



**ESTADO LIBRE ASOCIADO DE PUERTO RICO
OFICINA DEL COMISIONADO DE SEGUROS**

October 18, 2006

RULING NO.: N-AM-9-66-2005

**TO ALL DOMESTIC INSURERS AND ALL SERVICE PROVIDERS
AUTHORIZED TO ISSUE SERVICES CONTRACTS IN PUERTO RICO**

SERVICE CONTRACT PROVIDER REQUIREMENTS

Dear Ladies and Gentlemen:

The Office of the Commissioner of Insurance, "hereinafter OCS", has received a considerable number of applications from entities interested in obtaining a permit in order to issue service contracts in Puerto Rico. In the evaluation process of said applications, we have detected that the cost to the consumer for the contracts which they propose to sell vary significantly from one another without being able to distinguish if such variation respond to the extension of the coverage. This does not allow the OCS to evaluate whether the consumer is paying a fair and reasonable fee for the offered services.

On the other hand, and particularly with extended warranty contracts, we observed that the cost of the contract is charged to the consumer since the day the object of the contract is purchased¹, although the coverage is activated, in most cases, once the warranty of the manufacturer expires.

Therefore, recognizing that the sale of service contracts has proliferated in Puerto Rico, and for the sake of providing the Puerto Rican consumer confidence in that they will receive services according to paid prices, pursuant to the provisions of

¹ This situation is clearer and relevant in extended warranty contracts for automobiles, and musters greater relevance due to the manner in which these contracts are marketed.

Article 2.030(2) of the Insurance Code of Puerto Rico, 26 L.P.R.A. sec. 203(2), we establish the following:

1. According to the procedure established by the OCS for service contract providers, it must be presented, at the moment of submitting a filing for evaluation, a certification declaring that the fees to be charged under the program are adequate and not excessive. If the service contract is specifically to provide the service of extended warranty and the fees are collected since the consumer buys the product with the manufacturer's warranty in place, the certification must also confirm that the fees have been discounted, and that they represent the present value in consideration of the period of the manufacturer's warranty or the period that has not elapsed of the manufacturer's warranty. The certification has to be signed by a qualified actuary. In addition, the certification must be prepared every two years, while the product is in force, and must be submitted to this Office no later than March 31 of the year following said period. Notwithstanding, those authorized providers whom have not presented a certification by the date of this ruling letter, shall submit their corresponding certification for the year 2005, on March 31, 2006.
2. Service contracts that specifically provide the service of extended warranty, and whose fees are collected since the consumer purchases the product, must include a cancellation clause specifying that, if there is a cancellation during the period in which the manufacturer's warranty is still in place, the amount to be returned shall be determined as it is described next. In case that the pro rata earned amount is greater than \$65.00 multiplied by the year(s) in effect of the service contract before the expiration of the manufacturer's warranty, only the product of this quantity will be retain as a minimum premium in the event of a cancellation. If the pro rata earned amount is less than said product, then the retention will be the pro rata earned amount. This provision is necessary since it has been brought to our attention that these types of contracts are being cancelled pro rata, and in occasion excessive amounts are earned when the property is declared a total loss during the period in which the product still has in effect the manufacturer's warranty, specifically in regarding to automobile losses due to theft or collision in the first few years of financing. The amount hereby established has the purpose of considering the additional provisions for the incidental payments of other services that extended warranties have, as well as, the coverage that some of them offer for certain parts not covered by the warranty.

3. Whenever the charges for the services contract are included in the financing agreement of the product, the cancellation clause in the service contract must establish that in case of cancellation, the return premium check will be issued on behalf of the contract owner and the finance entity. It is indispensable that the contract owner retains the right to endorse the check, in order to have the opportunity to require that the financing account be adjusted when crediting said amount to the account. We want to emphasize that there are occasions in which a service contract cancellation is processed without necessarily resulting from the repossession or total loss of the financed property.
4. All service contract providers that will use a reimbursement policy to guarantee their obligations under the contract shall submit a certification from the insurer who issues the policy expressing that they in fact will issued the policy to the provider, at the rates that for the services that the policy guaranties the OCS has approved to the insurer.

All service contracts in force, regardless of when they were approved by the OCS, are hereby amended by this ruling letter in regards to their cancellation clause, and therefore all service contract providers shall proceed accordingly with what is hereby established.

Cordially,

Dorelisse Juarbe-Jiménez
Commissioner of Insurance