CITY AND COUNTY OF SAN FRANCISCO
OFFICE OF THE CONTROLLER
FINANCIAL AUDITS DIVISION

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February 23, 2006 Audit Number 04038

San Francisco Airport Commission
P.O. Box 8097
San Francisco International Airport
San Francisco, CA 94128

Subject: **Review of CPA Audits of Alamo Rent-A-Car, Inc. and National Car Rental System, Inc.**
Reporting Period: January 1, 2003 through December 31, 2004
Reported Revenues: $71,926,041

President and Members:

The Airport Commission (Commission) has an agreement with Alamo Rent-A-Car, Inc. (Alamo) to operate an automobile rental service at the San Francisco International Airport (SFO). Alamo operated independently until November 1, 2002, when ANC Rental Corporation (ANC) began operating both Alamo and National Car Rental System, Inc. (National) as one operation at SFO. ANC used the agreement between Alamo and the Commission to operate the two car rental companies, and reported to the Airport consolidated revenues of Alamo and National. In October 2003, Vanguard Car Rental USA Inc. (Vanguard) acquired both Alamo and National car rental companies from ANC. According to Vanguard's manager for airport accounting, Vanguard continued to report the consolidated revenues of Alamo and National to the Airport Department (Airport). Since Vanguard consolidated the revenues of Alamo and National when reporting revenues to the Airport, our review covers these consolidated revenues.

As allowed by the agreement (Section 3.04), the Airport Director issued a memo in June 2002 that required car rental companies to submit an annual audit performed by a certified public accountant (CPA). Vanguard submitted an annual audit report for each year of our audit period, which was from January 1, 2003 through December 31, 2004. Vanguard's audit report covered the revenues of both Alamo and National. To assess whether we should conduct a separate audit of Vanguard's operations at SFO, we performed steps to assure us that the CPA's audits were adequate. We also verified whether the consolidated revenues of Alamo and National that Vanguard reported to the Airport agreed with the revenues reported by the CPA.

To obtain assurance that the audits were adequate, we reviewed the two annual audit reports that Vanguard submitted to the Airport. We also asked Vanguard's CPA about the procedures it performed in conducting the audits. Because we found that the CPA's procedures were adequate, we will not conduct a separate audit of Vanguard. However, to obtain further assurance that Vanguard properly reported its revenues to the Airport, we performed a limited review of Vanguard's revenue accounts that it uses to report its monthly revenues to the Airport. During our review, we identified the following matters:

1. Vanguard improperly deducted the amounts of one of its customer discounts accounts from the gross revenues it reported to the Airport during the audit period, and owes the Airport $37,241. Vanguard has two accounts that include customer discounts. One account is called the "coupon account", which is for discounts given to the customer at the time of the rental and the amount of this account is allowable as a deduction from gross revenues. The other account is called the "customer adjustment at the counter account", which is for discounts given to the customer when the customer returns the rental vehicle and the amount of this account is unallowable as a deduction from gross revenues. According to the agreement (Section 3.01), Vanguard is prohibited from reducing its gross revenues by credits for any reason. The airport director clarified the usage of credits in his September 2003 letter to all car rental companies. The letter stated that discounts taken before or at the time of the rental are allowed as a deduction from gross revenues, but retroactive discounts are not allowed as a deduction from gross revenues.

   According to its staff, Vanguard did not deduct either of the two customer discounts accounts from its gross revenues in its monthly report to the Airport from January 2003 to April 2004. However, the CPA excluded these customer discounts in the gross revenues shown in its audit report. The Airport provided a credit to Vanguard based on the CPA report when the over-reported gross revenues resulted in Vanguard paying the percentage rent. Vanguard staff informed us that Vanguard began deducting both of these customer discounts from its gross revenues in its May 2004 monthly report to the Airport. Deducting the "coupon account" amounts from gross revenues was proper because these discounts were given at the time of the rental. However, deducting the "customer adjustment at the counter account" amounts from gross revenues was improper because these discounts were given upon return of the rental vehicle.

   For 2003, the under-reported amounts in "customer adjustment at the counter account" did not affect the rent paid because Vanguard only paid the minimum rent. We determined that these under-reported gross revenues would not have caused Vanguard to owe the Airport additional rent.

