No. 08-56750

UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

MICHAEL SHAMES, et al.,

Plaintiffs-Appellants,

v.

CALIFORNIA TRAVEL AND TOURISM COMMISSION,

Defendant-Appellee.

Appeal from the United States District Court
for the Southern District of California
(No. 3:07-cv-02174-H-WMC, Hon. Marilyn L. Huff, U.S.D.J.)

BRIEF FOR AMICUS CURIAE AMERICAN ANTITRUST INSTITUTE SUPPORTING PLAINTIFFS-APPELLANTS' PETITION FOR REHEARING AND REHEARING EN BANC

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CORPORATE DISCLOSURE STATEMENT

Pursuant to Fed. R. App. P. 26.1, the American Antitrust Institute states that it is a nonprofit corporation and, as such, no entity has any ownership interest in it.

TABLE OF CONTENTS

TABLE OF AUTHORITIES

Statutes

Cal. Civil Code

Cal. Gov't Code

Other Authorities

INTEREST OF AMICUS CURIAE

The American Antitrust Institute (AAI) is an independent non-profit education, research, and advocacy organization devoted to advancing the role of competition in the economy, protecting consumers, and sustaining the vitality of the antitrust laws. AAI is managed by its Board of Directors with the guidance of an Advisory Board consisting of over 100 prominent antitrust lawyers, law professors, economists and business leaders.[1] AAI submits that rehearing is necessary because the panel decision rests on a misunderstanding of both prongs of the "state action" defense. If left standing, this decision will encourage the misuse of state statutes to immunize unauthorized and unjustified agreements in restraint of trade to the detriment of the economy and in conflict with our fundamental national policy in favor of free and open competitive markets.

INTRODUCTION AND SUMMARY OF ARGUMENT

The panel decision in this case has created a dangerously expansive interpretation of the "state action" defense. The panel inferred immunity even though the state law at issue cannot reasonably be read to authorize or

[1] AAI's Board of Directors alone has approved this filing for AAI. The individual views of members of the Advisory Board may differ from AAI's positions. No person other than AAI or its counsel has authored any part of this brief or made a monetary contribution to fund its preparation or submission.

even contemplate the alleged underlying illegal conduct, namely a price-fixing cartel intended to exploit consumers and defeat the ordinary market process. *See Catalano, Inc. v. Target Sales, Inc.*, 446 U.S. 643, 649 (1980) (agreement "extinguishing one form of competition among . . . sellers" is unlawful per se). Rather, the panel has interpreted a statute that permits an *individual* passenger car rental company or other business that pays an assessment to the California Travel and Tourism Commission (CTTC) to "pass on some or all of the assessment" to customers, as authorizing competing businesses *collectively* to agree with each other and the CTTC that they will pass on the entire assessment as well as airport concession fees. Moreover, the panel has exempted the CTTC from any active state supervision requirement, treating it as equivalent to a traditional state agency, notwithstanding that the CTTC is dominated by private interests.

The panel's decision cannot be reconciled with well-established Supreme Court and Ninth Circuit state action precedent and sound antitrust policy. The Supreme Court has fashioned stringent standards for the application of the state action defense to private or quasi-governmental actors, which it set forth in a two prong test in *California Retail Liquor Dealers Ass'n v. Midcal Aluminum, Inc.*, 445 U.S. 97 (1980): First, has the state "clearly articulated" its intention to replace competition with regulation

in some sector of its economy? *Id.* at 105. And, second, has the state "actively supervised" the regulatory scheme to ensure that it operates in the public interest? *Id.* "Both [requirements] are directed at ensuring that particular anticompetitive mechanisms operate because of deliberate and intended state policy." *F.T.C. v. Ticor Title Ins. Co.*, 504 U.S. 621, 636 (1992).

