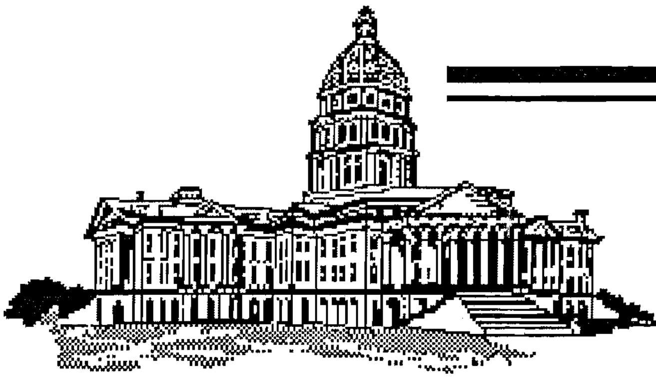

PERFORMANCE AUDIT REPORT

VEHICLE RENTAL AGENCIES:

Reviewing Compliance with Vehicle Registration and Insurance Laws

A Report to the Legislative Post Audit Committee
By the Legislative Division of Post Audit
State of Kansas
June 1984

84-41

PERFORMANCE AUDIT REPORT

Vehicle Rental Agencies: Reviewing Compliance With Vehicle Registration and Insurance Laws

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OBTAINING AUDIT INFORMATION

This audit was conducted by Leo Hafner, senior auditor; and Curt Winegarner, auditor, of the Division's staff. Mr. Hafner was the project leader. If you need any additional information about the audit's findings, please contact Mr. Hafner at the Division's offices.

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All motor vehicles intended for use on Kansas highways are required to be registered in Kansas unless specifically exempted by law or by an interstate agreement executed by the Director of Vehicles. These interstate agreements allow vehicle rental companies operating on an interstate basis to register their cars proportionally in each state in which they do business.

The auditors visited 20 rental agencies in Kansas City, Salina, Topeka, and Wichita to determine if statutory registration requirements were being met. They found that several companies which operate on an interstate basis do not appear to have the appropriate number of vehicles registered in Kansas. Two of the companies they checked had no vehicles registered in Kansas.

No one in the State currently audits vehicle rental companies for compliance with registration laws. To do so would require traveling to corporate offices of the larger interstate companies. Such audits could possibly be conducted by auditors within the Department of Revenue, but further study would be needed to determine if the additional taxes and registration fees which might be generated would be sufficient to cover the costs of the audits.

Are Appropriate Property Taxes Being Paid on Rental Vehicles?

Kansas law does not allow a motor vehicle to be registered in the State unless the appropriate property taxes have been paid. Therefore, to the extent that rental vehicles are being registered in Kansas, the property taxes are being paid. However, companies that do not have the proper number of vehicles registered in Kansas also are not paying the appropriate amount of property taxes in the State.

The auditors also noted that several companies have rental locations in more than one county but register all of their vehicles in one county. The law is not specific regarding where cars should be registered and taxes paid when rental offices are in more than one county. The legislature may wish to clarify the law in this regard.

Is The Insurance Coverage Required By State Law Being Maintained on Rental Vehicles?

All vehicles operated on Kansas highways must be covered by liability insurance that meets minimum levels of coverage set by statute unless the owner qualifies as a self-insuror. Kansas enforces this mandate by requiring all owners to provide the name of their insurance company and the policy number when registering their vehicles. This information is subject to verification by the Department of Revenue. The auditors noted that other states do not necessarily require insurance as a prerequisite for registering vehicles. As a result, it may not be possible to know that a rental vehicle registered in another state and operated in Kansas is uninsured, until that vehicle is involved in an accident. The best control over this appears to be making sure that all rental companies register some of their vehicles in Kansas, thereby subjecting them to the insurance verification procedures involved when a vehicle is registered.

The auditors requested the Department of Revenue to verify that insurance coverage was maintained for the rental vehicles owned by the companies included in this audit. Many of the insurance companies have been slow in responding to the verification request. However, based on the responses received prior to publication of this report, no significant problems exist.

