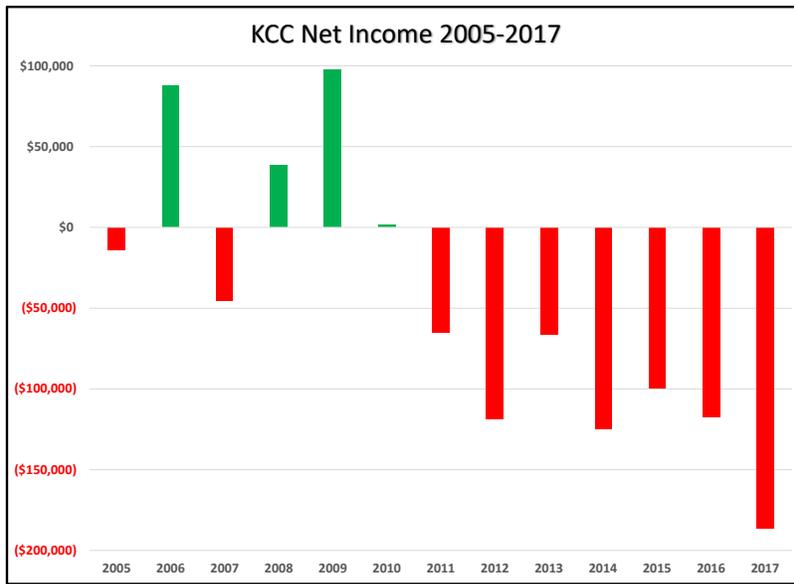
Ms. Main believes the booking increase is due to increased business rather than a difference in the methodology used to estimate bookings compared to her predecessor.<sup>3</sup>

**KCC EXPENSES AND PROFITABILITY**

CHI provides the City with monthly profit and loss statements that summarize the month and year to date activity. These profit and loss statements do not include certain expenses that are paid directly by the City, such as debt service, third floor expenses paid to Kitsap Transit, insurance, water/sewer/stormwater, grounds and maintenance costs, and other miscellaneous charges. The following comments are based on the profit and loss statements provided by CHI.

During the 13-year period from 2005 through 2017, KCC lost \$611,815, which is an average of \$47,063 lost per year. KCC had four profitable years in 2006 and 2008 through 2010 during which time it reported profits totaling \$225,245. From 2011 through 2017, KCC reported seven consecutive years of losses totaling \$777,821, an annual average of \$111,117. The chart below depicts annual net income/loss from 2005 through 2017:

<sup>3</sup> Ms. Main replaced Arne Bakker as KCC general manager in August 2017.



The table below summarizes KCC’s revenue, expenses, CHI compensation, and net income<sup>4</sup>:

Year	Revenue	Operating Expenses	Subtotal	Base Mgmt Fee	Incentive Fee	Net Income
2005	\$ 1,122,133	\$ 1,047,349	\$ 74,784	\$ 72,000	\$ 16,832	\$ (14,048)
2006	1,334,546	1,154,939	179,607	72,000	20,018	87,589
2007	1,303,549	1,252,187	51,362	77,000	19,553	(45,191)
2008	1,458,725	1,314,509	144,216	84,000	21,861	38,355
2009	1,423,126	1,220,239	202,887	84,000	21,386	97,501
2010	1,257,593	1,152,929	104,664	84,000	18,864	1,800
2011	1,193,309	1,156,585	36,724	84,000	17,901	(65,177)
2012	1,185,923	1,202,731	(16,808)	84,000	17,781	(118,589)
2013	1,239,957	1,203,448	36,509	84,000	18,565	(66,056)
2014	1,141,244	1,165,290	(24,046)	84,000	16,710	(124,756)
2015	1,275,488	1,281,325	(5,837)	74,000	19,417	(99,254)
2016	1,190,423	1,207,570	(17,147)	82,500	17,854	(117,501)
2017	1,192,755	1,271,352	(78,597)	90,000	17,891	(186,488)
<b>Total</b>	<b>\$ 16,318,771</b>	<b>\$ 15,630,453</b>	<b>\$ 688,318</b>	<b>\$ 1,055,500</b>	<b>\$ 244,633</b>	<b>\$(611,815)</b>

