



Service Contracts & Extended Warranties

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Kentucky as a Service Contract Hub

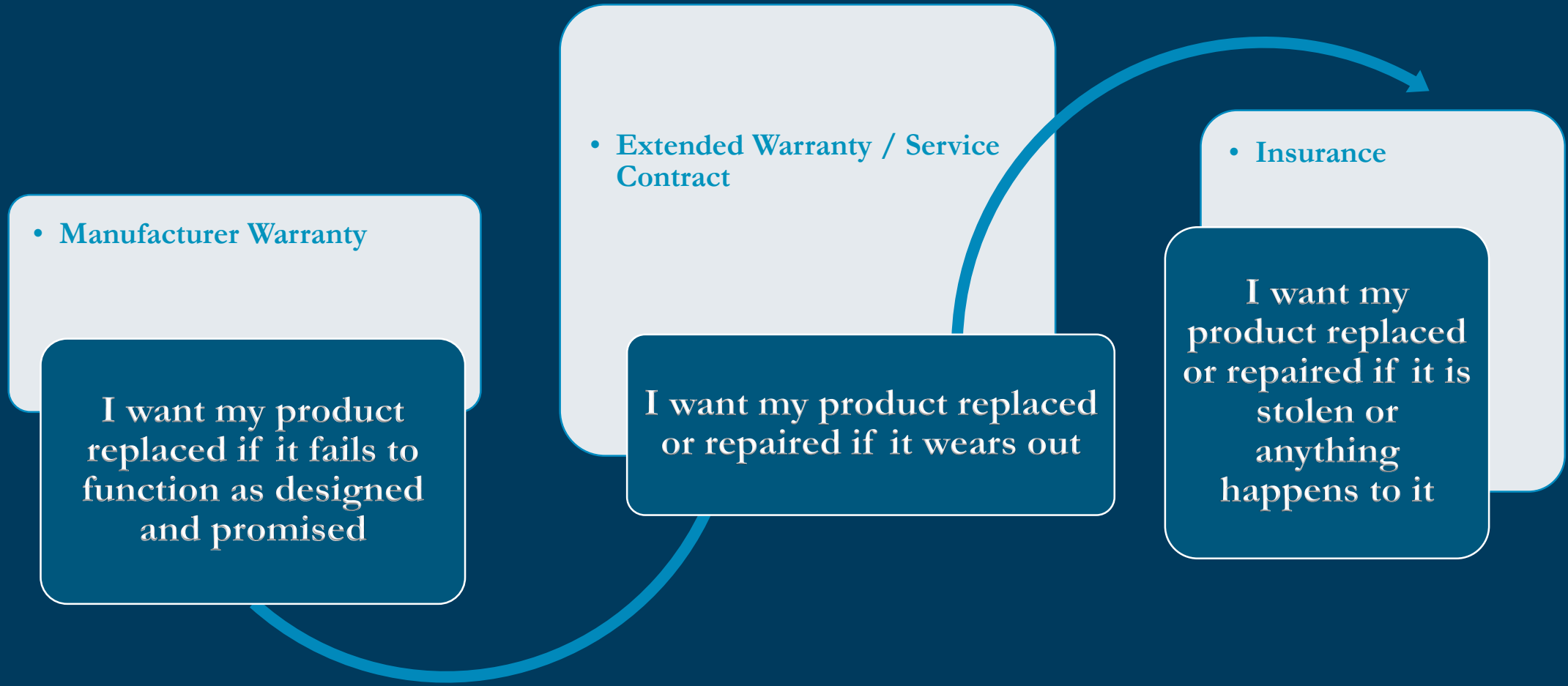
➤ “The city of Louisville, Kentucky, home of both General Electric's Appliance Park and United Parcel Service's Worldport, **has become a major hub for the warranty industry.** AIG Warranty Solutions is just across the Ohio River in Jeffersonville, Indiana, Best Buy's Geek Squad City is just south of the airport, and several new start-ups are downtown.”

