

**Washington State Auditor's Office**  
**Financial Statements Audit Report**

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**Cultural Development Authority of  
King County  
(4Culture)**

Audit Period  
January 1, 2007 through December 31, 2007

Report No. 75428

Issue Date  
**October 13, 2008**



WASHINGTON  
**BRIAN SONNTAG**  
STATE AUDITOR



**Washington State Auditor  
Brian Sonntag**

October 13, 2008

Board of Directors  
4Culture  
Seattle, Washington

***Report on Financial Statements***

Please find attached our report on 4Culture's financial statements.

We are issuing this report in order to provide information on the Authority's financial condition.

In addition to this work, we look at other areas of our audit client's operations for compliance with state laws and regulations. The results of that audit will be included in a separately issued accountability report.

Sincerely,

**BRIAN SONNTAG, CGFM**  
STATE AUDITOR

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King County  
January 1, 2007 through December 31, 2007**

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# Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters in Accordance with *Government Auditing Standards*

## 4Culture King County January 1, 2007 through December 31, 2007

Board of Directors  
4Culture  
Seattle, Washington

We have audited the financial statements of the governmental activities and each major fund of 4Culture, a component unit of King County, Washington, as of and for the year ended December 31, 2007, which collectively comprise the Authority's basic financial statements and have issued our report thereon dated September 22, 2008.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to the financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

### ***INTERNAL CONTROL OVER FINANCIAL REPORTING***

In planning and performing our audit, we considered the Authority's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions 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 control deficiency 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 misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the Authority's ability to initiate, authorize, record, process or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the Authority's financial statements that is more than inconsequential will not be prevented or detected by the Authority's internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control.

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

## **COMPLIANCE AND OTHER MATTERS**

As part of obtaining reasonable assurance about whether the Authority's financial statements are free of material misstatement, we performed tests of the Authority's 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*.

This report is intended for the information and use of management and the Board of Directors. However, this report is a matter of public record and its distribution is not limited. It also serves to disseminate information to the public as a reporting tool to help citizens assess government operations.

A handwritten signature in black ink, appearing to read "Brian Sonntag". The signature is fluid and cursive, with the first name "Brian" and last name "Sonntag" clearly distinguishable.

**BRIAN SONNTAG, CGFM**  
STATE AUDITOR

September 22, 2008

# Independent Auditor's Report on Financial Statements

## **4Culture King County January 1, 2007 through December 31, 2007**

Board of Directors  
4Culture  
Seattle, Washington

We have audited the accompanying financial statements of the governmental activities and each major fund of 4Culture, a component unit of King County, Washington, as of and for the year ended December 31, 2007, which collectively comprise the Authority's basic financial statements as listed on page 5. These financial statements are the responsibility of the Authority's management. Our responsibility is to express opinions 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 of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities and each major fund of 4Culture, as of December 31, 2007, and the respective changes in financial position and the respective budgetary comparison for the General Fund, Lodging Tax Special Revenue Fund and 1% for Art Special Revenue Funds for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report on our consideration of the 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* and should be considered in assessing the results of our audit.

The management's discussion and analysis on pages 6 through 9 is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of

management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

A handwritten signature in black ink, appearing to read "Brian Sonntag". The signature is fluid and cursive, with the first name "Brian" and last name "Sonntag" clearly distinguishable.

**BRIAN SONNTAG, CGFM**  
STATE AUDITOR

September 22, 2008

# Financial Section

## **4Culture King County January 1, 2007 through December 31, 2007**

### ***REQUIRED SUPPLEMENTAL INFORMATION***

Management's Discussion and Analysis – 2007

### ***BASIC FINANCIAL STATEMENTS***

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Statement of Activities – 2007

Balance Sheet – Governmental Funds – 2007

Statement of Revenues, Expenditures and Changes in Fund Balances – Governmental Funds –  
2007

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**CULTURAL DEVELOPMENT AUTHORITY OF KING COUNTY**  
**dba 4CULTURE**  
**Management's Discussion and Analysis**  
**For the Year Ended December 31, 2007**

**MANAGEMENT DISCUSSION AND ANALYSIS**



This discussion and analysis of the financial performance of 4Culture, the Cultural Development Authority of King County (the CDA), presents a narrative overview and analysis of the financial activities of the CDA for the year ended December 31, 2007. This information should be considered in conjunction with the CDA's financial statements and notes to the financial statements, which follow.

**FINANCIAL HIGHLIGHTS – 2007**

As of December 31, 2007, the CDA's total net assets were \$29.1 million, including \$13.7 million of restricted net assets expendable for programs, \$19.1 million of nonexpendable net assets restricted for a permanent endowment, and a \$3.7 million deficit in unrestricted net assets. As of December 31, 2007, the CDA's total fund balances were \$38.0 million, including \$25.1 million reserved for encumbrances and a permanent endowment.

