

*Colorado Legislative Council Staff Fiscal Note*

**STATE  
REVISED FISCAL IMPACT**

(replaces fiscal note dated February 25, 2014)

<b>Drafting Number:</b> LLS 14-0741	<b>Date:</b> April 17, 2014
<b>Prime Sponsor(s):</b> Rep. Williams	<b>Bill Status:</b> Senate Business, Labor, & Technology
Sen. Jahn; Balmer	<b>Fiscal Analyst:</b> Alex Schatz (303-866-4375)

**SHORT TITLE:** CONSUMER GOODS SERVICE CONTRACTS REGUL CHANGES

<b>Fiscal Impact Summary*</b>	<b>FY 2014-2015</b>	<b>FY 2015-2016</b>
<b>State Revenue</b>	<b>\$ 27,000</b>	<b>\$27,000</b>
General Fund	Minimal increase.	Minimal increase.
Cash Funds	27,000	27,000
<b>State Expenditures</b>	<b>\$15,470</b>	<b>\$26,854</b>
Cash Funds	13,560	23,476
Centrally Appropriated Costs**	1,910	3,378
<b>FTE Position Change</b>	0.2 FTE	0.3 FTE
<b>Appropriation Required:</b> \$13,560 - Department of Regulatory Agencies (FY 2014-15)		

\* This summary shows changes from current law under the bill for each fiscal year.

\*\* These costs are not included in the bill's appropriation. See the State Expenditures section for more information.

**Summary of Legislation**

This bill provides for the limited regulation of consumer goods service contracts, in which a consumer pays a premium for the repair, replacement, or maintenance of, or indemnification for, a tangible product with a value of at least \$100.

Service contract providers are required to:

- register with the Division of Insurance (DOI) in the Department of Regulatory Agencies, and pay an annual fee sufficient to defray the DOI's direct and indirect costs under the bill;
- provide consumers with a copy of the service contract and, if the consumer enters into a contract, a receipt of purchase;
- disclose the price and specific terms of a service contract;
- cancel the service contract in certain circumstances and after following specific procedures;
- maintain adequate financial capacity to fulfill their obligations, according to certain options provided in the bill;
- avoid presenting the company or its products as insurance; and
- keep certain records until the company's obligations in Colorado are fully discharged.

The bill also requires companies that reinsure consumer good service contracts to fully cover the obligations of the service contract provider and to pay insurance premium taxes on reinsurance premiums. Premiums paid by a consumer to the service contract provider are not subject to insurance premium taxes.

The bill provides for enforcement of its provisions by the DOI. The DOI may investigate violations of the bill, including examining the records of service contract providers. At its discretion, the DOI may issue cease and desist orders, assess civil penalties of up to \$500 per violation, or pursue legal action in the courts, including injunctive relief and restitution.

The bill regulates only certain aspects of a service contract provider's operations, and does not regulate warranties, home warranty service contracts, motor vehicle service contracts, and certain other service contracts.

## **Background**

House Bill 14-1199 is based on the Service Contracts Model Act. The Model Act was adopted by the National Association of Insurance Commissioners in 1995 to meet the goal of establishing limited authority for a state insurance commissioner to act upon consumer complaints or the potential insolvency of a service contract provider. The Model Act was then modified for the purposes of regulating home warranty service contracts, and a version of this legislation was enacted in Colorado. As noted in the 2007 Sunset Review of Colorado's regulation of home warranty service contracts, DORA does not enforce home warranty service contracts but recourse may be available under the Colorado Consumer Protection Act or the Unfair Practices Act.

Under current law, DOI Regulation 5-1-12 distinguishes between written agreements that fall within the definition of insurance, as regulated by the DOI, and other warranties and service contracts. Under Regulation 5-1-12, if repair, replacement, or maintenance under a service contract are not provided by the service contract provider or a predetermined, limited group of contractors, or if a service contract provides for indemnification rather than repair, replacement, or maintenance, the product is regulated as insurance rather than an exempt service contract. Currently, DORA receives approximately 65 complaints per year regarding service contracts but is precluded from taking action in most cases by its lack of legal authority.

There are at least 100 service contract providers operating in Colorado who will be subject to regulation under the bill.

## **State Revenue**

Approximately \$27,000 in cash fund revenue from registration fees is generated by the bill each fiscal year starting in FY 2014-15. The bill also results in a minimal increase in state General Fund and cash fund revenue from DOI examination of service contract providers.

**Assumptions.** The DOI will assess sufficient registration fees in each fiscal year to pay for a full year of operations, including fees collected in FY 2014-15. Registration fees are deposited in the Division of Insurance Cash Fund.

**Fee impact on service contract providers.** Section 2-2-322, C.R.S., requires legislative service agency review of measures which create or increase any fee collected by a state agency. An estimated fee of approximately \$270 will be paid each service contract provider to the Division of Insurance Cash Fund. The Commissioner of Insurance in DOI will establish and adjust the exact registration fee according to actual costs and number of registrants. Table 1 summarizes the fee impact of this bill.