The Supreme Court has held that "state-action immunity is disfavored, much as are repeals by implication," *id.*, "because of Congress's 'overarching and fundamental policies' protecting competition," *Columbia Steel Casting Co., Inc. v. Portland General Electric Co.*, 111 F.3d 1427, 1436 (9th Cir. 1996) (quoting *City of Lafayette v. Louisiana Power & Light Co.*, 435 U.S. 389, 398-99 (1978)). And this Court has recognized that "a broad interpretation of the doctrine" is inappropriate because it "may inadvertently extend immunity to anticompetitive activity which the states did not intend to sanction." *Cost Management Services, Inc. v. Washington Natural Gas Co.*, 99 F.3d 937, 941 (9th Cir. 1996). Indeed, a strict application of the state action defense is entirely consistent with federalism values because "[b]y adhering in most cases to fundamental and accepted assumptions about the benefits of competition within the framework of the

antitrust laws, we increase the States' regulatory flexibility." *Ticor*, 504 U.S. at 636.

The goal of the state action doctrine, therefore, is to balance the national interest in competition with an acceptance of reasoned state decisions to replace competition to achieve defined state objectives, allowing no more interference with the national norms of competition than is necessary to achieve those state goals. The panel decision does not demonstrate that kind of a nuanced balancing of competition with articulated state interests. It undermines the requirement of "clear articulation" of the state policies for eliminating the competitive market, and it erroneously expands the exception to the state supervision requirement applicable to municipalities and traditional state agencies. Hence, the opinion, if not corrected, will give more sway to private parties to engage in price fixing under the "cloak" of state authorization and oversight. Rehearing, or rehearing en banc, is essential due to the exceptional importance of maintaining clear, coherent, and appropriate standards for claims of state action immunity.

ARGUMENT

I. THE PANEL DECISION UNDERMINES THE CLEAR-ARTICULATION REQUIREMENT

A. The Statute Does Not Authorize Price Fixing of Car Rentals

One searches in vain through the California Codes and even the brief of the CTTC for the "forthright and clear statement" required by *Midcal* that the State of California has authorized horizontal price fixing by car rental companies. *Columbia Steel*, 111 F.3d at 1439; *see Ticor*, 501 U.S. at 636 ("[O]ur insistence on real compliance with both parts of the *Midcal* test will make clear that the State is responsible for the price fixing it has sanctioned and undertaken to control."). The purpose of the CTTC is "to increase the number of persons traveling to and within California." Cal. Gov't Code §13995.41. Nothing in the California Tourism Marketing Act allows the CTTC or its participants to regulate the prices or pricing policies of car rental firms or any other component of the travel and tourism industry, nor creates standards or mechanisms for reviewing the reasonableness of the prices or pricing policies. On the contrary, in its policy declaration, the Act emphasizes the goal of retaining for participating enterprises' freedom of action with respect to advertising, and by logical extension, all other aspects of their businesses: "These programs are not intended to . . . impede the right or ability of individual business to conduct activities designed to increase . . .

their own respective shares of the California tourism market, and nothing . . . shall prevent an individual business or participant in the industry from seeking to expand its market through [other] means . . . ." Cal. Gov't Code § 13995.1(d)(5).

The Act does authorize the CTTC to collect fees from passenger car rental companies and other businesses in the tourism industry, and permits individual companies to pass on some or all of those fees as a separate charge to their customers. The express language of the statute confers discretion on each assessed company to determine whether and how much of these fees should be passed on. The relevant provision of the Government Code, which is applicable to all assessed companies, provides:

> Notwithstanding any other provision of law, an assessed business *may* pass on some or all of the assessment to customers. An assessed business that is passing on the assessment *may*, but shall not be required to, separately identify or itemize the assessment on any document provided to a customer.

Cal. Gov't Code, § 13995.65(f) (emphasis added).

Specifically with respect to the passenger car rental companies, a provision added by AB 2592 provides:

> When providing a quote, or imposing charges for a rental, the rental company *may* separately state the rental rate, taxes, customer facility charge, if any, airport concession fee, *if any*, tourism commission assessment, *if any*, and a mileage charge, if

> any, that a renter must pay to hire or lease the vehicle for the period of time to which the rental rate applies.

