Financial Statements

State Fair of Texas
Years Ended December 31, 2017 and 2016
With Report of Independent Auditors

Ernst & Young LLP

Building a better
working world

State Fair of Texas

Financial Statements

Years Ended December 31, 2017 and 2016

Contents

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Report of Independent Auditors

The Board of Directors
State Fair of Texas

We have audited the accompanying financial statements of State Fair of Texas, a not-for-profit Texas corporation, which comprise the statements of financial position as of December 31, 2017 and 2016, and the related statements of activities and 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 conformity with U.S. generally accepted accounting principles; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free of material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in 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 involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the 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, the financial position of State Fair of Texas at December 31, 2017 and 2016, and the results of its changes in net assets and its cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

Ernst + Young LLP

April 17, 2018

State Fair of Texas

Statements of Financial Position

	December 31 2017	December 31 2016
Assets		
Current assets:		
Cash	**$ 139,041**	$ 344,299
Restricted cash for Fair Park major maintenance projects	**6,534,355**	–
Investments	**46,376,404**	49,267,357
Accounts receivable, less allowances for uncollectible accounts of $10,190 and $24,427 in 2017 and 2016, respectively	**246,166**	330,345
Pledges receivable, net	**–**	850
Inventories, net	**278,935**	289,263
Prepaid expenses	**252,129**	329,336
Total current assets	**53,827,030**	50,561,450
Property and leasehold improvements, at cost:		
Midway improvements	**13,998,323**	13,978,714
Amusement rides	**21,809,038**	21,697,034
Buildings and improvements	**20,594,525**	18,675,336
Furniture, fixtures, and equipment	**9,669,965**	9,068,649
Construction-in-progress	**342,162**	49,379
Land	**5,058,422**	5,058,422
Total property and leasehold improvements	**71,472,435**	68,527,534
Less accumulated depreciation and amortization	**(45,212,734)**	(41,761,657)
Property and leasehold improvements, net	**26,259,701**	26,765,877
Pledges receivable, net	**–**	14,315
Deferred compensation	**1,431,653**	1,146,151
Total assets	**$ 81,518,384**	$ 78,487,793
Liabilities and net assets		
Current liabilities:		
Accounts payable and accrued liabilities	**$ 6,615,831**	$ 7,814,827
Accrued Fair Park major maintenance projects	**6,912,208**	2,177,626
Current advanceable term loan payable	**–**	1,011,491
Other long-term pledges	**–**	14,315
Total current liabilities	**13,528,039**	11,018,259
Long-term advanceable term loan payable	**–**	1,095,783
Deferred rent liability	**8,632,770**	7,936,890
Deferred compensation	**1,431,653**	1,146,151
Total liabilities	**23,592,462**	21,197,083
Net assets:		
Unrestricted, including $10.6 million and $9.5 million of Board-designated funds in 2017 and 2016, respectively	**56,886,703**	56,136,436
Temporarily restricted	**997,550**	1,112,605
Permanently restricted	**41,669**	41,669
Total net assets	**57,925,922**	57,290,710
Total liabilities and net assets	**$ 81,518,384**	$ 78,487,793

See accompanying notes.

