

Metropolitan Nashville Airport Authority

MEMORANDUM

TO: Douglas E. Kreulen, Acting President and CEO

CC: Michael Lee, Chief Commercial Officer
Davita Taylor, Chief of Staff, Bd. Liaison, Business Diversity Development
Rebecca Ramsey, Director of Concessions

FROM: Tiffany Underwood, Internal Auditor

DATE: November 10, 2017

SUBJ: Avis Budget Car Rental

Background

Rental Car Concession Agreement:

On January 4, 2010, the Avis Budget Group, Inc. (“Avis Budget”) entered into a Concession Agreement with the Metropolitan Nashville Airport Authority (“Authority”). The Concession Agreement granted Avis Budget the right to operate a rental car concession at the Airport for a period of fifteen (15) years, commencing on the opening date of the Consolidated Rental Car (“CONRAC”) Facility (November 1, 2011). The Concession Agreement included a renewal option of five (5) years, commencing on the expiration of the initial lease term.

The Concession Agreement required Avis Budget to pay to the Authority the greater of a minimum annual guarantee (“MAG”), which was subject to an annual adjustment based on prior year rentals, or 10% of gross revenue. The required percentage of gross revenue would increase to 11% in the eleventh Agreement Year. The current MAG for November 2015, to October 2016 is \$3,066,535.

In addition to the MAG and/or the percentage of gross revenue payments required, Avis Budget would pay to the Authority monthly Terminal Counter Rent in the amount of Thirty-Six Dollars and 00/100 (\$36) per square foot (“psf”) per annum. Avis Budget was awarded the use of 1,127 square foot of counter space in the Terminal; therefore, Avis Budget’s Terminal Counter Rent due per annum was Forty Thousand Five Hundred Seventy-Two Dollars and 00/100 (\$40,572).

The Concession Agreement stated that Avis Budget would furnish a written statement to the Authority, certified by a responsible officer of Avis Budget that the MAG and the percentage payment paid by the Concessionaire to the Authority, during the preceding contract year, were

made in accordance with the terms of the Concession Agreement. The statement would contain gross revenues as shown on the books and records of Avis Budget that were used to compute the percentage payments made to the Authority. Additionally, the statement would be accompanied by a report from a certified public accountant (“CPA”) confirming they had reviewed the Statement of Gross Revenues and the Concessionaire’s payments to the Authority and found them to be in compliance with the terms of the Concession Agreement.

On November 1, 2011, the Authority entered into the First Amendment to the Concession Agreement, which revised certain definitions and corrected grammatical errors identified in the Concession Agreement.

Additionally, on November 1, 2011, the Authority opened the CONRAC Facility, effectively beginning the terms of the Concession and the Facility Lease Agreements.

On September 1, 2014, the Second Amendment to the Concession Agreement was entered into between the Authority and Avis Budget. The Second Amendment added ZipCar as a brand for Avis Budget, changed the definition of Gross Revenues, and defined concession fees for ZipCar.

In accordance with the terms of the Concession Agreement, Avis Budget would pay to the Authority the greater of the MAG of \$3,065,535 or 10% of gross revenues. The following are the gross revenue and percentage payment provisions for Avis Budget per the Statement of Gross Revenues for the Year Ended October 31, 2016, provided by Cohn Reznick, LLP.

Month	Gross Revenues
November 2015	\$3,090,253
December	2,530,305
January 2016	2,348,682
February	2,412,320
March	3,122,446
April	3,351,191
May	3,940,583
June	4,006,483
July	3,628,279
August	3,166,815
September	3,375,758
October	3,626,162
Total Gross Revenue	<u>\$38,599,277</u>
Contractual Percentage Rate	X 10%
Calculated Percentage Payment	<u>\$3,859,928</u>
Minimum Annual Guarantee	<u>\$3,066,535</u>
Amount Paid by Avis Budget	<u>\$3,861,096</u>
(Under)/Over Payment	<u>\$1,168</u>

Avis Budget's percentage payments from the gross revenues were \$3,859,928. Thus, the percentage payment paid to the Authority was greater than the MAG. The amount paid by Avis Budget to the Authority for the Year Ended October 31, 2016, was \$3,861,096; therefore, Avis Budget had an overpayment of rent due to the Authority in the amount of \$1,168. Accordingly, Avis Budget was due a credit for the overpayment of rent.