Total net assets of the CDA increased by \$7.4 million for the year ended December 31, 2007. This increase was composed of \$16.5 million of total revenues, \$8.9 million of total expenses, and \$0.2 million of net asset transfers to King County. Total fund balances of the CDA increased by \$8.2 million for the year ended December 31, 2007. This increase was composed of \$17.6 million of total fund revenues, \$8.8 million of total fund expenditures, and \$0.6 million of net fund transfers to King County.

**OVERVIEW OF THE FINANCIAL STATEMENTS**

This discussion and analysis is intended to serve as an introduction to the CDA's basic financial statements, which include three components: (1) government-wide financial statements; (2) fund financial statements; and (3) notes to the financial statements.

Government-wide financial statements

The government-wide financial statements are designed to provide readers with a broad overview of the CDA's finances in a manner similar to a private sector business. The statement of net assets provides information about the CDA's financial position, including assets, liabilities and net assets, which assists in assessing the CDA's financial position at the end of the year. The statement of activities presents information on how the CDA's net assets changed during the fiscal year. Over time, increase or decreases in the CDA's net assets may serve as a useful indicator of whether the financial position of the CDA is improving or deteriorating.

The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. This basis of accounting is similar to that used by most businesses, taking into account revenues and expenses connected with the current fiscal year, regardless of the timing of cash receipts and payments.

The CDA's activities in 2007 are all classified as governmental activities, which are principally supported by intergovernmental revenues. The CDA reported no business-type activities in 2007, which are intended to recover all or a significant portion of their costs through user fees and charges to external users of services.

Fund Financial Statements

The CDA, like other public authorities and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. All CDA funds used in 2007 are categorized as major governmental funds. Governmental fund financial statements are reported using

the current financial resources measurement focus and the modified accrual basis of accounting. The statements focus on how cash and other financial assets can be readily converted to financial resources and the balances left at year-end that are available for use. Such information can be useful in determining whether there will be adequate financial resources to meet the current needs of the CDA. The CDA presents a combining balance sheet and combining statement of revenues, expenditures, and changes in fund balances for its funds. Each of these statements provides a reconciliation to the government-wide financial statements.

Notes to the Financial Statements

The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements.

**GOVERNMENT-WIDE FINANCIAL ANALYSIS**

Analysis of Net Assets

At December 31, 2007, total net assets of the CDA were \$29,092,309, an increase of 34% over net assets at the end of 2006. Net assets included \$13,663,946 of restricted net assets expendable for programs; \$19,105,147 of nonexpendable net assets restricted for a permanent endowment; and a \$3,676,784 deficit in unrestricted net assets.

	Net Assets as of December 31,	
	<u>2007</u>	<u>2006</u>
<b>Assets:</b>		
Cash and cash equivalents	\$13,590,738	\$12,957,239
Investments	23,506,179	15,730,559
Other assets	<u>2,051,634</u>	<u>2,053,672</u>
Total assets	<u>39,148,551</u>	<u>30,741,470</u>
<b>Liabilities:</b>		
Current liabilities	6,379,458	5,018,967
Noncurrent liabilities	<u>3,676,784</u>	<u>4,052,326</u>
Total liabilities	<u>10,056,242</u>	<u>9,071,293</u>
<b>Net Assets:</b>		
Invested in capital assets, net of related debt	-	-
Restricted		
Expendable	13,663,946	10,817,133
Nonexpendable	19,105,147	14,905,370
Unrestricted	<u>(3,676,784)</u>	<u>(4,052,326)</u>
Total net assets	<u>\$29,092,309</u>	<u>\$21,670,177</u>

Other assets primarily include a receivable from King County for lodging tax revenues. Current liabilities include \$5.8 million of unearned revenues related to the One Percent for Art program. Noncurrent liabilities represent required future transfers to King County for the principal portion of County debt service on County bonds issued for cultural purposes before December 31, 2002.

Changes in restricted expendable net assets are the result of timing differences between the recognition of individual programs' revenues and their related expenditures. Nonexpendable net assets will increase each year due to required transfers of 40% of annual lodging tax revenues to the endowment fund. The deficit in unrestricted net assets, which corresponds to noncurrent liabilities for required future transfers to King County for County debt service, is the result of the CDA having long-term commitments that are greater than currently available resources. The deficit in unrestricted net assets will decrease each year as the CDA makes required future transfers to King County for County debt service on County bonds issued for cultural purposes before December 31, 2002.

### Analysis of Changes in Net Assets

The CDA's total net assets increased \$7,422,132, or 34%, during 2007. The following information reflects how the CDA's net assets changed during the fiscal year.

