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Report to the Chairman, Subcommittee on the District of Columbia, Committee on Government Reform and Oversight, House of Representatives

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DISTRICT OF COLUMBIA

Status of the Proposed New Convention Center Project

GAO

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The Honorable Thomas M. Davis, III
Chairman, Subcommittee on the
District of Columbia
Committee on Government Reform
and Oversight
House of Representatives

Dear Mr. Chairman:

You requested that we monitor and periodically report on the progress of the proposed new convention center project for Washington, D.C. This report, our fourth on this issue, discusses the project's approval process, building design, estimated costs, dedicated revenues, and financing plans.

The Washington Convention Center Authority (WCCA), an independent authority of the District Government, is responsible for the management and development of the new convention center.

Results in Brief

WCCA is faced with the challenge of obtaining sufficient financing for the construction of the proposed new convention center project. The total cost—predevelopment and construction, including contingencies—of the proposed new convention center is now estimated to be about $650 million, excluding $87 million of borrowing costs and certain reserve requirements. WCCA already has sufficient funds from dedicated taxes for the $40 million in projected predevelopment costs of which a reported $15.6 million was expended as of July 31, 1997. However, funding for the entire estimated $610 million in construction cost is uncertain at this time.

WCCA plans to issue revenue bonds backed by dedicated taxes to finance a portion of the construction cost of the project. However, WCCA would need to have its authority to use the taxes currently dedicated to the predevelopment costs of the project expanded to include using them for construction and would have to adopt and submit for City Council review a resolution authorizing the issuance of revenue bonds. The current stream of existing annual dedicated tax revenues is not sufficient to support the debt required to fund the project's estimated construction cost. The current earmarked tax collections are estimated to support a revenue bond issuance of $423 million. WCCA estimated that if $51 million of interest earnings from investment of bond proceeds as well as

$30 million of cash on hand from dedicated taxes as of July 31, 1997, which is estimated to be available for construction, are added to the estimated $423 million, total estimated revenues would amount to $504 million. However, this would leave a shortfall of approximately $106 million. Assuming currently estimated costs are substantially accurate, WCCA would need about $114 million ($106 million plus an additional estimated $8 million to satisfy an operation and maintenance reserve) if it were to enter the market in October 1997, as originally contemplated, to obtain bond financing. WCCA, with the assistance of financial advisors, has been exploring financing options such as additional funds from the District, federal funding, and sale of the existing convention center to supplement the dedicated tax revenues.

Also, before the project can move forward, the National Capital Planning Commission (NCPC), the central agency for conducting planning and development activities for federal lands and facilities in the National Capitol Region, including the District of Columbia, must approve the concept design as well as address community concerns regarding the project. Since our December 1996 report, WCCA's estimated completion date has slipped 1 year to December 31, 2000, and based on the delays and approvals required, this date is uncertain.

Background

Plans for the new convention center were initiated in 1993 by the District's Hotel and Restaurant Associations, the Convention and Visitors Association, and the District of Columbia government. The Washington Convention Center Authority Act of 1994[1] (1994 Act) authorizes WCCA to construct, maintain, and operate the new convention center, as well as maintain and operate the existing convention center. The current design calls for a total of 2.1 million gross square feet, which includes approximately 730,000 square feet of prime exhibit space compared to the existing convention center which has a total of 800,000 gross square feet, including 381,000 gross square feet of exhibit space. According to the 1997 Market Demand Update for the Washington, D.C., Convention Center, the proposed new convention center is projected to rank eighth, based on the gross square feet of prime exhibit space, in the United States when completed, and the size of the proposed new convention center should remain highly marketable into the 21st century.

[1]The WCCA was created by the Washington Convention Center Authority Act of 1994, D.C. Law 10-188, September 28, 1994, 41 DC 5333, 6823, D.C. Code Ann. secs. 9-801 through 9-819.

In August 1994, when the District created WCCA, it also earmarked additional revenues to finance the project. Section 301 of the 1994 Act amended the District of Columbia Income and Franchise Tax Act of 1947 (1) to decrease the tax on the privilege of corporations, financial institutions, and unincorporated businesses to do business in the District from 10 percent of taxable income to 9.5 percent of taxable income and (2) to impose a surtax of 2.5 percent on the 9.5 percent tax. Amounts collected from the surtax are to be transferred to the WCCA.[2]

Sections 302 and 303 of the 1994 Act amended the District of Columbia Sales Tax Act and the District of Columbia Compensating Use Tax Act, respectively (1) to decrease the tax rate from 11 percent to 10.5 percent on hotel gross receipts and to add an additional tax of 2.5 percent on hotel gross receipts and (2) to add an additional tax of 1 percent to the 9 percent tax on the gross receipts from the sales of food or drink (including alcohol) to be consumed on the premises and from the rental of vehicles and trailers. Amounts collected from the additional taxes are to be transferred to the WCCA.[3]

Section 304 of the 1994 Act amended the Hotel Occupancy and Surtax on Corporations and Unincorporated Business Tax Act of 1977 to provide 40 percent of the $1.50 tax already being collected on the occupancy of each hotel room to the WCCA and to allocate the remaining 60 percent as follows: 50 percent to the Washington Convention and Visitors Association, 37.5 percent to the Mayor's Committee to Promote Washington, and 12.5 percent to WCCA for advertising and promotion.[4]

The fourth sentence of section 446 of the Home Rule Act, D.C. Code Ann. 47-304 (1981), as amended, provides that "...no amount may be obligated or expended by any officer or employee of the District of Columbia government unless such amount has been approved by an act of Congress, and then only according to such act."[5] Section 101 of the District of Columbia Convention Center and Sports Arena Authorization Act of 1995, (Public Law No. 104-28, 109 Stat. 267 (1995), D.C. Code sec. 47-396.1 (1981, 1996 supp.)), authorized WCCA's use of the revenues attributable to sections

[2]D.C. Code Ann. secs. 47-1807.2, 47-1807.2a, 47-1808.3, 47-1808.3a (1981, 1996 Supp.).