➤ Warranty Week, November 14, 2019

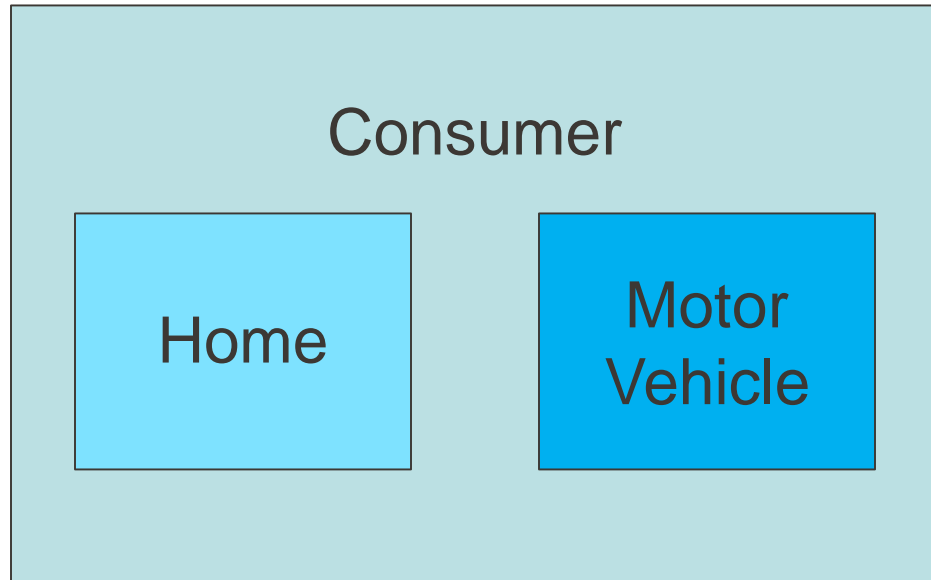
What is a Service Contract?

- Service contracts are a kind of “quazi-insurance.”
 - The service contract **Provider**, or obligor, assumes the risk of indemnifying the contract holder for the cost of repairing or replacing property covered by the service contract.
 - Service Contracts may only cover loss due to a defect in materials or workmanship, or normal wear and tear.
 - Service Contracts cannot cover loss from theft or loss.
- Service contracts are carved out of the insurance code in most states and regulated separately.

Product Spectrum



Types of Service Contracts



Home and Motor Vehicle Contracts are often regulated differently than other consumer service contracts



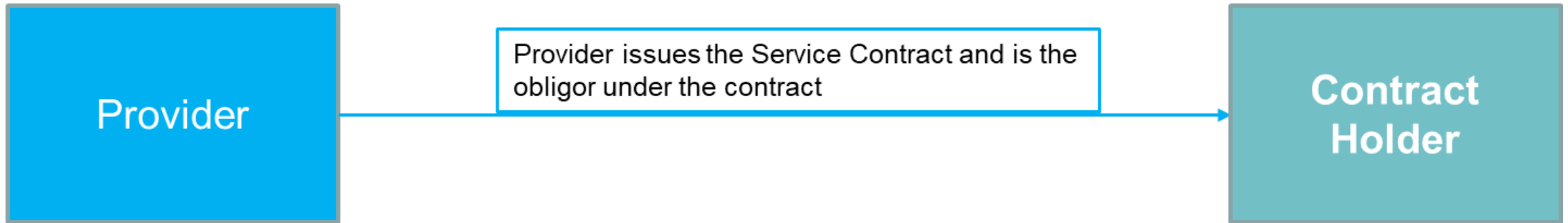
Uncertainty exists with regards to the application of service contract regulations in the commercial context.



Service Contract Provider

- The entity that issues the service contract and is obligated to perform under the service contract by either:
 - (1) providing the covered repair service;
or
 - (2) indemnifying the contract holder for the cost of replacing the covered item.
- Many states require service contract providers to register with regulatory agency (often the Department of Insurance) or obtain a license to issue service contracts.