Cal. Civil Code § 1936.01(b)(2) (emphasis added); *see also id.* § 1936.01(b)(3) ("*If* . . . tourism commission assessments are imposed, the rental company shall do each of the following . . . .").

In short, it is plain that the statute merely permits car rental companies and other assessed businesses individually to pass on some or all of the assessment to customers. But it leaves it to normal, competitive marketplace forces to determine the ultimate impact of the assessments on consumers. While the industry as a whole might prefer to see a uniform pass on, maverick firms may instead choose to compete on these fees to gain market share — conduct which is expressly protected by the statute and which is alleged to have been squelched in this case.

The panel thought it significant that "[s]everal provisions refer to the tourism fee being collected 'from the renter,'" slip op. at 8287, but it is obvious from the "if any" language that the fees would not necessarily be imposed on the renter. *See also* Mem. of Points and Authorities in Support of the Rental Car Defendants' Motion to Dismiss the First Amended Complaint 12 (May 29, 2008) ("California Civil Code Section 1936.01(b)(2) makes this pass through permissive, rather than mandatory.").

The panel also thought it significant that the legislature "gave an express grant of state antitrust immunity to state actors complying with the enabling statute." Slip op. at 8287. But this exemption is quite limited. It provides, "proof that the act that is complained of was done in compliance with the provisions of this chapter is a complete defense" to a state antitrust claim. Cal. Gov't Code § 13995.90. This provision begs the question of whether the act complained of – an agreement to pass on the tourism commission assessment and airport concession fees in full – was done "in compliance" with the statute. This provision seems to have been intended to immunize industry's role in setting the assessments from the CTTC, the procedures for which are spelled out in great detail in the statute.

B. The Panel Misconstrued the "Foreseeability" Test

Recognizing that there was no express authorization for price fixing by the car rental companies, the panel decision adopted the view that such conduct was "foreseeable." This was erroneous in two respects. As an initial matter, the opinion conflates the apparent (foreseeable) expectation of the legislature that individual car rental companies were likely to pass on some or all of the fees they paid with an expectation that the companies would do so by an agreement among themselves facilitated by the CTTC. The panel cites evidence in the legislative history suggesting "that the

legislature envisioned the fee being uniformly passed onto rental car customers," and that the legislature contemplated "an industry-wide price hike;" indeed it was warned against such an outcome. Slip op. at 8286-7.

However, whether the rental car companies would uniformly, but *unilaterally*, pass on the tourism assessment and the airport concession fees is quite different from whether they would *agree* to do so, as even the rental car companies themselves emphasized in their motions to dismiss the amended complaint for failure to state a plausible claim of conspiracy.[2] The former may be "anticompetitive" in the sense that consumers are harmed, but it is entirely lawful under the antitrust laws; the latter may constitute criminal conduct. That the panel missed this distinction is evidenced by its contention that "in *Omni* the Supreme Court was clear that there is no 'conspiracy' exception to state action immunity." Slip op. at 8288 (citing *City of Columbia v. Omni Outdoor Advertising, Inc.*, 499 U.S. 365, 374-75 (1991)). Yet *Omni* simply established the point that an allegation of a

[2] *See, e.g.,* Reply Memorandum in Support of the Rental Car Defendants' Motion to Dismiss the First Amended Complaint 1 (July 7, 2008) (arguing that "the Rental Car Defendants – each acting in its unilateral best interest – would want to pass through to consumers two fees that legislation specifically authorized them to pass through"). The district court found that the amended complaint did allege a plausible conspiracy and that issue is not before the Court. Of course, insofar as a conspiracy was necessary to make the pass-through stick, an industry-wide pass through plainly was not inevitable.

conspiracy between government actors and private actors is insufficient to strip a municipality of state action immunity to which it is otherwise entitled. *Omni* did not alter *Midcal*'s "clear articulation" requirement, nor suggest that a conspiracy to raise prices is a foreseeable consequence of a statutory authorization of unilateral price increases.

