INTERNAL AUDIT REPORT

LEASE AND CONCESSION AGREEMENT AUDIT

CLEAR CHANNEL OUTDOOR, INC. DBA CLEAR CHANNEL AIRPORTS

August 1, 2012 – July 31, 2015

ISSUE DATE: March 24, 2017
REPORT NO. 2017-03

EXECUTIVE SUMMARY

AUDIT OBJECTIVES AND SCOPE

The purpose of the audit was to determine whether Port management monitoring controls are adequate and effective to ensure:

1. Clear Channel reported concession fees were complete, properly calculated, and remitted timely to the Port.

2. Clear Channel complied with significant financial terms of the lease and concession agreement.

We reviewed and analyzed records for the Agreement period August 1, 2012 – July 31, 2015.

Details of our audit's scope and methodology are on page 2.

BACKGROUND

The lease agreement with the Port authorizes Clear Channel Outdoor, Inc., doing business as Clear Channel Airports (Clear Channel), to management the public advertisements at the Seattle Tacoma International Airport.

The terms of the agreement provide for fixed Minimum Annual Guarantee (MAG) of $5 million annually. In addition, the agreement requires a concession fee equal to 70% of gross receipts, provided the concession fee is higher than the MAG payment.

AUDIT RESULT

Port management monitoring controls were reasonably effective and Clear Channel complied with the significant financial provisions of the agreement. However, certain gross receipts were underreported. We recommend that Port management seek recovery of $7,821 in additional concession fees. See Findings 1 under the Schedule of Findings.

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TRANSMITTAL LETTER

Audit Committee
Port of Seattle
Seattle, Washington

We have completed the audit of Clear Channel Outdoors Inc. (dba Clear Channel Airports). We reviewed information for the period August 1, 2012 – July 31, 2015.

We conducted the audit in accordance with Generally Accepted Government Auditing Standards and the International Standards for the Professional Practice of Internal Auditing. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

We extend our appreciation to the management and staff of the Aviation Business Development Department, Accounting and Financial Reporting for their assistance and cooperation during the audit.

Joyce Kirangi, CPA, CGMA
Director, Internal Audit

AUDIT TEAM	RESPONSIBLE MANAGEMENT TEAM
Margaret Songtantaruk, Senior Auditor	Jim Schone, Director, AV Business Development
	Lionel Vincenti, Sr. Manager ADR, AV Business Development
	Rudy Caluza, Director, Accounting Financial Reporting

BACKGROUND

Lease agreement number 000950 authorizes Clear Channel Outdoor, Inc., dba Clear Channel Airports (Clear Channel) to management the publicly advertisement at the Seattle Tacoma International Airport.

The terms of the agreement provide for fixed Minimum Annual Guarantee (MAG) at $5 million annually. In additional, the agreement requires a concession fee equal to 70% of gross receipts, provided the concession percentage fee is higher than the MAG payment.

The following are the only agreed-upon deductions allowed in the agreement:

a. Standard commissions paid by Concessionaire to a recognized advertising agency.
b. Customary allowances for discounts actually made by Concessionaire to its advertising customers.
c. Reimbursements made to Concessionaire for actual, out-of-pocket costs associated with telephone services on any traveler's information boards or courtesy van information boards.
d. The amount of any sales tax or other excise tax imposed upon the customer and collected by Concessionaire as agent for the taxing body imposing the tax and billed to the customer as a separate item.

FINANCIAL HIGHLIGHTS

KEY FINANCIAL RESULTS FOR CLEAR CHANNEL AIRPORTS		
AGREEMENT PERIOD	**REPORTEDGROSS REVENUES**	**CONCESSION PAID**
2012-2013	$3,956,648	$5,000,000
2013-2014	$5,122,345	5,000,000
2014-2015	$7,842,258	5,489,580
TOTAL	**$16,921,252**	**$15,489,580**

Data Source: PeopleSoft Financials & Propworks

AUDIT SCOPE AND METHODOLOGY

We reviewed information for the period August 1, 2012 – July 31, 2015, utilizing a risk-based approach from planning to examination. We gathered information through document requests, research, interview, observations, and data analysis.

We applied detailed audit procedures to areas with the highest likelihood of significant negative impact as follows:

1. Determine whether Port management monitoring controls are adequate and effective to ensure reported concession fees were properly calculated and remitted timely to the Port.
    - Reviewed the Lessee's chart of accounts to determine whether all applicable revenue accounts were included in the revenues reported to the Port.
    - Validated General Ledger gross receipts and agreed to sub-ledger accounts receivable.
    - Reconciled the reported revenue to Lessee's general ledger and financial statement by account.
    - Tested a risk-based sample:
        - To determine if revenue deductions were valid.
        - Verified the Accounts Receivables were consistent with the contracts between Clear Channel and its customers.
    - Analyzed Port records to determine the timeliness of submitted MAG and concession percentage fee payments.

2. Determine whether Clear Channel complied with significant financial terms of the lease and concession agreement by reviewing the:
    - Agreement to identify significant financial compliance requirements.
    - Insurance coverage and surety company bond to ensure amounts complied with lease terms.
    - Annual report was submitted timely to the Port.

CONCLUSION

Port management monitoring controls were reasonably effective and Clear Channel complied with the significant financial provisions of the agreement. However, certain gross receipts were underreported. We recommend that Port management seek recovery of $7,821 in additional concession fees. See Findings 1 under the Schedule of Findings.

SCHEDULE OF FINDINGS AND RECOMMENDATIONS

1. GROSS REVENUES WERE UNDERRPORTED

The lease agreement, Section 1.10, stipulates:

"Gross Receipts" shall mean the aggregate gross amount of revenue derived by Concessionaire from operation of the Airport advertising and/or promotions concession, including the installation, placement, display, maintenance and operation of advertising display locations at the Airport, and all charges for services performed by Concessionaire or any persons, firms or corporations on its behalf, or any subtenants, licensees or concessionaires of Concessionaire, from, in or the Premises....

The analysis of the lessee's financial records and detailed transaction testing determined the lessee did not report the following three categories of gross receipts not excluded by the lease agreement:

- **Production Transit Revenue**

  Revenue derived from reimbursement by Clear Channel clients for out of pocket expenses on behalf of the advertiser for a third party to produce the advertising graphics to be posted.

- **Installation Services Revenue**

  Reimbursement by clients for out of pocket expenses incurred by Clear Channel, on behalf of the advertiser, for a third party to install their advertisement.

- **Gross Receipts Deduction**

  Clear Channel lacked evidence to support a reduction to gross revenue related to a customer refund.

FINANCIAL RESULTS FOR CLEAR CHANNEL AIRPORTS

AGREEMENT YEAR	REPORTED GROSS REVENUES	UNDER-REPORTED REVENUE	IMPACT TO CONCESSION FEE DUE TO PORT
2012-2013	3,956,648	78,036	0
2013-2014	5,122,346	19,219	0
2014-2015	7,842,258	11,172	7,821
CONCESSION FEE UNDERPAID - DUE TO PORT			7,821

Data Source: PeopleSoft Financials and PropWorks

RECOMMENDATIONS

We recommend management:

1. **Seek recovery of $7,821 for the underpaid concession fees and assess applicability of the one-time late fee and accrued interest, and seek recovery as appropriate.**
2. **Work with Clear Channel to ensure gross receipts subject to concession fees are completely reported.**

Management Response

Management concurs with the audit finding that the tenant did not report Gross Revenue in accordance with the lease. As a result, percentage rent remitted to the Port was lower than the amount due under the lease for lease year 2014/2015. Management will work with the tenant to recover rent and interest due to the Port in accordance with the lease.