On September 1, 2017, Finance initially determined that Avis Budget had an overpayment of rent due to the Authority in the amount of \$1,892 and issued Avis Budget a credit memo (CRM33617) for the overpayment. On September 15, 2017, Finance issued a revised determination that Avis Budget had an overpayment of rent due to the Authority in the amount of \$1,168, instead of the initial overpayment amount of \$1,892. Finance issued an invoice (INV33927) in the amount of \$724 for the amount that was initially over refunded. Finance based the determinations upon the MAG, percentage payment provisions, and the total rent paid by Avis Budget to the Authority for the Year Ended October 31, 2016.

CONRAC Facility Lease Agreement:

On January 4, 2010, Avis Budget entered into the CONRAC Facility Lease Agreement (“Facility Lease Agreement”) with the Authority and MPC CONRAC LLC. The Facility Lease Agreement granted Avis Budget the exclusive use of a designated area in the CONRAC Facility and use of the Quick Turn Around (“QTA”) equipment located in the CONRAC for a period of fifteen (15) years commencing on the opening date of the CONRAC Facility. The Facility Lease Agreement included a renewal option of five (5) years commencing on the expiration of the initial lease term.

In addition, the Facility Lease Agreement required Avis Budget to collect a daily Customer Facility Charge (“CFC”) for individual vehicle rental transactions at the Airport. The CFCs would be used to pay, or to reimburse the Authority for costs, fees, and expenses associated with the planning, design, construction, financing, maintenance and operation of the CONRAC Facility. The CFC rate was established at Four Dollars and 50/100 cents (\$4.50) per rental transaction in January 2010.

On November 1, 2011, the Authority entered into the First Amendment to the Facility Lease Agreement, which revised certain definitions and corrected grammatical errors identified in the Facility Lease Agreement.

On April 1, 2013, the Second Amendment to the Facility Lease Agreement was entered into between the Authority and Avis Budget. The Second Amendment added language to modify the requirements for the environmental insurance and modified various definitions in the Facility Lease Agreement.

Objectives

The objectives of the audit were as follows:

1. Determine the validity of gross revenue amounts reported and rent paid to the Authority;
2. Determine compliance with contract terms and operational requirements; and,
3. Document and evaluate existing internal controls.

Testing

In order to satisfy the audit objectives, the following tests were performed:

1. Determine the validity of gross revenue amounts reported and rent paid to the Authority by performing the following:
 - a. Select 3 months for detailed testing (May, June, and October 2016). For each month selected, perform the following:
 - i. Obtain the monthly fixed rent invoices from the Authority’s Accounts Receivable and verify that the rent amount agrees to the schedule of rental fees and charges in the Lease Agreements.

- ii. Obtain monthly revenue report and perform the following:
 - 1. Review report for mathematical accuracy.
 - 2. Tie amounts per report to amounts reported to the Authority.
 - 3. Select 5 consecutive days each month and perform the following:
 - a. Obtain the Daily Activity Report for the days selected.
 - b. Review report for mathematical accuracy.
 - c. Tie amounts per report to the monthly revenue report.
 - d. For a selection of rental agreements, tie all revenue information per the signed rental agreement to the Daily Activity Report.
 - e. Review rental agreements for mathematical accuracy.
 - f. Verify that the concession fee recovery on rental agreements agreed to the Concession Agreement.
 - 4. Review excluded amounts, such as carbon offset fees, surcharges, taxes, or discounts for appropriateness and compliance with Concession Agreement.
 - a. Review listing of the excluded discounts to ensure discounts were supported by corporate contract.
- iii. Obtain a copy of the company's general ledger.
 - 1. Verify that the revenue amounts per the general ledger were consistent with the revenue amounts reported to the Authority.
- iv. Obtain a copy of the Tennessee Sales and Use Tax form.
 - 1. Review tax returns for reasonableness and determine sales and use taxes were properly remitted to the State.
- v. Obtain a copy of the quarterly Motor Vehicle Rental Surcharge Tax form.
 - 1. Review tax returns for reasonableness and determine motor vehicle rental surcharge taxes were properly remitted.
- vi. Obtain a listing of rental agreements.
 - 1. Review listing to identify any missing rental agreement numbers (if agreements are sequentially numbered).
 - 2. Trace a selection of rental agreements for inclusion in the appropriate Daily Activity Report.
- vii. Obtain a listing of CFCs collected in the month of October 2016.
 - 1. Review report for mathematical accuracy.
 - 2. Tie amounts per report to amounts reported to the Authority.
 - 3. Select 5 consecutive days in October 2016 and perform the following:
 - a. Review report for mathematical accuracy.
 - b. Tie amounts per report to rental agreements.
 - c. For a selection of rental agreements, verify CFC per the signed rental agreement agree to the Daily Activity Report.
 - d. Verify CFC on rental agreements agree to Authority approved rate.
 - e. Verify the CFC rental days agree with the rental days on the Monthly Gross Revenue Report.
- viii. Identify all other non-rental and CFC revenues.