<b>Table 1. Annual fee Impact on service contract providers.</b>			
<b>Type of Fee</b>	<b>Proposed Fee</b>	<b>Number Affected</b>	<b>Total Fee Impact</b>
Service contract provider registration fee (annual)	\$270	100	\$27,000
<b>TOTAL</b>			<b>\$27,000</b>

**General Fund - taxes and penalties.** The bill clarifies that premiums paid for the reinsurance of service contracts are subject to insurance premium taxes, which will result in a minimal change in premium taxes, assuming most reinsurance producers already pay taxes on all premiums. The bill also permits the DOI to assess civil penalties, with a minimal increase in state revenue due to the discretion of DOI to pursue other disciplinary options, the \$500 cap on penalties per violation, and a small number of cases referred to enforcement.

**Cash Funds - assessment of examination costs.** Certain service contract providers are subject to assessment of examination costs incurred by the DOI. This increase in state revenue is based on a small number of examinations and results in minimal collections to the Division of Insurance Cash Fund. See the Technical or Mechanical Defects section for additional discussion regarding the bill's authority for this revenue source.

**State Expenditures**

The bill increases state expenditures by \$15,470 and 0.2 FTE in FY 2014-15 and \$26,854 and 0.3 FTE in FY 2015-16. Specific costs for DORA, with legal services provided by the Department of Law, are summarized in Table 2 and paid from the Division of Insurance Cash Fund. The bill also results in a minimal workload increase to the Judicial Branch and the Department of State.

<b>Table 2. Expenditures Under HB 14-1199</b>		
<b>Cost Components</b>	<b>FY 2014-15</b>	<b>FY 2015-16</b>
Personal Services	\$9,917	\$19,833
FTE	0.2	0.3
Legal Services (40 hours * 91.08/hour)	3,643	3,643
Centrally Appropriated Costs*	1,910	3,378
<b>TOTAL</b>	<b>\$15,470</b>	<b>\$26,854</b>

\* Centrally appropriated costs are not included in the bill's appropriation.

**Department of Regulatory Agencies.** Responding to an estimated 80 consumer complaints per year, including complaints related to the potential insolvency of a service contract provider, will increase workload for DOI staff by an estimated 640 hours per year. Specifically, complaint intake and initial investigation require 480 hours of work by a Rate/Financial Analyst II. Detailed examinations and preparation of disciplinary cases will require 160 hours of work by a Financial/Credit Examiner IV. Costs for personal services are prorated to one-half of annual costs in FY 2014-15 to account for the effective date of the bill on January 1, 2015.

To provide the DOI legal services necessitated by the bill, the workload of the Attorney General (Department of Law) will increase by approximately 40 hours per year starting in FY 2014-15. In FY 2014-15, this workload will consist primarily in advising the DOI on the scope of its authority and assisting with rulemaking. In FY 2015-16, this workload will consist primarily of assisting the DOI with occasional investigation and enforcement actions.

The fiscal note assumes that the DOI will not preemptively examine the records of service contract providers unless warranted by experience. If DOI's implementation of the bill is eventually expanded to include more use of such permissive authority in the bill, any requirement for additional resources will be addressed in the annual budget process.

**Judicial Branch.** By establishing new standards for consumer goods service contracts, the bill may increase the number of civil claims relating to these contracts, while also expediting the resolution of cases by clarifying the duties of consumers and service contract providers. The overall effect on the workload of trial courts is expected to be minimal and will not require new appropriations.

**Centrally appropriated costs.** Pursuant to a Joint Budget Committee policy, certain costs associated with this bill are addressed through the annual budget process and centrally appropriated in the Long Bill or supplemental appropriations bills, rather than in this bill. The centrally appropriated costs subject to this policy are estimated in the fiscal note for informational purposes and summarized in Table 3.

<b>Table 3. Centrally Appropriated Costs Under HB 14-1199*</b>		
<b>Cost Components</b>	<b>FY 2014-15</b>	<b>FY 2015-16</b>
Employee Insurance (Health, Life, Dental, and Short-term Disability)	\$1,221	\$1,841
Supplemental Employee Retirement Payments	689	1,537
<b>TOTAL</b>	<b>\$1,910</b>	<b>\$3,378</b>

\*More information is available at: <http://colorado.gov/fiscalnotes>

### **Technical or Mechanical Defects**

The bill does not specify that fees from service contract provider annual registrations will be deposited in the Division of Insurance Cash Fund. The fiscal note assumes that the DOI will account for these fees in the fund, which receives other fees from regulated entities. However, Section 10-1-103 (3), C.R.S., the enabling statute of the Division of Insurance Cash Fund, may require amendment to authorize service contract provider fees from the bill as a source to the fund.

The bill states that service contract providers bear the cost of examinations "in accordance with Section 10-1-205 (4)." No specific authority to assess examination costs is provided in this statute. Certain financial and market conduct examination costs are assessed to insurers under Section 10-1-204, C.R.S. The fiscal note assumes that relevant statutory authorities are applicable to service contract providers based on the bill's provision that the Commissioner of Insurance may conduct examinations under Sections 10-1-201 to 10-1-205, C.R.S.

**Effective Date**

The bill takes effect January 1, 2015, if no referendum petition is filed.

**State Appropriations**

For FY 2014-15, the bill requires, and includes, a cash fund appropriation of \$13,560 to the Department of Regulatory Agencies from the Division of Insurance Cash Fund, and an allocation of 0.2 FTE. Of this amount, \$3,643 is reappropriated to the Department of Law for legal services.

**State and Local Government Contacts**

Regulatory Agencies  
Judicial Branch

Personnel and Administration  
District Attorneys

Law  
State