

HOUSE OF REPRESENTATIVES STAFF ANALYSIS

BILL #: HB 1545 CS Warranty Associations
SPONSOR(S): Llorente and others
TIED BILLS: **IDEN./SIM. BILLS:** SB 2498

REFERENCE	ACTION	ANALYST	STAFF DIRECTOR
1) Insurance Committee	14 Y, 0 N	Sayler	Cooper
2) Civil Justice Committee	5 Y, 0 N, w/CS	Lammers	Billmeier
3) Commerce Council	8 Y, 0 N	Sayler	Bohannon
4) _____	_____	_____	_____
5) _____	_____	_____	_____

SUMMARY ANALYSIS

Since April 23, 2002, vehicle protection products (VPPs) have been defined as motor vehicle service agreements, regulated under part I, ch. 634, F.S. Prior to that, this product was considered an insurance product to be regulated under the Department of Insurance (predecessor to the Office of Insurance Regulation). However, the determination that a vehicle protection product was an insurance product was not officially made until June 12, 2000, in a memorandum by the Department of Insurance (department). Vehicle protection products like "etch" have been sold since 1998.

Previously, when a VPP was defined to be a motor vehicle service agreement, an insurance product sold to a purchaser or lessee of a motor vehicle had to be properly disclosed on a statutorily specified form. If the disclosure on the incorrect form was intentional or the insurance product was intentionally not disclosed to the buyer, a cause of action potentially existed under the penalty provisions of chapters 520 and 521, F.S., with the possibility of significant liability exposure for dealers selling this product prior to April 23, 2002.

Section one of HB 1545 applies to the period running from January 1, 1998 to April 23, 2002, setting aside penalty provisions of ss. 520.12; 521.006; and 634.271(1), F.S., and stating that these penalties provisions do not apply to any violation arising out of chs. 520, 521, and 634, F.S., if the VPP, contract, or agreement was disclosed to the consumer in writing at the time of purchase in a retail installment contract or lease. This bill requires that if there is a violation where statutory penalties do not apply, the court shall award actual damages and costs, including a reasonable attorney's fee. Nothing in the newly created subsection shall trigger the penalty provisions listed in chs. 520, 521, and 634, F.S.

Upon becoming law, section one of this bill shall apply retroactively to January 1, 1998. The retroactive application is intended to close the window period from January 1, 1998, to April 23, 2002, when vehicle protection products might be classified as "insurance products."

The bill also amends the definition of service warranty found in s. 634.401(13), F.S., to include coverage or indemnification for repair, replacement, or maintenance of a consumer product, for failure due to structural or operational defects, for normal wear and tear, and for damage caused by power surges or accidental damage from handling. Additionally, the bill provides that maintenance service contracts that cover accidental damage must be covered by the contractual liability policy s. 634.406(3), F.S.

This bill will have an unknown fiscal impact on the private sector, as it may discourage lawsuits filed against motor vehicle dealers for failure to disclose the vehicle protection product as insurance prior to April 23, 2002.

The bill takes effect upon becoming a law; section one applies retroactively to January 1, 1998.

This document does not reflect the intent or official position of the bill sponsor or House of Representatives.

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FULL ANALYSIS

I. SUBSTANTIVE ANALYSIS

A. HOUSE PRINCIPLES ANALYSIS:

Provide limited government – This bill retroactively applies to January 1, 1998 and attempts to close a window for filing a cause of action potentially arising from a determination by the Office of Insurance Regulation in 2000 that a vehicle protection product was an insurance product. In 2002, the Legislature amended s. 634.011(7), F.S., to define a vehicle protection product as a motor vehicle service agreement for the purposes of regulation under ch. 634, part I, F.S. This bill is intended to retroactively protect sellers of vehicle protection products who sold these products prior to April 23, 2002, and who sold them in good faith not knowing that they were insurance products.

B. EFFECT OF PROPOSED CHANGES:

Background

Vehicle Protection Products

A vehicle protection product (VPP) is a motor vehicle service agreement that is regulated under ch. 634, part I of the Florida Statutes. According to s. 634.011(7)(b)(1)(b), F.S., a VPP is defined as “a product or system installed or applied to a motor vehicle or designed to prevent the theft of the motor vehicle or assist in the recovery of the stolen motor vehicle.”