Ms. Main stated minimum wage increases have impacted KCC’s profitability. [In 2005, minimum wage was \\$7.35 per hour. In 2018, Washington State has the second highest minimum wage in the United States at \\$11.50 per hour, yielding a 4.34 percent annual average minimum wage increase from 2005 to 2018. In comparison, the Seattle-Tacoma-Bremerton Consumer Price Index \(CPI-U\) from 2005 to 2017<sup>5</sup> averaged 2.6 percent growth. However, the Washington hourly minimum wage rate did not experience a significant increase until 2017, when it increased 16.16 percent compared to 2016.](#) Thus, it seems the lack of profits attributable to Washington’s minimum wage increases may be primarily applicable to 2017 and 2018.<sup>6</sup>

<sup>4</sup> Amounts exclude expenses paid directly by the City, including debt service, third floor expenses paid to Kitsap Transit, insurance, water/sewer/stormwater, grounds and maintenance costs, and other miscellaneous charges.

<sup>5</sup> 2018 CPI data is not yet available. The average minimum wage increase in Washington from 2005 to 2017 is 4.14 percent.

<sup>6</sup> 2018 budget is for a loss of \$137,000.



Although all Washington employers are faced with the minimum wage increases, Ms. Main stated it is a challenge to set menu prices that are both competitive and cover minimum wage increases.<sup>7</sup> Another challenge Ms. Main cited in terms of competitive pricing is that some of KCC's competition have other revenue sources, such as gambling and/or lodging, which enable them to offer more competitive event pricing. Ms. Main stated the KCC also loses some business due to insufficient lodging accommodations, which should be alleviated in 2020 with the expected opening of the adjacent Cambria Hotel that CHI is under contract to manage.

### INCREASE REVENUE AND MANAGE DIRECT COSTS

[The table below is sorted by net income \(highest to lowest\) as a percent of revenue.](#) The top portion of the chart shows the profitable years and the lower portion shows the loss years. Notably, annual average revenue in the profitable years is about \$164,000 greater than the loss years. Also worth noting is annual average direct costs, which are primarily direct labor costs, are about six percent less in the profitable years compared to the loss years. While the conversation for generating more profits at the KCC frequently focuses on increasing revenue, it appears a more in-depth review of direct costs may also be warranted.

Description	Revenue	Cost of Sales (food, bev, etc)	Direct Expenses (direct payroll, etc)	General & Admin Expenses	Net Income (Loss)
Profitable years:					
2009	\$ 1,423,126	16.28%	33.78%	\$613,217	6.85%
2006	\$ 1,334,546	19.52%	37.41%	\$487,301	6.56%
2008	\$ 1,458,725	16.88%	39.31%	\$600,649	2.63%
2010	\$ 1,257,593	18.52%	37.09%	\$556,520	0.14%
<b>Average</b>	<b>\$ 1,368,497</b>	<b>17.80%</b>	<b>36.90%</b>	<b>\$564,422</b>	<b>4.05%</b>
Loss years:					
2005	\$ 1,122,133	19.71%	42.67%	\$436,243	-1.25%
2007	\$ 1,303,549	21.72%	40.11%	\$542,760	-3.47%
2013	\$ 1,239,957	19.07%	41.82%	\$551,013	-5.33%
2011	\$ 1,193,309	19.22%	39.70%	\$555,417	-5.46%
2015	\$ 1,275,488	16.69%	43.69%	\$604,636	-7.78%
2016	\$ 1,190,423	16.11%	43.68%	\$596,164	-9.87%
2012	\$ 1,185,923	20.11%	44.02%	\$543,908	-10.00%
2014	\$ 1,141,244	17.69%	45.55%	\$544,297	-10.93%
2017	\$ 1,192,755	15.96%	42.39%	\$683,228	-15.64%
<b>Average</b>	<b>\$ 1,204,976</b>	<b>18.48%</b>	<b>42.63%</b>	<b>\$561,963</b>	<b>-7.75%</b>
<b>Average difference</b>	<b>\$ (163,522)</b>	<b>0.68%</b>	<b>5.73%</b>	<b>-\$2,459</b>	<b>-11.79%</b>

### OTHER REVENUE AND EXPENSE

In addition to operating revenue and expense reported by CHI, the City accounts for parking revenue and other City-paid expenses associated with the KCC. In its funding discussions, the City expressed its expectation that parking revenue from the KCC parking garage (aka Harborside Garage, which is also the name of the parking garage at Burwell and Washington)

<sup>7</sup> To help control rising labor costs, on March 1, 2018 CHI reduced the portion of the 20 percent service charge paid to the servers from 60 to 50 percent.



would cover the cost of the bond. The KCC parking revenue (parking fees and estimated ticket revenue<sup>8</sup>) averaged \$600,000 annually from 2015 through 2017.