State Fair of Texas

Statements of Activities

Years Ended December 31, 2017 and 2016

	2017				2016			
	Unrestricted	**Temporarily Restricted**	**Permanently Restricted**	**Total**	**Unrestricted**	**Temporarily Restricted**	**Permanently Restricted**	**Total**
Revenues:								
Concessions and admissions	**$ 44,292,956**	**$ –**	**$ –**	**$ 44,292,956**	$ 46,699,473	$ –	$ –	$ 46,699,473
Exhibit space and other rentals	**5,066,587**	**–**	**–**	**5,066,587**	5,066,219	–	–	5,066,219
Contributions	**2,784,161**	**523,445**	**–**	**3,307,606**	2,508,915	478,705	–	2,987,620
Interest income and dividends	**317,850**	**–**	**–**	**317,850**	111,925	–	–	111,925
Other	**56,531**	**–**	**–**	**56,531**	48,809	–	–	48,809
Net assets released from restrictions	**638,500**	**(638,500)**	**–**	**–**	544,812	(544,812)	–	–
Total revenues	**53,156,585**	**(115,055)**		**53,041,530**	54,980,153	(66,107)	–	54,914,046
Expenses:								
Fair-time expenses	**19,301,462**	**–**	**–**	**19,301,462**	19,448,629	–	–	19,448,629
Maintenance and repairs	**12,647,593**	**–**	**–**	**12,647,593**	10,109,930	–	–	10,109,930
Non-fair-time events and exhibits	**536,045**	**–**	**–**	**536,045**	679,764	–	–	679,764
Salaries and wages	**8,654,215**	**–**	**–**	**8,654,215**	8,220,191	–	–	8,220,191
General and administrative	**9,969,468**	**–**	**–**	**9,969,468**	8,969,061	–	–	8,969,061
Interest	**–**	**–**	**–**	**–**	38,581	–	–	38,581
Depreciation and amortization	**3,458,268**	**–**	**–**	**3,458,268**	3,687,739	–	–	3,687,739
Total expenses	**54,567,051**	**–**	**–**	**54,567,051**	51,153,895	–	–	51,153,895
Excess of expenses over revenues	**(1,410,466)**	**(115,055)**	**–**	**(1,525,521)**	3,826,258	(66,107)	–	3,760,151
Realized and unrealized investment gains	**2,160,733**	**–**	**–**	**2,160,733**	928,215	–	–	928,215
Change in net assets	**750,267**	**(115,055)**	**–**	**635,212**	4,754,473	(66,107)	–	4,688,366
Net assets at beginning of year	**56,136,436**	**1,112,605**	**41,669**	**57,290,710**	51,381,963	1,178,712	41,669	52,602,344
Net assets at end of year	**$ 56,886,703**	**$ 997,550**	**$ 41,669**	**$ 57,925,922**	$ 56,136,436	$ 1,112,605	$ 41,669	$ 57,290,710

See accompanying notes.

State Fair of Texas

Statements of Cash Flows

	Year Ended December 31 2017	2016
Operating activities		
Change in net assets	**$ 635,212**	$ 4,688,366
Adjustments to reconcile change in net assets to net cash provided by operating activities:		
Realized and unrealized investment gains	**(2,160,733)**	(928,215)
Depreciation and amortization	**3,458,268**	3,687,739
Changes in assets and liabilities:		
Decrease in accounts receivable	**84,179**	226,300
Decrease in pledges receivable, net	**850**	–
Decrease in inventories, net	**10,328**	18,708
Decrease (increase) in prepaid expenses	**77,207**	(6,177)
Increase in accounts payable, accrued liabilities, and deferred rent	**4,231,468**	4,227,613
Net cash provided by operating activities	**6,336,779**	11,914,334
Investing activities		
Capital expenditures for property and leasehold improvements	**(2,952,094)**	(1,249,510)
Purchase of investments	**(6,804,762)**	(10,466,051)
Sales and maturities of investments	**5,322,093**	10,382
Net cash used in investing activities	**(4,434,763)**	(11,705,179)
Financing activities		
Payments on credit facilities	**(2,107,274)**	(1,011,491)
Net cash used in financing activities	**(2,107,274)**	(1,011,491)
Net decrease in cash	**(205,258)**	(802,336)
Cash at beginning of year	**344,299**	1,146,635
Cash at end of year	**$ 139,041**	$ 344,299
Cash payments for interest	**$ –**	$ 38,581

See accompanying notes.

1. Nature of Operations

State Fair of Texas (the Fair) is a not-for-profit Texas corporation organized to conduct an annual fair. The Fair's mission is to celebrate all things Texan by promoting agriculture, education, and community involvement through quality entertainment in a family-friendly environment.