VPPs include car alarms, window-etching of vehicle identification numbers, and other applications that deter theft of automobiles.¹ Ordinarily, consumers purchasing such products are required to have comprehensive automobile insurance² and may receive certain benefits in the event their car is stolen and not returned within a specific time period or is completely destroyed. Such benefits may include the costs above what an automobile insurer pays as the actual cash value and the amount of the actual cost of a new or used replacement vehicle, and may also include payment of incidental expenses such as a rental vehicle, vehicle registration and sales tax. These benefits generally exclude the cash value of the stolen vehicle itself and cannot duplicate any benefits or expenses paid to the service agreement holder by the insurer providing comprehensive motor vehicle insurance coverage on the stolen motor vehicle. Alternatively, some products pay a flat dollar amount. The theory behind classifying a theft prevention product as a “warranty” is that the product did not function as originally intended, and the service agreement company honors its warranty on the product by paying the costs to “make the consumer whole” by assuring there are no out of pocket expenses the consumer would have to pay. The cost of an anti-theft guarantees depends on the year and mileage of the vehicle.

Vehicle Protection Product Defined as Insurance Product in 2000

In 2000, the Florida Department of Insurance (now known as the Office of Insurance Regulation or OIR) was asked by an out-of-state corporation to make a determination about whether a vehicle protection product it planned to sell was an insurance product or a manufacturer’s warranty.³ This company wanted to sell a “window-etching” product commonly called “etch.” Etch products engrave the vehicle identification number into vehicle’s windows and are designed to deter theft and aid in recovery of the vehicle. In a memorandum, OIR determined that the etch VPP was an insurance product and

¹ The following paragraph adapted from 2002 Senate Bill 2102 Staff Analysis, February 18, 2002.

² Comprehensive insurance pays for losses from incidents other than a collision, such as theft, fire, windstorm, vandalism, or flood. It also covers damages caused by falling objects or hitting an animal. Such insurance is not a mandatory coverage in Florida.

³ See Department of Insurance Memorandum of June 12, 2000, RE: Window Etching Theft Guard Registration Forms – Foresight Group.

not a manufacturer's warranty. It based its conclusion upon the 1999 statutory definition of insurance in s. 624.02, F.S., and upon five insurance criteria outlined in *Professional Lens Plan, Inc. v. Department of Insurance*, 387 So.2d 548 (Fla. 1st DCA 1980).

Prior to the redefinition of VPP in 2002, OIR had the authority to regulate it as an insurance product.⁴ As an insurance product, the seller would have to be licensed to sell insurance and all such products would be regulated as insurance. According to the 2002 staff analysis for SB 2102, OIR had not received any consumer complaints as to the sale of the vehicle protection agreements and had not initiated any administrative actions in this area,⁵ although in 2003, one company was fined \$27,000 as a result of selling etch products without a proper license.⁶

Vehicle Protection Product Defined as Motor Vehicle Service Agreement in 2002

In response to the precursor of the OIR's determination that "etch" was an insurance product, the Legislature in 2002 passed SB 2102, which amended s. 634.011(7), F.S., to include VPPs, like etch, within the definition of motor vehicle service agreements. This statutory definition of etch as a motor vehicle service agreement took effect on April 23, 2002, when the Governor signed SB 2102 into law. From that date, a vehicle protection product would be regulated as a motor vehicle service agreement.

Motor Vehicle Service Agreement

Motor vehicle service agreement companies are regulated under part I, chapter 634, F.S.⁷ A motor vehicle service agreement (MVSA) means a contract or agreement indemnifying the service agreement holder (purchaser) for the motor vehicle listed on the service agreement against loss caused by failure of any mechanical or other component part.⁸ Such service agreements are generally considered *not* to be insurance products because a warranty promises to indemnify against defects in the article sold, while insurance indemnifies against loss or damage resulting from perils outside of and unrelated to defects in the article itself.⁹ Motor vehicle service agreement companies must be licensed through the OIR to conduct business in the state. Such companies must meet financial solvency, marketing and sales requirements and are examined by the department every 3 years.

