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Re: **Interpretive Opinion No. 01-15, Applicability of Tennessee Code Annotated § 56-6-126 to Proposed Automobile Service Contracts.**

Dear Ms. Kerns,

This letter is written in response to your inquiry submitted on or about October 10, 2014 to the Division of Insurance of the Tennessee Department of Commerce and Insurance ("Division"). Your inquiry requested guidance as to whether agreements ensuring damage coverage for normal wear and tear on leased vehicles is an exempt service contract as defined by Tennessee Code Annotated ("Tenn. Code Ann.") § 56-2-126 (2011).

Specifically, you asked whether service contracts to cover damage resulting from normal wear and tear on a leased vehicle, up to a certain specified amount, are exempt from regulation by the Division under Tenn. Code Ann. § 56-6-126.

The facts as understood by the Division are as follows: a company plans to offer contracts to lessees of vehicles from dealerships which will, at the end of the vehicle lease, cover damages determined by an independent third-party inspection professional to have been caused by reasonably anticipated, or normal, wear and tear on the vehicle not covered in the lessee's lease agreement with the dealership. Normal wear and tear is contractually defined as:

> [D]amage or deterioration to the [v]ehicle that is not allowable wear and tear as defined in [y]our [l]ease and for which [y]ou become responsible upon [l]ease [e]nd. Normal [w]ear and [t]ear only includes minor and reasonable wear and tear that a vehicle sustains in everyday routine, ordinary and anticipated operation.

(emphasis omitted). Specific covered repairs, replacements, or reimbursements are not identified in the contract. This contract will either directly pay for any necessary repairs or replacements or

provide reimbursement for additional costs imposed by the lessor dealership due to this normal wear and tear. These contracts will not cover any type of consequential damage.

The business of selling service contracts is not considered the practice of insurance in the State of Tennessee and is thus exempt from insurance regulation. Tenn. Code Ann. § 56-2-126(a). Under Tennessee Insurance Law, a service contract is, in pertinent part, "a contract or agreement for a separately stated consideration for a specific duration to perform the service, repair, replacement or maintenance of property or indemnification for service, repair, replacement or maintenance, for the operational or structural failure due to a defect in materials, workmanship, or normal wear and tear . . . ." Tenn. Code Ann. § 56-2-126(b). Such a service contract, synonymous with an automobile extended warranty, by design, provides protection to purchasers from damage or loss caused by some imperfection or failure in the construction or design of the automobile or any of its components. *See* Tenn. Op. Att'y. Gen. 85-038 (1986).

Essentially, such a warrant assures purchasers that the automobile purchased will work as intended; but does not contemplate damage caused by unforeseen, albeit reasonably anticipated, outside forces. The service contract as described above seeks to cover damages caused by events unrelated to the performance of manufactured components on the vehicle. Rather, this contract contemplates damages caused by exterior forces in the everyday use of the vehicle. Such coverage constitutes insurance, thus rendering Tenn. Code Ann. § 56-6-126 inapplicable.

Furthermore, if a guarantee offered in a future service contract is independent of the contract giving rise to the service contract and provides some protection greater than the remedies available in the underlying contract, the service contract is one for insurance. *H&R Block E. Tax Servs. v. State*, 267 S.W. 3d 848, 865 (Tenn. Ct. App. 2008). By design, the aforementioned service contracts offer coverage both outside of the underlying lease agreement and expand upon the coverage available through that underlying agreement. Additionally, contracts for future services which predominantly serve to indemnify are considered insurance under Tennessee Insurance Law. *Id.* The essence of the service contracts described herein is to indemnify lessees for damages not covered in their lease agreement. Lastly, if such a service contract is contingent on some event which gives rise to the protections offered in the service contract, the contract will be considered one for insurance. *Id.* Again, the coverage contemplated here is contingent on whether or not the damage in question is contemplated in the lessee's lease agreement with the dealership. This service contract consistently satisfies the attributes of a contract for insurance, subjecting it to regulation by Tennessee Insurance Law.

Please note that the Division has not made an independent investigation of the facts to determine the accuracy or completeness of the information supplied, but has instead relied solely upon the information you have provided. If such information is incorrect or changes substantially, it would be necessary for the Division to reconsider the matter and the position stated herein would be void. This letter expresses the Division's position on enforcement action only and does not purport to express legal conclusions on the issues presented. This position is furnished solely for the benefit and use of the entities described herein. Please be advised that further publication or use of this position may only be made with the Division's prior written consent.

This response by the Division is to a specific fact situation relating to interpretation of Tenn. Code Ann. § 56-6-126 and should not be construed as a legal position or opinion of the Commissioner of the Tennessee Department of Commerce and Insurance or of any other official in the Department. Please note that the conclusions contained herein are based upon the representations that have been made to the Division, and any different facts or conditions might require a different response. As each inquiry is reviewed on the specific facts presented, this response is based only on such facts and may not be used as precedent by any person or entity. Any variation in the facts presented to the Division by Ms. Shirley F. Kerns could result in a different conclusion than asserted herein.

If you have further questions or concerns regarding this letter, please feel free to contact me.

By:

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