2. Summary of Significant Accounting Policies

A summary of significant accounting policies consistently applied in the preparation of the accompanying consolidated financial statements under U.S. generally accepted accounting principles (GAAP) is as follows:

Net Assets

Unrestricted Net Assets – Unrestricted net assets result from the operation of the annual fair, non-fair-time events, and general operations of the organization, including a reserve fund required by an agreement with the City of Dallas (see Note 3). In 2017 and 2016, the board-designated reserve fund was maintained at $10.6 million and $9.5 million, respectively. Realized and unrealized gains from reserve fund investments are included in realized and unrealized investment gains. Interest and dividends from reserve fund investments are included in interest income and dividends.

Temporarily Restricted Net Assets – Temporarily restricted net assets are those net assets whose use has been limited by the donor to a specific time period or purpose. These net assets are transferred to unrestricted net assets when the donor restriction is met. Temporarily restricted net assets comprise contributions received that will be awarded as scholarships in future years.

Permanently Restricted Net Assets – Permanently restricted net assets require that the principal be invested in perpetuity and that only the income be expended for designated purposes. Permanently restricted net assets represent a livestock premium endowment contribution received by the Fair. The interest received from this endowment is restricted by the donor for purposes of livestock auction premiums at the annual youth livestock auction.

Net Assets Released From Restrictions – Net assets were released from donor restrictions by making scholarship payments (net of scholarship forfeitures) of $638,500 and $544,812 in 2017 and 2016, respectively.

2. Summary of Significant Accounting Policies (continued)

Cash and Investments

Cash represents funds on hand for current operations. At December 31, 2017 and 2016, cash equivalents of $29,531,578 and $36,778,636, respectively, are included with investments for financial statement presentation. Restricted cash at December 31, 2017 represents cash set aside for maintenance projects (See Note 3). Cash equivalents include investments in highly liquid securities with original maturities of approximately three months or less. Investments are recorded at fair value (see Note 5 and Note 8).

Accounts Receivable

Accounts receivable represent amounts due from the operation of the annual fair. The Fair maintains an allowance for estimated amounts of accounts receivable that may not be collectible based on historical collections.

Inventories

Inventories are stated at the lower of cost or market. Cost is determined using the average-cost method. For the years ended December 31, 2017 and 2016, the Fair recorded an inventory valuation reserve of $20,826 and $24,099, respectively.

Property and Leasehold Improvements

Property and leasehold improvements are stated at cost. Depreciation and amortization are recorded using the straight-line method using the lesser of the estimated useful lives or the lease term of the respective assets, ranging from 3 to 25 years. Management regularly considers whether facts or circumstances exist that would indicate that the carrying values of the property and leasehold improvements are impaired. The Fair has not recorded an impairment loss in 2017 or 2016 as a result of such consideration.

2. Summary of Significant Accounting Policies (continued)

Revenue Recognition

The Fair recognizes revenue when (i) persuasive evidence of an arrangement exists, (ii) delivery has occurred or services have been rendered, (iii) the sales price is fixed and determinable, and (iv) collectibility is reasonably assured. Generally, these criteria are met upon the receipt of cash for admission tickets, games, parking, and concessions. The Fair recognizes revenue for concessions, net of commissions paid to operators, in accordance with Accounting Standards Codification (ASC) 605-45, *Revenue Recognition – Principal Agent Considerations*. Commissions paid to operators were $36 million and $38 million for the years ended December 31, 2017 and 2016, respectively. The Fair also receives rental revenues for exhibit space during fair time, which are recognized ratably as the services are provided.