Motor vehicle service agreement forms must be filed with and approved by OIR; however, a company's rates need only be filed with OIR.¹⁰ Under the provisions of s. 634.282, F.S., the unfair or deceptive act provisions apply to motor vehicle service agreement companies and to persons who market and sell the service agreements. The deceptive act provisions apply to the advertising, sale, or delivery of motor vehicle service agreements. According to OIR information dated February 13, 2002, of the 162 warranty or service agreement companies in Florida, 50 were motor vehicle service agreement companies.¹¹

Potential Exposure to Lawsuits

According to a representative of the Florida Automobile Dealers Association, the proponents of this bill, motor vehicle dealers who sold VPP to consumers prior to April 23, 2002, (when the definition was changed to motor vehicle service agreements) could potentially be liable for severe statutory penalties under s. 520.12, F.S. or s. 521.006, F.S., depending on whether the alleged violation related a motor vehicle sale or lease. For instance, proponents argue that under s.520.12, F.S., automobile dealers

⁴ See Department of Insurance Memorandum of June 12, 2000, Re: Window Etching Theft Guard Registration Forms – Foresight Group.

⁵ 2002 Senate Bill 2102 Staff Analysis.

⁶ Email from Florida Department of Financial Services, April 7, 2005.

⁷ This paragraph is substantially adopted from the Senate Analysis for SB 2102, February 18, 2002.

⁸ Section 634.011, F.S.

⁹ 44 C.J.S., 473-4, Section 1.

¹⁰ The following paragraph adapted from 2002 Senate Bill 2102 Staff Analysis.

¹¹ The other warranty associations are home warranty associations (18), and service warranty associations (94).

are facing enormous liability because many dealers routinely sold the etch VPP and disclosed it on the Buyer's Order, instead of disclosing it on the Retail Installment Sales Contract (RISC) as a form of insurance product as required by s. 520.07(3)(d), F.S. Since it was not properly disclosed on the RISC, if it can be proved that the non-discloser was a "willful violation," then according s. 520.12(2), F.S., "the buyer may recover from the person committing such violation...an amount equal to any finance charge and any fees charged to the buyer by reason of delinquency, plus attorney's fees and costs incurred by the buyer to assert rights under this part."

In a hypothetical example provided by proponents of this bill, the finance charges potentially recoverable under s. 520.12, F.S., from a medium-sized dealer are quite significant. If a medium-sized dealer sold 100 cars at an approximate cost of \$18,000 each, financed at an 8% interest rate, the finance charge recoverable per car would be approximately \$3,898. Over a four-year period, a dealer's exposure to an Etch VPP class action lawsuit could exceed \$18.7 million.¹² This \$18.7 million does not include the attorney's fees and costs that the statute also allows.¹³

According to both opponents and proponents of this bill, some of these suits have been filed in Florida. The actual number of filed lawsuits is unknown, but according to conversations with both sides, the number is low.

Service Warranties

Section 634.401(13), F.S., currently defines a "service warranty" as "any warranty, guaranty, extended warranty or extended guaranty, maintenance service contract greater than 1 year in length," unless the warranty is:

- a maintenance service contract written for 1 year or less which does not contain provisions for indemnification and which does not provide a discount to the consumer for any combination of parts and labor in excess of 20 percent during the effective period of such contract.¹⁴

Motor vehicle service agreements, transactions exempt under s. 624.125, and certain home warranties are also excluded from this definition.¹⁵ A maintenance agreement includes any "other written promise to indemnify against the cost of repair or replacement of a consumer product in return for the payment of a segregated charge by the consumer."¹⁶ "The term 'service warranty' does not include service contracts between consumers and condominium associations."¹⁷

According to the Florida Automobile Dealers Association, these service warranties are typically sold by retailers to provide extended service on home appliances.

HB 1545

Section one applies to the period running from January 1, 1998, to April 23, 2002. It sets aside penalty provisions of s. 520.12, F.S. (Chapter on Retail Installment Sales), s. 521.006, F.S. (Chapter on Motor Vehicle Lease Disclosure), and s. 634.271(1), F.S. (Chapter on Warranty Associations). It provides that these penalties provisions do not apply for any violation arising out of chapters 520, 521, and 634 of the Florida Statutes if those violations relate to or are connected with sale of a VPP on the retail installment contract or lease or the failure to disclose a VPP on the retail installment contract or lease. The VPP could be the product, contract, or agreement that provides for the payment of vehicle protection expenses as defined by s. 634.011(7), F.S. The bill states that there is no violation if the

¹² Calculation based upon \$3,898 per contract x 100 financed vehicles per month x 48 months.

¹³ Hypothetical example on file with the Insurance Committee.

¹⁴ Section 634.401(13)(a), F.S.

¹⁵ *Id.*

¹⁶ Section 634.401(13).

¹⁷ *Id.* at (b).

product, contract, or agreement was disclosed to the consumer in writing at the time of purchase in a retail installment contract or lease. The provisions of this bill are effective so long as these conditions are met.

