Discovery Green Conservancy

Financial Statements
and Independent Auditors' Report
for the years ended June 30, 2018 and 2017

Blazek & Vetterling
CERTIFIED PUBLIC ACCOUNTANTS

Independent Auditors' Report

To the Board of Directors of
Discovery Green Conservancy:

We have audited the accompanying financial statements of Discovery Green Conservancy, which comprise the statements of financial position as of June 30, 2018 and 2017 and the related statements of activities and of cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

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

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform our audits to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, financial position of Discovery Green Conservancy as of June 30, 2018 and 2017 and the changes in its net assets and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Blazek & Vetterling

September 26, 2018

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Discovery Green Conservancy

Statements of Financial Position as of June 30, 2018 and 2017

	2018	2017
ASSETS		
Cash	$ 101,704	$ 1,365,094
Restaurant rent receivable	95,712	106,968
Receivable from Houston First Corporation *(Note 8)*	80,018	214,662
Prepaids and other receivables	122,415	150,817
Pledges receivable	53,634	184,845
Cash designated or restricted for capital improvements	8,819,071	967,003
Property and equipment, net *(Note 4)*	37,496,749	37,311,528
TOTAL ASSETS	$ 46,769,303	$ 40,300,917
LIABILITIES AND NET ASSETS		
Liabilities:		
Accounts payable	$ 343,192	$ 264,574
Accrued salaries and benefits	182,628	177,263
Deferred contribution revenue	520,750	405,000
Deferred venue revenue *(Note 9)*	499,427	574,443
Total liabilities	1,545,997	1,421,280
Net assets:		
Unrestricted *(Note 5)*	36,771,860	38,363,384
Temporarily restricted *(Note 6)*	8,451,446	516,253
Total net assets	45,223,306	38,879,637
TOTAL LIABILITIES AND NET ASSETS	$ 46,769,303	$ 40,300,917

See accompanying notes to financial statements.

Discovery Green Conservancy

Statement of Activities for the year ended June 30, 2018

	UNRESTRICTED	TEMPORARILY RESTRICTED	TOTAL
REVENUE:			
Venue rental *(Note 9)*	$ 752,580		$ 752,580
Management fees from Houston First Corporation *(Note 8)*	2,397,457		2,397,457
Restaurant rental income *(Note 10)*	819,296		819,296
Contributions *(Note 3)*	801,351	$ 9,216,146	10,017,497
In-kind contributions *(Note 7)*	462,879		462,879
Other income	(61,203)		(61,203)
Total revenue	5,172,360	9,216,146	14,388,506
Net assets released from restrictions:			
Expiration of time restrictions	105,861	(105,861)	
Capital expenditure	1,147,932	(1,147,932)	
Satisfaction of purpose restrictions	27,160	(27,160)	
Total	6,453,313	7,935,193	14,388,506
EXPENSES:			
Program expenses:			
Park operations	6,834,501		6,834,501
Park operations – in-kind *(Note 7)*	320,559		320,559
Total program expenses	7,155,060		7,155,060
Management and general	593,309		593,309
Fundraising	296,468		296,468
Total expenses	8,044,837		8,044,837
CHANGES IN NET ASSETS	(1,591,524)	7,935,193	6,343,669
Net assets, beginning of year	38,363,384	516,253	38,879,637
Net assets, end of year	$ 36,771,860	$ 8,451,446	$ 45,223,306

See accompanying notes to financial statements.

Discovery Green Conservancy

Statement of Activities for the year ended June 30, 2017

	UNRESTRICTED	TEMPORARILY RESTRICTED	TOTAL
REVENUE:			
Venue rental *(Note 9)*	$ 2,373,430		$ 2,373,430
Management fees from Houston First Corporation *(Note 8)*	1,553,941		1,553,941
Restaurant rental income *(Note 10)*	1,281,055		1,281,055
Contributions *(Note 3)*	941,390	$ 92,782	1,034,172
In-kind contributions *(Note 7)*	861,913		861,913
Special events	169,513		169,513
Direct donor benefits	(24,067)		(24,067)
Total revenue	7,157,175	92,782	7,249,957
Net assets released from restrictions:			
Expiration of time restrictions	105,532	(105,532)	
Capital expenditure	82,474	(82,474)	
Satisfaction of purpose restrictions	7,750	(7,750)	
Total	7,352,931	(102,974)	7,249,957
EXPENSES:			
Program expenses:			
Park operations	6,649,883		6,649,883
Park operations – in-kind *(Note 7)*	703,146		703,146
Total program expenses	7,353,029		7,353,029
Management and general	653,715		653,715
Fundraising	217,532		217,532
Total expenses	8,224,276		8,224,276
CHANGES IN NET ASSETS	(871,345)	(102,974)	(974,319)
Net assets, beginning of year	39,234,729	619,227	39,853,956
Net assets, end of year	$ 38,363,384	$ 516,253	$ 38,879,637

See accompanying notes to financial statements.