Nonprofit Financial Statement Presentation

In August 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2016-14, *Presentation of Financial Statements of Not-for-Profit Entities*. Among other requirements, the ASU will require nonprofits to present two classes of net assets, those with and those without donor restrictions. It will also require information about expenses to be reported in one location that disaggregates functional expense classifications by their natural classification, and the nonprofit will be required to provide qualitative and quantitative information about how they manage their liquidity and quantitative information about the availability of financial assets at the balance sheet date to meet cash needs for general expenditures within one year of that date. The ASU is effective for annual financial statements issued for fiscal years beginning after December 15, 2017.

Revenue From Contracts With Customers

In May 2014, the FASB issued a new revenue accounting standard, together with subsequent amendments, updates, and extension of the effective date (collectively, the New Revenue Standard), which supersedes most existing revenue guidance.

The New Revenue Standard provides for a single comprehensive principles-based standard for revenue recognition through the application of the following five-step process:

Step1: Identify the contract(s) with a customer.

Step 2: Identify performance obligations in the contract.

2. Summary of Significant Accounting Policies (continued)

Step 3: Determine the transaction price.

Step 4: Allocate the transaction price to the performance obligations in the contract.

Step 5: Recognize revenue when (or as) the entity satisfies a performance obligation.

This five-step process will require significant management judgment in addition to changing the way many companies recognize revenue in their financial statements. Additionally, and among other provisions, the New Revenue Standard requires expanded quantitative and qualitative disclosures, including disclosure about the nature, amount, timing and uncertainty of revenue.

The provisions of the New Revenue Standard are effective for annual periods beginning after December 15, 2018, including interim periods within those years, by applying either the full retrospective method or the cumulative catch-up transition method. The full retrospective method requires application of the provisions of the New Revenue Standard for all periods presented, while the cumulative catch-up transition method requires the application of the provisions of the New Revenue Standard as of the date of adoption with the cumulative effect of the retrospective application of the provisions as an adjustment through retained earnings. Early adoption is permitted starting with annual periods beginning after December 31, 2016. Currently, the Fair is assessing the effects of adopting the New Revenue Standard. The Fair does not plan to early adopt.

Leases

In February 2016, the FASB issued ASU 2016-02, codifying ASC 842, *Leases*. This requires lessees to recognize leases on-balance sheet and disclose key information about leasing arrangements. Leases will be recognized as finance or operating, with recognition affecting the pattern and classification of expense recognition in the statement of activities. The provisions of the Standard are effective for annual periods beginning after December 15, 2019; early adoption is permitted starting with annual periods beginning after December 31, 2016. Currently, the Fair is assessing the effects of adopting the Lease Standard. The Fair does not plan to early adopt.

2. Summary of Significant Accounting Policies (continued)

Expense Categories

Fair-time expenses include all incremental costs associated with setup, operation, and takedown of the annual fair. Salaries and wages consist of payroll and related costs for all full-time and part-time employees. General and administrative expenses consist of general corporate overhead incurred by the Fair for its operations. Maintenance and repair expenses consist of the general maintenance and repairs associated with the operation of the annual fair, as well as the expenses associated with major maintenance projects the Fair will undertake for the year (see Note 3).

Advertising Costs

Advertising costs, which are expensed as incurred, were $1.8 million and $1.7 million for the years ended December 31, 2017 and 2016, respectively, and are included in general and administrative expense on the statements of activities.

Income Taxes

The Fair is exempt from federal income taxes under Section 501(a) of the Internal Revenue Code (IRC) as an organization described in Section 501(c)(3). The Fair receives certain contributions to partially offset the costs of various events at the annual fair. The Fair believes such contributions are related to its tax-exempt purpose and, accordingly, excludes such amounts from its unrelated business income computation.

Risk Concentration

Financial instruments that potentially subject the Fair to concentrations of credit risk are primarily marketable securities (including cash equivalents) and accounts receivable. The Fair places its investments in common stocks and bonds issued by publicly traded corporations and fixed-income securities issued by federal agencies. The Fair maintains an allowance for losses based upon the expected collectibility of all accounts receivable. Certain deposit amounts exceed current Federal Deposit Insurance Corporation insurance limitations at December 31, 2017 and 2016.