This bill provides that if there is a violation where statutory penalties do not apply, the court shall award actual damages and costs, including a reasonable attorney's fee. The bill requires that nothing in the newly created subsection trigger the penalty provisions listed in chapters 520, 521, and 634 of the Florida Statutes.

Section one of the bill applies retroactively to January 1, 1998, thereby covering the window period from January 1, 1998, to April 23, 2002, when VPPs might be alleged to be "insurance products," thereby possibly foreclosing or minimizing the possibility of current and future lawsuits brought against the sellers of VPPs who did not disclose those VPPs as "insurance products" in accordance with chapters 520 and 521, F.S.

Section two of the bill amends s. 634.401(13), F.S., to define a service warranty as any warranty, guaranty, extended warranty or extended guaranty equal to or greater than 1 year in length, which is for a specific duration to perform the repair, replacement, or maintenance of a consumer product or for indemnification for repair, replacement, or maintenance, for the operational or structural failure due to a defect in materials or workmanship, normal wear and tear, power surge or accidental damage from handling.

According to an industry representative, the amendment to s. 634.401(13) will bring Florida law into conformity with model language from the National Association of Insurance Commissioners, except for the additional words providing warranty coverage for damage from accidents or power surges. Current Florida law does not include warranty coverage for accidental damage or damage from power surges, although sixteen states do.¹⁸ Power surge or accidental damage is currently only covered by indemnity insurance.¹⁹ However, an insurance company may dispute a claim of accidental damage, thus offering less certain protection than a warranty covering accidental damage, which provides a guarantee that the damaged product will be replaced.²⁰

A service warranty does not include any warranty meeting the exemption in s. 634.401(13)(a), which exempts maintenance service contracts of less than 1 year duration, which do not provide a discount of more than 20 percent for parts and labor under the contract, for motor vehicle service agreements, transactions exempt under s. 624.125, and home warranties regulated under parts I and II of chapter 634.

The bill further provides that maintenance service contracts that include coverage for accidental damage from handling must be covered by the contractual liability referenced in s. 634.406(3), F.S. Section 634.406(3)(a)-(b) provides that a contractual liability policy must cover 100 percent of claim exposure, and the policy must state that the insurer will pay losses and unearned premium refunds if the service warranty does not fulfill its contractual obligation for any reason. The insurer or association must give a policy holder 60 days' written notice before cancellation or non-renewal of a policy.²¹ The insurance policy must insure all warranty contracts issued while the policy was in effect, regardless of whether the premium has been submitted to the insurer.²² If the service warranty holder cancels the warranty, it is the responsibility of the policy issuer to fully refund any unearned premium to the consumer, subject to cancellation fees.²³ An association may not use both an unearned premium reserve and contractual liability insurance simultaneously, although an association may use both types of coverage on different policies, as long as it is able to distinguish how each individual warranty is

¹⁸ Conversation with representative for Assurant and the American Bankers Insurance Group, April 19, 2005.

¹⁹ *Id.*

²⁰ *Id.*

²¹ Section 634.406(3)(c), F.S.

²² *Id.* at (d).

²³ *Id.* at (e).

covered.²⁴ This provision was added to the bill in response to concerns from OIR regarding the solvency of insurance companies, since the extension of warranty coverage will result in increased liability and additional claims against the providers of warranty coverage.

This bill shall take effect upon becoming law, except that section one shall apply retroactively to January 1, 1998.

C. SECTION DIRECTORY:

Section 1 – Amends s. 634.271, F.S., to preclude the application of statutory penalties relating to the sale of vehicle protection products sold prior to April 23, 2002.

Section 2 – Amends the definition of “service warranty” found in s. 634.401(13), F.S.

Section 3 – Creates an unnamed section providing that contracts including coverage for accidental damage from handling must be covered by the liability policy referenced in s. 634.406(3), F.S.

Section 4 – Provides that this bill shall take effect upon becoming law, except that section one shall apply retroactively to January 1, 1998, upon becoming law.

II. FISCAL ANALYSIS & ECONOMIC IMPACT STATEMENT

A. FISCAL IMPACT ON STATE GOVERNMENT:

1. Revenues:

No anticipated impact.

2. Expenditures:

No anticipated impact.

B. FISCAL IMPACT ON LOCAL GOVERNMENTS:

1. Revenues:

No anticipated impact.