1. Determine whether or not they should be included in gross revenue.
 2. Determine whether or not they should be subject to the contractual percentage payment.
2. Determine compliance with contract terms and operational requirements by performing the following:
- a. Determine Avis Budget is meeting operational requirements.
 - i. Through observations, determine Avis Budget is conducting their operations in safe, clean, orderly, and inviting conditions. No trash or debris should be allowed to accumulate or be stored on any portion of the premises.
 - ii. Verify Avis Budget is responding to customer complaints in writing within 5 days of receipt.
 - iii. Determine Avis Budget's operating hours and observe that the customer service counter is open during scheduled hours.
 - iv. Determine Avis Budget has an active, qualified, competent manager or a qualified assistant manager on site.
 - v. Through observations, determine that employees are well trained, experienced, uniformed, professional, and courteous.
 - vi. Through observations, determine Avis Budget is adhering to the Authority's no smoking policy in the terminal.
 - b. Determine Avis Budget locations within a three-mile radius of the airport have a place on their rental agreement for the customer to indicate by their signature they are not an airport customer.
 - c. Obtain a current listing of all vehicles in the fleet.
 - i. Review the list to ensure that no automobile being used is more than three model years old.
 - d. Verify Avis Budget has met Disadvantaged Business Enterprise ("DBE") Program requirements established in the contract.
 - e. Verify Avis Budget has submitted an annual drug free workplace affidavit.
 - f. Determine Avis Budget maintains adequate insurance coverage.
 - i. Obtain a copy of the current certificates of insurance on file for the general liability, workers compensation and property damage insurance.
 - ii. Verify that the comprehensive general liability, automobile, workers compensation property damage, and environmental insurance coverage meets or exceeds the amounts specified in the contract.
 - iii. Verify the company/companies providing general liability, automobile, workers compensation, property damage and environmental insurance are admitted to do business in Tennessee and rated not less than the minimum rating for insurance carriers or approved by the Authority's CFO.
 - iv. Verify that the certificate of insurance is current and adheres to all other contract terms.
 - g. Determine Avis Budget maintains an Irrevocable Letter of Credit ("LOC").
 - i. Obtain a copy of the current LOC.
 - ii. Verify that the LOC coverage meets or exceeds the amount specified in the contract.
 - iii. Verify that the LOC is current and adheres to all other contract terms.
3. Determine compliance with facility lease agreement terms by performing the following:

- a. Verify Avis Budget and the Authority are conducting quarterly inspections of the CONRAC facility and CONRAC facility sites.
 - b. Determine Avis Budget is maintaining copies of material safety data sheets for hazardous substances used or stored at the premises.
4. Document and evaluate existing internal controls by performing the following:
- a. Interview Avis Budget personnel regarding the current internal controls in place. Such control areas should include, but not limited to:
 - i. Ensuring all rental contract are accounted for.
 - ii. The issuance of voids, credits, refunds or adjustments.
 - iii. Exceptions from standard pricing.
 - iv. The review of customer's documentation and identification prior to rental.
 - b. Determine whether Avis Budget has had any rental cars stolen from the Nashville Airport for the period November 2015 to the current period. Review and evaluate the internal controls surrounding the security of rental cars. Discuss stolen car experience with Avis Budget personnel (if applicable).
 - c. Perform testing of internal controls as identified.
 - d. Identify and document any areas of improvement.