2. Summary of Significant Accounting Policies (continued)

Use of Estimates

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates.

3. Relationship With the City of Dallas

Fair Park Agreement

The annual fair is held on the premises owned by the City of Dallas (the City) known as Fair Park

In 2003, the Fair entered into the Fair Park Agreement (the Agreement) with the City, which gives possession and occupancy of Fair Park to the Fair for approximately 24 days in September and October for the operation of the annual fair and the University of Texas-University of Oklahoma football game in the Cotton Bowl Stadium (Cotton Bowl) and for a period not to exceed 60 days prior to the annual fair and 30 days after the annual fair for setup and takedown, respectively. The Fair is also responsible for the operation of the midway area of Fair Park throughout the year. The initial term of the Agreement expires on January 1, 2028, with two automatic five-year extended terms unless the City or the Fair elects not to extend the Agreement.

In 2017, the Fair and the City clarified terms of the Agreement in a memorandum of understanding (the MOU) with a commencement date of June 28, 2017.The MOU confirms both parties understanding and application of certain provisions and terms of the Fair Park contract between the City and the State Fair of Texas and does not modify, alter, or amend the original Fair Park contract.

Contractual Payments

In exchange for use of Fair Park during the period of the fair, the Fair pays the City an annual escalating rental fee, which the City is required to place in a special account to be used only for the operation, maintenance, development, and improvement of Fair Park. Additionally, in accordance with the Agreement, the Fair pays an annual $50,000 marketing fee to the City and is required to spend at least $150,000 annually on community outreach programs and cultural

3. Relationship With the City of Dallas (continued)

facilities within Fair Park. In 2017 and 2016, the Fair spent $221,000 and $239,639, respectively, on payments directly to Fair Park cultural facilities. The marketing fee and cultural facility payments are reflected as an expense in the general and administrative category on the statements of activities.

In November 2006, the First Amendment (the Amendment) to the Agreement was executed. The Amendment provides that the Fair will perform or fund a maximum of $19.5 million in improvements to the Cotton Bowl, including installation of a high-definition scoreboard and sound system, design and engineering, seating replacement, concrete repair and weatherproofing, and cleaning and refurbishment of interior and exterior surfaces. Through December 31, 2007, the Fair incurred and funded to the City the maximum commitment of $19.5 million per the Amendment. In exchange, the City will provide rent abatements to the Fair totaling $13.9 million commencing in the fourth quarter of 2006 through the first quarter of 2018.

Major Maintenance and Capital Expenditures

The Agreement provides that the Fair applies the excess of its revenues, less its expenses and after all reasonable and prudent reserves are funded, on major maintenance, and capital expenditures for development and enhancement of Fair Park and the Fair. Major maintenance projects are improvements to City-owned Fair Park real property and are classified as an expense on the statements of activities. Per the Agreement, the net revenues, as defined, allocated by the Fair and the City for major maintenance projects are deposited into a Fair-restricted account known as the Fair Park Improvement Fund.

In accordance with the Agreement, the Fair funds and maintains a minimum of $4.5 million as part of its reasonable and prudent reserves in order to provide a sound financial basis for the future economic integrity of the Fair. As stated within the MOU, the reserve fund is subject to adjustment by the Fair's Board of Directors in accordance with best practices for nonprofit organizations. Currently, the reserve fund is calculated to approximate 25% of the average for the five-year preceding total expenses as stated within the audited financial statements.

The reserve fund may be used only upon authorization by the Board of Directors of the Fair to fund the future operation of the annual fair. If the Fair elects to utilize the reserve fund, the fund must be restored to a minimum of $4.5 million as soon thereafter as reasonably possible. The reserve fund is classified as a Board-designated fund within unrestricted net assets on the statement of financial position (see Note 2).