VEHICLE RENTAL AGENCIES:

REVIEWING COMPLIANCE WITH VEHICLE REGISTRATION AND INSURANCE LAWS

This performance audit of firms engaged in the business of leasing and renting motor vehicles was requested by the Senate Transportation and Utilities Committee. Many of these companies do business in a number of states, and the Committee wanted to know whether vehicles were being appropriately licensed, taxed, and covered by insurance. At its March 15, 1984 meeting, the Legislative Post Audit Committee directed its staff to conduct the audit. The audit addressed three main questions.

--Are rental vehicles being properly registered and licensed?
--Are the appropriate property taxes being paid on rental vehicles?
--Is the insurance coverage required by State law being maintained on rental vehicles?

To answer these questions the auditors reviewed rental transactions and vehicle registrations for a total of 20 rental agencies in Kansas City, Salina, Topeka, and Wichita. The agencies visited by the auditors included corporate branch offices of national chains, local licensees of large national firms, smaller interstate firms, and single-location Kansas agencies. The agencies visited are all listed in Appendix A of this report. The auditors also mailed questionnaires about vehicle registrations and insurance to some of the larger firms covered by this audit. Finally, insurance coverage was verified for rental agencies with cars registered in Kansas. The auditors' findings are discussed in the sections that follow.

Are Rental Vehicles Being Properly Registered as Required by Law?

Requirements for the registration and licensure of motor vehicles are generally contained in Chapter 8, Article One of the Kansas Statutes. The law requires every motor vehicle owner to apply for and obtain registration in Kansas for all vehicles intended to be operated in the State. This requirement applies even if the owner is not a Kansas resident and even though the vehicle may be based in a state other than Kansas.

There are three basic conditions under which the requirement to register all vehicles intended to be operated in Kansas need not be met. The first of those conditions is if a vehicle is specifically exempted under K.S.A. 8-128. Exempted vehicles include farm machinery, road construction equipment, fire trucks, school buses, and the like. This exemption does not include rental vehicles.

The second exception is provided in K.S.A. 8-138a. This statute allows out-of-state owners to operate their vehicles in Kansas without obtaining a Kansas registration provided that the vehicle is used primarily for the transportation of the driver and one or more non-paying passengers. This privilege is granted only to residents of states granting the same privilege to Kansas residents. This appears to provide a blanket reciprocity for non-commercial vehicles and would not affect the need for car rental firms to register their vehicles in the State.

The third exception applies to those who are allowed to operate vehicles in Kansas without registering them in this State under an interstate agreement authorized by K.S.A. 8-127 and K.S.A. 74-4302. Such interstate agreements do apply directly to car rental agencies and are explained in more detail below.

Interstate Rental Agencies May Operate Cars in Kansas With Out-of-State Registrations, But They Must Register a Portion of their Fleet in Kansas

Although the law contains no specific provision that directly exempts rental vehicles from the requirement to be registered in Kansas, it does grant authority to the Director of Vehicles under K.S.A. 8-127 and K.S.A. 74-4302 to enter into agreements or contracts with other states to allow for reciprocal registration of vehicles. The Director of Vehicles has entered into such reciprocity agreements. As a result, rental companies that operate on an interstate basis may operate vehicles in Kansas that are registered in another state if they meet the requirements of the interstate agreements.

Although several agreements exist, the one that applies to the largest number of states is called the International Registration Plan. The Plan includes Kansas, 28 other states and one Canadian province. Under the Plan, companies that rent passenger cars must register vehicles in each state in which they have rental locations. The number of cars registered in each state in the current year should be representative of the portion of gross rental revenues derived from business in that state during the previous year.

Some Interstate Firms Appear to Have an Insufficient Number of Vehicles Registered in Kansas

To verify with certainty that interstate rental firms are registering the proper number of vehicles in Kansas, the auditors would have to travel to the corporate headquarters for each company and verify the number of vehicles in the rental fleet, the revenues generated in each state, and the number of vehicles registered in each state. Such a verification was not possible within the scope of this audit.

Instead, the auditors used two methods to obtain information about the level of compliance with Kansas' vehicle registration laws. The primary method involved visiting 20 rental locations for agencies operating in Kansas and reviewing rental contracts to determine how many of the cars rented in Kansas were actually registered in Kansas. Then, for some of the larger companies which appeared to have few rental vehicles registered in Kansas, the auditors mailed a questionnaire to the company to obtain information about the size of their rental fleet, the level of rental revenues generated in Kansas, and the number of cars they had registered in Kansas. The auditors' findings indicate that some firms appear to be in compliance with the law while others are not registering the proper number of vehicles in Kansas.