[3]D.C. Code Ann. secs. 47-2002, 47-2002.2, 47-2002.3, 47-2202, 47-2202.1, 47-2202.2 (1981, 1996 Supp.).

[4]D.C. Code Ann. secs. 47-3202, 47-3206 (1981, 1996 Supp.).

[5]As discussed later in this report, sections 11508 and 11509 of the Balanced Budget Act of 1997, have authorized the District to issue revenue bonds backed by a pledge of dedicated taxes and to use such taxes to pay the principal and interest on such bonds without further action by Congress.

301-304 of the 1994 Act to financing the operation and maintenance of the existing convention center and for the preconstruction activities relating to the new convention center.[6]

According to WCCA officials, the proposed new convention center is intended to allow the District to compete for larger conventions and trade shows. A 1993 feasibility study by Deloitte & Touche, commissioned by the local hospitality industry, stated that even though the District is viewed as a desirable location, the existing convention center, which has about 381,000 gross square feet of exhibit space, is small compared to the convention centers of other cities such as Atlanta, New York, Chicago, and Philadelphia.

The original proposal from the 1993 feasibility study called for building a new convention center in two phases with the first phase to be completed at the end of 1997 with approximately 554,000 gross square feet of exhibit space and the second phase to be completed at the end of 1999 with another 254,000 gross square feet of exhibit space. Since that study was completed, WCCA has ruled out a two-phase development project because the first phase essentially would not provide enough exhibit space to compete with cities with larger convention centers. The cost of both phases was estimated at $521 million.

In addition, the 1993 feasibility study, which was projected through the year 2003, estimated that direct and indirect economic benefits to the District from the construction of the project would include 560 new jobs, $4 million in increased revenue, and $260 million in other economic output such as spending related to convention center operations and development. For the Washington metropolitan area, the study projected 1,600 jobs, $28 million in incremental taxes, and $558 million in economic activity. Projected long-term benefits by the fifth year of operation of the new convention center included 2,500 permanent jobs, $44 million in incremental taxes, and $640 million in incremental economic output for the District. WCCA contracted with a management consulting firm to update the 1993 feasibility study, which will include an update of the economic benefits to the District. The study is expected to be completed by September 30, 1997.

The current master plan calls for constructing a new convention center at Mount Vernon Square, the legislatively[7] preferred site, located at Ninth

[6]See also sec. 208(c) of the 1994 Act, D.C. Code Ann. sec. 9-809(c) (1981) (1995 Rep. Vol.).

[7]Sec. 101(12) of the 1994 Act, D.C. Code Ann. sec. 9-801(12) (1981).

Street and Mount Vernon Place, North West. In the 1993 feasibility study, eight potential sites were identified and evaluated against certain criteria such as physical and location characteristics, historic preservation, parking, and cost, including land acquisition and construction. As a result of this analysis, the Mount Vernon Square site was determined to be the preferred site due to its close proximity to the District's downtown businesses and because the District owns the majority of the land, thus, minimizing the cost of land acquisition.

Objectives, Scope, and Methodology

To determine the status of the proposed new convention center project, we interviewed WCCA officials, contractors, regulatory agencies (National Capital Planning Commission and the Advisory Council on Historic Preservation), and District officials to determine and assess WCCA's progress toward meeting critical milestones.

We reviewed the master plan, which contains the concept design and requirements for the new convention center, and compared the design to the existing facility to determine if the new convention center will provide additional exhibit space. We also compared the new convention center exhibit space to facilities in other cities, based on the 1997 Market Demand Update, to determine the ranking in terms of prime exhibit space once the project is completed.

We analyzed the current predevelopment and construction cost estimates for the project as of May 31, 1997, to determine how they compare to the previous cost estimates prepared by WCCA. We reviewed documents and held discussions with WCCA officials to obtain reasons for variations from previous cost estimates for the proposed new convention center.

We reviewed financial records and current balances to determine the amount of dedicated taxes reported as collected and transferred to WCCA. In addition, we reviewed the lockbox procedures that were established to collect the dedicated taxes.

We also reviewed WCCA's plans for financing the new convention center project to determine whether adequate funding is available to finance the project. In addition, we reviewed alternative sources of financing proposed by WCCA.

We conducted our review between March 1997 and July 1997 in accordance with generally accepted government auditing standards. Also, we considered the results of previous work.[8] While we reviewed transactions to determine the reasonableness of the dedicated taxes collected, deposited, and transferred to WCCA, we did not audit the reported taxes collected and deposited for the new convention center project to determine if the District government accurately calculated and transferred all dedicated taxes to WCCA's escrow account.

We requested written comments on a draft of this report from the Mayor of the District of Columbia or his designee. These comments are discussed in the "District's Comments and Our Evaluation" section and are reprinted in appendix I.

Status of Approval Process for the Proposed New Convention Center

The project has reached the regulatory review phase which involves the WCCA obtaining necessary permits, reviews and approvals from federal and local regulatory agencies.