   For 2004, Vanguard paid the percentage rent because it exceeded the minimum rent. However, Vanguard improperly excluded the "customer adjustment at the counter account" amount of $372,411 from audited revenues. This occurred in two different ways during the year:

   - From January to April 2004, Vanguard did not exclude its customer discounts, totaling $114,219, in the monthly report of gross revenues it submitted to the Airport. However, the CPA did exclude these customer discounts in the gross revenues shown in its annual audit report. Because the "customer adjustment at the counter account", totaling $48,040, was one of the customer discounts that the CPA excluded from gross revenues, the CPA improperly excluded $48,040 from its reported gross revenues for the year.

   - Beginning in May 2004, Vanguard excluded all customer discounts in the monthly report of gross revenues it submitted to the Airport. Because the "customer adjustment at the counter account", totaling $324,371, was one of the customer discounts that Vanguard began excluding, Vanguard improperly excluded $324,371 from its reported revenues.

During 2004 Vanguard paid percentage rent in some months and in other months it paid the monthly minimum rent and, as a result, a true up of the rent owed was necessary. Further, because the audited gross revenues were less than the reported gross revenues, Vanguard overpaid its rent. Based on the gross revenues shown in the CPA report, which accounted for the true-up and over-reported gross revenues, the Airport provided a credit totaling $330,740 to Vanguard. However, Vanguard improperly excluded the "customer adjustment at the counter account" amount of $372,411 from its reported gross revenues for the year. Because the percentage rent is 10 percent of gross revenues, Vanguard owes the Airport rent of $37,241 for this improperly excluded discount.

We recommend that the Airport collect from Vanguard the $37,241 in underpaid rent because Vanguard and its CPA erroneously excluded from gross revenues the customer discounts given upon return of the rented vehicles. We also recommend that the Airport require Vanguard to revise any monthly report that excluded the customer adjustments subsequent to our audit period and pay any percentage rent that is due. Further, the Airport should require Vanguard to begin properly accounting for these customer credits in reporting its monthly gross revenues.

2. The CPA audit report did not include a schedule that compared the audited revenues to the revenues Vanguard reported to the Airport. The Airport Director's June 2002 memo required Vanguard's auditor to compare the audited revenues to the revenues Vanguard reported to the Airport, and to explain any difference. While the CPA did not compare the audited revenues to reported revenues, Vanguard submitted with each audit report a reconciliation of the audited and reported revenues, and explained the differences. The table below details the differences between the reported and audited revenues during the audit period:

Reported and Audited Revenues
January 1, 2003 Through December 31, 2004

Year	Reported Revenues	Audited Revenues	Differences
2003	$34,813,813	$34,403,939	$409,874
2004	37,112,228	37,019,446	92,782
Total	$71,926,041	$71,423,385	$502,656

While Vanguard provided the appropriate information for the Airport to determine the reasons between the audited and reported revenues, the Airport director's letter requires the CPA to make this comparison and determine the reasons for any significant differences.

We recommend that the Airport require Vanguard have its CPA include in future audit reports a schedule that compares the audited and reported revenues, and explains any significant difference.

3. Vanguard did not submit either of the two audit reports timely. The agreement (Section 3.04) requires Vanguard to submit a CPA audit report within 90 days of the start of each lease year. Because the lease year starts on December 30, Vanguard must submit the CPA audit report by March 30. Since the Airport did not keep a log of when it received the audit reports until late 2004 according to Airport accounting staff, we do not know when the Airport received the 2003 audit report. However, since the only documented date is the audit report date of July 16, 2004, Vanguard's 2003 audit report was at least 108 days late. For the 2004 audit report, the Airport's log shows that the Airport received the report on August 26, 2005, or 149 days late. The agreement (Section 8) authorizes the Airport to assess a $500 fine per violation day for late submission of required reports, which would include the CPA audit report.

   We recommend that the Airport require Vanguard to submit its annual CPA audit report by March 30 of each year. Further, the Airport should consider imposing the $500 per day fine if Vanguard fails to comply with this requirement in future lease years.

We are advising you of these findings so that you can take the appropriate actions to resolve them. The Controller's Financial Audits Division will be working with the Airport Department to follow up in six months on the status of the recommendations made in this letter. Please call me at (415) 554-7656 or Edwin De Jesus at (415) 554-7636 if we can be of further assistance on these matters.

Sincerely,

Original signed by:
Ben Carlick
Audit Manager

cc: John Martin, Airport Director
Gary Franzella, Assistant Deputy Director Aviation and Concessions
Ben Kutnick, Airport Finance Director
Mark Ezell, Manager-Airport Accounting, Vanguard Car Rental USA
Noriaki Hirasuna, Director, Controller's Financial Audits Division

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