

SERVICE CONTRACT PROVIDERS AND ADMINISTRATORS

Occupations Code

Title 8. Regulation of Environmental and Industrial Trades

Chapter 1304

Administered by the Texas Department of Licensing and Regulation

(Effective September 1, 2009)

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SUBCHAPTER A. GENERAL PROVISIONS

Sec. 1304.001. Short Title

This chapter may be cited as the Service Contract Regulatory Act.

Sec. 1304.002. Definitions

In this chapter:

- (1) "Administrator" means a person, other than the provider of the service contract or an employee of the provider, who is responsible for the third-party administration of a service contract.
- (2) "Commission" means the Texas Commission of Licensing and Regulation.
- (3) "Consumer" means an individual who, for a purpose other than resale, buys tangible personal property that is:
 - (A) distributed in commerce; and
 - (B) normally used for personal, family, or household purposes and not for business or research purposes.
- (4) "Department" means the Texas Department of Licensing and Regulation.
- (5-a) "Executive director" means the executive director of the department.
- (6) "Person" means an individual or an association, company, corporation, partnership, or other group.
- (7) "Provider" means a person who is contractually obligated to a service contract holder under the terms of a service contract.
- (8) "Reimbursement insurance policy" means a policy of insurance issued to a provider to:
 - (A) reimburse the provider under a service contract the provider issued or sold; or
 - (B) pay on behalf of the provider all covered contractual obligations that are incurred by the provider under a service contract the provider issued or sold and that the provider does not perform.
- (9) "Service contract holder" means a person who purchases or otherwise holds a service contract.

Sec. 1304.003. Service Contract

- (a) In this chapter, "service contract" means an agreement:
 - (1) that is entered into for a separately stated consideration and for a specified term; and
 - (2) under which a provider agrees to repair, replace, or maintain a product, or provide indemnification for the repair, replacement, or maintenance of a product, for operational or structural failure or damage caused by a defect in materials or workmanship or by normal wear.
- (b) A service contract may also provide for:
 - (1) incidental payment or indemnity under limited circumstances, including towing, rental, and emergency road service;

- (2) the repair or replacement of a product for damage resulting from a power surge or for accidental damage incurred in handling the product; or
 - (3) identity recovery, as defined by Section 1306.002, if the service contract is financed under Chapter 348, Finance Code.
- (c) For purposes of Subsection (a), normal wear for a motor vehicle may include minor and reasonable wear and tear that a vehicle sustains in everyday ordinary operation including:
- (1) small dents, dings, and creases repairable by the process of paintless dent removal without affecting the existing paint finish and without replacing vehicle body panels or sanding, bonding, or painting;
 - (2) small windshield chips and cracks repairable without replacement of the entire windshield;
 - (3) worn tire tread;
 - (4) worn interior fabric or carpet items; and
 - (5) tire and wheel damage resulting from ordinary road hazards such as potholes, rocks, wood debris, metal parts, glass, plastic, or composite scraps.
- (d) Subsection (c)(5) does not apply to tire damage covered under an agreement sold by a tire manufacturer.

Sec. 1304.0035. Controlling Person

- (a) In this chapter, "controlling person" means an individual who:
- (1) possesses direct or indirect control of at least 25 percent of the voting securities of a corporation;
 - (2) possesses the authority to set policy and direct the management of a business entity;
 - (3) is the president, the secretary, or a director of a corporation; or
 - (4) is a general partner of a partnership.
- (b) An individual who is a controlling person of a corporation or other business entity that is the general partner of a limited partnership is a controlling person of the limited partnership.

Sec. 1304.004. Exemptions

- (a) In this section:
- (1) "Maintenance agreement" means an agreement that provides only for scheduled maintenance for a limited period.
 - (2) "Warranty" means an undertaking made solely by the manufacturer or importer of a product or the seller of a product or service that:
 - (A) guarantees indemnity for a defective part, mechanical or electrical breakdown, or labor cost or guarantees another remedial measure, including the repair or replacement of the product or the repetition of service;
 - (B) is made without payment of additional consideration;
 - (C) is not negotiated or separated from the sale of the product or service; and

(D) is incidental to the sale of the product or service.