Discovery Green Conservancy

Statements of Cash Flows for the years ended June 30, 2018 and 2017

	2018	2017
CASH FLOWS FROM OPERATING ACTIVITIES:		
Changes in net assets	$ 6,343,669	$ (974,319)
Adjustments to reconcile changes in net assets to net cash provided (used) by operating activities:		
Depreciation	928,216	912,916
Contributions restricted for property and equipment	(9,066,656)	
Changes in operating assets and liabilities:		
Restaurant rent receivable	11,256	14,646
Receivable from Houston First Corporation	134,644	(214,662)
Prepaids and other receivables	28,402	(37,872)
Pledges receivable	131,211	25,655
Accounts payable	78,618	169,785
Accrued salaries and benefits	5,365	(3,284)
Deferred revenue	40,734	907,416
Net cash provided (used) by operating activities	(1,364,541)	800,281
CASH FLOWS FROM INVESTING ACTIVITIES:		
Net change in cash designated or restricted for capital improvements	(7,852,068)	32,174
Cash paid for property and equipment	(1,113,437)	(196,372)
Net cash used by investing activities	(8,965,505)	(164,198)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from contributions restricted for property and equipment	9,066,656	48,395
NET CHANGE IN CASH	(1,263,390)	684,478
Cash, beginning of year	1,365,094	680,616
Cash, end of year	$ 101,704	$ 1,365,094

See accompanying notes to financial statements.

NOTE 1 – ORGANIZATION

Organization – Discovery Green Conservancy (the Conservancy) is a nonprofit organization incorporated in 2004. The Conservancy is responsible for the operation and promotion of a downtown park (Discovery Green) located across from the George R. Brown Convention Center in downtown Houston, Texas.

In 2004, the Conservancy entered into a Development Management Agreement with the Houston Downtown Park Corporation (the Corporation) for the design, development, financing, and construction management of Discovery Green. The Corporation is a Texas nonprofit local government corporation created by the City of Houston (the City) to acquire and hold land for Discovery Green and to contract for the design, development, construction, operation, and promotion of Discovery Green. Upon acquisition of approximately twelve acres of land for Discovery Green, the Conservancy transferred the land to the Corporation, but retained an amenities easement. The amenities easement is used for light retail, restaurant, and other amenities for park users.

The Conservancy entered into an Operating Agreement with the Corporation to operate Discovery Green for an initial term of 50 years commencing in April 2008, the date of the park dedication. The agreement includes two 25-year renewal terms. Under the Operating Agreement, the Conservancy is paid an annual management fee by the City through Houston First Corporation, a City component unit (see Note 9). The Conservancy must operate Discovery Green in accordance with the Operating Agreement, which requires that the property be used solely as an urban park and restricts the types of events that can be held at Discovery Green. It also gives the right to the Conservancy to market Discovery Green and to establish reasonable venue rental rates and park rules.

Federal income tax status – The Conservancy is exempt from federal income tax under §501(c)(3) of the Internal Revenue Code and is classified as a public charity under §509(a)(1) and §170(b)(1)(A)(vi).

NOTE 2 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Cash – Demand deposits exceed the federally insured limit per depositor per institution.

Pledges receivable that are expected to be collected within one year are reported at net realizable value. Amounts expected to be collected in future years are discounted to estimate the present value of future cash flows.

Property and equipment is reported at cost, if purchased, or at fair value at the date of gift, if donated. The Conservancy capitalizes property and equipment that have a cost or fair value of $1,000 or greater and an estimated useful life of more than one year. The Conservancy recognizes depreciation for leasehold improvements and furniture, fixtures and equipment using the straight-line method over the estimated useful lives of the assets, ranging from 5 to 50 years. Works of art are not depreciated.

Net asset classification – Contributions and the related net assets are classified based on the existence or absence of donor-imposed restrictions, as follows:

- *Unrestricted net assets* include those net assets whose use is not restricted by donor-imposed stipulations, even though their use may be limited in other respects, such as by contract or board designation.
- *Temporarily restricted net assets* include contributions restricted by the donor for specific purposes or time periods. When a purpose restriction is accomplished or a time restriction ends, temporarily restricted net assets are released to unrestricted net assets.