NCPC is reviewing the design of the project as provided by law.[9] During its approval process, NCPC is also considering the environmental impact of the conceptual design on the construction site and neighborhood. The environmental impact study (EIS) is complete and was reviewed by the federal Environmental Protection Agency (EPA). According to WCCA's Manager of Contracts, NCPC did not receive comments from EPA within the comment period.

Also, NCPC, WCCA, the Advisory Council on Historic Preservation, the District of Columbia State Historic Preservation Officer, the Mayor, and the Chair of the D.C. City Council, entered into a Memorandum of Agreement (MOA) on September 12, 1997, following consultations under section 106 of the National Historic Preservation Act.[10] The MOA contains a plan to mitigate a number of community, business, civic, and historic preservation concerns regarding the project. As a result of the signing of the MOA, NCPC has resumed consideration of the project and has scheduled

[8] District of Columbia: Status of Convention Center Project (GAO/AIMD-94-191, September 15, 1994), District of Columbia: Status of Sports Arena and Convention Center Projects (GAO/T-AIMD-95-189, July 12, 1995), District of Columbia: Status of Sports Arena and Convention Center Projects (GAO/T-AIMD-95-221), Status of Convention Center Project (GAO/AIMD-96-44R, February 21, 1996), and District of Columbia: Status of the New Convention Center Project (GAO/AIMD-97-17, December 20, 1996).

[9] Section 5 of the Act of June 6, 1924, as amended, 40 U.S.C. sec. 71d(c) (1994) and section 16 of the Act of June 20, 1938, D.C. Code Ann. sec. 5-432 (1981). See generally 40 U.S.C. secs. 71-71i (1994).

[10] 16 U.S.C. sec. 470f (1994) and its implementing regulations, 36 C.F.R. Part 800 (1996).

hearings on the proposed convention center for September 22 and 25, 1997.

Another critical phase in the development process of the project is obtaining authority to use the dedicated revenues attributable to section 301-304 of the 1994 Act to finance the construction of the project. Next, WCCA would have to adopt a resolution to issue the revenue bonds (subject to the City Council review). As part of the financing phase, WCCA would be required to obtain a credit rating for revenue bond financing from rating agencies. Based on WCCA's current schedule, the financing phase is scheduled for completion in late Fall of 1997, and groundbreaking is planned for late 1997 or early 1998. When we last reported in December 1996,[11] WCCA estimated that the project would be completed by December 31, 1999. The estimated completion date is now December 31, 2000. However, if more delays occur in the regulatory process and the finalization of a financing plan, this project could be further delayed.

WCCA has to acquire 15 remaining parcels of land for the Mount Vernon Square site. According to WCCA officials, the District does not anticipate any problems in acquiring the remaining properties, either by negotiated sale or, if necessary, by exercise of its power of eminent domain.[12]

New Convention Center Master Plan

According to requirements in the master plan, which WCCA officials told us are still the current thinking, the proposed new convention center will almost double the exhibit space for conventions and expositions available at the existing convention center. The current convention center has 800,000 gross square feet consisting of 381,000 gross square feet of exhibit space on two levels. The upper level has three exhibit halls with 276,000 square feet of exhibit space; the lower level contains 105,000 square feet of exhibit space.

The master plan for the proposed new convention center calls for a partially below-ground facility with approximately 2.1 million gross square feet that includes 730,000 gross square feet of prime exhibit space. The master plan organizes the new facility into three buildings with the approximate height ranging from 35 feet on the northern end to 130 feet on

[11]See footnote 8 in this report.

[12]D.C. Code Ann. sec. 16-1311 (1981).

the southern end of the complex consistent with the Building Height Act restriction.[13]

The proposed new convention center would have four levels with a completely below ground exhibit level containing 500,000 square feet of contiguous exhibit space and adjacent loading docks. The street level would consist primarily of lobby/registration space, meeting rooms, service/support space with some retail and community space on the perimeter. The upper level has additional meeting rooms and 230,000 square feet of column free exhibit space. The ballroom level (the fourth level) also includes the central kitchen.

The current convention center is ranked 30th, in terms of prime exhibit space, among competing convention centers in the United States, and the proposed new convention center is expected to be ranked eighth after completion, as shown in table 1.

Table 1: Ranking of Major Convention Centers' Prime Exhibit Space

City/convention center	Prime exhibit space (gross square feet)	Ranking
Chicago (McCormick Place)	2,128,500	1
Orlando (Orange County)	1,100,600	2
New Orleans (Ernest N. Morial)	1,100,000	3
Las Vegas (Las Vegas)	970,000	4
Atlanta (Georgia World Congress)	950,000	5
Las Vegas (Sands Expo)	935,000	6
New York (Jacob K. Javits)	760,000	7
District of Columbia (New Convention Center)	730,000	8
District of Columbia (Existing Convention Center)	381,000	30

Source: Market Demand Update for the Washington, D.C. Convention Center, Deloitte & Touche LLP, February 1997.

According to WCCA officials, the current master plan contemplates a state of the art facility with technology, including fiber optics and improved telecommunications capabilities to meet future District demands for convention exhibit space. To compete with other convention centers, WCCA's proposed plan would increase the number of loading docks, column spacing, ceiling heights, and floor loads in the exhibit space to attract some of the major trade shows.

[13]Section 5 of the Act of June 1, 1910, as amended, D.C. Code Ann. sec. 5-405 (1981).

WCCA must obtain NCPC's and the City Council's approvals before the project can move forward. In addition, WCCA's Board of Directors has determined that the "design build method" for the proposed new convention center would best meet WCCA's cost and scheduling requirements for the new convention center.