2. Expenditures:

No anticipated impact.

C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:

This bill may minimize the fiscal impact arising from liability lawsuits by statutorily changing what remedies are available to holders of VPPs purchased prior to April 23, 2002. These changes are to apply retroactively to January 1, 1998, enclosing the statutory limitation period in which potential lawsuits could be filed.

According to the proponents of this bill, many motor vehicle dealers who sold such products prior to April 23, 2002, could be potentially liable to pay millions of dollars in penalties arising from class action lawsuits concerning a product no longer defined as insurance (see example above). The proponents would argue that it was a technical, unintended oversight on the part of these dealers. They also argue that if OIR had been concerned about Florida dealers improperly selling this particular “insurance product,” OIR would have pursued enforcement actions against them.

²⁴ *Id.* at (f).

D. FISCAL COMMENTS:

None.

III. COMMENTS

A. CONSTITUTIONAL ISSUES:

1. Applicability of Municipality/County Mandates Provision:

The municipal/county mandates provision in section 18 of article VII of the Florida Constitution does not appear to be applicable since the bill does not appear to require counties or municipalities to take action requiring the expenditure of funds, does not appear to reduce the authority that counties or municipalities have to raise revenue in the aggregate, and does not appear to reduce the percentage of state tax shared with counties or municipalities.

2. Other:

Retroactivity

Florida courts have found that the Legislature has the authority to apply law retroactively as long as the new law does not infringe upon constitutional due process rights or impair a party's vested rights.²⁵ If a statute is intended or interpreted to have a retroactive effect, it must then be determined whether it infringes upon constitutionally protected rights.²⁶ This analysis involves a determination of whether the retroactive change impairs or abrogates a vested right, which would then create due process concerns. If a statutory change impairs or abrogates an expectant or contingent right, it is less likely to raise due process concerns.²⁷ Courts have used a weighing process to decide whether to sustain the retroactive application of a statute that has three considerations: the strength of the public interest served by the statute, the extent to which the right affected is abrogated, and the nature of the right affected.²⁸ Retroactive application of a civil statute has generally been found to be a violation of constitutional limits on legislative power when the statute "impairs vested rights, creates new obligations, or imposes new penalties."²⁹

This bill would not create any retroactive obligations or impose any retroactive penalties, although it could be argued that the bill impairs the vested rights of purchasers of VPPs prior to their legislative reclassification as motor vehicle service agreements in 2002. However, while the bill takes away the right to statutory penalties under chapters 520 and 521, the bill still allows recovery of actual damages and costs, including reasonable attorney's fees. Thus, to the extent that any consumers may have been harmed by the improper or unlicensed sale of a VPP as an insurance product, those consumers retain the ability to recover their actual damages.

B. RULE-MAKING AUTHORITY:

None.

C. DRAFTING ISSUES OR OTHER COMMENTS:

²⁵ *Dept. of Transportation v. Knowles*, 402 So. 2d 1155, 1157 (Fla. 1981). *Village of El Portal v. City of Miami Shores*, 362 So. 2d 275, 277 (Fla. 1978) (citing *McCord v. Smith*, 43 So. 2d 704, 708-709 (Fla. 1949)).

²⁶ *Promontory Enterprises, Inc. v. Southern Engineering & Contracting, Inc.*, 864 So.2d 479, 483 (Fla. 5th DCA 2004).

²⁷ See *R.A.M. of South Florida, Inc. v. WCI Communities, Inc.*, 869 So.2d 1210, 1218 (Fla. 2d DCA 2004); *Promontory*, 864 So. 2d at 483 (other citations omitted).

²⁸ *Knowles*, 402 So. 2d at 1158.

²⁹ *R.A.M.*, 869 So. 2d at 1217 (quoting *State Farm Mut. Auto. Ins. Co. v. LaForet*, 658 So. 2d 55, 61 (Fla. 1995))

As mentioned above, it is not clear by the language of the bill, what situation would constitute a “violation for which such statutory damages do not apply” and trigger the remedy “the court shall award actual damages and costs, including a reasonable attorney’s fee.”

IV. AMENDMENTS/COMMITTEE SUBSTITUTE & COMBINED BILL CHANGES

The Civil Justice Committee considered this bill on April 13, 2005, and adopted it with one amendment, changing the definition of “service warranty” and requiring contracts including coverage for accidental damage to be covered by a statutory contractual liability policy. The bill was reported favorably as a committee substitute.