

BILL ANALYSIS

SENATE JUDICIARY COMMITTEE  
Senator Ellen M. Corbett, Chair  
2007-2008 Regular Session

SB 1059	S
Senator Migden	B
As Amended April 8, 2008	
Hearing Date: April 15, 2008	1
Insurance Code	0
KB:rm	5
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SUBJECT

Vehicle insurance: aftermarket parts

DESCRIPTION

This bill would:

prohibit an insurer from requiring the installation of an "aftermarket part" on a vehicle if the part to be replaced is under an existing original manufacturer's warranty, unless such aftermarket parts are required to be used under the terms of the claimant's contract;

prohibit the insurer from limiting payment to the cost of an aftermarket part when an original equipment manufacturer (OEM) part is installed; and

for the purposes of this bill, define "aftermarket part" as any engine and its components, cooling system, air conditioning system, or corrosion protection.

This bill would only apply up to a maximum of three years after the vehicle was sold as new.

BACKGROUND

There is an ongoing controversy surrounding the use of non-original equipment manufacturer parts (non-OEM) during automotive repairs. Non-OEM parts used in repairs may include aftermarket parts made by companies other than the vehicle manufacturer or its licensees, used or salvaged OEM parts that are recycled usually without refurbishment, and

(more)

remanufactured parts that have been returned to "like new" condition by repairing or rebuilding. Non-OEM aftermarket parts generally are reverse engineered or copied from a sampling of OEM parts. There is no broad consensus as to the quality of aftermarket parts in comparison to OEM parts and they may be better, worse, or of equal quality depending on the individual part.

The Certified Automotive Parts Association (CAPA) is an independent certification organization supported by the aftermarket part industry and insurers. CAPA, the only organization that certifies aftermarket parts, says it has established a testing and inspection program and standards for aftermarket parts in order to ensure that they are of like kind and quality in form, fit, and function to car company brand parts. According to CAPA, competitive replacement parts are typically 34%-83% less expensive than car company brand replacement parts. CAPA, however, only certifies approximately 15% of the non-OEM parts on the market. Some parts that are certified by CAPA have been subsequently de-certified after the parts fail to perform as intended.

At the root of this controversy is how the required use of aftermarket parts during auto repair by insurers can adversely affect a vehicle owner's warranty. Many vehicle manufacturers provide comprehensive or limited warranties for specific parts or systems. Generally, the auto manufacturer will maintain the vehicle factory warranty for the replacement part and any other adjoining or associated parts or systems when original equipment manufacturer (OEM) parts are used in a repair. If a non-OEM aftermarket part is used and it subsequently contributes to the operational failure of the vehicle, the manufacturer may void the warranty pursuant to federal law. (15 U.S.C. 2302.) Any replacement part, whether OEM or non-OEM, would come with an individual part warranty for failure of that part for a specified period of time. However, the replacement part warranty would not cover any subsequent damage to the car caused by failure of that part. For example, if a cooling sensor or a radiator fails, the engine may overheat and seriously damage the engine. In such a situation, the original warranty would no longer cover the damage caused by the failed part, and while the failed part would be replaced, the parts warranty would not extend to pay for

repairs to the damaged engine.

This bill seeks to prevent insurers from unilaterally requiring vehicle owners to use aftermarket parts during a collision repair under the insurance contract, thereby ensuring that the manufacturer's warranty remains valid.

#### CHANGES TO EXISTING LAW

Existing law provides that no insurer may require the use of non-original manufacturer (non-OEM) aftermarket crash parts in the repair of an insured's vehicle, unless the consumer is advised in a written estimate of the use of non-OEM parts before repairs are made. (Business & Professions Code 9875 et seq.)

Existing law defines "an aftermarket crash part" as a "replacement for any of the non-mechanical sheet metal or plastic parts which generally constitute the exterior of a motor vehicle, including inner and outer panels." (Business & Professions Code 9875 et seq.)

Existing law defines "non-original equipment manufacturer (non-OEM) aftermarket crash part" as aftermarket crash parts not made for or by the manufacturer of the motor vehicle. (Business & Professions Code 9875 et seq.)

