



**Bureau of Electronic and Appliance Repair,
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Service Contract Working Group
Initial Meeting – October 22, 2015
Meeting Synopsis

Attendees:

Members: Christine Brandt, Macy's
Scott Cowells, Best Buy
Donald Erwin, Certified Service Manager
Jerry Gallardo, Department of Insurance
Ken Levine, Cozen O'Conner/Consumer Credit Industry Association
Matt Nowels, Meenan Law Firm (Service Contract Industry Council-SCIC)
(attended for Stephen McDaniel)

(all public members attended via teleconference)

Govt. Personnel: Dale Chassé, Deputy Bureau Chief
Michelle Linton-Shedd, Sr. Licensing Analyst
Justin Paddock, Bureau Chief
Karen Skelton, Licensing and Policy Manager
Donald Watts, Licensing Analyst
Michael Weiss, Licensing Technician

Additional stakeholders listened in by phone.

Purpose of the Working Group

Ms. Skelton welcomed the group, and the participants introduced themselves.

She provided an overview and background information on the Bureau's service contract program, which has grown by 10,000 registrants since its inception in 1994. She stated that a market study had been conducted in 1999, and there had been a number of changes in legislation and the marketplace since that time.

She stated the Bureau would like to get a clear picture of the current market and future trends. The Bureau is aware of certain shifts in the industry, based on filings received at the Bureau, including new contract offerings, new products, new relationships between companies behind the service contracts and other issues.

The Bureau is soliciting the assistance of the working group to provide information on offerings, review of California law and regulations (Bureau statute and Song-Beverly Consumer Warranty Act), gain a perspective on consumer and business issues related to service contracts, and to discuss relevant issues and develop recommendations for a report to be completed by the end of October 2016. The working group is made up of representatives of service contract administrators, manufacturers, retailers, servicers, the California Department of Insurance (CDOI) and we hope to add additional consumer advocate representation, so that all perspectives and concerns are addressed.

As CDOI regulates insurance products that have some cross-over with the Bureau's regulations (home protection plan appliances and portable electronics insurance), it is important that there is a clear understanding of each authority and what constitutes these different types of plans, and ensure there is no conflict and that businesses are licensed with the correct entity.

History of Bureau industry regulation – Current Law

Ms. Linton-Shedd provided a history of the service contract industry under the Bureau's regulation (see attached History of Bureau Industry Regulation and Current Law Regarding Service Contracts - Talking Points)

Ms. Brandt asked what year furniture and jewelry were added to service contract regulation. Ms. Linton-Shedd responded that it was January 2004. Ms. Brandt also asked if the increase in registrations was a result of the new product categories added. Ms. Skelton confirmed that was part of the increase, but that the population continued to increase every year, as a result of new offerings by retailers, especially in the cellular telephone arena.

Bureau Statute/Regulations vs. Department of Insurance

Ms. Skelton then stated that there is some overlap with the Department of Insurance in regard to home protection plans which can cover consumer appliances and consumer portable electronic devices, where there are insurance offerings for these type of equipment as well.

Mr. Gallardo stated he was not familiar with the portable electronic insurance, which is a new type, but that he was familiar with the statutes regarding home protection plans, which are contracts related to the sale of a home or for a homeowner purchasing at a later point that covers the repair or replacement of components, systems or appliances within a home. Offering these protection contracts does require a Home Protection Company license with CDOI, with the requirement of being an admitted insurer, in accordance with Insurance Code section 120. The companies are not allowed to collect a commission on these type of protection contracts. There are fiscal requirements, minimum net worth, reserves held on unearned premiums for future claims.

Ms. Skelton said the Bureau will do more research and provide information for future meetings on the portable electronic insurance. Also making sure we can identify on documents we may receive what is a policy vs. a contract.

Mr. Gallardo mentioned that CDOI also covered vehicle service contracts. Ms. Skelton stated the Bureau does not regulate these types of contracts.

Bureau Observations/Findings

Mr. Watts presented information on

- Blanket contracts that cover multiple items added at random times. These contracts are not considered valid as they require constant amendments.

Mr. Paddock asked if any awareness of the companies trying to expand into this area.

Mr. Nowels stated he would take the issue back to SCIC to discuss.

- “Lifetime warranties” are one offering the Bureau is primarily seeing on jewelry contracts, which are being offered most frequently on jewelry. Per the Department’s legal staff they meet the duration requirement, however, the definition of “lifetime” must be expressed clearly in the contract to the consumer to be able for them to understand the terms of the contract, and proration of fees in event of a cancellation.

Mr. Erwin asked to clarify what “lifetime” really is, and Mr. Watts reiterated that it must be clearly expressed.