Conclusion

Based upon the audit, the following was determined with respect to the stated objectives:

1. Commercial Development did not maintain inspection reports to document inspections of the CONRAC facility and facility sites, as noted in Finding #1.
2. Proper monitoring tools were not in place to support the accuracy of Avis Budget's ACDBE expenditures, as noted in Finding #2.
3. Commercial Development did not ensure that Avis Budget maintained continuous security coverage at all times, as noted in Finding #3.
4. Commercial Development did not ensure that Avis Budget maintained the proper security amount at all times, as noted in Finding #4.

Finding # 1

Observation

Commercial Development did not maintain inspection reports to document inspections of the CONRAC facility and facility sites.

Background

Article 14, Repair and Maintenance, Section 7, Quarterly Condition Surveys, of the Facility Lease Agreement requires the Authority and/or MPC CONRAC LLC and the RACs, together with the Facility Manager, to conduct an inspection of the CONRAC facility and the CONRAC

facility sites quarterly to observe and note the condition of cleanliness of and existing damage to the CONRAC facility and CONRAC facility sites and to determine repairs and maintenance required to be performed.

An objective of the audit was to determine whether Commercial Development was conducting quarterly inspections of the CONRAC facility and facility sites and maintaining appropriate inspection reports for documentation. Through testing, quarterly inspection reports were requested for the period of October 1, 2015, through June 30, 2016. Reports were provided by Commercial Development for each quarterly period, except for the quarter ending June 30, 2016. Since the inspection report for the period ending June 30, 2016 was not available; Internal Audit was unable to verify that an inspection had been conducted.

Recommendation

Commercial Development should conduct quarterly inspections of the CONRAC facility and facility sites and maintain formal inspection reports for documentation purposes.

Management Response

On December 8, 2017, Commercial Development will conduct the next CONRAC inspection and maintain proper inspection reports for documentation purposes.

Finding #2

Observation

Proper monitoring tools were not in place to support the accuracy of Avis Budget's ACDBE expenditures.

Background

According to 49 CFR 23.29, What Monitoring and Compliance Must Recipients Follow, recipients must implement appropriate mechanisms to ensure compliance with the requirements of the ACDBE program by all participants in the program. The recipient must include in the concession program the specific provisions to be inserted into the concession agreements and management contracts setting forth the enforcement mechanisms and other means to ensure compliance. These provisions must include monitoring and enforcement mechanism to verify that the work committed to ACDBEs is actually performed by the ACDBEs. This mechanism must include a written certification that the recipient has reviewed records of all contracts, leases, joint venture agreements, or other concession-related agreements and monitored the work on-site at the airport for this purpose. The monitoring to which this paragraph refers may be conducted in conjunction with monitoring of concession performance for other purposes.

Article 8, Accounting Procedures: Audit, Section 1, Same Rights and Obligations, of the Concession Agreement allows the Authority to have the same rights and obligations with

respect to the Concessionaire’s books and records and the inspection/audit thereof under this Concession Agreement as the parties have under Article 8 of the Lease Agreement.

Article 8, Accounting Procedures: Audit, Section 2, Audit, of the Facility Lease Agreement states that representatives designated by Authority shall be allowed to inspect and audit Concessionaire’s books of accounts and records with reference to the determination of any matters relevant to the lease agreement at all reasonable times.

Furthermore, the FAA confirmed on August 30, 2017, through email, that airports are required to ensure that ACDBEs being counting are performing a commercially useful function and required to ensure the amounts being reported are correct, including the counting of ACDBE participation towards their goals.

An objective of the audit was to verify that BDD had proper monitoring tools in place to ensure that ACDBE amounts being reported and counted in participation are correct.

