

Sonoma County

Auditor-Controller-Treasurer-Tax Collector

Internal Audit Report

**Follow-Up:
Charles M. Schulz – Sonoma County Airport
Revenue Generating Lease Audit**

Original Report Dated:
May 28, 2015

Engagement No: 3045
Report Date: October 7, 2016



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Executive Summary

As part of the 2015/2016 Annual Audit Plan, the Internal Audit Division of the Sonoma County Auditor-Controller-Treasurer-Tax Collector's Office (ACTTC) conducted a follow-up of Charles M. Schulz – Sonoma County Airport (Airport) Revenue Generating Lease Audit report dated May 28, 2015. The report contained eleven recommendations, with ten remaining outstanding. Seven of the eleven recommendations were from a prior year audit. All recommendations had been accepted by management. The following observations are noted with regard to the outstanding recommendations as a result of this follow-up:

- Three recommendations were implemented
- Six recommendations were in the process of being implemented.
- One recommendation was no longer applicable due to change in contracting

By implementing the above three recommendations, the Airport is better able to ensure that operators comply with lease terms and report income accurately.

Background, Objective, Scope, and Methodology

Background

At the request of Charles M. Schulz Sonoma County Airport (Airport) management ACTTC audited gross receipts and rents reported to the Airport by Avis Budget Car Rental, LLC (Avis Budget) and North Coast Air, Inc. (NCA).

Airport management was concerned that Avis Budget and NCA may not have accurately reported their gross receipts and calculated and paid rents in accordance with their lease agreements. They were also not certain if a claim by Avis Budget that it over paid the County \$10,099 was accurate.

Objective

The objective of this follow-up audit was to determine the status of implementation of recommendations contained in the Revenue Generating Lease Audit report dated May 25, 2015 and, where applicable, the impact of actions taken by management.

Scope

Our procedures were limited to inquiry and review of evidence supporting actions taken by Airport Management and/or the County, as of December 31, 2015, towards implementation of the report recommendations. We performed an inquiry with the management of the Airport and reviewed supporting documentation submitted to us.

Methodology

We conducted the follow-up audit in accordance with the International Standards for the Professional Practice of Internal Auditing (Standards). These Standards require that we identify, analyze, evaluate, and document sufficient information and evidence to achieve audit objectives. We believe that the evidence obtained provides a reasonable basis for the conclusion contained in our audit report. The Standards require that we establish a follow-up process to monitor and ensure that management has effectively implemented actions or that senior management has accepted the risk of not taking actions.

Prior Recommendations and Current Status

The following is a discussion of the implementation status of prior recommendations from our Revenue Generating Lease Audit report dated May 28, 2015. Each recommendation is referenced to the section of the report where it is discussed.

A) North Coast Air (NCA)

Recommendation # 1.

The Airport should enforce the lease agreement and calculate and pursue collection as amounts become due.

The Airport should consider charging interest in addition to the penalty on all past due rent.

Current Status: In Process:

Airport Management is in the process of implementing new income reporting procedures. These procedures will require operators to complete a standard form, documenting the gross collection and calculating the amount due to the Airport. The Airport staff will review this form and follow up if the amounts remitted do not agree with the calculated amounts.

According to County Counsel, the Airport can legally charge a late penalty or interest, not both. Thus, the Airport will continue its practice to only charge the 10% penalty as it is unlikely that annualized interest will exceed the 10% onetime penalty.

Recommendation # 2.

The Airport should: a) Require NCA to timely submit monthly and annual statements with supporting details from its accounting system. b) Review the documentation provided by NCA to identify and settle under or over payments in a timely manner. c) Invoice NCA for \$10,530 due from the 2013 gross sales.

Current Status: In Process:

Airport Management is currently working with NCA to negotiate a solution where NCA will true up estimated monthly payments on a quarterly basis. NCA remitted to the Airport \$10,530 owed from the 2013 gross sales. The Airport Management expects to fully implement this recommendations by the end of fiscal year 2016.

Recommendation # 3.

The Airport should: a) Require NCA to bring its insurance policy in compliance with the lease terms. b) Periodically review insurance policies for compliance with lease terms. c) Consult with the County's Risk Management function and determine if insurance requirements are adequate.

Current Status: Implemented:

NCA's current insurance policy complies with the lease terms. The Airport Management is utilizing a Lease Management System that alerts Airport Personnel when insurance policies are about to expire and continues to do so until the policy is made current.

Prior Recommendations and Current Status

B) Avis Budget Rental Car

Recommendation # 4.