	<u>2007</u>	<u>2006</u>
Revenues:		
Lodging tax revenues	\$10,499,444	\$ 8,783,039
Program support from King County	3,258,528	2,719,940
Other program revenues	441,588	285,425
Investment Earnings	<u>2,295,877</u>	<u>985,585</u>
Total revenues	<u>16,495,437</u>	<u>12,773,989</u>
Expenses:		
Arts and cultural support	6,592,355	3,981,304
Public art projects	1,760,347	1,523,399
Management and general supporting activities	<u>531,219</u>	<u>377,227</u>
Total expenses	<u>8,883,921</u>	<u>5,881,930</u>
Increase in net assets before transfers	<u>7,611,516</u>	<u>6,892,059</u>
Transfers:		
Transfers to King County for County debt interest	<u>(189,384)</u>	<u>(210,284)</u>
Total transfers	<u>(189,384)</u>	<u>(210,284)</u>
Total increase in net assets	<u>\$ 7,422,132</u>	<u>\$ 6,681,775</u>

Program support from King County includes revenues for the One Percent for Art program, revenues for grants to be managed by the CDA and awarded by King County to other organizations, and special appropriations for arts and cultural programs managed by the CDA.

Arts and cultural support expense amounts and allocations are incurred in accordance with requirements specified in the King County Code. Public art projects expenses are partially dependent on the timing of King County construction projects.

Transfers of \$189,384 to King County in 2007 were the required transfer of 2007 lodging tax receipts back to King County for County debt service interest.

### **ANALYSIS OF FUNDS**

As noted earlier, the CDA uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

The CDA's total governmental fund balances at December 31, 2007 were \$38.0 million, including (1) \$2.3 million in the general fund; (2) \$8.4 million in the lodging tax special revenue fund; (3) \$5.8 million in the 1% for art special revenue fund; and (4) \$21.5 million in the cultural endowment permanent fund. Approximately 66% (\$25.1 million) of the fund balance is reserved to indicate that it is not available for new spending due to certain legal restrictions on its use.

Total fund balances of the CDA increased by \$8.2 million for the year ended December 31, 2007. This increase was composed of (1) \$17.6 million of total fund revenues; (2) \$8.8 million of total fund expenditures; and (3) \$0.6 million of fund transfers out to King County.

Total fund revenues of \$17.6 million in 2007 included (1) \$10.5 million of program revenues for lodging tax receipts from King County; (2) \$2.2 million of program revenues from King County for the One Percent for Art program; (3) \$2.2 million of other KC grants and program support; and (4) \$2.3 million of net investment earnings. Other revenues included fees from consulting services and grants and contributions from other sources.

Total expenditures of \$8.8 million in 2007 included (1) \$6.6 million for arts and cultural support and other program expenses; (2) \$1.7 million for public art projects; and (3) \$0.5 million for management and general supporting activities.

Fund transfers out of \$0.6 million were for 2007 lodging tax receipts transferred back to King County for debt service requirements on County bonds issued for cultural purposes before December 31, 2002.

Significant interfund transfers included a \$4.2 million transfer from the lodging tax special revenue fund to the cultural endowment permanent fund as required by law for 40% of the total current year lodging tax receipts.

## **ECONOMIC FACTORS AND NEXT YEAR'S BUDGETS**

Revenues and expenses to be recognized in the 2008 government-wide statement of activities are expected to remain at 2007 levels in all categories except for a projected decrease of \$0.5 million in investment earnings. Revenues, expenditures and interfund transfers in the 2008 fund financial statements are expected to remain at 2007 levels in all categories except for a projected decrease of \$0.5 million in investment earnings.

The CDA relies heavily on King County support to accomplish its mission and programs. Reduction or elimination of King County funding sources such as lodging tax receipts could have a substantial detrimental impact on the CDA operations. No such reductions are anticipated in 2008; however, legislation providing for the use of lodging tax receipts for cultural purposes in King County is currently scheduled to expire in 2012.

## **REQUESTS FOR INFORMATION**

This financial report is designed to provide a general overview of the CDA's finances for all those with an interest in the CDA's finances. Questions concerning any of the information provided in this report, or requests for additional financial information, should be addressed to the CDA's finance department at 4Culture, 101 Prefontaine PI S, Seattle, WA 98104.

CULTURAL DEVELOPMENT AUTHORITY OF KING COUNTY  
 dba 4CULTURE  
 STATEMENT OF NET ASSETS  
 DECEMBER 31, 2007

	<u>Governmental Activities</u>	<u>Business-type Activities</u>	<u>Total</u>
<b>ASSETS</b>			
Cash and cash equivalents	\$ 13,590,738	\$ -	\$ 13,590,738
Due from King County	1,381,233	-	1,381,233
Receivables and other assets, net	670,401	-	670,401
Investments	<u>23,506,179</u>	<u>-</u>	<u>23,506,179</u>
Total assets	<u>39,148,551</u>	<u>-</u>	<u>39,148,551</u>
<b>LIABILITIES</b>			
Accounts payable and other accrued liabilities	571,224	-	571,224
Unearned revenues	5,808,234	-	5,808,234
Noncurrent liabilities			
Due within one year	390,484	-	390,484
Due in more than one year	<u>3,286,300</u>	<u>-</u>	<u>3,286,300</u>
Total liabilities	<u>10,056,242</u>	<u>-</u>	<u>10,056,242</u>
<b>NET ASSETS</b>			
Invested in capital assets, net of related debt	-	-	-
Restricted			
Expendable	13,663,946	-	13,663,946
Nonexpendable	19,105,147	-	19,105,147
Unrestricted	<u>(3,676,784)</u>	<u>-</u>	<u>(3,676,784)</u>
Total net assets	<u>\$ 29,092,309</u>	<u>\$ -</u>	<u>\$ 29,092,309</u>

See accompanying notes to financial statements.