Through audit testing, it was determined that Avis Budget files quarterly ACDBE compliance reports listing the vendors, service provided, current expenditure amount, year to date amount, etc. The amounts listed on the ACDBE compliance reports are lump sum expenditures from each vendor separated out by Avis Budget’s four brands including: Avis, Budget, Payless and ZipCar. A sample compliance report is included below for the Avis brand.

DBE Compliance Report
Nashville International Airport - 4104N20
Avis Rent A Car System, LLC

REPORTING PERIOD: **Oct-16** **Dec-16**

Vendor Name	Classification	Services Provided	Certification	Ethnicity	Current Period Paid Amount	YTD Amount
Sample Vendor	DBE	New Car Dealer	Tennessee - DBE/UCP	Non-Ethnic (Female)	\$100,000	\$1,000,000

Avis Budget does not submit and BDD does not request any additional support to determine the accuracy of the numbers listed on the ACDBE compliance reports. Without additional support, it is not possible to determine that the accuracy of the numbers listed on the ACDBE compliance report. Specifically, support is needed for ACDBEs that are locally certified by the UCP in Tennessee and are included in the participation calculation.

Recommendation

BDD should require Avis Budget to provide supporting documentation to the Authority to verify the accuracy of Avis Budget’s ACDBE expenditures.

Management Response

By November 2017, BDD will notify Avis Budget of the requirement to submit backup documentation for ACDBE firm participation. In addition, BDD will coordinate with Commercial Development to ensure all rental car companies are notified of the new requirement of submitting supporting documentation with their quarterly ACDBE compliance report.

Finding #3

Observation

Commercial Development did not ensure that Avis Budget maintained continuous security coverage at all times.

Background

Article 9, Security, Section 1, Security, of the Facility Lease Agreement states that the Concessionaire shall, upon execution of this Lease Agreement, obtain and deliver to the Authority one of the following to secure Concessionaire's full performance of this Lease Agreement and the Concession Agreement, including the payment of all fees and other amounts now or hereafter payable to or required to be remitted to Authority under either this Lease Agreement or the Concession Agreement ("Security"): a) a good and sufficient irrevocable stand-by letter of credit in the form of Exhibit F hereto and acceptable to Authority in a stated amount equal to the Security Amount, or b) a good and sufficient surety bond in the form of Exhibit G hereto and acceptable to Authority in a stated amount equal to one hundred twenty-five percent (125%) of the Security Amount. The form, provisions and nature of the Security, and the identity of the issuer thereof, shall at all times be subject to the Authority's approval. The security shall remain in place at all times throughout the full lease term and throughout any holdover period.

Article 9, Security, Section 1, Security, of the Concession Agreement states that Article 9, Security, Section 1, Security, of the Facility Lease Agreement is specifically incorporated in the Concession Agreement by reference; provided, however, Concessionaire shall not be required to provide additional Security under the Concession Agreement. The Security provided under the Lease Agreement shall secure the Concessionaire's full performance of the Concession Agreement. The Security shall remain in place at all times throughout the full Lease Term and throughout any holdover period.

An objective of the audit was to determine that Avis Budget maintained security coverage at all times. Through audit testing, it was determined that on April 24, 2014, Avis Budget provided Bond No. CMS0283441 to meet the security requirements set forth in the Concession and Facility Lease Agreement. The security bond expired on April 24, 2015. A continuation certificate was not in place until November 15, 2015. Accordingly, there was a lapse in security from April 24, 2015 to November 15, 2015, or approximately 205 days.

Recommendation

Commercial Development should set up alerts to monitor the expiration date of the security coverage to ensure that there is not a lapse in coverage.

Management Response

On October 4, 2017, alerts were set up in the ABM system to monitor the expiration dates of the security coverage to ensure there are no future issues with lapse in coverage.

Finding #4

Observation

Commercial Development did not ensure that Avis Budget maintained the proper security amount at all times.