The Airport should develop the following procedures to assist in reviewing Avis Budget's calculation of rent: 1) Summarize terms of the lease agreement relevant to the calculation of rents and use as reference when recalculating rent reported by Avis Budget. 2) Require Avis Budget to provide details necessary for Airport staff to recalculate rent. 3) Periodically review the lease agreements to ensure that Avis Budget is correctly applying the terms.

The Airport should provide Avis Budget a credit of \$37,289 against future rents, unless credits have already been applied.

Current Status: Implemented:

Airport Management has taken steps to ensure the lease payment database, that has a summary of lease terms, is kept up to date and made available to personnel receiving the payments. A notification system has been implemented that alerts Airport personnel of the requirement to perform annual Minimum Annual Guarantee (MAG) calculations. This allows the Airport to timely notify rental car companies of the new monthly payment amounts.

The credit of approximately \$37k has been fully applied to the account of Avis Budget.

Status of Prior Audit Recommendations - PropJet

The following recommendations and agreed upon procedures are status updated from the prior Audit recommendations from the Airport Lease Revenue Audit Report 3045 dated April 23, 2013

Recommendations # 2 & # 3.

The Airport should require PropJet Aviation LLC, to recalculate gross receipts for 2012, 2010 and 2009. The cost of freight should not be excluded, the recalculation should include amounts received for parts where gross profit exceeds 8%, and any other revenue unless specifically excluded from the Agreement. The Airport should require PropJet to submit monthly percentage rent reports which show the method of computation of gross receipts from commercial activity at the airport. The report should include gross receipts before deductions and a detailed list by account of deductions to arrive at the adjusted gross receipts used for the rent calculation.

Current Status: In Process:

Airport Management has taken the same implementation actions as stated in item #1 above of implementing a new income reporting form. The form will be provided with the new Operating Agreement that any tenant will use the form when remitting payments to the Airport. Airport staff receiving payments will verify the math to confirm that the total amount paid is 3% of the gross income reported. Airport Management expects this recommendation to be fully implemented by end of fiscal year 2017.

Recommendation # 4.

PropJet Statement of Annual Gross Receipts - We recommend that the Airport require PropJet Aviation LLC to begin submitting a statement of annual gross receipts within 60 days after close of the calendar year.

Prior Recommendations and Current Status

Current Status: In Process:

Airport Management has been working with PropJet to ensure an Annual Gross Receipts report is received timely in accordance with the lease terms. Airport Management worked with PropJet to recalculate gross receipts for 2012, 2010, and 2009. Airport Management is in the process of finalizing the new lease from PropJet and will be adding requirements in the income and gross receipts reporting form to ensure cost of freight is not being excluded and parts exceeding 8% in gross profit are included.

Recommendation # 5.

Modify Operating Agreement - We recommend that the Airport remove the language related to submitting statistical information, respecting Operator's operations at the Airport, from Section 5.3 from the Agreement.

Current Status: In Process:

Airport Management is in the process of updating Operating Agreements which when complete, will not include the language related to submitting statistical information from Operating Agreements.

Airport management expects full implementation of recommendations 4 and 5 by the end of August 2016.

Recommendation # 6.

Schedule of Operating Hours: We recommend that the Airport require PropJet Aviation to begin submitting a written schedule delineating the operating hours and operating procedures of its aircraft maintenance service at the Airport.

Current Status: No Longer Applicable:

A new term sheet outlining completed lease negotiations has been signed by both Airport Management and PropJet. As PropJet is moving from an Operating Agreement to a full term Lease agreement, this requirement for hours of operations as outlined in an Operating Agreement may not be incorporated in the fully executed lease agreement.

Recommendation # 7.

The Airport should obtain and review PropJet Aviation's insurance policy for adequacy of coverage. Risk Management and County Counsel should be consulted as necessary. Operating agreement insurance requirements should be updated accordingly. A policy should be implemented which includes a more robust follow up process and addresses lapses in insurance coverage.

Current Status: Implemented:

Airport Management has worked with PropJet to ensure their insurance certificates are up to date and coverage is adequate. The current insurance requirements for PropJet are in effect as evidenced with the \$2,000,000 liability insurance certificate. The lease management system alerts, as outlined in NCA Recommendation #3 above are also in place for PropJet. A new lease with PropJet will not be executed if insurance certificates are not received by the Airport.

Prior Recommendations, Current Status and Staff Acknowledgement

ACTTC noted the Airport and PropJet are currently in negotiations to move PropJet from an operating agreement to a full lease agreement. Airport Management expects the new lease agreement to address the recommendations for PropJet that are currently in “In Process.”

Staff Acknowledgement

We would like to thank Airport Management and staff for their helpfulness and cooperation in conducting this follow-up audit. If you have any further questions regarding this report, please contact the auditor-in-charge, Ryan Burns at (707) 565-8304.