Service Contract Provider

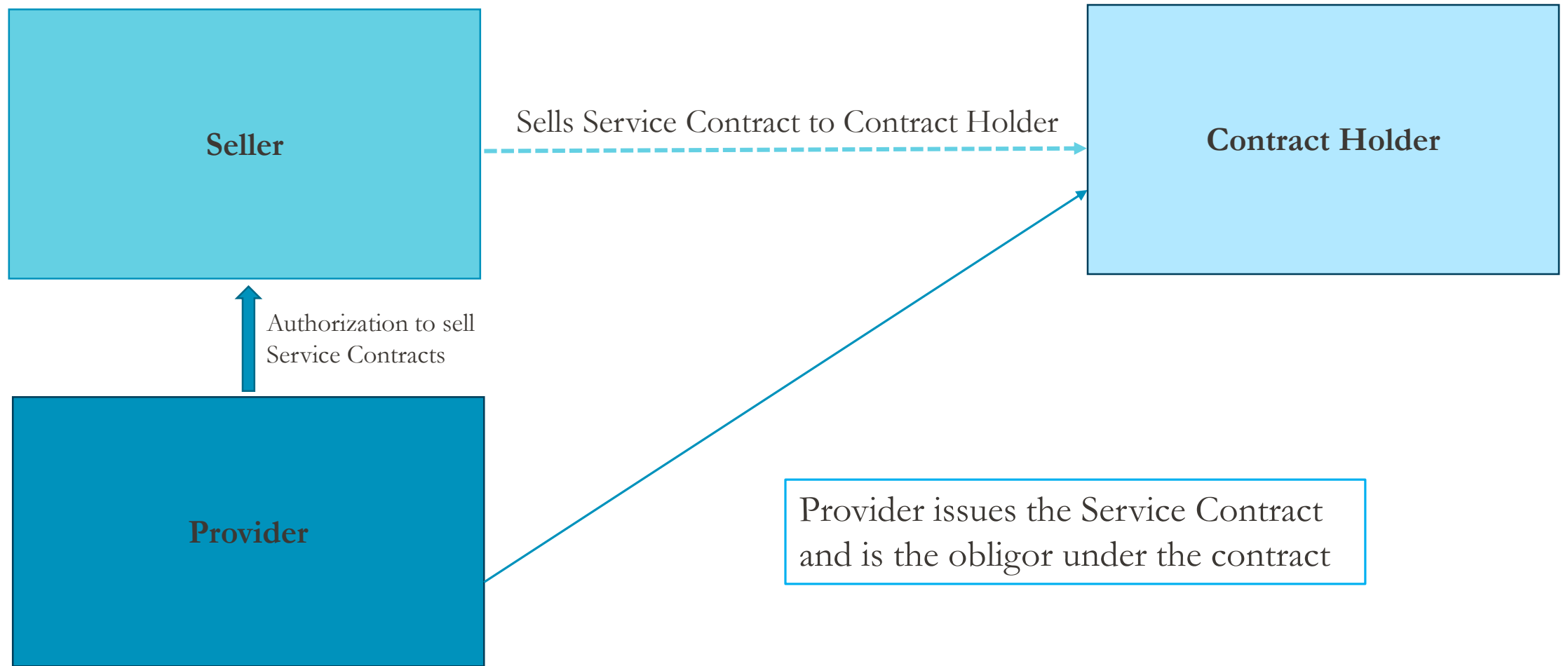




Service Contract Seller

- Service Contract Providers can either sell service contracts directly to consumers or engage **Sellers** to sell service contracts on the Provider's behalf.

Service Contract Seller





Financial Security Requirements

- Most states require service contract Providers to demonstrate financial security as an assurance that they can meet their contractual obligations to consumers.
- Providers can fulfil the financial security requirement by insuring 100% of their service contract risk under a **Contractual Liability Insurance Policy (CLIP)** also known as **Service Contract Reimbursement Insurance**.