Existing law regulates the business of automotive repair dealers through the Automotive Repair Act, enforced by the Director of the Bureau of Automotive Repair (BAR). (Business & Professions Code 9880 et seq.)

Existing regulations provide that no insurer shall require the use of non-OEM replacement crash parts, unless the parts are at least equal to the OEM parts in terms of kind, quality, safety, fit and performance, and provide a warranty to that effect. (10 C.C.R. 2695.8.)

Existing regulations require insurers specifying the use of non-OEM parts to pay the cost of any modifications to the parts that may be necessary to effect the repair. (10 C.C.R. 2695.8.)

Existing regulations requires insurers to provide each insured with an Auto Body Repair Consumer Bill of Rights,

either at the time the insured applies for an automobile insurance policy, at the time the policy is issued, or following an accident or loss that is reported to the insurer, specifying that the consumer is entitled to:

- a) Select the auto body repair shop to repair the auto body damage covered by the policy. An insurance company shall not require the repairs to be done at a specific auto body repair shop;
- b) An itemized written estimate for auto body repairs and, upon completion of repairs, a detailed invoice. The estimate and the invoice must include an itemized list of parts and labor, along with the total price for the work performed. The estimate and invoice must also identify all parts as new, used, aftermarket, reconditioned, or rebuilt;
- c) Be informed about coverage for towing and storage services;
- d) Be informed about the extent of coverage, if any, for a replacement rental vehicle while a damaged vehicle is being repaired; and
- e) Be informed about where to report suspected fraud or other complaints or concerns about auto body repairs. (10 C.C.R. 2695.85.)

This bill would make it unlawful for an insurer to require the installation of an "aftermarket part" on a vehicle if the part to be replaced is under the existing original manufacturer's warranty, for up to three years from the date the vehicle is sold as new, unless such aftermarket parts are required to be used under the terms of the claimant's contract.

This bill would make it unlawful for the insurer to limit payment to the cost of installing an aftermarket part when an OEM part is used.

This bill would define "aftermarket part" for this purpose as any engine and its components, cooling system, air conditioning system, and corrosion protection part that was not manufactured, fabricated, or supplied for, or by, the original manufacturer of the vehicle.

COMMENT

1. Stated need for the bill

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According to the author, SB 1059 is needed to protect vehicle owners from unknowingly voiding the car manufacturer's warranty. Auto repair shops through the state cite that every day, insurers refuse to pay or limit payment for the use of factory parts on new cars. Consequently, every day new car warranties are put at risk along with the occupants of the vehicle.

The Collision Repair Association of California, the sponsor of this measure, states that assessment of this measure requires an understanding of direct repair programs (DRPs). A DRP is a confidential agreement between the insurer and an auto repair dealer which includes insurer directives on what type of parts the repair dealer is to use in making collision repairs. Aftermarket parts are favored by insurers because they generally cost less than OEM parts. Under a DRP, the auto repair shop may agree to use aftermarket parts in return for referrals from the insurer, or to avoid having customers steered away.

The sponsor believes that decisions on the use of aftermarket or OEM parts on a vehicle under warranty should be left up to the licensed repairer and the vehicle owner, not the insurer. Policyholders pay substantial collision premiums in order for their vehicle to be returned to pre-accident condition and, as such, replacement parts should not lead to a diminishment of the vehicle warranty that existed prior to the accident.

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2. This bill would require specific disclosures in insurance contracts which require claimants to use aftermarket parts in repairs to new vehicles

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At the crux of this bill is the desire to provide consumers with choices in the type of repair coverage included in their insurance contracts for brand new vehicles. Vehicle owners who pay high premiums for their vehicles to be restored to pre-accident condition should not subsequently be required to use aftermarket parts, especially if the vehicle's warranty could be compromised. This is especially important in the case of leased vehicles where a consumer has a legal obligation to return the vehicle to the lessor in pre-accident

condition. On the other hand, a vehicle owner who prefers the use of aftermarket parts in order to keep premium and repair costs down should also have that

option available.