The design/build approach combines the responsibilities for designing and constructing the project in a single entity rather than separating the responsibilities among a number of entities. To mitigate development risks, WCCA's design/build contract would need to include performance clauses with specificity to prevent cost overruns and construction delays.

Estimated Project Costs

The estimated total predevelopment and construction costs, including contingencies, of the proposed new convention center have increased by a net of $100 million to approximately $650 million[14] from the $550 million that was last reported.[15] The increase is caused by several factors, primarily a $118 million increase in construction cost, now estimated to be about $534 million, excluding contingencies, compared to the previous estimate of $416 million and offsetting declines in predevelopment costs. Table 2 highlights the total estimated project costs for the new convention center. The increase in the construction costs are primarily associated with (1) additional steel necessary to construct the facility, (2) excavation and slurry wall costs from lowering the building 50 feet below ground to reduce the building height above ground, (3) shifting the building mass south, (4) providing retail and community space on the perimeter, (5) reducing construction across L Street which requires finished elevations on both sides of the street, and (6) allowing M Street to remain open for local traffic, which requires creating an overpass over the street and reinforcing the street over the below ground exhibit space. The majority of these revisions are in response to NCPC's concerns, the section 106 mitigation plan (required by the National Historic Preservation Act), and community concerns.

[14]The $650 million does not include WCCA's preliminary estimate of approximately $87.3 million in borrowing costs and certain reserve requirements. These costs are $12.2 million for bond insurance, underwriter's discount, and cost of issuance; a debt service reserve of $16.7 million; an operation and maintenance/marketing reserve of $46.2 million (including $16.2 million for marketing); and a capital reserve of $12.2 million. According to WCCA, this information was developed as of August 28, 1997. This information was provided to GAO on September 10, 1997.

[15]See footnote 8 in this report.

Table 2: Total Estimated Project Costs and Expenditures for the New Convention Center

Category	Four-year estimate as of 10/23/96	Revised 4-year estimate as of 5/31/97	Increase (decrease)	Expenditures as of 7/31/97
Total predevelopment cost/expenditures[a]	$63,531,212	$39,911,731	($23,619,418)	$15,629,953
Construction costs				
Building and site	347,750,000	417,500,000	69,750,000	0
Other construction costs	41,500,000	76,714,269	35,214,269	0
Fixtures/furnishings/equipment	27,000,000	40,000,000	13,000,000	0
Total construction costs/expenditures	**$416,250,000**	**$534,214,269**	**$117,964,269**	**0**
Total predevelopment and construction costs/expenditures	**$479,781,212**	**$574,126,000**	**$94,344,788**	**$15,629,953**
Project contingency	$70,218,788	$75,874,000	$5,655,212	0
Total project costs/expenditures	**$550,000,000**	**$650,000,000**	**$100,000,000**	**$15,629,953**

Source: WCCA. We did not independently verify this information.

[a]Includes cost for land acquisition.

Estimated contingencies are up approximately $6 million over the previous estimate of $70 million. The increase is due primarily to Section 106 mitigation and other regulatory issues, such as the implementation of the transportation management plan.

Predevelopment costs, down $24 million from the previous estimate of $64 million, fell largely because certain costs previously budgeted for bond insurance and investment banking services will now be paid from future bond proceeds.[16] As of July 31, 1997, WCCA incurred predevelopment costs of approximately $15.6 million, which are primarily for program management services, architect/engineering design, environmental impact study, land acquisition, and legal services.

Dedicated Tax Revenue Collections

WCCA receives a portion of the District's hotel sales and use taxes, hotel occupancy tax, corporation franchise, and unincorporated business taxes to help fund operations of the existing convention center and the predevelopment costs of the proposed new convention center.[17] Since

[16]See footnote 14 for an explanation of the cost of borrowing.

[17]A portion of the dedicated taxes are required by law to be allocated to the WCCA for advertising and promotion. In addition, a portion of the dedicated taxes are allocated for use by the Washington Convention and Visitors Association and the Mayor's Committee to Promote Washington. Approximately $5.2 million and $5 million was allocated for these purposes in 1996 and 1995, respectively.

October 1994, taxes have been collected monthly, and based on audited financial statements,[18] WCCA had received approximately $33 million and $35.5 million in tax revenues for fiscal years 1995 and 1996, respectively. The District projects tax revenues to WCCA of about $35 million for fiscal year 1997 and average annual amounts of about $36 million for fiscal years 1998 to 2002.

As of July 31, 1997, WCCA had received about $97 million in dedicated tax revenues. WCCA had invested approximately $67.6 million of the $97 million in Fannie Mae and Freddie Mac discount notes, which are earning an average of about 5.5 percent annually. Table 3 highlights the receipts and disbursements from the dedicated tax revenues collected since inception in fiscal year 1995.

Table 3: Washington Convention Center Authority Dedicated Tax Revenues, October 1, 1994 - July 31, 1997

Revenues		
Dedicated taxes received by WCCA		$97,081,948
Interest received from investments		3,491,899
Interest on bank account balances		421,105
Total revenues		**$100,994,952**
Expenditures		
Predevelopment expenditures	$15,629,953	
Operating subsidy	8,225,000	
Repayment of loan from Rainy Day Fund[a]	4,200,000	
Bank charges	6,955	
Total expenditures		**$28,061,908**
Funds available end of period		$72,933,044
Investments		$67,579,640
Cash balance		**$ 5,353,404**

[a]The Rainy Day Fund provides funds to the District of Columbia to be used at the discretion of the Mayor and the City Council for mandatory and unavoidable expenses. In the case of WCCA, Rainy Day Funds were used to continue operations of the existing convention center while awaiting congressional approval on the use of the dedicated tax revenues.