Financial Security Options

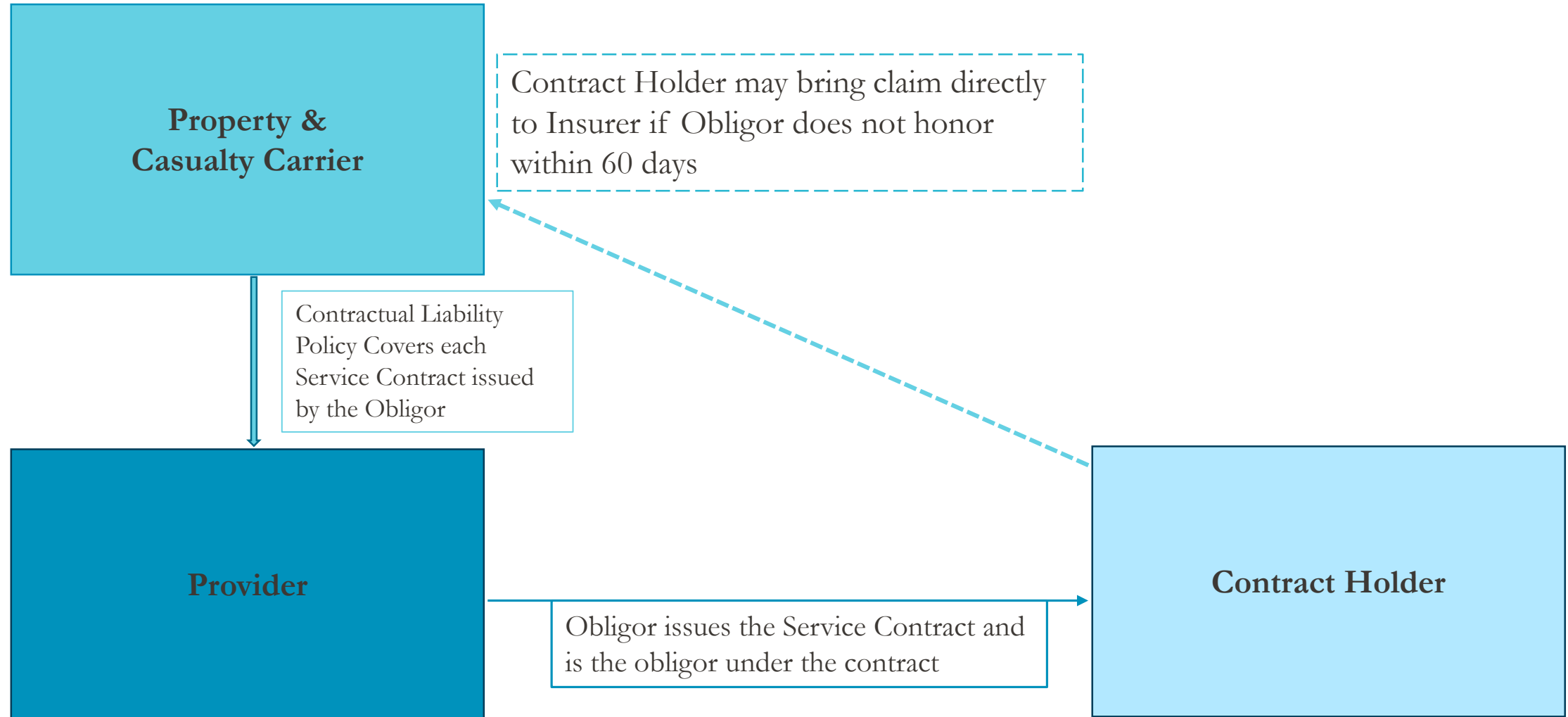
Contractual Liability Insurance	Funded Reserve Account	Net Worth
Ensure all service contracts under a reimbursement insurance policy issued by an insurer authorized to transact insurance in this state	<p>Maintain a funded reserve account for obligations under its contracts issued and outstanding in this state. The reserves shall not be less than [forty percent (40%)] of gross consideration received, less claims paid, on the sale of the service contract for all in-force contracts; and</p> <p>Place in trust with the commissioner a financial security deposit, having a value of not less than five percent [(5%)] of the gross consideration received, less claims paid, on the sale of the service contract for all service contracts issued and in force, but not less than [\$25,000]</p>	<p>Maintain a net worth of \$100 million.</p> <p>If the provider's parent company is used to satisfy the net worth requirement then the parent company may need agree to guarantee the obligations of the provider</p>



Contractual Liability Insurance

- Indemnifies the covered service contract Provider for all losses and loss adjustment expenses incurred on covered service contracts.
 - Providers typically pay premium to the insurer on a per-contract basis.
 - The issuing carrier must have a Certificate of Authority to issue property and casualty insurance.
- P&C Carriers that issue CLIPs are subject to regulation under the insurance code, including special requirements for CLIPs