Venue rental income and management fees are recognized when the related services are provided. Venue rentals received in advance are reported as deferred venue revenue until earned.

Restaurant rental income (excluding contingent rentals) is recognized on a straight-line basis over the scheduled lease term. Contingent rental income is recognized as revenue on a monthly basis as the leasee achieves the specified target.

Contributions are recognized as revenue at fair value when an unconditional commitment is received from the donor. Contributions received with donor stipulations that limit their use are classified as restricted support. Conditional contributions are recognized in the same manner when the conditions are substantially met. Conditional contributions in which the funds are received in advance are recorded as deferred contribution revenue.

In-kind materials, use of facilities, and services – In-kind materials and use of facilities are recognized at fair value as unrestricted contributions when an unconditional commitment is received from the donor. The related expense is recognized as the item is used. Contributions of services are recognized when services received (a) create or enhance nonfinancial assets or (b) require specialized skills, are provided by individuals possessing those skills, and would typically need to be purchased if not provided by donation.

Special event revenue is recognized when the event occurs. Amounts received in advance are reported as deferred contribution revenue until earned.

Advertising costs are expensed as incurred. Advertising expense of $461,179 was recognized in 2018 and $842,924 in 2017.

Estimates – Management must make estimates and assumptions to prepare financial statements in accordance with generally accepted accounting principles. These estimates and assumptions affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities, the amounts of reported revenue and expenses, and the allocation of expenses among various functions. Actual results could vary from the estimates that were used.

Recent financial accounting pronouncements – In August 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2016-14, *Not-for-Profit Entities (Topic 958): Presentation of Financial Statements of Not-for-Profit Entities.* The amendments in this ASU are aimed at providing more useful information to users of not-for-profit financial statements. Under this ASU, net assets will be presented in two classes: *net assets with donor restrictions* and *net assets without donor restrictions* and underwater endowments will be grouped with *net assets with donor restrictions.* New or enhanced disclosures will be required about the nature and composition of net assets, and the liquidity and availability of resources for general operating expenditures within one year of the balance sheet date. Expenses will be required to be presented by both nature and function and investment return will be presented net of external and direct internal investment expenses. Absent explicit donor stipulations, restrictions on long-lived assets will expire when assets are placed in service. The Conservancy is required to adopt this ASU for fiscal year 2019. Adoption of this ASU will impact the presentation and disclosures of the financial statements.

In June 2018, the FASB issued ASU 2018-08, *Not-for-Profit Entities (Topic 958): Clarifying the Scope and the Accounting Guidance for Contributions Received and Contributions Made*. The amendments in this ASU clarify and improve current guidance about whether a transfer of assets (or the reduction, settlement, or cancellation of liabilities) is a contribution or an exchange transaction and provide additional guidance on determining whether a contribution is conditional or unconditional. This ASU could impact the timing of revenue recognition and the financial statement disclosures related to such transactions. The Conservancy is required to apply the amendments in its June 30, 2020 financial statements. The amendments should be applied on a modified prospective basis, but retrospective application also is permitted. Management has not determined the eventual method of adoption of the ASU or the impact on the financial statements.

In November 2016, FASB issued ASU 2016-18, *Statement of Cash Flows – Restricted Cash,* which requires the statement of cash flows to explain the change in the total of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents. Prior to adoption, restricted cash and cash equivalents were excluded from beginning and ending cash and cash equivalents in the statement of cash flows. Discovery Green is required to adopt this ASU for fiscal year 2020 and must be applied retrospectively. This change will have no impact on net assets or changes in net assets.

NOTE 3 – CONDITIONAL CONTRIBUTIONS

The Conservancy enters into sponsorship agreements with organizations in which the sponsoring organization is to be a titled sponsor for certain events held by the Conservancy. In fiscal year 2016, the Conservancy entered into a sponsorship agreement with an organization totaling $775,000. As of June 30, 2018, $220,000 has been recognized as contribution revenue as the conditions have been met. At June 30, 2018 and 2017, $215,000 and $360,000, respectively, is included in deferred contribution revenue related to this agreement. At June 30, 2018, $550,000 has not been recognized as the conditions have not been met. Additionally, at June 30, 2018 and 2017, $260,750 and $50,000, respectively, of deferred special event revenue is included in deferred contribution revenue as the events had not occurred as of the respective fiscal year ends.