Ms. Brandt asked what the financial backing requirements were for a “lifetime” contract. Ms. Skelton stated they were the same for all contracts. The financial backing must be maintained while the contract is in force by one of the financial alternatives allowed by law.

Mr. Watts continued the presentation with the following topics:

- Rebranding contracts – the contracts are very generic, but when sent to retailer, the look of the contract changes, logos, form number that don’t correlate and it is sometimes difficult to ascertain that the content is for a contract that has already been approved.
- Retail affiliate programs – also called volume buyers, bundlers, etc., who work between the administrator and various retailers to offer packages of contracts. These companies are not required to be registered as they are not obligated to the consumer, nor do they interact with consumers. The challenge comes when the communication gets broken between administrator and retailers because information is not conveyed (e.g. administrator doesn’t know a certain retailer is selling their contracts, contracts may be outdated, etc.)

- Mobile phone companies offering both service contracts and portable electronic insurance – some carriers have a brochure that lists both offerings. There is a challenge educating retailers and carriers, along with consumers about what type of product is being sold.

Mr. Nowels reiterated the issue for clarification and stated SCIC will be able to contribute information, as they were involved with legislation around the US regarding the insurance on these devices, and agreed that educating the retailers would be a key component, and the cognizance on the insurance policies that there may be some overlapping coverage.

File Audits

Mr. Watts provided information on findings from the Bureau's file reviews it has been conducting over the last year. Of note were:

- Insurance cancellation - Some insurance policies do not contain the required provision that makes the insurer responsible for notifying the Bureau of cancellation. The Bureau has been notifying companies as discrepancies are discovered and has been getting compliance from most companies upon notification.

Ms. Brandt asked for clarification if this was the consumer cancelling. Mr. Watts stated it was not, this was the cancellation of an insurance policy that covered all the contracts sold.

- Determining which contracts are active – it is difficult to ascertain if a contract is an additional filing, replacement for a prior contract, which ones are still in force, and which have been discontinued. Even administrators cannot always verify with certainty which contracts are still being sold. The Bureau would like to archive 'inactive' contracts, where they are still accessible, but not taking up room in the file. The Bureau often receives contracts from retailers that have not been submitted.

Mr. Chassé asked if the Bureau ever received consumer complaints where the contract was not on file. Ms. Skelton responded that it did occur, and sometimes it was just an oversight in failing to file or it was a contract which was inadvertently distributed to a California retailer, but sometimes it was a 'rogue' contract that doesn't meet the requirements of the Song-Beverly Consumer Warranty Act.

Mr. Nowels asked if the Bureau was interested in when the contract was no longer being sold, or when all were no longer in force, since there can be a lapse in the discontinuation of an offering, but the contracts are still active until they expire. Ms. Skelton stated we needed to really know both – when it was no longer being sold, but also when the last contract expires so that if an issue came up with a consumer contract that was still valid, the Bureau could still reference it.

Mr. Paddock stated the purpose was for active enforcement when Bureau field staff visited retailers to know what they should be seeing out there.

Mr. Watts conveyed that the Bureau will still keep a copy of the contract via scanned archive even when no longer active for historical use/reference.

- Relating sellers to administrators – the Bureau has been challenged in keeping track of what sellers sell which administrator contracts, and ensuring the relationship nexus is maintained in our database to reflect changes. Mr. Watts suggested that the administrators provide us with the registration of the sellers to facilitate cross-referencing and keeping the records up to date.

Licensing/Compliance Assistance

Ms. Linton-Shedd provided information on the Bureau's licensing processes and best practices (please see attached document – Service Contract Licensing and Renewals)

Ms. Skelton also interjected that the Bureau also needed to identify internet retailers offering contracts to California consumers. If compliance is not easily gained, the information is given to the Bureau's Enforcement Unit to pursue. Mr. Nowels stated that SCIC can put out a reminder to their membership that the internet retailers do require registration in California.

Mr. Paddock stated that the Bureau would be putting information up on the website regarding the meeting and issues discussed, but that if anyone had any other questions or comments to consider, to bring it to the Bureau's attention to add for discussion.

Mr. Watts discussed the requirement that companies provide proof of financial backing at renewal. He also brought up that companies that utilize the Form 10-K/20-F method need to provide the amount of the total deferred revenues for the service contracts in force for the Bureau to determine if the financial backing is adequate along with the Form 10K/20-F.

Mr. Watts also stated we do not receive updated information routinely from sellers, such as when they change administrators, new contracts, etc, and also stated administrators have a responsibility to make sure their contracts are being sold properly.