Contractual Liability Insurance





Contractual Liability Insurance Regulation

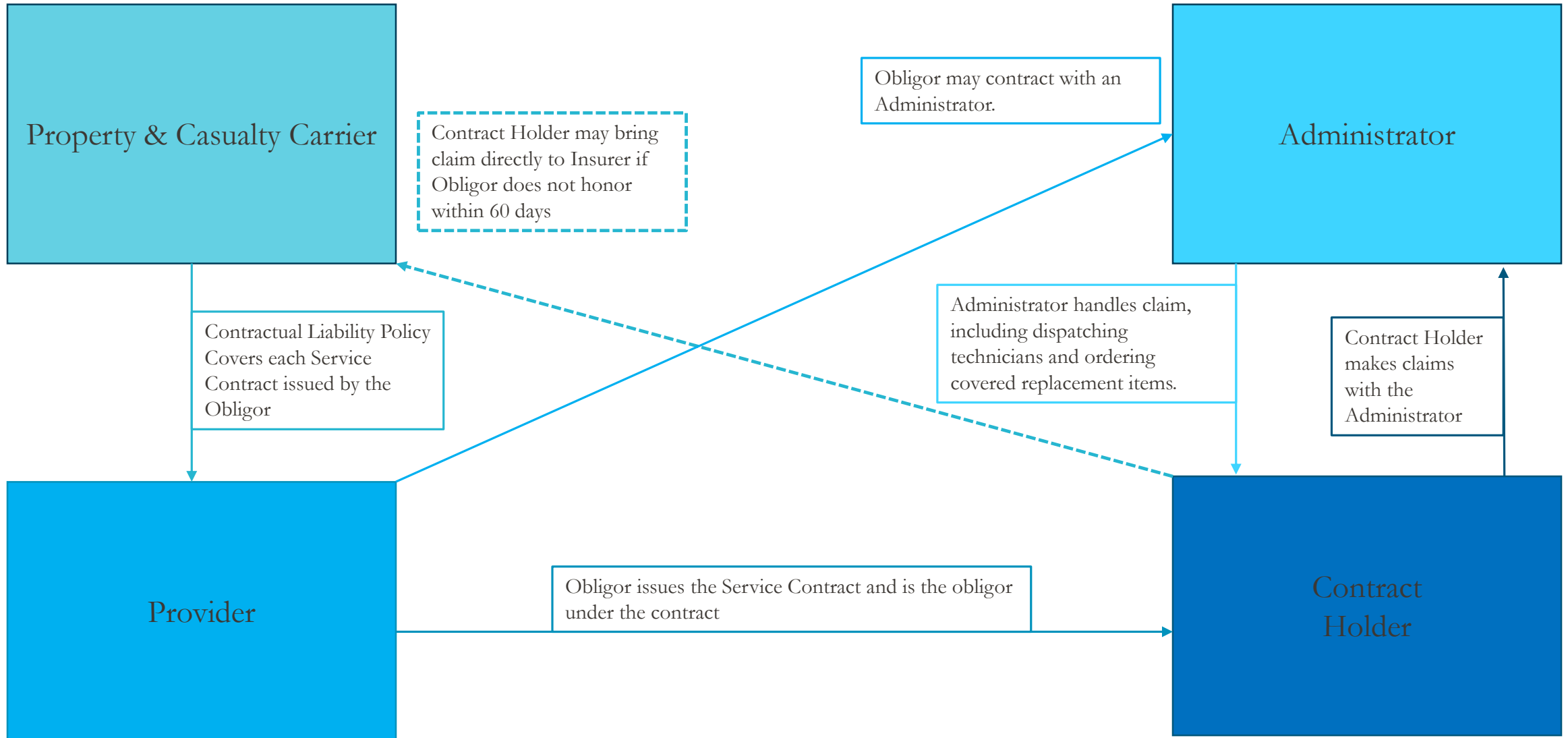
- The CLIP policy and the covered service contracts must clearly state that if the Provider fails to fulfill a claim or grant a valid refund request within a certain time period (usually 60 days), the consumer can bring the claim straight to the insurer.
- The insurer must be prepared to dispatch a technician to provide the covered repair service, not simply make a payment to the consumer.



Administrators

- Service contract providers may appoint **Administrators** to handle claims and dispatch technicians to perform covered repair services.
- Administrators maintain networks of technicians and verify that the technicians have the requisite registration where necessary to perform repairs.
- Administrators may also order replacement products or pay replacement allowances to contract holders where replacing a covered product is less costly than the repair.

Service Contract Administrators





Modernizing Kentucky's Service Contract Laws

- Kentucky is in the minority of states that has not adopted the NAIC Service Contract Model Act, which was developed in 1997.
- Several states have improved upon the model and expanded the scope of what a service contract can do
- As a “major hub” in the industry, Kentucky is well-positioned to modernize its service contract laws and adopt policies to encourage innovation.



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thank you