(b) This chapter does not apply to:

- (1) a warranty;
- (2) a maintenance agreement;
- (3) a service contract sold or offered for sale to a person who is not a consumer;
- (4) a residential service contract sold by an entity licensed by the Texas Real Estate Commission under Chapter 1303;
- (5) an agreement issued by an automobile service club that holds a certificate of authority under Chapter 722, Transportation Code;
- (6) a service contract sold by a motor vehicle dealer on a motor vehicle sold by that dealer, if the dealer:
 - (A) is the provider;
 - (B) is licensed as a motor vehicle dealer under Chapter 2301; and
 - (C) covers its obligations under the service contract with a reimbursement insurance policy; or
- (7) a contract offered by a local exchange telephone company that provides for the repair of inside telephone wiring, if:
 - (A) the contract term does not exceed one month; and
 - (B) the consumer can terminate the contract before a new contract term begins without liability except for payment of charges for the term that has begun.

Sec. 1304.005. Exemptions From Certain Other Laws

Marketing, selling, offering for sale, issuing, making, proposing to make, and administering a service contract are exempt from:

- (1) Chapter 1303;
- (2) Chapter 722, Transportation Code; and
- (3) the Insurance Code and other laws of this state regulating the business of insurance.

Sec. 1304.006. Purchase Requirement Prohibited

A person, including a bank, a savings and loan association, a lending institution, or the manufacturer or seller of a product, may not require the purchase of a service contract as a condition of a loan or the sale of property.

Sec. 1304.007. General Investigative Power of Executive Director

- (a) The executive director may investigate a provider, administrator, or other person as necessary to enforce this chapter and protect service contract holders in this state.

- (b) On request of the executive director, a provider shall make the records required by Section 1304.155 available to the executive director as necessary to enable the executive director to reasonably determine compliance with this chapter.

SUBCHAPTER C. REGISTRATION REQUIREMENTS

Sec. 1304.101. Registration Required; Exemption From Other Licensing Requirements

- (a) A person may not operate as a provider or administrator of service contracts sold in this state unless the person is registered with the department.
- (b) Except for the registration requirement of this subchapter, a provider, service contract seller, administrator, or other person who markets, sells, or offers to sell service contracts is exempt from any licensing requirement of this state that relates to an activity regulated under this chapter.

Section 1304.101(a) as amended by HB 1286 of the 79th Legislature take effect March 1, 2006

Sec. 1304.102. Application for Registration or Renewal; General Requirements

- (a) An applicant for registration or registration renewal must submit an application to the executive director.
- (b) The application must:
 - (1) be in the form prescribed by the executive director; and
 - (2) include evidence satisfactory to the executive director of compliance with the applicable financial security requirements prescribed by Section 1304.151, if the application is for a provider registration or renewal.
- (c) The department may refuse to issue or renew a registration if the applicant or a controlling person of the applicant has violated this chapter or a rule or order issued by the commission or executive director.
- (d) A person who makes a false statement in an application or in any document provided with an application is subject to disciplinary action under Subchapter E, including denial of the application or suspension or revocation of a registration.

Sec. 1304.1025. Additional Registration and Renewal Requirements for Providers

- (a) In addition to the requirements of Section 1304.102, an applicant for issuance or renewal of a provider registration must file with the application:
 - (1) the reimbursement insurance policy, if the provider is using a reimbursement insurance policy; and
 - (2) a biographical affidavit, in a form prescribed by the executive director, for each controlling person of the provider.
- (b) The executive director may not issue or renew a registration to a provider unless the provider provides evidence to the executive director that:
 - (1) each controlling person of the provider is trustworthy and can competently manage the affairs of the provider in compliance with this chapter; and
 - (2) the provider can meet the provider's obligations under service contracts and this chapter.
- (c) Not later than the 30th day after the date of a provider's initial registration, the provider must provide to the department a list of any Internet website address through which a consumer may purchase the provider's service contracts and the name, assumed name, street address, and telephone number of:

- (1) any administrator appointed by the provider under Section 1304.153; and
- (2) any seller of the provider's service contracts, other than a seller that is:
 - (A) an employee of this provider; or
 - (B) a business with a physical location in this state at which a consumer may purchase a service contract.
- (d) The provider shall update the list required by Subsection (c) with each renewal.

Sec. 1304.103. Registration and Renewal Fees

- (a) The executive director shall develop a tiered schedule of registration and renewal fees under which a provider's fee is based on the number of service contracts the provider sold in this state during the preceding 12-month period.
- (b) The commission shall set the amounts of fees to cover the costs of administering this chapter, including registration and renewal fees for administrators.
- (c) To register or renew a registration, a provider or administrator must pay the appropriate fee.