Second, insofar as the panel found that the legislature foresaw, and therefore authorized, rental car companies to *conspire* to pass on the tourism commission assessment and airport concession fees in full, the panel's foreseeability standard was far too expansive and inconsistent with Supreme Court and Ninth Circuit precedent. Certainly, the CTTC provides a forum at which collusion might occur, and it could use its authority to enforce the resulting cartel. Indeed, the use of the CTTC by the auto rental industry would solve the most vexing problems for a cartel: creating a common price and punishing defectors in an effective way. But the fact that the California legislature may have been negligent in the way it created the CTTC in that it made collusion and its enforcement easier hardly satisfies the foreseeability standard in the case law.

Foreseeability is a concept well known in the law of torts, where it has two distinct meanings. In intentional torts, a consequence that an actor foresees as "substantially certain" to occur is an "intended" consequence

even if the actor did not affirmatively desire that result. *See Restatement (Third) of Torts: Liab. Physical Harm* § 1 (2005). In negligence, every imaginable consequence is foreseeable at some degree of probability. *See id.*, § 3, comment f. It would be incongruous if antitrust immunity were to arise from legislative negligence as opposed to a determination that the anticompetitive consequence was an intended (i.e., substantially certain) result of the legislation, and the case law does not support such a result. *Cf. Ticor*, 504 U.S. at 636 (noting that compliance with *Midcal*'s first prong shows "that the State has not acted through inadvertence").

The Supreme Court has held that an intent to restrict competition is clearly articulated by a state legislative scheme only when it is express or substantially certain to follow from the statute. In *Town of Hallie,* where the Court first used the term "foreseeably" in the state action context, it did so to recognize the inevitable consequences of the statutory scheme created by the legislature.[3] *Omni* applied a similar test: "The very purpose of zoning

[3] *Town of Hallie v. City of Eau Claire*, 471 U.S. 34, 43 (1985). Wisconsin's legislature had conferred the right on local units of government to require as a condition of providing water and sewer service that the area benefiting must also annex to the locality providing such service. The consequent limit on the market for local government services was an inevitable aspect of the legislative scheme. Similarly in *Southern Motor Carriers*, the fact that the legislatures in the affected states had provided for a rate regulatory system meant that regulation had necessarily replaced competition. *See Southern Motor Carriers Rate Conference, Inc. v. United States*, 471 U.S. 48 (1985).

regulation is to displace unfettered business freedom in a manner that regularly has the effect of preventing normal acts of competition, particularly on the part of new entrants. A municipal ordinance restricting the size, location, and spacing of billboards (surely a common form of zoning) *necessarily* protects existing billboards against some competition from newcomers." 499 U.S. at 373 (emphasis added).

The Ninth Circuit itself has in the past rejected a broad foreseeability test for determining whether anticompetitive conduct has been authorized by the state. In *Cost Management Services*, the Court recognized that "the relevant question is whether the regulatory structure which has been adopted by the state has specifically authorized the conduct alleged to violate the Sherman Act." 99 F.3d at 942. And in *Columbia Steel*, the Court rejected the argument that a state's express authorization that two utilities could exchange electric facilities and customers located in overlapping parcels, which created de facto exclusive territories, constituted authorization for the utilities to agree to divide their territories and not to compete for new customers in the future, notwithstanding that the public utility commission subsequently stated that was exactly its intent in approving the property transfer. 111 F.3d at 1439, 1441-42. The Court repeatedly emphasized that the commission had failed to provide "the forthright and clear statement [to

displace competition with monopolies] that it takes to satisfy *Midcal*'s stringent requirements." *Id.* at 1439. Indeed, the Court on rehearing reversed its prior acceptance of a foreseeability test, stating that "'express authorization [is] the necessary predicate for the Supreme Court's foreseeability test.'" *Id.* at 1444 (quoting amicus curiae brief of the Department of Justice) (brackets in original).