CULTURAL DEVELOPMENT AUTHORITY OF KING COUNTY  
 dba 4CULTURE  
 STATEMENT OF ACTIVITIES  
 FOR THE YEAR ENDED DECEMBER 31, 2007

Program	Expenses	Program Revenues			Net Revenue and Changes in Net Assets
		Charges for Services	Operating Grants and Contributions	Capital Grants and Contributions	
					Total
Governmental Activities:					
Arts and cultural programs	\$ 8,883,921	\$ 278,343	\$ 13,921,217	\$ -	<u>\$ 5,315,639</u>
General revenues and transfers:					
Interest earnings					2,295,877
Transfers of lodging tax revenues to King County for debt service interest					(189,384)
Total general revenues and transfers					<u>2,106,493</u>
Change in net assets					7,422,132
Net Assets - January 1, 2007					21,670,177
Net Assets - December 31, 2007					<u>\$ 29,092,309</u>

See accompanying notes to financial statements.

CULTURAL DEVELOPMENT AUTHORITY OF KING COUNTY  
 dba 4CULTURE  
 BALANCE SHEET - GOVERNMENTAL FUNDS  
 DECEMBER 31, 2007

	General Fund	Lodging Tax Special Revenue Fund	1% for Art Special Revenue Fund	Cultural Endowment Fund	Total Governmental Funds
<b>ASSETS</b>					
Cash and cash equivalents	\$ 2,792,329	\$ 3,455,464	\$ 2,534,394	\$ 4,808,551	\$ 13,590,738
Receivable, net & other	102,312	812	(4,315)	-	98,809
Due from a primary government	55,000	1,326,233	-	-	1,381,233
Interfund Receivable/Payable	-	-	173,853	529,812	703,665
Investments	-	4,148,381	3,209,276	16,148,522	23,506,179
<b>TOTAL ASSETS</b>	<b><u>\$ 2,949,641</u></b>	<b><u>\$ 8,930,890</u></b>	<b><u>\$ 5,913,208</u></b>	<b><u>\$ 21,486,885</u></b>	<b><u>\$ 39,280,624</u></b>
<b>LIABILITIES</b>					
Accounts payable	\$ 85,438	\$ 224,165	\$ 79,951	\$ -	\$ 389,554
P/R and other accrued liabilities	93,187	63,460	25,023	-	181,670
Contracts payable	-	-	-	-	-
Interfund Payable	496,723	206,942	-	-	703,665
<b>Total Liabilities</b>	<b><u>675,348</u></b>	<b><u>494,567</u></b>	<b><u>104,974</u></b>	<b><u>-</u></b>	<b><u>1,274,889</u></b>
<b>FUND BALANCES</b>					
Reserved - Encumbrances	2,256,114	2,751,049	1,012,816	-	6,019,979
Reserved - Endowment	-	-	-	19,105,147	19,105,147
Unreserved - Designated	-	5,685,274	3,510,961	-	9,196,235
Unreserved - Undesignated	18,179	-	1,284,457	2,381,738	3,684,374
<b>Total Fund Balances</b>	<b><u>2,274,293</u></b>	<b><u>8,436,323</u></b>	<b><u>5,808,234</u></b>	<b><u>21,486,885</u></b>	<b><u>38,005,735</u></b>
<b>TOTAL LIABILITIES AND FUND BALANCES</b>	<b><u>\$ 2,949,641</u></b>	<b><u>\$ 8,930,890</u></b>	<b><u>\$ 5,913,208</u></b>	<b><u>\$ 21,486,885</u></b>	

Reconciliation of total governmental fund balances to net assets:

Noncurrent liabilities are not due and payable in the current period and are not reported on the fund balance sheet	\$ (3,676,784)
Public art unearned revenues are not due and payable in the current period and are not reported on the	(5,808,234)
Fixed assets and long-term prepaid rent are not current financial resources and are not reported on the fund balance sheet	571,592
<b>Total net assets of governmental activities:</b>	<b><u>\$ 29,092,309</u></b>

See accompanying notes to financial statements.