The table below shows the results of the auditors' field visits for the 14 rental locations having less than 100 percent of their rental fleet registered in Kansas. The companies are grouped into three categories. The first group shows large national chains with local operations that are owned by Kansas companies or individuals. The second group includes corporate branch offices of large national rental agencies (these branches are owned by the corporation, not by a Kansas operator). The third group includes smaller firms that have Kansas locations as well as locations in other states.

Kansas-Owned Licensees of Large National Firms	Transactions Reviewed	Transactions With Kansas Registrations	Percent
National Car Rental			
Salina	76	44	57.9%
Wichita	128	112	87.5
Avis Rent-A-Car			
Salina	25	21	84.0
Hertz Rent-A-Car			
Salina	63	52	82.5
Topeka	241	228	94.6
Corporate Branch Office of Large National Firms			
National Car Rental			
Overland Park	224	0	0.0%
Avis Rent-A-Car			
Overland Park	160	4	2.5
Topeka	167	7	4.2
Wichita	254	16	6.3
Hertz Rent-A-Car			
Wichita	256	231	90.2
Agency Rent-A-Car			
Overland Park	59	38	64.4
Wichita	48	13	27.1
Other Interstate Firms			
Kwik Auto Rental			
Overland Park	79	0	0.0%
All American Auto Rental			
Wichita	28	6	21.4

Kansas-owned licensees of large national firms appear to be in compliance with the law. Based on the auditors' review of rental agreements, Kansas-owned licensees of large national rental firms appeared to be operating within the law. As seen in the top portion of the table above, the rental transactions for most of these companies involved a Kansas-registered vehicle approximately 80 to 90 percent of the time. The 10 to 20 percent of rentals that do not bear Kansas registration appear to be one-way rentals of vehicles owned by the parent corporation or by an out-of-state licensee of the same rental company.

The only exception was the National Car Rental Office in Salina, at which only 57.8 percent of the transactions involved Kansas registered vehicles. Because all vehicles that belong to the Salina location were verified to be registered in Kansas, the auditors can only speculate that the National Car Rental office in Salina is a terminal point for a large number of corporately-owned own-way rentals which are subsequently routed back to the owning city.

Some agencies with out of State ownership appear to have few cars registered in Kansas. Several rental agencies may be in violation of Kansas Vehicle Registration laws. These agencies are found primarily within the bottom two groups shown in the table on page 3. As the table shows, out of 224 rental transactions reviewed for National Car Rental's Overland Park Office, none of the cars were registered in Kansas. Likewise, the auditors reviewed 581 separate rental transactions at the three Kansas offices owned by Avis Rent-A-Car and found that only 27 of those transactions (4.6 percent) involved cars that were registered in Kansas. These two agencies were in direct contrast with the Hertz Rent-A-Car Corporation, where the auditors found that over 90 percent of the 256 rental transactions reviewed involved a vehicle registered in Kansas.

For the smaller interstate agencies shown in the bottom third of the table, the auditors found what appeared to be a similar problem. At Kwik Auto Rental in Overland Park, the auditors reviewed 79 rental transactions and found that all of them involved cars registered in Missouri. The Department of Revenue's files contain no record of any vehicles registered in Kansas under the name of Kwik Auto Rental. A low percentage of Kansas registered vehicles was also noted during the auditors' review of transactions of All American Auto Rental in Wichita. However, the Department of Revenue's records show a number of vehicles registered under the name of this company or its parent corporation.

Some firms confirm non-compliance. The auditors sent a brief questionnaire to each of four firms which appeared to have an insufficient number of vehicles registered in Kansas. Those questionnaires requested information about the number of vehicles in the company's rental fleet, the number of cars the company registered in Kansas, the method for determining the number of cars to be registered in each state, and the percent of gross rental revenue generated in Kansas. Three of those four agencies provided the information requested by the auditors. Avis Rent-A-Car did not respond. The responses to those questionnaires can be seen below.