The panel distinguished *Columbia Steel* on the basis that "[t]he foreseeability test understandably had little application" because the City of Portland had specifically disapproved the utilities' attempt to establish exclusive territories. Slip op. at 8284 & n.3. However, the conduct of the city was irrelevant to whether the state utility commission, which had the exclusive authority to approve the creation of exclusive service territories, *see Columbia Steel*, 114 F.3d at 1433 n.2, had intended to authorize the market division, and the panel had originally found the restriction on competition was a natural and foreseeable result of the commission's order, *id.* at 1443. The difference between *Columbia Steel* and this case is that in *Columbia Steel*, the Court asked whether the specific alleged anticompetitive conduct was authorized, without regard to foreseeability, while the panel in this case found authorization on the basis of foreseeability, precisely what *Columbia Steel* said was impermissible.

The problem with the open-ended reading of statutes illustrated by the panel opinion is a recurring one among lower federal courts. Informed observers have repeatedly criticized this misuse of the foreseeability approach. In its 2007 report, the bipartisan Antitrust Modernization Commission, created by Congress, observed:

> Following *Town of Hallie*, some courts have applied a low standard for "foreseeability," reasoning that once a state authorizes certain conduct, anticompetitive forms of that conduct may occur and therefore are "foreseeable." To say that anticompetitive types of conduct are "foreseeable" in this way, however, is not the same as finding "a deliberate and intended state policy" to replace competition with regulation.

Antitrust Modernization Comm'n, *Report and Recommendations* 372 (2007) (quoting *Ticor*, 504 U.S. at 636). In this, the AMC echoed the FTC's criticism of a loose foreseeability standard. *See* Office of Policy Planning, Federal Trade Commission, *Report of the State Action Task Force* 25-26 (2003). The AMC observed:

> As the FTC State Action Report pointed out, "'foreseeability' is a matter of degree. The foreseeability test can work well if "the displacement of competition is inherent in the nature of the legislation itself." If the grant of authority is "competition-neutral," however, the mere possibility of anticompetitive conduct is not sufficient to support a finding of a clearly articulated state policy to displace competition.

AMC Report at 372 (quoting FTC State Action Report and ABA Comments).

In sum, the panel decision reflects a serious misapplication of the standards for interpreting state statutes that arguably might authorize anticompetitive conduct. The decision suggests that if a state law makes collusion more possible either by bringing potential conspirators together or by providing a means that might be suborned to reduce the costs of enforcing a cartel, then the state has authorized the cartel, which is clearly contrary to Supreme Court precedent.

II. THE PANEL DECISION ERRONEOUSLY EXPANDS THE EXCEPTION TO THE ACTIVE-SUPERVISION REQUIREMENT

The panel decision commits a second error that is also very troublesome from the perspective of effective protection of the public interest in robust competition: it confers the status of state agency on the CTTC, thus avoiding the requirement of active state supervision, not only with respect to the allegations in this case, but in any federal antitrust claim against the CTTC. By misconstruing the status and role of the governance of the CTTC and misapplying the relevant case law, the panel has adopted an unnecessarily expansive exception to the active supervision requirement that threatens to swallow the rule. The CTTC's management is in the hands of the private industries which it purports to "regulate," which is exactly the situation in which active state supervision is required to ensure that any

anticompetitive conduct in fact serve the state's goals. *See* 1A Phillip E. Areeda & Herbert Hovenkamp, *Antitrust Law* ¶ 227a (3d ed. 2006) ("[W]e would never conclude that a body has more of the attributes of a 'sovereign' not requiring supervision when the controlling number of its members are engaged in business in the very market that the organization purports to regulate.").