Source: WCCA. We did not independently verify this information.

In our December 1996 report,[19] we stated that WCCA is considering the use of revenue bonds, backed by the dedicated taxes, to finance the construction cost of the project. Also, during our discussions with rating agencies officials, they informed us that the rating might be improved if

[18]Washington Convention Center Authority, Financial Statements, September 30, 1996 and 1995, audited by KPMG Peat Marwick LLP.

[19]See footnote 8 in this report.

the collection process for the dedicated taxes were separated from the District's tax collection process. Since that time, the District has separated the dedicated taxes from the District's tax collection process by having businesses send the dedicated tax payments directly to lockboxes under the control of the banks. As of February 1997, lockboxes have been established at Signet Bank and First Union Bank for the collection of all the dedicated convention center taxes, and the banks will now be responsible for transferring these tax revenues to WCCA.

Further, based on a report by the District of Columbia Auditor,[20] which discusses the convention center dedicated tax revenues, WCCA was entitled to approximately $1 million in additional dedicated tax revenues from the District. The District subsequently transferred the $1 million to WCCA. The dedicated tax revenues became effective as of fiscal year 1995, and, according to the District of Columbia Auditor, the shortfall in tax revenues transferred to WCCA occurred primarily in the early months of fiscal year 1995. Based on the audit, the underpayment occurred primarily due to the Department of Finance and Revenue's (DFR) failure to calculate the additional dedicated taxes owed the WCCA based upon reconciliations of sales and use tax payments that were completed 60 to 90 days after DFR's initial reporting period. Based upon these reconciliations, additional dedicated taxes should have been transferred to the WCCA. Thus, the establishment of lockboxes for the collection of the dedicated tax revenues could result in more timely and accurate receipt of revenues as well as improve the likelihood for an investment grade rating should WCCA decide to issue revenue bonds to finance the construction cost of the project.

Financing Plans

WCCA plans to issue revenue bonds backed by dedicated taxes to finance the construction cost of the project.[21] Section 490 of the Home Rule Act (Public Law No. 93-198, as amended) was recently amended to authorize the District to issue revenue bonds backed by a pledge of dedicated taxes to finance various capital projects or other undertakings, including

[20]Washington Convention Center Authority, Accounts and Operations for Fiscal Years 1995 and 1996, June 24, 1997.

[21]Generally, District revenue bonds may be financed by a pledge of available revenues (including dedicated taxes and fees), assets or property (or security therein), or by a mortgage on real property. Otherwise, they do not involve the pledge of or involve the full faith and credit or taxing power of the District (other than with respect to any dedicated taxes) and are not debts of the District. D.C. Code Ann. § 47-334 (1981) as amended by section 11508 of the Balanced Budget Act of 1997 (1997 Act), set forth in 143 Cong. Rec. H6165-67 (daily ed. July 29, 1997).

convention facilities.[22] In addition, the fourth sentence of section 446 of the Home Rule Act was recently amended to, among other things, authorize the District to disburse dedicated tax revenues to pay the principal of, interest on, or premium for any authorized revenue bond without further action by the Congress.[23] However, the 1997 Act did not expand the authority to use the tax revenues attributable to sections 301-304 of the 1994 Act to construct the new convention center. In addition, section 204 of the 1994 Act[24] provides that WCCA may not adopt a resolution to authorize a bond issuance without submitting the resolution to the City Council for a 30-day review period during which the Council may adopt a resolution disapproving the bond issuance. Assuming that WCCA receives authority to use the revenues attributable to sections 301-304 of the 1994 Act for constructing the project and that the City Council does not disapprove the bond issuance, current projections of future dedicated tax revenues are not sufficient to support debt service costs for the full amount of the estimated construction cost.[25]

In March 1997, WCCA engaged a financial advisory services firm[26] to provide various financial services related to the convention center finances. In its proposal dated May 15, 1997, as well as subsequent proposals since May, the financial advisory services firm outlined several financing options for WCCA such as the issuance of revenue bonds, federal grants, lease arrangements, sale of the existing convention center, vendor participation/naming rights, and reallocation of a portion of the hotel occupancy tax. Table 4 depicts a financing option that WCCA is considering, assuming that all necessary approvals are granted regarding the use of currently dedicated revenues. As stated previously, the total cost of the project is estimated at $650 million—$610 million is estimated

[22]D.C. Code Ann. sec. 47-334 (a)(1), (c), as amended by section 11508 of the 1997 Act, 143 Cong. Rec. H6165 (daily ed. July 29, 1997). Prior to the 1997 Act's amendment, section 490(c) precluded the District from pledging taxes to pay the principal, interest, or other charges due on revenue bonds. D.C. Code Ann. sec. 47-334(c) (1981).

[23]Section 446 of the Home Rule Act, as amended by section 11509 of the 1997 Act, set forth in 143 Cong. Rec. H6167 (daily ed. July 29, 1997). See also section 490(f)(3) of the Home Rule Act as amended by section 11508 of the 1997 Act.

[24]D.C. Code Ann. sec. 9-805(a) (1995 Rep. Vol.).