Mr. Coyne stated approximately 10 percent of parking patrollers' time and 25 percent of the meter technician's time is spent in the KCC parking garage. Assuming 17.5 percent<sup>9</sup> of total parking expenses is a reasonable estimate of parking expenses associated with the KCC garage, [KCC annual average parking garage net income from 2015 through 2017 would be approximately \\$450,000. The average interest payment on debt service from 2015 through 2017 was \\$277,000](#), leaving approximately \$173,000 per year on average to cover City-paid expenses, such as third floor expenses paid to Kitsap Transit, insurance, water/sewer/stormwater, grounds and maintenance costs, and other miscellaneous charges.

[City-paid expenses related to KCC from 2015 through 2017 averaged \\$141,000](#). Thus, during this time frame, the KCC parking garage revenue was more than sufficient to cover estimated KCC parking expenses, the interest portion of KCC debt service, and City-paid expenses associated with KCC operations.<sup>10</sup>

Importantly, the KCC has two new expenses beginning in 2018: repayment of the funds used for the third floor improvements (approximately \$95,000 per year) and rent for the third floor ([just over \\$100,000 per year.](#)) When the City moved forward with the 2013/2014 third floor expansion, it was estimated that the expansion would result in \$500,000 in increased annual revenue for the facility starting upon completion, which would generate sufficient profit to pay the third floor expansion loan and rent. However, revenue remained flat and the KCC continues to have annual losses. The City is currently seeking other ways to pay these additional expenses, such as additional lodging tax funds and revised lease terms.

### **KCC PERFORMANCE**

Following each KCC event, a survey is sent to the meeting planner inquiring as to their perception of the quality of service, facilities, value, food and beverage. [Below is a summary of KCC's ratings based on these surveys from 2015 through July 30, 2018:](#)

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<sup>8</sup> Matthew Coyne, Impark manager, estimated ten percent of the City's parking ticket revenue comes from the KCC parking garage

<sup>9</sup> Average of 10 and 25 percent.

<sup>10</sup> Based on the cited estimates, KCC parking revenue less parking expenses, less debt service interest, less City-paid expenses totaled \$42,000 from 2015 through 2017.



Service	Rating			
	2015	2016	2017	As of 7/30/2018
Surveys processed	94	73	88	44
Overall	96.7	98.2	98.3	94.8
Food and beverage	99.2	97.6	97.0	89.0
Value for the price	91.4	92.0	94.6	88.8
Catering/event manager	93.1	98.7	NA	NA
Food quality	93.3	96.3	97.1	95.5
Banquet facilities	100.0	97.8	98.0	95.8
Meeting facilities	96.3	98.2	98.2	94.9
Audio visual	92.6	96.7	95.1	93.7
Sales manager	96.8	97.4	98.6	93.7
Billing	96.5	98.4	97.2	96.8
Event planning manager	96.3	99.2	98.7	92.6
Meal and break service	95.7	97.8	97.6	98.0
Banquet team	95.6	99.2	98.5	96.0
Banquet manager/captain	96.9	NA	NA	NA
Average per report	95.6	97.7	97.7	94.4

Although there is a slight decline in customer ratings for the above metrics during the first half of 2018 compared to the prior three years, KCC was consistently rated in the mid to upper 90s by its customers from 2015 through July 2018.

**OTHER WASHINGTON CITY/PFD-OWNED CONVENTION/CONFERENCE CENTERS<sup>11</sup>**

A number of Washington cities own a convention or conference center. Mr. Pitts and Mike Riley<sup>12</sup> stated it would be helpful to include information in this report regarding who manages the convention centers, fees paid to the management companies, and the profitability of the other convention centers. In addition, I reviewed subsidies provided to these other convention/conference centers. Other event centers considered in the review are the Three Rivers Convention Center (owned by the Kennewick PFD), Lynnwood Convention Center (owned by the Lynnwood PFD), Ocean Shores Convention Center, Bell Harbor International Conference Center (owned by Port of Seattle), Wenatchee Convention Center, and the Yakima Convention Center.