CULTURAL DEVELOPMENT AUTHORITY OF KING COUNTY  
dba 4CULTURE  
STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES  
GOVERNMENTAL FUNDS  
FOR THE YEAR ENDED DECEMBER 31, 2007

	General Fund	Lodging Tax Special Revenue Fund	1% for Art Special Revenue Fund	Cultural Endowment Fund	Total Governmental Funds
<b>REVENUES</b>					
Program Support from King County	\$ 2,198,479	\$ -	\$ 2,162,899	\$ -	\$ 4,361,378
Hotel/Motel Tax Gross Receipts	-	10,499,444	-	-	10,499,444
Investment Earnings	165,466	397,012	356,924	1,376,475	2,295,877
Miscellaneous	391,400	49,908	280	-	441,588
<b>Total Revenues</b>	<u>2,755,345</u>	<u>10,946,364</u>	<u>2,520,103</u>	<u>1,376,475</u>	<u>17,598,287</u>
<b>EXPENDITURES</b>					
Arts and cultural program activities	2,221,948	4,356,574	-	-	6,578,522
Public art program activities	437,942	-	1,311,009	-	1,748,951
Management and general supporting activities	524,242	-	-	-	524,242
<b>Total Expenditures</b>	<u>3,184,132</u>	<u>4,356,574</u>	<u>1,311,009</u>	<u>-</u>	<u>8,851,715</u>
Excess (deficiency) of revenues over (under) expenditures	<u>(428,787)</u>	<u>6,589,790</u>	<u>1,209,094</u>	<u>1,376,475</u>	<u>8,746,572</u>
<b>OTHER FINANCING SOURCES (USES)</b>					
Transfers to King County for debt service	-	(564,927)	-	-	(564,927)
Interfund transfers in (out)	585,271	(4,678,804)	(106,244)	4,199,777	-
<b>Total Other Financing Sources (uses)</b>	<u>585,271</u>	<u>(5,243,731)</u>	<u>(106,244)</u>	<u>4,199,777</u>	<u>(564,927)</u>
Net changes in fund balances	156,484	1,346,059	1,102,850	5,576,252	8,181,645
Fund Balances - January 1, 2007	2,117,809	7,090,264	4,705,384	15,910,633	29,824,090
<b>Fund Balances - December 31, 2007</b>	<u>\$ 2,274,293</u>	<u>\$ 8,436,323</u>	<u>\$ 5,808,234</u>	<u>\$ 21,486,885</u>	<u>\$ 38,005,735</u>

Reconciliation of changes in fund balances to changes in net assets:

Net change in fund balances - total governmental funds	\$ 8,181,645
Transfers to King County for principal debt service consume current financial resources of funds but do not affect net assets	375,543
Depreciation of fixed assets and amortization of prepaid rent reduce net assets but do not consume current financial resources of funds	(32,206)
Public art fund balances are classified as unearned revenue on the government-wide statement of net assets, thus the net	(1,102,850)
<b>Change in net assets of governmental activities</b>	<u>\$ 7,422,132</u>

See accompanying notes to financial statements.



**CULTURAL DEVELOPMENT AUTHORITY OF KING COUNTY**  
**dba 4CULTURE**  
**Notes to Financial Statements**  
**December 31, 2007**

**NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

Organization

The Cultural Development Authority of King County (CDA), dba 4Culture, is a public authority organized pursuant to the State of Washington RCW 35.21.730 through 35.21.759 and King County Ordinance 14482. The CDA was formerly the Office of Cultural Resources (OCR), a King County agency, and is now responsible for programs previously administered by the OCR. The CDA commenced operations on January 1, 2003, and began doing business as “4Culture” effective April 4, 2004. Per King County Ordinance 14482, the CDA was created “exclusively to support, advocate for and preserve the cultural resources of the region in a manner that fosters excellence, vitality and diversity. The authority shall further the goals and objectives of the King County Comprehensive Plan, establish cultural resource policies and operate in a manner that ensures King County citizens and visitors have access to high-quality cultural programs and experiences.” The CDA operates in a manner that combines public sector resources and accountability with private sector entrepreneurial responsiveness to offer King County citizens and visitors a variety of programs and services that enhance opportunities to participate in arts, heritage, historic preservation, and public art.

The CDA is located in Seattle, Washington and is governed by a 15-member Board of Directors and five ex-officio members. The Directors are appointed by the King County Executive and confirmed by the King County Council. The CDA receives various funds from King County and other sources that are designated for arts, cultural and public art use, including a portion of the revenue generated by the King County lodging tax and one percent of King County expenditures for certain construction projects.

The CDA prepares and issues its own financial statements, including government-wide financial statements, which are audited by the State Auditor. These statements may be obtained from the finance department at 4Culture, 101 Prefontaine PI S, Suite 200, Seattle, WA 98104. In addition, the CDA is included as a component unit in King County’s annual financial statements.

Income Tax Status

For federal tax purposes, the CDA is considered an integral part of King County and accordingly is exempt from federal income taxes. Contributions to the CDA for public purposes are charitable contributions deductible to the extent provided in Section 170 of the Internal Revenue Code.