[25]The D.C. Auditor is required to annually audit the accounts of the WCCA and determine whether the revenues from the dedicated taxes are sufficient to meet the projected expenditures and reserve requirements for the upcoming year. If they are not sufficient, Section 305 of the Washington Convention Center Authority Act requires the mayor to impose a surtax on convention center dedicated taxes, excluding the tax on the sale of restaurant meals and alcoholic beverages to eliminate the projected deficit.

[26]Columbia Equity Financial Corporation and Evensen Dodge Incorporated.

for construction costs, including contingencies, and $40 million is estimated for predevelopment costs. WCCA already has sufficient funds from dedicated taxes for predevelopment activities. However, the funding for the construction cost is uncertain at this time. Based on WCCA's estimate, table 4 shows a financing gap of $106 million that must be addressed before WCCA can enter the bond market. We have projected the estimated shortfall to be about $114 million since WCCA will need an additional $8 million to satisfy a $30 million operation and maintenance reserve, which is required by the rating agencies before WCCA can enter the bond market.[27]

Table 4: A Financing Option for the Construction Cost of the New Convention Center

Dollars in millions

Estimated construction cost to be financed (including contingencies):		$610	
Funding sources:			
Senior and junior lien bonds	$423		
Interest earnings from construction fund	51		
Cash on hand (WCCA)	30	504	
Shortfall			**$106**

Source: WCCA. This table does not include $40 million of dedicated tax revenue, which is already available to fund predevelopment costs. The senior and junior lien bonds are based on a 30-year term.

The following information describes the above financing option in more detail.

Senior and Junior Lien Bonds. The foundation of WCCA's financing plan is to generate the maximum amount of revenue bond funding for the construction cost of the new convention center project, which, according to the financial advisors, could be accomplished by using a senior lien and junior lien bond structure.[28] As previously stated, WCCA collects approximately $35 million annually from the dedicated tax revenues. Of

[27]This does not include $16.2 million in an additional reserve for marketing that was subsequently disclosed in information presented in footnote 14.

[28]Senior lien debt has first priority on the revenue pledged to the bonds. Junior lien debt has priority claims on residual dedicated revenue.

this amount, approximately $7.5[29] million is needed annually for operating expenses of the existing convention center, which leaves approximately $27.5 million as collateral for the issuance of revenue bonds. According to WCCA's financial advisors, the $27.5 million in annual revenue would support approximately $423 million in bond proceeds, assuming an average interest rate of about 6.3 percent.[30]

Senior lien bondholders will be provided higher coverage,[31] and this financing will be based on historical tax collections of the dedicated tax revenues. Junior lien bondholders will accept some of the credit risk of projected growth in the dedicated revenues, and this financing structure will be predicated on a 1 percent growth per year in the dedicated tax revenues.

A critical component of financing costs involves the level of risk associated with the bond. Higher risk bonds generally have higher interest rates, may require insurance, or may require the issuer to set up large debt service reserves. Officials at bond rating agencies have indicated that a number of factors are important in their assessment of bonds that are backed by dedicated revenues. First, if the bond is backed by a tax, the collection history of the tax is important. Bonds backed by taxes that have a solid collection history are less risky than those backed by new or unproven taxes. Second, the tax backing for a bond is less risky if it is assessed on a broader range of goods, services, or population. Third, revenue streams that have some legislative risk (that is, revenues based on an appropriation) make the bond higher risk. Finally, the general economic strength of the area is critical to the bond assessment.

Since the majority of the funds, 69 percent ($423 million of $610 million), for the financing of the convention center is expected to come from bonds backed by the dedicated tax revenues, we have attempted to determine the

[29]Operation and Maintenance (O&M) expenses have historically exceeded revenues derived from operations. In 1997, the deficit is projected to be about $7 million. According to the financial advisors, this is not unusual for a convention center. Based on industry standards of performance, it has been estimated that O&M expenses will stabilize at a modest $1 million deficit in the year 2008. In the interim, the deficit has been projected to increase to $9 million per year as the WCCA increases expenditures to market the new convention center and then gradually decline from that level as WCCA operations stabilize.

[30]This interest rate assumption was based on the prevailing interest rate as of May 21, 1997, and the projected issuance date of the bonds was October 1997.

[31]The senior lien bonds are structured based on 1.50 times coverage of historical collections of the dedicated revenues. The junior lien bonds are structured based on a 1.25 times coverage based on a projected growth in dedicated revenues of one percent per year. The junior lien bonds carry an interest rate 50 basis points higher than the senior lien securities. The bonds are assumed to be sold in November of 1997 and proceeds are drawn down over an 18-month draw schedule commencing in January 1998.

collection history of the taxes and the District's assumptions regarding future collections. As previously stated, the dedicated taxes are derived from portions of the District's hotel occupancy, the corporation franchise, the unincorporated business franchise, and sales and use taxes (restaurant meals, rental cars, and hotel rates). These taxes are not new. The majority of the taxes was generated from rate increases of existing taxes (corporation franchise and unincorporated business franchise and sales and use taxes), and the rest (hotel occupancy tax) was diverted from taxes that previously went to the District's general fund.