Sec. 1304.104. Information Concerning Number of Service Contracts Sold

Information concerning the number of service contracts sold by a provider that is submitted under Section 1304.103:

- (1) is a trade secret to which Section 552.110, Government Code, applies; and
- (2) may be used only by the executive director and the department in developing the tiered fee schedule under Section 1304.103.

Sec. 1304.105. Renewal.

The commission shall adopt rules regarding the renewal of a registration issued under this chapter.

SUBCHAPTER D. PRACTICE BY SERVICE CONTRACT PROVIDERS AND ADMINISTRATORS

Sec. 1304.151. Financial Security Requirements

- (a) To ensure the faithful performance of a provider's obligations to its service contract holders, each provider must:
 - (1) insure the provider's service contracts under a reimbursement insurance policy issued by an insurer authorized to transact insurance in this state or by a surplus lines insurer eligible to place coverage in this state under Chapter 981, Insurance Code;
 - (2) maintain a funded reserve account covering the provider's obligations under its service contracts that are issued and outstanding in this state and place in trust with the executive director a financial security deposit consisting of:
 - (A) a surety bond issued by an authorized surety;
 - (B) securities of the type eligible for deposit by an authorized insurer in this state;
 - (C) a statutory deposit of cash or cash equivalents;

- (D) a letter of credit issued by a qualified financial institution; or
 - (E) another form of security prescribed by rules adopted by the commission; or
- (3) maintain, or have a parent company that maintains, a net worth or stockholders' equity of at least \$100 million.
- (b) If the provider ensures its obligations under Subsection (a)(2), the amount maintained in the reserve account may not be less than an amount equal to 40 percent of the gross consideration the provider received from consumers from the sale of all service contracts issued and outstanding in this state, minus any claims paid. The executive director may review and examine the reserve account. The amount of the security deposit may not be less than the greater of:
- (1) \$25,000; or
 - (2) an amount equal to five percent of the gross consideration the provider received from consumers from the sale of all service contracts issued and outstanding in this state, minus any claims paid.
- (c) If the provider ensures its obligations under Subsection (a)(3), the provider must give to the executive director on request:
- (1) a copy of the provider's or the provider's parent company's most recent Form 10-K or Form 20-F filed with the Securities and Exchange Commission within the preceding calendar year; or
 - (2) if the provider or the provider's parent company does not file with the Securities and Exchange Commission, a copy of the provider's or the provider's parent company's audited financial statements showing a net worth of the provider or its parent company of at least \$100 million.
- (d) If the provider's parent company's Form 10-K, Form 20-F, or audited financial statements are filed to show that the provider meets the financial security requirement, the parent company shall agree to guarantee the obligations of the provider relating to service contracts sold by the provider in this state.
- (e) The executive director may not require a provider to meet any additional financial security requirement.

Sec. 1304.152. Reimbursement Insurance Policy

- (a) A reimbursement insurance policy that a provider uses to comply with Sections 1304.1025 and 1304.151(a)(1) must state that:
- (1) the insurer that issued the policy shall:
 - (A) reimburse or pay on behalf of the provider any covered amount the provider is legally obligated to pay; or
 - (B) provide the service that the provider is legally obligated to perform according to the provider's contractual obligations under the insured service contract;
 - (2) if the covered service is not provided to a service contract holder not later than the 60th day after the date of proof of loss, the insurer shall pay the covered amount directly to the service contract holder or provide the required service; and
 - (3) if a refund is not paid to the service contract holder or credited to the service contract holder's account as required by Section 1304.158, the insurer, after receiving written notice, shall pay the refund amount directly to the service contract holder.