Major Programs

The CDA manages and administers two major programs as described below. Other CDA activities include management and maintenance of the King County art collection, management of grants from King County and other sources, and providing fee-based public art consulting services.

Lodging Tax Revenues – As authorized by the State of Washington RCW 67.28.180, King County collects taxes on certain lodging transactions subject to the tax under RCW 82.08. The County receives a credit against a portion of the State of Washington sales tax for these local lodging tax revenues, allowing use of the lodging tax revenues for local purposes. In accordance with RCW 67.28.180 and King County Code (KCC) chapters 4.08, 4.42 and 2.48, seventy percent of total annual lodging tax revenues in excess of \$5.3 million (required for annual Kingdome debt service) are allocated to the CDA to be used for the support of the arts, the performing arts, art museums, heritage museums and cultural museums of King County. The annual lodging tax revenues transferred to the CDA are allocated in the following order per KCC 4.42.025: 1) forty percent is transferred to the CDA’s cultural endowment permanent fund; 2) support of related administration costs of the cultural programs administered by the CDA; 3) division of lodging tax revenues after the previous allocations between arts programs and heritage programs with at

least twenty percent allocated to heritage programs; 4) transfers back to King County for debt service requirements on County bonds issued for cultural purposes prior to December 31, 2002; and 5) allocation within arts and heritage programs to sustained support, cultural facilities, special projects and cultural education according to percentages as proscribed in KCC 4.42.025. All lodging tax receipts received by the CDA are accounted for in a separate special revenue fund. Legislation providing for the use of lodging taxes in King County for cultural purposes is currently scheduled to expire at the end of 2012.

One Percent for Art Program – In accordance with KCC chapters 4.08, 4.40 and 2.46, all eligible King County capital improvement projects that are publicly accessible and visible, or for which there is a need for mitigation, contribute an amount equal to one percent of the eligible project costs to the public art program, which is appropriated by King County and transferred to the CDA on an annual basis. The one percent receipts by the CDA are used to support the selection, acquisition, and display of works of art; artist fees, design, planning and predesign service contracts and commissions; expenses for technical assistance provided by architects and/or engineers; repair and maintenance of public artworks accessioned into the county's public art collection; public art program administrative expenses relating to acquiring, developing or maintaining public art; costs of communicating with and receiving input from citizens, working with professional artists, introduction of public art to children, and education of the public about the county's rich cultural and artistic heritage; and documentation and public education material for the public art program. All one percent for art receipts received by the CDA are accounted for in a separate special revenue fund.

#### Government-wide and Fund Financial Statements

The government-wide financial statements (i.e., the statement of net assets and the statement of activities) report information on all activities of the CDA. Governmental activities, which normally are supported by taxes and intergovernmental revenues, are reported separately from business-type activities, which rely to a significant extent on fees and charges for support. The CDA reported no business-type activities in 2007.

The Statement of Activities demonstrates the degree to which the expenses of a given function are offset by program revenues. Direct expenses are those that are clearly identifiable with a specific function. Program revenues include: (1) grants and contributions that are restricted to meeting the operation requirements of a particular function; and (2) charges to customers who purchase services provided by a given function. Investment earnings are reported as general revenues.

Separate financial statements are provided for governmental funds. Major individual governmental funds are reported as separate columns in the fund financial statements.

#### Basis of Accounting, Measurement Focus, and Financial Statement Presentation

The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting in conformity with generally accepted accounting principles. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

Governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. Transfers for debt service are recorded only when the payments are due.

## Major Governmental Funds

All funds used by the CDA in 2007 are classified as major governmental funds, as follows:

The General Fund is the CDA's primary operating fund. It accounts for all financial resources of the CDA except those required to be accounted for in another fund.

The Lodging Tax Special Revenue Fund is used to receive and manage all lodging tax revenues transferred from King County and designated for cultural purposes in accordance with the State of Washington RCW 67.28.180A(3)(a) and K.C.C. chapters 4.08, 4.42 or 2.48 or by similar statutory and ordinance authority.

The One Percent for Art Special Revenue Fund is used to receive and manage all one percent for art allocations transferred from King County in accordance with K.C.C. chapters 4.08, 4.40 and 2.46, or by similar statutory and ordinance authority.

The Cultural Resources Endowment Permanent Fund is used to receive and manage 40% of the annual lodging tax revenues in accordance with K.C.C chapter 4.08.195. This 40% annual application is required through December 31, 2012. The principal portion of the fund is permanent and irreducible. Interest earnings in the fund are available for use.

## Cash and Cash Equivalents

For the purposes of the statement of net assets, cash and cash equivalents include funds held in the Washington State Local Government Investment Pool since these funds can be liquidated on demand.

## Long-Term Prepaid Rent

Certain expenditures capitalized as long-term prepaid rent at the inception of the CDA's current lease for office space are amortized over the 29-year life of the lease.