**Management Companies and Compensation**

The following chart shows the name of the management companies at each of the aforementioned facilities, the 2016 management compensation structure, and 2016 management fees paid:

<sup>11</sup> KCC revenue and expenses shown in this report section are based on the City's income statements and include city expenses not reported on the CHI-provided income statements.

<sup>12</sup> Bremerton Assistant Finance Director.



City	Management Company	Annual Base Fee	Variable Fee		2016 Revenue	2016 Total Mgmt. Fees	Fees as % Revenue
			Amount	Comment			
Bremerton	Columbia Hospitality	\$82,500	1.5% gross revenue		\$1,191,102	\$100,354	8.4%
Kennewick (PFD)	VenuWorks	\$93,000	Lesser of 1) annual base fee and 2) 15% of naming rights, display advertising fee, and sponsorship revenue, and 8% F&B revenue.		\$2,273,630	\$197,779	8.7%
Lynnwood (PFD)	SMG	\$120,000	40% Based on various performance measures; 60% based on profit improvement year to year	\$120,000 max	\$4,635,710	\$240,000	5.2%
Ocean Shores	City	\$0		\$0	\$158,043	\$0	0.0%
Seattle/Bell Harbor	Columbia Hospitality	3.5% Gross revenue	Normally, 15% Net income if net income >15% gross revenue, otherwise \$0. Temporary Minimum Assured Fee.		\$6,241,442	\$537,082	8.6%
Wenatchee	NorthCoast Washington, aka Coast Hotels	\$0	8% Gross revenue >\$750,000 paid by contractor to City	Contractor pays City	\$79,477	NA	NA
Yakima	Yakima Valley Visitors and Convention Bureau	\$395,000	None		\$764,451	\$395,000	51.7%

The following points are worth noting:

- The Ocean Shores Convention Center is fully operated by city employees so there are no management company fees.
- At the Port of Seattle’s Bell Harbor International Conference Center, CHI is temporarily receiving a Minimum Assured Fee (from 2016 through 2018) in lieu of its Incentive Management Fee to mitigate any shortfall they may experience during the redevelopment of the cruise terminal where the conference center is located. In 2016, this additional fee was \$318,660. From 2013 through 2015, CHI’s Incentive Management Fee (variable fee) averaged \$208,952.
- The fees paid at the Yakima Convention Center include \$186,000 management fee, \$184,000 professional services fee that includes sales salaries, and \$25,000 consultant fee. Because some salaries are included in at least one of the fees, this fee structure may not be comparable to other fee structures in this analysis. For example, sales salaries at KCC are reported as expenses on the profit and loss statement.
- The basis for variable fees at the different locations includes percent of revenue or net income, percent of revenue over a certain threshold, and performance measures and improvements.

**Profitability**

Of the seven event centers reviewed, the Port of Seattle’s Bell Harbor International Conference Center is the only one with profitable operations. [The chart below](#) summarizes 2016 revenue and expense from each facility, excluding subsidies such as lodging, sales, and real estate excise tax:



Convention Center Location	Convention Center		Revenue
	Revenue	Expense	Less Expense
Bremerton	\$ 1,191,102	\$ 1,473,947	\$ (282,845)
Kennewick	2,273,630	3,541,101	(1,267,471)
Lynnwood	4,635,710	5,658,854	(1,023,144)
Ocean Shores	158,043	785,956	(627,913)
Seattle Bell Harbor	6,241,442	6,069,904	171,538
Wenatchee	79,477	941,020	(861,543)
Yakima	764,451	1,641,685	(877,234)

Notably, during the three years (2013 through 2015) prior to Seattle’s cruise terminal redevelopment that began in 2016, Bell Harbor’s annual net income averaged \$1.2 million. Also worth noting is that beginning in 2015, Wenatchee entered a new concession agreement that allows the management company, Coast Hotels, to manage and market the convention center as they see fit and return a percentage of revenue back to the city for debt service and long term upkeep. Accordingly, the amounts shown above only include the City of Wenatchee’s portion of revenue and expense.

