HOUSE OF REPRESENTATIVES STAFF ANALYSIS

BILL #: HB 97 Motor Vehicle Service Agreement Companies
SPONSOR(S): Mahon
TIED BILLS: **IDEN./SIM. BILLS:** SB 1426

REFERENCE	ACTION	ANALYST	STAFF DIRECTOR
1) Insurance Committee		Sayler	Cooper
2) Civil Justice Committee			
3) Commerce Council			
4)			
5)			

SUMMARY ANALYSIS

Motor vehicle service agreement companies sell motor vehicle service agreements that indemnify a service agreement holder for a motor vehicle against loss caused by failure of any mechanical or other component part that does not function as it was originally intended. These companies must be licensed by the Office of Insurance Regulation and must submit forms for approval.

Currently, motor vehicle service agreement companies operating under part 1 of Chapter 634, F.S., must decide whether motor vehicle service agreements that they issue to purchasers will be covered by the statutorily mandated 50-percent reserve or a contractual liability coverage that covers 100-percent of the service agreements written.

This bill allows companies writing motor vehicle service agreements (MVSA) that maintain net assets of at least $5 million to simultaneously use the 50-percent reserve and the contractual liability coverage for specific blocks of new service agreements produced by specific salespersons. These companies can assign how a block of new service agreement obligations will be covered. The company can simultaneously assign one block of MVSAs sold by one specific salesperson to be covered by the 50-percent reserve and another block of MVSAs sold by one specific salesperson to be covered by a contractual liability insurance policy.

The bill requires the service company to be able to distinguish how each individual MVSA agreement is covered.

This bill provides a minimal positive fiscal impact for a very narrow spectrum of motor vehicle service agreement providers.

FULL ANALYSIS

I. SUBSTANTIVE ANALYSIS

A. HOUSE PRINCIPLES ANALYSIS:

Provide limited government – This bill allows motor vehicle service providers with the requisite assets more flexibility in assigning whether individual MVSAs will be covered by a 50-percent reserve or a contractual liability insurance coverage policy.

B. EFFECT OF PROPOSED CHANGES:

Background

Warranty Associations: Motor Vehicle Service Agreement Companies

The Department of Financial Services is authorized to regulate the salespersons and representatives who sell warranties (as part of the department's authority to license and regulate insurance agents). Warranty associations are regulated by the Office of Insurance Regulation (OIR) under chapter 634, F.S., and include motor vehicle service agreement companies, home warranty associations, and service warranty associations.

Motor vehicle service agreement companies (service companies) sell motor vehicle service agreements (MVSA) that indemnify a service agreement holder for a motor vehicle against loss caused by failure of any mechanical or other component part that does not function as it was originally intended. Motor vehicle service agreement companies are regulated exclusively under Part I, Chapter 634, F.S., except as otherwise provided in that part. Motor vehicle service agreement companies must file their rates and premiums with OIR, but the rates are not subject to disapproval by OIR. These companies must be licensed by the Office of Insurance Regulation and must submit forms for approval.

The Insurance Code authorizes a motor vehicle service agreement company to guarantee or warrant a consumer's motor vehicle and its component parts for any mechanical failure that arises out of the use or operation of the vehicle after the expiration of the manufacturer's warranty.

Motor vehicle service agreements (MVSA) are typically marketed through automobile dealerships, and the dealerships may obtain an agent license to market motor vehicle service agreements. The employees of the automobile dealership may sell motor vehicle service agreements under the dealership's license.

Solvency and Licensure Requirements

In order to be licensed, a service company must meet financial solvency, marketing and sales requirements, and be examined by OIR every 3 years. The financial solvency provisions generally require a service company to have and maintain minimum net assets of $500,000.[1] The solvency provisions, among other things, also require a service company to maintain an unearned premium reserve consisting of unencumbered assets equal to a minimum of 50 percent of the unearned gross written premium on each motor vehicle service agreement, and require amortization of this reserve pro rata over the duration of the service agreement. These assets must be held in the form of cash or invested in securities.[2] However, a motor vehicle service agreement company does not have to maintain reserves of 50-percent of its unearned gross written premiums if the company complies with the following:

[1] Section 634.041(6), F.S.
[2] Section 634.041(8)(a)1., F.S.

- The company must purchase and maintain a contractual liability insurance policy to insure 100-percent of its service contract obligations.
- If the service agreement company does not meet its contractual obligations, the contractual liability insurance policy binds its issuer to pay or cause to be paid to the service agreement holder all legitimate claims and cancellation refunds for all service agreements issued by the service agreement company while the policy was in effect.
- If the issuer of the contractual liability policy is fulfilling the service agreements covered by the contractual liability policy and the service agreement holder cancels the service agreement, the issuer must make a full refund of any unearned premium to the consumer, subject to the cancellation fee provisions of s. 634.121(5), F.S. The sales representative and agent must refund to the contractual liability policy issuer their unearned pro rata commission.
- The policy may not be canceled, terminated, or non-renewed by the insurer or the service agreement company unless a 90-day written notice has been given to the department by the insurer before the date of the cancellation, termination, or non-renewal.
- The service agreement company must provide OIR with claims statistics.