- (a-1) For a reimbursement insurance policy to comply with Section 1304.151(a)(1), the insurer issuing the policy must:
- (1) maintain surplus as to policyholders and paid-in capital of at least \$15 million and annually file with the executive director copies of the insurer's audited financial statements, National Association of Insurance Commissioners annual statement, and actuarial certification if the certification is required and filed in the insurer's state of domicile; or
 - (2) maintain surplus as to policyholders and paid-in capital of at least \$10 million but not more than \$15 million, demonstrate to the satisfaction of the executive director that the insurer maintains a ratio of net written premiums, wherever written, to surplus as to policyholders and paid-in capital of not more than three to one, and annually file with the executive director copies of the insurer's audited financial statements, National Association of Insurance Commissioners annual statement, and actuarial certification if the certification is required and filed in the insurer's state of domicile.
- (b) The insurer may not cancel the reimbursement insurance policy until the insurer delivers to the provider and the executive director a written notice of cancellation that complies with the notice requirements prescribed by Subchapters B and C, Chapter 551, Insurance Code, for cancellation of an insurance policy under those subchapters. Cancellation of the policy does not affect the insurer's liability for a service contract issued by the provider and insured under the policy before the effective date of the cancellation.
- (b-1) If the insurer or provider cancels the reimbursement insurance policy, the provider named on the policy may not issue a new service contract after the effective date of the cancellation unless:
- (1) the provider files with the executive director a copy of a new policy that meets the requirements of this section and that provides coverage after that date; or
 - (2) the provider complies with other financial security requirements provided by Section 1304.151(a).
- (c) A provider is considered the agent of an insurer that issues a reimbursement insurance policy for purposes of obligating the insurer to the service contract holder in accordance with the service contract and this chapter. The insurer issuing the reimbursement insurance policy is considered to have received the premium for the policy on the date the service contract holder pays the purchase price of the service contract.
- (d) This chapter does not prevent or limit the right of the insurer to seek indemnification or subrogation against a provider for any amount the insurer pays or is obligated to pay to a service contract holder on behalf of the provider.
- (e) In this section, "net written premiums" means the sum of direct written premiums and assumed reinsurance premiums, minus ceded reinsurance premiums.

Sec. 1304.153. Appointment and Responsibilities of Administrator

- (a) A provider may appoint an administrator registered under this chapter to be responsible for:
- (1) all or any part of the administration or sale of service contracts; and
 - (2) compliance with this chapter, except for Section 1304.151.
- (b) The appointment of an administrator under this section does not affect a provider's responsibility to comply with this chapter.

Section 1304.153 as amended by HB 1286 of the 79th Legislature take effect March 1, 2006

Sec. 1304.154. Provider Requirements

A provider may not sell, offer for sale, or issue a service contract in this state unless the provider gives the service contract holder:

- (1) a receipt for, or other written evidence of, the purchase of the contract; and
- (2) a copy of the contract within a reasonable period after the date of purchase.

Sec. 1304.155. Provider Records

(a) A provider shall maintain accurate accounts, books, and other records regarding transactions regulated under this chapter. The provider's records must include:

- (1) a copy of each unique form of service contract sold;
- (2) the name and address of each service contract holder who provided the holder's name and address;
- (3) a list of each location at which the provider's service contracts are marketed, sold, or offered for sale; and
- (4) written claims files that contain at least the date and a description of each claim related to the service contracts.

(b) The records required by this section may be maintained in an electronic medium or through other recordkeeping technology. If a record is not in a hard copy, the provider must be able to reformat the record into a legible hard copy at the request of the executive director.

(c) Except as provided by Subsection (d), a provider shall retain the records required by this section until at least the first anniversary of the expiration date of the specified period of coverage under the service contract.

(d) A provider that discontinues business in this state shall retain its records until the provider furnishes the executive director with proof satisfactory to the executive director that the provider has discharged all obligations to service contract holders in this state.

(e) An administrator appointed to maintain the provider's records is responsible for compliance with this section to the same extent as the provider.

Sec. 1304.156. Form of Service Contract and Required Disclosures

(a) A service contract marketed, sold, offered for sale, issued, made, proposed to be made, or administered in this state must:

- (1) be written, printed, or typed in clear, understandable language that is easy to read;
- (2) state the name and address of the provider;
- (3) state the purchase price of the contract and the terms under which the contract is sold;
- (4) state the terms and restrictions governing cancellation of the contract by the provider or the service contract holder before the expiration date of the contract;
- (5) identify:
 - (A) any administrator;