Please also note the amounts shown above for KCC exclude parking revenue and expense, and debt service. Bell Harbor also excludes debt service. The remaining properties appear to have interest or debt service reported in the amounts shown above.

**Lodging Taxes and Other Event Center Subsidy**

The lodging tax is a consumer tax on lodging charges for periods of less than 30 consecutive days for hotels, motels, rooming houses, private campgrounds, RV parks, and similar facilities. The guiding principle for the use of lodging taxes is that they be used for activities, operations and expenditures designed to increase tourism. Specifically, lodging taxes can be used for:

- Tourism marketing;
- Marketing and operations of special events and festivals designed to attract tourists;
- Operations and capital expenditures of tourism-related facilities owned or operated by a municipality or a public facilities district; or
- Operations of tourism-related facilities owned or operated by nonprofit organizations (RCW 67.28.1816).

In addition to lodging taxes, some city-owned event centers receive subsidies from other taxes (sales) and the general fund. [The following table](#) shows how much lodging tax and other subsidy was provided to each event center in 2016:



Convention Center Location	Convention Center Subsidy		
	Lodging Tax	Other	Total
Bremerton	\$ 155,000	\$ 36,129	\$ 191,129
Kennewick	-	1,790,020	1,790,020
Lynnwood	1,160,061	1,696,558	2,856,619
Ocean Shores	595,479	30,000	625,479
Seattle Bell Harbor	-	-	-
Wenatchee	1,145,514	-	1,145,514
Yakima	705,578	100,000	805,578
<b>Total</b>	<b>\$ 3,761,632</b>	<b>\$ 3,652,707</b>	<b>\$ 7,414,339</b>

Research indicates it was originally expected that the Bell Harbor International Conference Center would need to be subsidized; however, Bell Harbor has been profitable and has not needed to be subsidized. As shown above, of the remaining event centers, KCC receives significantly less subsidy than the others. Notably, some conference centers pledged lodging taxes to fund the conference center; Bremerton uses KCC parking garage revenue to cover its debt service. A more complete analysis of conference center funding and subsidies can be performed at your request.

The table below shows the 2016 subsidies in light of 2016 revenue and expense. As shown, KCC's subsidy as a percent of revenue is substantially less than most other event centers:<sup>13</sup>

Convention Center Location	Convention Center		Revenue Less Expense	Conv. Ctr. Subsidy	Total	Subsidy % Of Revenue	Expense Includes
	Revenue	Expense					
Bremerton	\$ 1,191,102	\$ 1,473,947	\$ (282,845)	\$ 191,129	\$ (91,716)	16.0%	3% capital reserve
Kennewick	2,273,630	3,541,101	(1,267,471)	1,790,020	522,549	78.7%	Cap imp, deprec, debt service
Lynnwood	4,635,710	5,658,854	(1,023,144)	2,856,619	1,833,475	61.6%	Deprec, interest
Ocean Shores	158,043	785,956	(627,913)	625,479	(2,434)	395.8%	Interfund loan expense (\$51K).
Seattle Bell Harbor	6,241,442	6,069,904	171,538	-	171,538	0.0%	3% capital reserve
Wenatchee	79,477	941,020	(861,543)	1,145,514	283,971	1441.3%	Capital outlay and debt service
Yakima	764,451	1,641,685	(877,234)	805,578	(71,656)	105.4%	Underlying expense data unavailable

In 2017, the City was awarded \$345,000 by the Lodging Tax Advisory Committee ("LTAC") for 2018, which includes \$250,000 for operations (versus the prior years \$155,000), plus a one-time award of \$95,000 for debt service related to the Third Floor expansion.<sup>14</sup> In 2018, Mr. Pitts requested \$200,000 for debt service (in addition to the \$250,000 multi year award for operations). The LTAC recommended awarding \$75,000 of the additional \$200,000 requested. City Council rejected LTAC's recommendations and asked the LTAC to reconsider half of the 16 recommended allocations. LTAC met on September 6, 2018 and increased the KCC award recommendation to \$100,000, which City Council approved on October 3, 2018.

<sup>13</sup> Amounts shown for Bremerton do not include City-paid operating expenses, debt service, or the parking revenue used to pay KCC debt service.

<sup>14</sup> The \$95,000 increase from \$155,000 to \$250,000 is a multi-year award for five years. The \$95,000 for debt service was awarded for 2018 only.