## Capital Assets

Capital assets are recorded at cost or, if donated, at the estimated fair value on the date of donation. The CDA capitalizes equipment with a value of \$10,000 or more. Depreciation is computed using the straight-line method over the estimated useful life of the asset.

## Unearned Revenues

Unearned revenues represent the total amounts collected from King County for the One Percent for Art program for which the revenue recognition criteria have not been met. The CDA recognizes revenue for this program to the extent that expenditures are incurred in the current fiscal year.

## Compensated Absences

The CDA employees earn 12 sick days per year and 12 to 30 days of vacation per year, depending on length of service. An unlimited amount of sick leave and 30 days of vacation may be accrued. Unused sick leave is forfeited upon termination of employment.

## Use of Estimates

Management uses estimates and assumptions in reporting certain amounts and disclosures, and actual results could differ from those estimates.

## **NOTE 2 – DEPOSITS WITH FINANCIAL INSTITUTIONS AND INVESTMENTS**

### Deposits

The CDA maintains a deposit relationship with a local commercial bank. All deposits with this qualified public depository that are not insured by the Federal Deposit Insurance Corporation (FDIC) are fully collateralized by the Public Deposit Protection Commission of the State of Washington (PDPC); accordingly, the CDA has no custodial credit risk for its deposits. Carrying amounts of deposits for book purposes are materially the same as bank balances.

### Investments

The CDA has an investment policy to guide the management of its assets and help ensure that all investment activity is within the regulations established by State and County law. The primary objective is the preservation of principal.

State statutes authorize the CDA to invest in certificates, notes, or bonds of the United States, and other obligations of the United States or its agencies or any corporation wholly owned by the government of the United States. Statutes also authorize the CDA to invest in banker's acceptances purchased on the secondary market, federal home loan bank notes and bonds, federal land bank bonds, federal national mortgage association notes and debentures and guaranteed certificates of participation. The CDA is also authorized to invest in the Washington State Local Government Investment Pool (LGIP), which is comparable to a Rule 2a-7 money market fund recognized by the Securities and Exchange Commission. The LGIP funds are limited to high quality obligations with limited maximum and average maturities, with the effect of minimizing both market and credit risk.

The schedule below shows the types of investments, the average interest rate and the effective duration limits of all CDA investments as of December 31, 2007:

<u>Investment Type</u>	<u>Fair Market</u>	<u>Cost</u>	<u>Average Interest Rate</u>	<u>Effective Duration (Yrs)</u>
Washington State LGIP	\$ 13,136,255	\$ 13,136,255	4.56%	0.003
U.S. Treasury Notes	11,788,430	11,448,741	4.19%	3.563
Federal Home Loan Mortgage Corp Notes	2,948,084	2,899,768	5.05%	3.350
Federal National Mortgage Assn Notes	7,284,847	7,142,069	4.96%	5.428
Federal Home Loan Bank Bonds	<u>1,484,818</u>	<u>1,455,691</u>	<u>4.12%</u>	<u>2.980</u>
Totals	<u>\$ 36,642,434</u>	<u>\$ 36,082,524</u>	<u>4.54%</u>	<u>2.617</u>

Interest Rate Risk – Investments - Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. Through its investment policy, the CDA manages its exposure to interest rates risk by setting maturity and effective duration limits for its portfolio. At December 31, 2007, the combined weighted average effective duration of the CDA's portfolio was 2.617 years.

Credit risk - Credit risk is the risk that an issuer will not fulfill its obligations. At December 31, 2007 all issuers of investments in the CDA portfolio had a Standard & Poor's rating of "AAA". The Washington State Local Government Investment Pool is not rated.

Concentration of credit risk - Concentration of credit risk is the risk of loss attributed to the magnitude of the CDA's investment in a single issuer. At December 31, 2007, the CDA had concentrations greater than 5 percent of its total portfolio in the following issuers: Washington State Local Government Investment Pool – 36%, U.S. Treasury Obligations – 32%, Federal National Mortgage Association – 20% and Federal Home Loan Mortgage Corporation – 8%.

**NOTE 3 – RESTRICTED ASSETS**

The CDA assets include assets restricted for the following purposes:

King County one percent for art program	\$ 5,913,208
Arts, cultural and other public art programs	14,130,196
Cultural program endowment fund principal	<u>19,105,147</u>
Total CDA restricted assets	<u>\$39,148,551</u>

**NOTE 4 – RESTRICTED AND UNRESTRICTED NET ASSETS**

Restricted expendable net assets - \$13,663,946 is restricted by RCW and King County ordinance for use for arts and heritage cultural program awards according to a specified formula.

Restricted nonexpendable net assets - \$19,105,147 is the principal portion of a permanent endowment funded from a portion of the lodging tax revenues pursuant to RCW 67.28.180.3(e) and King County ordinance to finance future arts and heritage cultural programs.