- (B) the contract seller; and
 - (C) the service contract holder, if the service contract holder provides the holder's name;
 - (6) state the amount of any deductible;
 - (7) specify the products and services to be provided under the contract and any limitation, exception, or exclusion;
 - (8) specify any restriction governing the transferability of the contract;
 - (9) state the duties of the service contract holder, including any duty to protect against any further damage and any requirement to follow the instructions in the owner's manual; and
 - (10) state whether the contract provides for or excludes consequential damages or preexisting conditions, if applicable.
- (b) The identity of a person described by Subsection (a)(5) is not required to be preprinted on the service contract and may be added to the contract at the time of sale.
 - (c) The purchase price is not required to be preprinted on the service contract and may be negotiated with the service contract holder at the time of sale.
 - (d) A service contract insured under a reimbursement insurance policy under Section 1304.151(a)(1) must:
 - (1) state the name and address of the insurer;
 - (2) state that the service contract holder may apply for reimbursement directly to the insurer if:
 - (A) a covered service is not provided to the service contract holder by the provider not later than the 60th day after the date of proof of loss; or
 - (B) a refund or credit is not paid before the 46th day after the date on which the contract is returned to the provider under Section 1304.158; and
 - (3) contain a statement substantially similar to the following: "Obligations of the provider under this service contract are insured under a service contract reimbursement insurance policy."
 - (e) A service contract that is not insured under a reimbursement insurance policy must contain a statement substantially similar to the following: "Obligations of the provider under this service contract are backed by the full faith and credit of the provider."

Sec. 1304.157. Returning a Service Contract

A service contract must require the provider to allow the service contract holder to return the contract to the provider not later than:

- (1) the 20th day after the date the contract is mailed to the service contract holder; or
- (2) the 10th day after the date of delivery, if the contract is delivered to the service contract holder at the time of sale.

Sec. 1304.158. Voiding a Service Contract

- (a) If a service contract holder returns a service contract in accordance with Section 1304.157 and a claim has not been made under the contract before the contract is returned, the contract is void.

- (b) A service contract holder may void the service contract at a later time as provided by the contract.
- (c) If a service contract is voided, the provider shall refund to the service contract holder or credit to the account of the service contract holder the full purchase price of the contract. If the provider does not pay the refund or credit the service contract holder's account before the 46th day after the date the contract is returned to the provider, the provider is liable to the service contract holder for a penalty each month an amount remains outstanding. The monthly penalty may not exceed 10 percent of the amount outstanding.
- (d) The right to void a service contract is not transferable.

Sec. 1304.159. Canceling a Service Contract

- (a) A provider may cancel a service contract by mailing a written notice of cancellation to the service contract holder at the service contract holder's last known address according to the records of the provider. The provider must mail the notice before the fifth day preceding the effective date of the cancellation. The notice must state the effective date of the cancellation and the reason for the cancellation.
- (b) The provider is not required to provide prior notice of cancellation if the service contract is canceled because of:
 - (1) nonpayment of the consideration for the contract;
 - (2) a material misrepresentation by the service contract holder to the provider; or
 - (3) a substantial breach of a duty by the service contract holder relating to the covered product or its use.

Sec. 1304.160. Limitations on Provider Name

- (a) A provider may not use a name that:
 - (1) includes "insurance," "casualty," "surety," or "mutual" or any other word descriptive of the insurance, casualty, or surety business; or
 - (2) is deceptively similar to the name or description of an insurance or surety corporation or to the name of any other provider.
- (b) A provider may include in its name "guaranty" or a similar word.
- (c) This section does not apply to a provider that, before September 1, 1999, included a word prohibited under this section in its name. A provider described by this subsection must include in each service contract a statement substantially similar to the following: "This agreement is not an insurance contract."

Sec. 1304.161. Misleading Statements Prohibited

A provider or the provider's representative may not, in the provider's service contracts or literature:

- (1) make, permit, or cause to be made any false or misleading statement; or
- (2) deliberately omit a material statement if the omission would be considered misleading.

SUBCHAPTER E. DISCIPLINARY ACTION

Sec. 1304.201. Disciplinary Action

On a finding that a ground for disciplinary action exists under this chapter, the commission may impose an administrative sanction, including an administrative penalty, as provided by Chapter 51.

Sec. 1304.202. Injunctive Relief; Civil Penalty

- (a) The executive director may institute an action under Section 51.352 for injunctive relief to restrain a violation or a threatened violation of this chapter or an order issued or rule adopted under this chapter.
- (b) In addition to the injunctive relief provided by Subsection (a), the executive director may institute an action for a civil penalty as provided by Section 51.352. The amount of a civil penalty assessed under this section may not exceed:
 - (1) \$2,500 for each violation; or
 - (2) \$50,000 in the aggregate for all violations of a similar nature.

Sec. 1304.203. Multiple Violations

For purposes of this subchapter, violations are of a similar nature if the violations consist of the same or a similar course of conduct, action, or practice, regardless of the number of times the conduct, act, or practice occurred.

Sec. 1304.204. Administrative Procedure

Sections 51.310 and 51.354 apply to disciplinary action taken under this chapter.