### LEASE NAMING RIGHTS

During an Audit Committee meeting, Darryl Riley, a citizen member of the committee, suggested the City consider leasing the naming rights to the KCC. It is not uncommon for a sports facility or convention center to lease naming rights. Noted local examples of sport facilities include CenturyLink Field, home of the Seahawks, and Safeco Field, home of the Mariners. In 2005, the University of Washington sold naming rights of its stadium to Alaska Airlines for \$41 million over a ten year period – the stadium is officially called Alaska Airlines Field at Husky Stadium.

In Omaha, Nebraska, CHI Health, part of Catholic Health Initiatives, bought the naming rights to the Omaha arena and convention center for \$23.6 million over a 20 year period.<sup>15</sup> An August 28, 2018 Kitsap Sun article indicated the Central Kitsap School District sold the naming rights for its new stadium and athletic complex to Kitsap Credit Union for \$500,000.

The Interlocal Agreement regarding Funding, Development, and Operation of the Kitsap Regional Conference Center - Section 13E states, “The Conference Center shall be named the Kitsap Regional Conference Center unless otherwise agreed by the PFD.” Thus, any name change would require agreement by the PFD.

### OTHER CONFERENCE CENTER BENEFITS

Research indicates conference centers generally create additional measures of economic impact resulting from visitor spending (direct economic impact), plus tax revenues and jobs created (indirect economic impact). Visitor spending includes lodging, transportation, registration fees, food, shopping, recreation, entertainment, etc.

[In March 2018, a consulting firm prepared an Economic Impact Estimate for the Lynnwood Convention Center.](#) The study estimated the convention center visitors spent (direct economic impact) approximately 3.7 times the amount of revenue generated from the convention center operations. [The study estimated there was an additional 2.7 times revenue related to indirect economic impact.](#) In total, the study estimated the economic impact was approximately 6.4 times the convention center revenue. The economic multiplier is significantly impacted by the percentage of event attendees who travel from out of town and stay in hotels, a metric that is not tracked by the KCC.

Ms. Main stated that in her experience the economic multiplier is generally from 1.75 to 3.0 times conference center revenue. The higher end of the range is typically for multiple day events. Ms. Main stated she conservatively estimates the total economic multiplier for the KCC at 1.75. Based on KCC’s historical annual revenue average of \$1.2 million and assuming Ms. Main’s estimate is reasonable,<sup>16</sup> the economic impact from the KCC could be an estimated \$2 million per year.

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<sup>15</sup> In addition to the naming rights, CHI Health will get to use the convention center for company events twice a year and one “VIP reception” for as many as 30 employees or business associations, as well as a couple other perks. A CHI representative stated they would like to use the arena and convention center for health screenings, health education events and as a blessing for staff.

<sup>16</sup> Assessing the reasonableness of Ms. Main’s estimate is beyond the scope of this report.



## CONCLUSION

The KCC operation has an established record of being unprofitable unless parking income is allocated to the KCC Fund. In my experience, historical results are generally a good basis for projecting future earnings unless a significant change alters the course. It is possible that Ms. Main's leadership or the new Cambria Hotel will be the change that makes the KCC profitable. Whether the KCC is profitable or not, it is a beautiful event facility that has attracted developers and others (approximately 31,500 guests per year) to Bremerton.

With the December 31, 2019 CHI contract expiration approaching, Mayor Wheeler and Mr. Pitts expressed an interest in issuing an RFP for KCC management services. Utilizing an RFP gives the City an opportunity to evaluate the qualifications of different vendors, helps ensure services are provided at a competitive rate, and gives the City a better opportunity to see what other contract terms could be available to the City. It also give other vendors a chance to compete for the City's business.

Irrespective of which company manages the KCC, if the management compensation includes an incentive component, the City could consider aligning the incentive fee to a desired metric, such as net income, achieving budgets, and/or performance rather than the current revenue metric.

The City may also want consider a more in-depth review of KCC's direct and/or labor expenses.

Please contact me if you have questions or need additional information.

Sincerely,

Jennifer L. Sims CPA/CFF, CFE  
City Auditor

cc: Mayor Wheeler  
City Council  
DeWayne Pitts, Finance Director  
Mike Riley, Assistant Finance Director  
Lori Main, KCC General Manager