Background

Article 9, Security, Section 1, Security, of the Facility Lease Agreement states that the Concessionaire shall, upon execution of this Lease Agreement, obtain and deliver to Authority one of the following to secure Concessionaire's full performance of this Lease Agreement and the Concession Agreement, including the payment of all fees and other amounts now or hereafter payable to or required to be remitted to Authority under either this Lease Agreement or the Concession Agreement ("Security"): a) a good and sufficient irrevocable stand-by letter of credit in the form of Exhibit F hereto and acceptable to Authority in a stated amount equal to the Security Amount, or b) a good and sufficient surety bond in the form of Exhibit G hereto and acceptable to Authority in a stated amount equal to one hundred twenty-five percent (125%) of the Security Amount. The form, provisions and nature of the Security, and the identity of the issuer thereof, shall at all times be subject to the Authority's approval. The security shall remain in place at all times throughout the full lease term and throughout any holdover period.

Attachment 1, Definitions, of the Facility Lease Agreement defines the Security Amount as an amount equal to fifty percent (50%) of the Concessionaire's Minimum Annual Guarantee for such Agreement Year plus an amount equal to three (3) monthly installments of the Terminal Counter Rent. Attachment 1, Definitions, of the Facility Lease Agreement defines Minimum Annual Guarantee as an amount equal to eighty-five percent (85%) of the Concession Fee due for the immediately preceding Concession Agreement Year. Attachment 1, Definitions, of the Facility Lease Agreement defines Terminal Counter Rent as the rent due for each Concession Agreement Year in an amount equal to the product of Thirty-Six Dollars (\$36) multiplied by the number of square feet included within the Terminal Counter Space. Exhibit A, Terminal Counter Space, of the Concession Agreement lists approximately 1,127 SF as the amount of Terminal Counter Space designated to Avis Budget; therefore, Avis Budget's monthly Terminal Counter rent due is \$3,381.

Article 9, Security, Section 1, Security, of the Concession Agreement states that Article 9, Security, Section 1, Security, of the Facility Lease Agreement is specifically incorporated in the Concession Agreement by reference; provided, however, Concessionaire shall not be required to provide additional Security under the Concession Agreement. The Security provided under the Lease Agreement shall secure the Concessionaire's full performance of the Concession Agreement. The Security shall remain in place at all times throughout the full Lease Term and throughout any holdover period.

An objective of the audit was to determine Avis Budget maintained the proper amount of security coverage at all times. Attachment 1, Definitions, of the Facility Lease Agreement defines the Security Amount as an amount equal to fifty percent (50%) of the Concessionaire's Minimum Annual Guarantee for such Agreement Year plus an amount equal to three (3) monthly installments of the Terminal Counter Rent.

On April 24, 2014, Avis Budget provided Bond No. CMS0283441, in the amount of \$1,780,184, to meet the security requirements set forth in the Concession and Facility Lease Agreements.

On March 9, 2016, Commercial Development, by letter of notification, adjusted the MAG, for the period November 1, 2015 to October 31, 2016, to \$3,066,535. The security coverage amount should include half of the MAG, or \$1,533,268, and three months of terminal rent, at the monthly amount of \$3,381, totaling \$10,143. Accordingly, the security coverage amount due after the adjustment of the MAG should have been \$1,929,263, as detailed in the table below.

Bond Security Calculation	Monthly Installment	Multiplied by	Equals Amount in Security
50% of MAG	\$3,066,535	50%	\$1,533,268
+ 3 Months Counter Rent	3,381	3	10,143
Security Amount for Letter of Credit			\$1,543,411
x Premium for Obtaining Bond Security			125%
Security Amount for Bond			\$1,929,263

Through audit testing, it was determined that Avis Budget did not increase the security coverage amount, after the adjustment of the MAG, from \$1,780,184 to \$1,929,263. Accordingly, Avis Budget's security coverage amount was underfunded in the amount of \$149,079 for the period of March 2016, to April 2017, as detailed in the table below.

Security Coverage Analysis	Amount
Required Security	\$1,929,263
Security Coverage	1,780,184
Under Funded	\$149,079

Recommendation

Commercial Development should review the security coverage amount when the MAG or terminal rent is adjusted to ensure that Avis Budget maintains the proper security coverage at all times.

Management Response

In the 3rd quarter of FY18, Commercial Development will review the MAG and terminal rent for rental car companies and ensure the security amounts are calculated properly, as stated in the agreement.