3. Relationship With the City of Dallas (continued)

In 2017, the Fair spent approximately $11.7 million on the development and enhancement of Fair Park, comprising approximately $8.7 million on capital expenditures and $3.0 million on major maintenance projects. In 2016, the Fair spent approximately $8.1 million on the development and enhancement of Fair Park, comprising approximately $6.8 million on capital expenditures and $1.3 million on major maintenance projects. The capital expenditures are recognized as assets on the statements of financial position, and the major maintenance projects are recognized as an expense in the maintenance and repairs category on the statement of activities.

At December 31, 2017, approximately $6.9 million of the major maintenance expense was accrued and classified as a current liability on the statement of financial position to reflect several major maintenance projects that were not yet completed at year-end 2017. The $6.9 million accrual comprises approximately $0.4 million for 2016 projects and $6.5 million for 2017 projects. In accordance with the MOU, the $6.5 million is deposited in the Fair Park Improvement Fund and is reflected as restricted cash for Fair Park major maintenance projects on the statement of financial position.

4. Commitments and Contingencies

The Fair is involved in various legal proceedings arising from its operation of the annual fair. In the opinion of management, after consultation with legal counsel, the ultimate liability, if any, from such legal proceedings will not have a material impact on the Fair's financial position or results of operations.

Future minimum lease commitments, including rental escalations and abatements, required under operating leases as of December 31, 2017, are as follows:

2018	$ 1,432,873
2019	1,636,550
2020	1,633,970
2021	1,621,524
2022	1,559,294
Thereafter	8,754,647
	$ 16,638,858

Rent expense of approximately $696,000 was incurred during each of the years ended December 31, 2017 and 2016.

5. Investments

The aggregate carrying amount of available-for-sale investments by asset type is as follows at December 31:

	2017		2016	
	Cost	**Fair Value**	**Cost**	**Fair Value**
Money market accounts	**$ 29,492,779**	**$ 29,531,578**	$ 36,764,467	$ 36,778,636
Domestic corporate bonds	**11,902,113**	**11,920,852**	1,507,880	1,511,960
U.S. short-term government bond fund	**374,549**	**373,247**	372,469	369,955
Domestic common stocks	**6,930,811**	**11,085,082**	7,775,154	10,606,806
	$ 48,700,252	**$ 52,910,759**	$ 46,419,970	$ 49,267,357

Net realized gains on investments were $797,613 and $180,281 for the years ended December 31, 2017 and 2016, respectively. Net unrealized gains on investments were $1,363,120 and $747,934 for the years ended December 31, 2017 and 2016, respectively. The Fair recognized investment income of $317,850 and $111,925, net of investment expenses of $96,765 and $57,975, for the years ended December 31, 2017 and 2016, respectively. This is recorded in interest income and dividends revenue in the accompanying statements of activities.

6. Credit Facilities

In January 2007, the Fair executed a $15.0 million advanceable term loan transaction (the Loan) with a bank. Proceeds from the Loan were used to finance improvements to the Cotton Bowl as agreed to by the Fair and the City in the Amendment. The Loan term was 12 years with interest at the British Bankers Association one-month floating London Interbank Offered Rate (LIBOR) plus 1.0%. Interest-only was payable monthly for the first year, with principal and interest payable monthly after the first anniversary of the Loan. The Loan may be repaid in full or in part at any time without any prepayment fee. The Fair pledged certain land and a building as collateral for the Loan. Additionally, the Loan provided for certain restrictive covenants that the Fair must maintain in 2007 and thereafter. These covenants comprised various ratios and restrictions on the Fair's assets and debt. The balance of the loan was $2,107,274 at December 31, 2016. In January 2017, the Fair repaid the Loan in full effective January 3, 2017. Principal applied to the payoff of the loan was $2,107,274 and interest of $2,953. All collateral associated with the loan has been released at December 31, 2017.