Unrestricted net assets - \$3,676,784 deficit is the result of long-term commitments that are greater than currently available resources. The deficit corresponds to the noncurrent liabilities recognized by the CDA for required future transfers to King County for County debt service. Per King County ordinance, these long-term commitments are to be funded by future lodging tax revenues.

**NOTE 5 – DEFINED BENEFIT PENSION PLANS**

All eligible CDA personnel participate in the Public Employees' Retirement Systems (PERS). PERS is a statewide local government retirement system administered by the State of Washington's Department of Retirement Systems.

**NOTE 6 – NONCURRENT LIABILITIES**

Per King County ordinance, the CDA must transfer back to King County a sufficient portion of the CDA's annual lodging tax receipts for King County to use for debt service requirements on County bonds issued for cultural purposes before December 31, 2002. The CDA recognizes a noncurrent liability on its government-wide statement of net assets equal to the outstanding principal amount of these County bonds. In 2007, the CDA transferred \$564,927 of 2007 lodging tax receipts back to King County for County debt service requirements, including \$375,543 for County bond principal and \$189,384 for County interest expense.

Future scheduled transfers back to King County of the CDA's annual lodging tax receipts are as follows:

	<u>Transfers for County bond Principal</u>	<u>Transfers for County bond Interest</u>	<u>Total Transfers</u>
2008	\$ 390,484	\$ 173,117	\$ 563,601
2009	410,836	155,669	566,505
2010	432,667	137,274	569,941
2011-2012	917,797	215,063	1,132,860
2013-2021	<u>1,525,000</u>	<u>374,063</u>	<u>1,899,063</u>
Totals	<u>\$ 3,676,784</u>	<u>\$ 1,055,186</u>	<u>\$ 4,731,970</u>

Legislation providing for the use of lodging taxes in King County for cultural purposes is currently scheduled to expire at the end of 2012.

## **NOTE 7 – COMMITMENTS**

### **Contracts and Awards**

Each year, the CDA awards numerous grants to local arts and heritage organizations through the Lodging Tax Revenues program. In addition, the CDA administers various other grants awarded by King County. The majority of these grants are reimbursement grants to the recipient for specific expenditures identified in the grant contract. Under generally accepted accounting principles, the CDA does not recognize a liability for these grants until the recipient organization has incurred the specified expenditures and invoiced the CDA. It is anticipated that all current outstanding awards will eventually be paid by the CDA. The total amount of outstanding awards and contracts at December 31, 2007 was \$2,751,049 for the Lodging Tax Revenues program and \$2,256,114 of other King County grants.

### **Operating Leases**

The CDA leases office equipment under noncancelable leases with various expiration dates. 2007 lease expense for office equipment was \$7,507; future minimum annual lease payments are approximately \$7,500.

The CDA leases office space under a lease expiring June 30, 2034. 2007 lease expense for office space was \$113,742. Minimum annual lease payments for 2008 are approximately \$116,000 with two percent annual increases thereafter. The cost of long-term prepaid rent incurred at the inception of the office space lease will be amortized over the life of the lease. Future annual amortization amounts are \$20,223.

## **NOTE 8 - SIGNIFICANT REVENUE CONCENTRATION**

As a former agency of King County, the CDA relies heavily on receipts from King County, including lodging tax revenues and the one percent for art transfers, to accomplish its mission and program goals. Reduction or elimination of King County funding sources could have a substantial detrimental impact on the CDA operations. Legislation providing for the use of lodging taxes in King County for cultural purposes is currently scheduled to expire at the end of 2012.



## **ABOUT THE STATE AUDITOR'S OFFICE**

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The State Auditor's Office is established in the state's Constitution and is part of the executive branch of state government. The State Auditor is elected by the citizens of Washington and serves four-year terms.

Our mission is to work in cooperation with our audit clients and citizens as an advocate for government accountability. As an elected agency, the State Auditor's Office has the independence necessary to objectively perform audits and investigations. Our audits are designed to comply with professional standards as well as to satisfy the requirements of federal, state, and local laws.

The State Auditor's Office has 300 employees who are located around the state to deliver our services effectively and efficiently. Approximately 65 percent of our staff are certified public accountants or hold other certifications and advanced degrees.

Our regular audits look at financial information and compliance with state, federal and local laws on the part of all local governments, including schools, and all state agencies, including institutions of higher education. We also perform fraud and whistleblower investigations. In addition, we have the authority to conduct performance audits of state agencies and local governments.

The results of our audits are widely distributed through a variety of reports, which are available on our Web site. We continue to refine our reporting efforts to ensure the results of our audits are useful and understandable.

We take our role as partners in accountability seriously. We provide training and technical assistance to governments and have an extensive program to coordinate audit efficiency and to ensure high-quality audits.

**State Auditor**  
**Chief of Staff**  
**Chief Policy Advisor**  
**Director of Administration**  
**Director of State and Local Audits**  
**Director of Performance Audit**  
**Director of Special Investigations**  
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**Web Site**

**[www.sao.wa.gov](http://www.sao.wa.gov)**