NOTE 4 – PROPERTY AND EQUIPMENT

Property and equipment is comprised of the following:

	2018	2017
Leasehold improvements	$ 36,649,154	$ 35,787,313
Furniture, fixtures and equipment	2,486,965	2,483,952
Depreciable property and equipment, at cost	39,136,119	38,271,265
Accumulated depreciation	(9,042,243)	(8,115,476)
Depreciable property and equipment, net	30,093,876	30,155,789
Dubuffet sculpture	6,786,119	6,786,119
Art exhibit and sculpture	170,757	170,757
Construction in progress	445,997	198,863
Property and equipment, net	$ 37,496,749	$ 37,311,528

NOTE 5 – UNRESTRICTED NET ASSETS

Unrestricted net assets consist of the following:

	2018	2017
Property and equipment, net	$ 37,050,752	$ 37,112,665
Undesignated	(778,892)	750,719
Board-designated maintenance fund	500,000	500,000
Total unrestricted net assets	$ 36,771,860	$ 38,363,384

NOTE 6 – TEMPORARILY RESTRICTED NET ASSETS

Temporarily restricted net assets are available for the following purposes:

	2018	2017
Renovation and repairs campaign	$ 8,187,243	$ 268,519
Dubuffet sculpture maintenance fund	198,484	198,484
Bayou Center Music Series	42,680	
Time restricted	23,039	49,250
Total temporarily restricted net assets	$ 8,451,446	$ 516,253

NOTE 7 – IN-KIND CONTRIBUTIONS

In-kind contributions were recognized as follows:

	2018	2017
Advertising – park operations	$ 320,559	$ 673,518
Advertising – management and general	110,865	145,327
Legal services – management and general	9,760	13,440
Other – park operations	21,695	29,628
Total in-kind contributions	$ 462,879	$ 861,913

NOTE 8 – HOUSTON FIRST CORPORATION MANAGEMENT FEES

In March 2017, the Conservancy entered into an annual agreement with Houston First Corporation to manage the event scheduling at Avenida Plaza with renewal for four one-year terms. The annual management fee is $120,000 plus costs of performances up to $1,000,000 per year. Revenue of $1,232,646 and $402,749 was reported in fiscal years 2018 and 2017, respectively. At June 30, 2018 and 2017, accounts receivable of $80,018 and $214,662, respectively, were due from Houston First Corporation.

The Conservancy also reported management fees for operating Discovery Green totaling $1,164,811 and $1,151,192 in fiscal years 2018 and 2017, respectively.

NOTE 9 – FACILITY LICENSE AGREEMENT

In 2017, the Conservancy entered into an agreement with a communications company to enhance wireless capabilities at Discovery Green by creating a common wireless communication network available to all wireless carriers by utilizing existing structures and therefore, minimizing the visual impact on Discovery Green. The effective date of the agreement was August 2016 for an initial term of ten years with automatic renewals of three additional five-year terms unless written notice is provided by either party within 180 days. The fee for the initial ten-year term is $550,000, which was received in fiscal year 2017. As of June 30, 2018 and 2017, $440,000 and $495,000, respectively, was reported as deferred revenue. Over the initial term of the agreement, Discovery Green will recognize future rent revenue as follows:

2019	$ 55,000
2020	55,000
2021	55,000
2022	55,000
2023 and thereafter	220,000
Total minimum lease payments	$ 440,000

NOTE 10 – RESTAURANT LEASE

In 2007, the Conservancy entered into a License and Concession Agreement with an organization for the construction and operation of the restaurants at Discovery Green. The initial term of the lease is ten years with two five-year renewal options. Under the agreement, the Conservancy receives a base rent determined as a percentage of annual gross revenue with a minimum base rent of $500,000 per year during the renewal term of the lease (contingent rent). The contingent rent is adjusted for inflation after the initial term. The agreement provides for additional rent equal to the amortization of a pre-opening allowance of $1,020,000, plus interest. The payment of the additional rent commenced in October 2008 with the final payment made in December 2017.

Contingent rent of $667,472 and $1,067,860 is included in restaurant rental income for fiscal years 2018 and 2017, respectively.

Restaurant leasehold improvements are approximately $8.9 million at June 30, 2018, and are included in property and equipment in the statement of financial position. Accumulated depreciation on the leasehold improvements under the operating lease was approximately $1,879,000 and $1,700,000 at June 30, 2018 and 2017, respectively.

NOTE 11 – SUBSEQUENT EVENTS

Management has evaluated subsequent events through September 26, 2018, which is the date that the financial statements were available for issuance. As a result of this evaluation, no events were identified that are required to be disclosed or would have a material impact on reported net assets or changes in net assets.