Company	Fleet Size	Number of Cars Registered in Kansas	Percent of Revenues Generated in Kansas	Proper Number of Registrations in Kansas
All American Auto Rental	10,000	37	.37%	37
Agency Rent-A-Car	14,213	69	1.08%	154
National Car Rental	68,000	-0-	.1%	68

As can be seen, only one of the responding agencies (All American Auto Rental) indicated that it had the proper percentage of its fleet registered in Kansas. Agency Rent-A-Car's response indicates that it has 85 fewer cars registered in Kansas than the law requires. Likewise, National Car Rental's response indicates that it should have at least 68 cars registered in Kansas. At the current time, none of National's vehicles are registered in this State. These responses, although unaudited, tend to support the findings of the auditors' field visits.

To Verify Compliance with Registration Laws Would Require an Audit Involving Work at the Corporate Headquarters

To accurately determine whether interstate rental companies are registering the proper number of cars in Kansas would require a more extensive review than the Committee authorized. Auditors would need to travel to corporate offices of leasing companies to verify the size of each company's rental fleet, the number of vehicles registered in each state, and the gross rental revenues derived in each state.

The Department of Revenue has two groups of auditors that could potentially perform such an audit. There are two auditors within the Motor Carrier Inspection Bureau who audit prorated carriers--primarily trucking companies--having their fleet proportionally registered in Kansas. These companies must register vehicles in Kansas under requirements that are similar to the requirements for car rental agencies. The major difference is that trucks are prorated on miles traveled in Kansas, and rental cars are prorated on the basis of revenues generated.

The Department also has an Audit Services Bureau whose auditors travel to offices of major corporations to audit for sales tax, income tax, and the like. It appears that when auditing the revenues of a rental company to determine the income taxes and other taxes due, the auditors could also check to determine that the proper number of vehicles were registered based on the revenue generated in Kansas.

However, before assigning such additional duties to either of the Department's audit groups, careful analysis would need to be done to ensure that the benefits derived in the form of additional property taxes and registration fees for the State are not outweighed by the cost of performing the additional audit work. That cost would need to be measured both in terms of personnel costs and in terms of other audit work which may need to be foregone to allow time to check on vehicle registrations.

Recommendation

> The Department of Revenue should study the issue of auditing vehicle registrations of rental companies to determine if such audits could be conducted on a cost effective basis by their Audit Services Bureau or by their auditors within the Motor Carrier Inspection Bureau.
>
> If auditing rental companies for vehicle registrations is not feasible, the Department should request each interstate rental

company to annually submit a statement indicating the portion of gross rental revenues generated in Kansas. Using this information, the Department should send a statement to each of these companies explaining the percentage of their vehicles that should be registered in Kansas during the upcoming registration year.

Are Appropriate Property Taxes Being Paid on Rental Vehicles?

Provisions for property taxes on motor vehicles are contained in Chapter 79, Article 51, of the Kansas Statutes. The property taxes are determined by taking 30 percent of the value of the vehicle as determined by a classification schedule developed by the Department of Revenue, and multiplying that amount by the county average tax rate for the county in which the vehicle is registered. Taxes on motor vehicles are levied annually to coincide with the registration year for each vehicle.

The law provides that a county treasurer shall not accept an application for registration of a vehicle unless the person registering the vehicle pays the applicable property taxes. Therefore, to the extent that rental vehicles are being properly registered in Kansas, it follows that the property taxes are being paid.

In Some Cases, the Law is Not Specific Regarding Where Vehicles Should be Registered and Taxes Should be Paid

During their testwork, the auditors noted companies with multiple rental locations in Kansas that registered all of their vehicles in one county. Three of the companies the auditors reviewed fit into this category. National Car Rental in Liberal owns rental locations in Dodge City, Garden City, Hays, Manhattan, and Topeka in addition to the Liberal location. However, according to records at the Department of Revenue, it appears that the company registers all of its cars in Seward County, where Liberal is located. A similar situation was noted for Harries Motor Company in Wakeeney, which operates Avis rental locations in Salina and Hays. All cars for this company appear to be registered in Trego County, where Wakeeney is located. Finally, Salina Leasing and Rental Inc., which operates Hertz locations in Salina, Manhattan, Hays, Great Bend, and Hutchinson, appears to have all of its cars registered in Saline County.