There is no dispute that the CTTC is controlled by private industry: 24 out of 37 commissioners are elected by industry. The panel thought it significant that "the CTTC is not *entirely* controlled by industry, as it has twelve governor-appointed commissioners and a governor-appointed Secretary." Slip op. at 8290 (emphasis added). But the members appointed by the governor, all of whom must be "professionally active in the tourism industry," Cal. Gov't Code, § 13995.40(b)(2)(A), like those elected by industry, "are appointed or elected to represent and serve the economic interests of [the various] tourism segments . . . ." *Id.*, § 13995.40(p). Moreover, while the panel emphasized that the CTTC "is under the oversight and control of the state via a gubernatorially-appointed Secretary," slip op. at 8290, the power of the Secretary to review and reverse actions taken by the CTTC is limited. *See* Cal. Govt. Code, § 13995.51(b) (authority limited to reviewing certain travel and expense costs, conflict of

interest claims, use of state funds, and contracts between the commission and a commissioner); *id.*, § 13995.45(d) (marketing plan of the CTTC is subject to the Secretary's approval, but that decision may be overridden by a vote of three-fifths of the commissioners in office).[4]

The panel decision is inconsistent with *Washington State Electrical Contractors Ass'n, Inc. v. Forrest*, 930 F.2d 736 (9th Cir. 1991), which reversed a lower court decision finding the Washington Apprenticeship and Training Council to be a state agency for purposes of state action immunity. This Court found that the "Council may not qualify as a stage agency" because it "has both public and private members, and the private members have their own agenda which may or may not be responsive to state labor policy." *Id.* at 737. In fact, the six "private" members were appointed by the state Director of Labor and Industries, while one public member was appointed by the Governor, and two state officials served as ex officio members. *See Washington State Electrical Contractors Ass'n v. Forrest*, 839 F.2d 547, 549 (9th Cir.), *vacated and remanded*, 488 U.S. 806 (1988). It follows from *Forrest* that the CTTC should not be considered a state

[4] While the Secretary does share control, with the commission, over the executive director, who is a state employee but paid from assessments, Cal. Gov't Code, § 13995.43, all other staff of the Commission are "employees solely of the commission," *id.*, § 13995.42(a).

agency because 36 out of 37 directors are private members, most of whom are not even appointed by a state official.

Contrary to the assertion of the panel, it is of no moment that the private members are appointed or elected from "different tourism industry categories whose interests will not always align." Slip op. at 8290. The issue is whether the interests of the governing members of the "agency" are aligned with the state's interest. *See Hass v. Oregon State Bar*, 883 F.2d 1453, 1459 (9th Cir. 1989) ("When there is no danger that the party engaging in alleged anticompetitive activity is pursuing interests other than those of the state, there is no reason to require the party to satisfy the 'active supervision' requirement."). That was arguably true for the Oregon Bar in *Hass*, insofar as the bar was an instrumentality of the Supreme Court of Oregon, but is certainly not the case for the CTTC.

The panel's expansive reading of the "agency exception" to the active state supervision requirement is an open invitation for all kinds of industries to lobby for legislation conferring unreviewable, self-regulatory authority to engage in anticompetitive conduct and is inconsistent with the well-established, limited scope of the state action doctrine.

CONCLUSION

Because the panel decision seriously weakens the stringent requirements for state action immunity and undermines the Sherman Act as a bulwark against private price-fixing agreements, this appeal should be reheard by the panel or reviewed en banc.

Respectfully submitted,

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s/ Richard Brunell

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CERTIFICATE OF COMPLIANCE WITH RULE 32(a)(7)(C)

Pursuant to Fed. R. App. P. 29(d) and Ninth Circuit Rule R. 32-1, this amicus brief is proportionally spaced, has a type of face of 14 points or more and contains 4135 words.

s/ Richard M. Brunell

Dated: July 9, 2010

CERTIFICATE OF SERVICE

I hereby certify that on July 9, 2010, I electronically filed the foregoing with the Clerk of the Court for the United States Court of Appeals for the Ninth Circuit by using the appellate CM/ECF system.

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