Mr. Watts then spoke about consistency in filings – specifically form numbers and revision dates are an issue. Without a form number, it is difficult to determine if the filing has already been reviewed or is new – and if there are several offerings, it makes it very difficult to ascertain which contract is under discussion. Revision dates are critical to determine the version. There has been a suggestion that the Bureau issues a contract number, but we are soliciting ideas to help facilitate the handling of identifying contracts and versions.

Song-Beverly Consumer Warranty Act

Ms. Skelton stated that she would provide members with the most current version of the Song-Beverly Consumer Warranty Act for review, and that the specific sections relating to service contracts were California Civil Code sections 1794.4 and 1794.41. As this is not part of the

Bureau law, but statewide law, the Bureau has no latitude to propose changes. She stated that one of the frustrations the Bureau experiences is that there is an inconsistency in the cancellation provisions based on the type of product, some were 30 days, some 60 days. She is asking that the work group consider if there should be consistency and what would be the appropriate cancellation time frame, if it were one for all products.

Mr. Erwin questioned if the Bureau had authority over certain sections of Song-Beverly. Ms. Skelton responded that the Bureau had authority only for the sections stated above that were specific to service contracts – sections 1794.4 and 1794.41.

Mr. Erwin presented a scenario if a television was purchased along with a service contract, in addition to the manufacturer's warranty being in place, extending the warranty for another four years. Since there is no service literature are parts available, so during the warranty the manufacturer replaces the unit. After the year, the contract is in force. Song-Beverly states that the manufacturer will provide parts and service literature for 7 years to the industry after manufacture. If the manufacturer does not provide an avenue for the repair with parts and literature, then the administrator must replace it for the consumer. He asked why the Bureau did not hold the manufacturer responsible for providing parts and literature.

Mr. Paddock responded the Bureau has no jurisdiction over the manufacturer, and if there was an alleged violation by a manufacturer, someone would have to bring a civil suit against them in court.

Mr. Erwin stated he had 2 legislators in San Diego who are willing to introduce legislation to give the Bureau authority over the manufacturers.

Mr. Paddock responded if legislation is introduced, the Bureau would be available to discuss as technical experts on the matter. The Bureau has no official position of whether or not manufacturers should be included under their jurisdiction, however if a bill was introduced, Mr. Paddock guaranteed that he and staff would be available to answer technical questions regarding the matter.

Mr. Paddock stated that a statement regarding the manufacturer issue would be included in our final report, but reiterated that the purpose of this working group was to address issues directly related to service contract regulation, enforcement, and compliance.

Comments regarding the Bureau

Mr. Nowels commented that working with Bureau staff on the file audits and appreciated the professionalism of staff and the attitude of the Department towards the approach and process of the 'getting it right'.

Ms. Skelton stated that while the term 'audit' was scary, it really was a review and the goal was compliance, and the Bureau had experienced a high level of cooperation.

Open Discussion

Mr. Nowels said not knowing what the boundaries are, but requested consideration of the National Model Act and its uniformity and fit with California's regulation as much as possible and also consideration of moving towards a more generic listing of products (e.g. consumer goods), instead of always having to revise the law to include additional products. Changes in technology and other new products require a legislative change for inclusion.

Ms. Skelton responded that these are the type of recommendations we are looking at for consideration for the group's discussion, especially ways that may remove obstacles for businesses, as long as adequate consumer protection was maintained.

Ms. Skelton also provided an example of a filing for a home security system. The only parts that fell within the scope of the jurisdiction were the video camera and the computer or tablet used in conjunction, so the company amended their contract to just include those items instead of the whole system. She reiterated that the Bureau was looking for suggestions that make regulation better in the industry

Mr. Paddock asked Mr. Nowels if he was aware of any potential changes in the National Model Act. It has remained primarily intact for years, however with each state there may be a slight modification to meet their regulation, but overall very consistent.

Ms. Skelton apologized for technical difficulties in getting members the 1999 market study, but the file size was too large for some mailboxes, however the Bureau will work on a way to get that study to all the members.

Mr. Watts stated he could get that posted to the Bureau website.

Ms. Skelton thanked everyone for their participation and stated the Bureau would be in contact with them regarding the next meeting and subject matter.

Mr. Levine asked if the Bureau envisioned doing another consumer survey like the one JD Franz had conducted in the 1999 survey.

Ms. Skelton responded it was a possibility and stated that one had just been done for a legislative report that had some service contract questions included and that she would provide those to the group for review to see if there was sufficient information, but also we might be able to utilize the Department's resources for an additional survey if warranted.

Ms. Skelton also stated that the Bureau's budget was limited, but appreciated that the group has representation by experts in the major parts of the industry.

Adjournment

Ms. Skelton closed stating that the Bureau is looking for ideas and suggestions that will make this report meaningful.