6. Credit Facilities (continued)

The Fair was party to an agreement with a bank for a $3 million revolving line of credit to fund seasonal working capital requirements in 2017 and 2016. The line of credit has a maturity date for any borrowings of one year from closing with interest at the one-month floating LIBOR plus 2% in 2017 and 2016. Interest is payable monthly, with all unpaid principal and interest payable on the maturity date. The revolving line of credit must maintain a zero balance for a minimum of 30 consecutive days during any 12-month period. The Fair pledged certain cash and investment accounts as security for any borrowings under the revolving line of credit. In 2017 and 2016, no borrowings were made under the line-of-credit arrangement.

7. Related-Party Transactions

The Fair conducts business with entities affiliated with members of the Board of Directors. With respect to the Fair and these entities, management believes such transactions are conducted in the normal course of business and in conformance with the Fair's Conflicts of Interest and Ethics Policy.

8. Fair Value Measurements

The FASB defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date in the principal or most advantageous market for that asset or liability. The FASB establishes a valuation hierarchy for disclosure of inputs used in measuring fair value. The hierarchy is defined as follows:

> Level 1 – Inputs are unadjusted quoted prices that are available in active markets for identical assets or liabilities.
>
> Level 2 – Inputs include quoted prices for similar assets and liabilities in active markets and quoted prices in non-active markets, inputs other than quoted prices that are observable, and inputs that are not directly observable but are corroborated by observable market data.
>
> Level 3 – Inputs that are unobservable and are supported by little or no market activity and reflect the use of significant management judgment.

8. Fair Value Measurements (continued)

A financial asset's or liability's classification within the hierarchy is determined based on the least reliable level of input that is significant to the fair value measurement. In determining fair value, the Fair used valuation techniques that maximized the use of observable inputs and minimized the use of unobservable inputs to the extent possible. The Fair also considered the counterparty and its own nonperformance risk in its assessment of fair value.

The Fair measures its assets and liabilities at fair value on a recurring basis as required; the fair value of the Fair's available-for-sale securities was estimated by using market quotes as of the last day of the period. Consequently, the Fair's available-for-sale securities of $52,910,759 and $49,267,357 were classified as Level 1 assets for the years ended December 31, 2017 and 2016, respectively.

9. Retirement Plans

401(k) Retirement Plan

The Fair adopted the State Fair of Texas Employees' 401(k) Retirement Plan (the 401(k) Plan) on behalf of its employees effective January 1, 1999. Employees may contribute a percentage of annual compensation to the 401(k) Plan, subject to statutory maximums. The Fair provides a contribution of 4% of each participant's annual salary. In addition, the Fair matches 50% of the first 4% of employee deferrals under the 401(k) Plan.

For the years ended December 31, 2017 and 2016, the Fair's contribution and plan administration expense totaled approximately $241,000 and $209,000, respectively.

9. Retirement Plans (continued)

Executive Deferred Compensation Plans

Effective January 1, 2007, the Fair established the State Fair of Texas 457(b) Executive Deferred Compensation Plan (the 457(b) Plan) for all eligible employees to defer a portion of their salary and incentive payment, if any. Eligible employees include any officer of the Fair with a title of vice president or above. Eligible employees are given the option to defer up to 50% of salary and up to 100% of incentive payment. The Fair matches 100% of the employee's deferral up to 6% of the employee's base salary. Under IRC Section 457(b), annual employee deferrals and employer matching contributions combined are limited to $17,500 in 2017 and 2016. Employee deferrals under the 457(b) Plan are vested immediately, while the Fair's portion vests at 20% increments over a five-year period. For the years ended December 31, 2017 and 2016, the Fair made matching contributions to the 457(b) Plan of approximately $75,000 and $66,000, respectively. Employee and employer contributions are invested at the direction of the employee. The fair market value of the deferred compensation funds is included in other assets, with an offsetting deferred compensation liability.

10. Subsequent Event

The Fair evaluated all material events occurring subsequent to the date of the financial statements up to April 17, 2018, the date the financial statements were available to be issued.

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