To determine if this practice was contrary to statute, the auditors reviewed the registration laws. K.S.A. 8-129 states that application to register a vehicle shall be made in the office of the county treasurer of the county in which the owner resides or has a bonafide place of business. Because these agencies have a bonafide place of business in several counties, they appear to have an option as to where to register their vehicles. This option directly affects how much tax is paid and where it is paid. For example, National Car Rental of Liberal maintains rental locations in six counties. The auditors assembled the tax rates for the 1985 registration year for three different classes of vehicles in those six counties. Those taxes are shown in the table below.

County	1985 Taxes Class 7 Vehicle	Class 10 Vehicle	Class 11 Vehicle
Ellis	$ 99.57	$153.18	$173.60
Finney	107.66	165.63	187.71
Ford	159.84	245.90	278.69
Riley	147.10	226.31	256.48
Shawnee	203.02	312.34	353.98
Seward	**126.81**	**195.10**	**221.11**

As shown in the table, there are wide variations in the property taxes assessed against motor vehicles in different counties. For example, in Shawnee County, the personal property taxes are 60 percent higher than in Seward County, where the vehicles are registered. In this particular example, however, the cars are not registered in the least expensive county where the company maintains a rental location. Both Ellis and Finney counties have lower tax rates than Seward county. Similar situations were noted for each of the other two companies as well. Thus it appears to be a matter of convenience that the vehicles are registered in the county where the company maintains its corporate office, rather than an attempt at avoiding taxes.

The State does not lose money regardless of where the vehicles are registered. The primary impact of registering vehicles all in one county is that no taxes are paid in the counties where the actual revenues are generated. Another impact could be a slight competitive advantage over other local firms if a multi-county operation registers all of its vehicles in a county with a substantially lower tax rate.

Recommendation

If the legislature perceives the lack of specificity about where to register rental cars to be a problem, K.S.A. 8-129 could be amended to specify where vehicles should be registered when a car rental company operates in more than one county.

Is The Insurance Coverage Required By State Law Being Maintained on Rental Vehicles?

Kansas law requires every motor vehicle operated on Kansas highways to be covered by motor vehicle liability insurance. The minimum limits for this insurance are contained in K.S.A. 40-3107. The owner of a vehicle can provide liability insurance in one of two ways. He or she can purchase a liability insurance policy that meets the minimum requirements of law or become self-insured as provided in K.S.A. 40-3104(d). In order to become self-insured, a vehicle owner must demonstrate the ability to pay any judgment arising out of vehicle ownership or use, must have a minimum of 25 vehicles registered in his or her name, and must obtain a certificate of self-insurance which is subject to the approval of the Insurance Commissioner.

Controls Have Been Established To Aid In the Enforcement of Insurance Requirements

A number of controls are built into the State's systems for regulating vehicles and insurance companies to ensure that proper motor vehicle coverage is maintained. First of all, K.S.A. 40-3118 provides that no vehicle may be registered in Kansas unless the owner has proper liability coverage. To enforce this law, the State requires vehicle owners to provide the name of their insurance company and policy number at the time they register their vehicles. To ensure that the insurance information provided is accurate, the Department of Revenue verifies the coverage with the insurance company for a sample of vehicle registrations.

In order to ensure that the statutory minimum limits of liability coverage are being maintained, the Insurance Commissioner, under K.S.A. 40-3106(b) requires all insurance companies doing business in Kansas to file a declaration stating that their motor vehicle insurance policies, wherever issued, will be considered to provide the minimum coverage required by Kansas law. This means that if a company is certified to do business in Kansas, its policies written on any vehicle in any state automatically conform to the Kansas minimums when that vehicle is driven in Kansas. This is true even if the stated limits of the policy are less than the minimums required by Kansas law.

Insurance companies not doing business in Kansas may also file a declaration with the Insurance Commissioner so that their insured will be in full compliance with Kansas laws when operating their vehicles in this State.