All funds or premiums remitted to an insurer by a motor vehicle service agreement company must remain in the care, custody, and control of the insurer and must be counted as an asset of the insurer. However, this requirement does not apply when the insurer and the motor vehicle service agreement company are affiliated companies and members of an insurance holding company system. If a service company chooses to comply with the requirements listed above but also maintains a reserve to pay claims, such reserve may only be considered an asset of the covered service company and may not be simultaneously counted as an asset of any other entity.[3]

A motor vehicle service agreement company wishing to offer vehicle protection service agreements must meet the requirements set forth in the list described above and certain other requirements when purchasing contractual liability insurance coverage. The contractual liability insurance policy must be issued by an insurance company not affiliated with the service agreement company, unless the insurance company has issued a contractual liability insurance policy to a service agreement company on or before January 1, 2002. Additionally, service agreements providing vehicle protection expenses may be sold only to a service agreement holder that has in-force comprehensive motor vehicle insurance coverage for the vehicle to be covered by the service agreement.[4]

Under current law, a motor vehicle service agreement company must satisfy all the requirements of part 1 of Chapter 634, F.S. A service company under Chapter 634 must maintain contractual liability for 100-percent of its outstanding liabilities under such agreements or maintain an unearned premium reserve account equal to 50-percent of the unearned gross premiums and 15-percent of such premiums must be deposited with the OIR. A motor vehicle service agreement company is currently required to maintain minimum net assets of $500,000 to maintain its license to write service agreements.

According to s. 634.041(9), F.S., service companies may not utilize both the 50-percent reserve and contractual liability insurance coverage simultaneously to cover its obligations. Contractual liability insurance coverage mentioned in statute is also known as contractual liability insurance policy (CLP). Accordingly, a service company may have CLP coverage on MVSAs previously sold and sell new service agreements covered by the 50-percent reserve requirement; or a service company may have contractual liability insurance coverage on new MVSAs sold and have the previously sold service agreements covered by the 50-reserve requirement. It just cannot do both simultaneously on new agreements being sold. The service company must be able to distinguish how each individual service

[3] Section 634.041(8)(b), F.S.
[4] Section 634.041(11), F.S.

agreement is covered – either by the 50-percent reserve or by contractual liability insurance policy coverage.

As a result, a company utilizing the 50-percent reserve must not allow its ratio of gross written premium in force to net assets to exceed 10 to 1. A service agreement company may not utilize both the CLP and the 50-percent reserve simultaneously. It must choose one or the other. An MVSA writer may switch back and forth between using the contractual liability insurance policy coverage and the premium reserve account, but may not use both at the same time.

According to OIR, the purpose of not mixing these methods of coverage is consumer protection. It is designed to prevent a contractual liability insurance coverage company from claiming that a certain block of MVSAs are not covered when the service company claims that they are covered. Such disputes could leave a holder of a valid service agreement without coverage. By requiring all motor vehicle service agreements written within a specified period of time to be covered by either a contractual liability insurance policy or by a 50-percent reserve, this can reduce the likelihood of disputes between a CLP company and a service company regarding what service agreements are covered.

Changes in the Law

This bill allows motor vehicle service agreement companies that maintain net assets of at least $5 million to simultaneously use the 50-percent reserve and the contractual liability coverage for specific blocks of new service agreement produced by specific salespersons. The service companies can assign how new blocks of MVSAs obligations are covered. The company can assign one block of service agreements sold by one specific salesperson to be covered by the 50-percent reserve and another block of MVSAs sold by one specific salesperson to be covered by contractual liability insurance policy coverage. The bill requires the service company to be able to distinguish how each individual MVSA agreement is covered.

C. SECTION DIRECTORY:

Section 1 – Amends s. 634.041(9), F.S., to add paragraph (b). This bill allows a company with $5 million in net assets to simultaneously use 50-percent reserve or CLP coverage for specific blocks of MVSAs written by a certain salesperson.

Section 2 – This bill provides a July 1, 2005, effective date.

II. FISCAL ANALYSIS & ECONOMIC IMPACT STATEMENT

A. FISCAL IMPACT ON STATE GOVERNMENT:

1. Revenues:

   None.

2. Expenditures:

   None.

B. FISCAL IMPACT ON LOCAL GOVERNMENTS:

1. Revenues:

   This bill is not anticipated to increase or decrease revenues.

2. Expenditures:

The bill does not require local governments to spend funds or to take action requiring the expenditure of funds.

C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:

This bill provides a minimal positive fiscal impact for a very narrow spectrum of motor vehicle service agreement providers.

D. FISCAL COMMENTS:

See Direct Economic Impact comment.

III. COMMENTS

A. CONSTITUTIONAL ISSUES:

1. Applicability of Municipality/County Mandates Provision:

The bill does not require counties or municipalities to spend funds or to take action requiring the expenditure of funds. The bill does not reduce the percentage of a state tax shared with counties or municipalities. The bill does not reduce the authority that municipalities have to raise revenue.

2. Other:

None.

B. RULE-MAKING AUTHORITY:

C. DRAFTING ISSUES OR OTHER COMMENTS:

The text lacks specificity. The phrase “specific blocks of new service agreements by specific salespersons” is unclear. There is nothing within the bill that defines the scope of the meaning for “specific blocks” or “specific salespersons.” Neither does the bill detail who is authorized to designate what is a “specific block” or who is a “specific salesperson.”

An amendment has been drafted to clarify the meaning of “specific blocks of new service agreements.”

The Office of Insurance Regulation, in its bill analysis, has voiced some concerns that this bill will make monitoring of the financial condition of service companies more difficult.[5] According to OIR, this bill could decrease the amount of consumer protection that current law provides and could open the door to disputes over whether the MVSA is covered by a 50-percent reserve or a CLP policy.[6]

IV. AMENDMENTS/COMMITTEE SUBSTITUTE & COMBINED BILL CHANGES

[5] Office of Insurance Regulation HB 97 bill analysis on file with the Insurance Committee.
[6] Based on telephone conversations with OIR, March 29, 2005.