The majority of the dedicated revenues that WCCA receives, approximately 79 percent in fiscal year 1996, is derived from sales and use taxes (restaurant and rental cars and hotel rates), which are parts of the District's general sales and use tax. Based on the District's Comprehensive Annual Financial Report (CAFR), in fiscal year 1996, the District collected $467.5 million in total general sales and use taxes, and WCCA received $27.9 million, or about 6 percent, of this total. The District is unable to disaggregate the specific taxes that are dedicated to WCCA from the general sales and use tax category, and as a result, the District could not provide us with audited historical data for these specific taxes. Based on information received from the District, we compared information from the District's Business Tax Information System to information reported in the District's CAFR, and that information reflects different amounts for the taxes for the same reporting periods. For example, in fiscal year 1995, the District's CAFR showed total general sales tax of $485.6 million and the Business Tax Information System showed $468.8 million, a difference of approximately $17 million. Therefore, it is difficult to discern how these specific taxes have performed over the past 5 years.[32] In addition, the District could not provide us with projections for these specific taxes for the next 5 years.

Construction Fund Earnings. WCCA's financial advisors project that WCCA could generate about $51 million in interest earnings from bond proceeds between 1997 and 2001. The bond proceeds would be deposited in a construction fund. During the construction period, funds that are not drawn from the account would be invested to generate the $51 million.

[32]Based on the CAFR, the District's total general sales and use tax receipts averaged $453 million annually for the past 5 years (fiscal year 1992 to 1996), or an average annual growth of about 1.4 percent. The general sales and use taxes peaked in fiscal year 1995 at about $486 million, declined to about $468 in fiscal year 1996, and, based on District's forecast, are expected to surpass the 1995 level until fiscal year 1999.

WCCA Cash-on-Hand. As of July 31, 1997, WCCA has on hand approximately $72.9 million in dedicated tax revenues, with $24.4 million earmarked for the remaining predevelopment costs, and about $2.5 million budgeted for additional operating subsidy of the existing convention center for the remainder of fiscal year 1997, leaving $46 million. WCCA plans to use $30 million of this money to help finance the construction cost of the project. The remaining $16 million as well as a projected $5.8 million in additional collection for the remaining months (August and September) of fiscal year 1997 is needed to establish an operation and maintenance reserve (O&M), which is required, by the rating agencies, to be available before WCCA enters the bond market. WCCA's financial advisors estimate that about $30 million would be required for the O&M reserve. It is projected that about $22 million would be available at the end of fiscal year 1997 to be applied toward the reserve. Thus, assuming currently estimated costs are substantially accurate, WCCA needs about $114 million ($106 million plus an additional $8 million for O&M reserve) if it were to enter the market in October, as originally planned, to obtain bond financing.

WCCA is considering several financing options to close the shortfall, such as reallocation of the total amount of hotel occupancy tax from the District, sale of the existing convention center, and federal grants. However, it is uncertain at this time as to the outcome of these options. For example, the disposition of the existing convention center would not occur for some time, and it is uncertain how much WCCA would benefit from its disposition/sale, especially since there is an outstanding debt of $75 million on this center. In addition, section 304 of the 1994 Act, D.C. Code Ann. sec. 47-3206 (1981, 1996 Supp.), makes 40 percent of the dedicated hotel occupancy tax available to WCCA for financing the project while the remaining 60 percent (about $5 million annually) is allocated for other purposes. WCCA is actively seeking to gain control of the 60 percent allocated for other purposes to assist it in closing a portion of the funding gap of the project. Table 5 highlights some of the financing options that WCCA is considering to close the funding gap.

Table 5: Other Construction Financing Options for the New Convention Center

Options	Proposed revenue source	Estimated/potential funding
Third lien bonds/cash flow sale[a]	Bond proceeds	$24 million
Additional funds from debt extension[b]	Bond proceeds	$20 million
Reallocation of existing dedicated taxes[c]	Dedicated taxes of $5 million	$80 million in bond proceeds
Debt service/DSRF investment agreement[d]	Accelerated interest earnings	$12 million
Federal assistance:		
Direct grant[e] Direct loan[f] Contingent guarantee[g]	Department of Transportation and other federal agencies, e.g., Department of Commerce, Department of Treasury, & Environmental Protection Agency	$45 million
Lease of the existing convention center[h]	General Services Administration (GSA)	$20.5 million (annual GSA lease payments)
Private sector participation in new facility[i]	Naming/vending rights; vendor financing	$25 million
Sale/disposition of existing convention center[j]	Sale/lease proceeds	$40 million
Special tax/development district on existing site[k]	Leveraging of future tax revenues	$50 million

(Table notes on next page)

[a]WCCA would sell third lien debt supported by the pledged revenues at a coverage of 110 percent. Revenues remaining after the payment of the senior and junior lien debt would be used to pay principal and interest on this third lien.

[b]The term of the bond would be extended from 30 years to as many as 40 years.

[c]The Washington Convention and Visitors Association and the Mayor's Committee to Promote Washington receive a portion of the hotel occupancy tax.

[d]Debt Service/Debt Service Reserve Fund (DSRF) Investment Agreement. A trust account would be established to receive dedicated revenues to pay bondholders. Under the terms of an investment agreement, WCCA would enter into an agreement with a third party giving that party the right, into the future, to invest these funds. In exchange for the future right to invest these funds, a third party will make an upfront payment to WCCA.

[e]Certain portions of the project may be eligible for conventional federal grant assistance (mass transit and certain environmental remediation costs). WCCA is currently researching whether this project may qualify for federal grants and loans.

[f]Long-term loan made for gap funding which would be repaid from negotiated sources of revenue.

[g]Interim financing vehicle to bridge time gap between project approvals and realization of later funds.

[h]GSA leases the existing site with guaranteed nonappropriation annual payments or GSA may seek private sector development partner and subleases.

[i]Vendors of certain services (such as communications and catering) may be willing to pay a lump sum for the rights to provide these services.

[j]The existing site could be sold at some point over the next 4 years.