Enforcing Insurance Requirements for Vehicles Registered Outside Kansas May Not Be Possible

Although Kansas has established controls to ensure that automobiles registered in the State have adequate liability insurance, other states do not necessarily maintain the same insurance requirements or controls that Kansas has established. In fact, officials in the Insurance Commissioner's Office indicated to the auditors that approximately 21 states do not have mandatory liability insurance requirements. The lack of insurance requirements in other states can impact the enforcement of insurance requirements for car rental agencies with non-Kansas vehicles, because there is little chance of knowing that such a vehicle is uninsured prior to involvement in an accident.

In reality, however, it appears that the risk from uninsured vehicles owned by car rental agencies may be small. Most car rental companies visited by the auditors appeared to provide a single blanket policy covering all of the vehicles they own. Therefore, to the extent that adequate coverage is provided for a company's cars registered in Kansas, it would appear that the same coverage is being provided for all cars owned by the company. The main risks appear to be from those companies which operate rental locations in Kansas but have no cars registered in this State, and from companies that may drop their insurance coverage after registering their vehicles.

The first of these groups, as mentioned earlier, already appears to be not in compliance with vehicle registration laws. Bringing these companies into compliance with the registration laws would also provide some assurance that the insurance requirements are being met. To determine if dropping insurance coverage was a problem, the auditors enlisted the aid of the Department of Revenue to verify that the stated insurance coverage was being maintained.

Rental Companies With Kansas-Registered Vehicles Appear to Be Maintaining the Required Insurance Coverage

The auditors attempted to verify that current insurance coverage was being maintained for the rental agencies they visited. Two of the companies indicated that they were self-insured. The auditors contacted the Insurance Commissioner's Office to verify that both of these companies did have an approved certificate of self-insurance on file. Two other companies had no vehicles registered in Kansas. As a result, it was not possible to verify that insurance coverage was being maintained.

For the remaining agencies, the auditors requested the Department of Revenue's Driver Control Bureau to use its authority to verify that insurance coverage was being maintained. The Department mailed requests to the insurance companies to verify that coverage was in effect. Many of these companies were slow in responding. Those that responded indicated that the proper coverage was in effect. Rather than delay the report, Legislative Post Audit decided to issue it with the findings in this area still somewhat incomplete. Should the remaining responses reveal any particular problems in this area. The Post Audit Committee will be informed at a later date.

Appendix A

Summary of Rental Locations Audited

	Number of Rental Transactions Reviewed	Number of Transactions Involving Kansas-Registered Vehicles
Kansas City		
Agency	59	38
Avis	160	4
Kwik Auto Rental	79	0
National Car Rental	224	0
Rent-A-Relic	78	78
Salina		
Avis	25	21
Hertz	63	52
National Car Rental	76	44
Payless Car Rental	18	18
U-Save Rent-A-Car	15	15
Wichita		
A-Used Car Rental	25	25
Agency Rent-A-Car	48	13
All American Auto Rental	28	6
Avis	254	16
Hertz	256	231
National Car Rental	128	112
Topeka		
Avis	167	7
Budget	52	52
Dodge City U.S.A.	29	29
Hertz	241	228

APPENDIX B

Agency Response

Kansas

DEPARTMENT OF REVENUE

State Office Building
TOPEKA, KANSAS 66625

June 20, 1984

RECEIVED
JUN 20 1984
LEGISLATIVE POST AUDIT

Mr. Meredith Williams
Legislative Division of Post Audit
Suite 301
Mills Building
Topeka, KS 66612

Dear Mr. Williams:

The Department of Revenue has read the Post Audit report and offers the following response:

The Department will mail questionnaires to the vehicle rental agencies, as Post Audit has, to determine compliance with Kansas registration laws. Any discrepancies indicating non-compliance will be investigated.

The Post Audit report identified the Department's concern whether conducting a specific audit on rental agencies would be cost effective. The report (page 2) outlines the amount of work involved in verifying whether an agency has correctly registered their fleet of vehicles. The Department questions whether the revenue generated would justify the expenditure.

In order to employ perhaps the most cost effective of options, the Audit Services Bureau will include a review of registration practices whenever there is reason to audit a rental agency for corporate or sales tax reasons.

Please be assured that the Department of Revenue will do its best to comply with the wishes of the Post Audit Committee.

Sincerely,

Harley T. Duncan

Harley T. Duncan
Secretary of Revenue

HTD:LDH:sc