[k]A tax increment district is developed on the existing site and/or its environs, and the revenues generated would be collected from assessments on any taxable real estate developed within this area.

District's Comments and Our Evaluation

On August 29, 1997, we provided the Mayor of the District Government with copies of a draft of this report for review and comment. In a September 9, 1997 meeting, WCCA officials, including the Project Director, General Counsel, and the Chief Financial Officer, generally concurred with our report and provided additional information. Written comments from the Mayor are reprinted as appendix I. We have incorporated changes as appropriate throughout the report.

WCCA provided updated information concerning its progress in obtaining the necessary regulatory approvals and developing a financing plan. Specifically, WCCA stated that it appears to have obtained consensus on an

MOA that will be signed by the necessary regulatory agencies. Since the Mayor commented on this report, all parties have signed the MOA, and NCPC has scheduled hearings on the proposed convention center for September 22 and 25, 1997, to consider site and design approval for the new convention center at Mount Vernon Square, alley and street closings, as well as the urban renewal plan amendments necessary to allow construction to begin at Mount Vernon Square. These are key issues that must be resolved before WCCA can proceed with the project.

WCCA told us that it has a financing plan to eliminate the funding gap for the proposed convention center. This plan proposes to reallocate the Hotel Occupancy Tax revenues imposed by D.C. Code Section 47-3206—and now available to the Washington Convention and Visitors Association and the Mayor's Committee to Promote Washington—for the payment of debt service for the new convention center. In addition, the term of convention center bonds would be authorized to mature in up to 40 years. Current law limits bond maturity to 30 years from issuance. WCCA is drafting legislation to authorize the above changes. Approval of these or alternative steps are key issues in moving ahead with the convention center project.

We are sending copies of this report to the Chairmen and Ranking Minority Members of the Senate and House Committees on Appropriations and their subcommittees on the District of Columbia; and the Senate Committee on Governmental Affairs, Subcommittee on Oversight of Government Management, Restructuring and the District of Columbia, and the Ranking Minority Member of your Subcommittee. Major contributors to this report are listed in appendix II. If you or your staff need further information, please contact me at (202) 512-4476.

Sincerely yours,

Gloria L. Jarmon

Gloria L. Jarmon
Director, Civil Audits

Comments From the District of Columbia

THE DISTRICT OF COLUMBIA
WASHINGTON, D.C. 20001

MARION BARRY, JR.
MAYOR

September 11, 1997

Mr. Gene L. Dodaro
Assistant Comptroller General
United States General Accounting Office
441 G Street, NW
Washington, DC 20548

Dear Mr. Dodaro:

Thank you for the opportunity to review the draft version of GAO's latest status report on the proposed new convention center. As you know, the proposed convention center at Mount Vernon Square is the District's largest and most important economic development project. It is a key component of the continued expansion of the District's economy. Successful completion will produce millions of dollars of new revenue for our city as well as create a substantial number of new hospitality related jobs.

The draft report produced by your staff was shared with the Washington Convention Center Authority (WCCA). WCCA staff, who meet regularly with GAO personnel, reviewed the draft report and have provided some suggested revisions. The report was also shared with WCCA's financial consultants who have made some revisions that would improve the information provided by the report.

You should also be aware that WCCA has made progress since July in working toward the necessary approvals and developing a financing plan that eliminates the funding gap associated with the new convention center. As the draft report indicates, WCCA has been attempting to address concerns raised by neighborhood groups and historic preservationists about the adverse impacts the proposed new convention center would have on historic landmarks in the surrounding area. Recently, WCCA appears to have obtained consensus on a Memorandum of Agreement (MOA) that addresses these concerns and it appears that all the necessary parties, i.e., the Advisory Council on Historic Preservation (ACHP), the National Capital Planning Commission (NCPC), and the District of Columbia State Historic Preservation Officer (DCSHPO), are prepared to sign the MOA.

Gene L. Dodaro
September 11, 1997
Page Two

This apparent consensus on an MOA will now allow NCPC to consider giving both site and design approval for the new convention center at Mount Vernon Square. NCPC will also give consideration to the alley and street closings, and the urban renewal plan amendments necessary to allow construction to begin at Mount Vernon Square. In anticipation of an MOA signed by the necessary parties, NCPC has scheduled hearings on the proposed new convention center on September 22 and 25, 1997.

With the assistance of its financial advisors and bond underwriters, WCCA has identified a financial plan that will eliminate the current funding gap for the new convention center. Under this plan, the Hotel Occupancy Tax imposed by D.C. Code §47-3206. A part of the revenues from this tax are directed to the Washington Convention and Visitors Association and the D.C. Committee to Promote, which engage in marketing efforts to attract conventions and visitors to the District. WCCA would reallocate these tax revenues for the payment of debt service and extend the term of convention center bonds to approximately 35 to 40 years. It is estimated these steps would give WCCA the ability fund on additional $80 million dollars in bond proceeds, thereby eliminating the funding gap. It is anticipated that the financing could be completed in late fall of this year after the Council, Financial Responsibility and Management Assistance Authority and Congress approve the necessary legislation. A groundbreaking would then follow in late 1997 or early 1998.

As always, the District of Columbia and WCCA appreciate the review of this project by GAO. We are confident that after GAO's review, Congress will be prepared to allow WCCA to move forward with the District's most important economic development project.

Sincerely,

Marion Barry

Marion Barry, Jr.
Mayor

cc: Louanner Peters
Chairperson
Washington Convention Center Authority

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