Under this bill, insurers may continue to require the use of aftermarket parts in repairs to new vehicles so long as that use is required or allowed by the claimant's insurance contract. This is intended to provide consumers with the option of choosing between insurance policies that cover the installation of OEM parts, and those that will require the use of aftermarket parts in repairs. Presumably, insurers will adjust their premiums to each policy accordingly, as some companies are already doing. However, if insurers are going to require the use of aftermarket parts in their policies, it should be done so explicitly so that consumers have notice at the outset of the contract.

The following amendment would ensure that the requirement to use aftermarket parts is clearly and conspicuously disclosed in bold type in the policy, and in any advertisement or sale of the insurance product.

On page 2, line 9, after contract insert "and is clearly and conspicuously disclosed in bold type in the front declaration page of the policy, and in any sale or advertisement of the insurance product."

3. This bill would prohibit an insurer from limiting payment for vehicle repairs to the cost of installing aftermarket parts when an OEM part is installed

As previously stated, some insurers may not specifically mandate the use of aftermarket parts during collision repairs, but they will instead limit the payment to the cost of installing aftermarket parts. This effectively forces the consumer to either pay the difference for OEM parts or use the aftermarket parts. This bill would prohibit insurers from limiting payments for vehicle repairs to the cost of installing aftermarket parts. However, this provision would not apply if the claimant's insurance contract specifically requires the use of aftermarket parts. In this situation, the consumer has the expectation that aftermarket parts will be utilized

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in repairs and the limitation of payment to the cost of such parts would be appropriate.

4. This bill would only apply to vehicles up to three years old

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The previous version of this bill would have applied to vehicles up to five years old. However, in response to concerns from the insurance industry, the bill was amended in the Senate Banking, Finance and Insurance Committee to only apply to vehicles up to three years old. The three-year time period is consistent with the average length of vehicle leases, which currently make up about 40% of the vehicle transactions. However, many new vehicles come with lengthier warranties that may be as long as seven years. Thus, while this bill would provide consumers with more options during the first few years of car ownership, it would not cover the entire length of the warranty for many vehicles. Consumers with lengthier warranties would continue to face the same predicament of having to pay out of pocket for OEM repairs or potentially compromising their warranties by using aftermarket parts.

5. Opposition's main arguments

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a) This bill creates a monopoly for car manufacturers

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Opponents argue that this bill would give car manufacturers a monopoly on the sale of replacements parts by precluding the use of non-OEM parts for vehicles up to three years old. They state that aftermarket parts offer high quality, and lower-cost alternatives, which has brought some downward pressure on the cost of OEM parts. Opponents assert that this bill would allow car manufacturers to charge exorbitant prices because they will no longer have any competition.

This argument is premised on the idea that this bill would impose a blanket prohibition on the entire use of aftermarket parts in repairs for new vehicles, which it does not. Rather, this bill would require disclosures in the insurance policy so that consumers

are aware of the extent of their coverage. Insurance companies would be free to require the use of aftermarket parts provided that they clearly and conspicuously disclose this requirement in the contract. Furthermore, this bill would only apply to vehicles that are up to three years old and would not affect the market for parts installed on older models.

b) This bill drives up the cost of insurance claims

Opponents argue that the cost for insurance companies to settle claims would dramatically increase due to the required use of more expensive OEM parts. These costs would be passed on to all consumers in the form of higher premiums.

There is no question that OEM parts are usually more expensive than aftermarket parts. However, under this bill, insurance companies would be free to adjust their premiums to reflect the higher cost as some are currently already doing. For consumers who agree to the use of aftermarket parts in their insurance contracts, the cost of insurance claims should remain the same, or decrease since the insurance industry has only recently, in the last ten years, shifted to the use of aftermarket parts instead of OEM parts and premiums may not yet have been adjusted to reflect the cost savings.

c) Existing state law already protects consumers

Opponents assert that existing law fully protects consumers with respect to the replacement of aftermarket crash parts. Business and Professions Code 9875 and 9875.1 provide that no insurer may require the use of non-OEM aftermarket crash parts in the repair of an insured's vehicle, unless the consumer is advised in a written estimate of the use of non-OEM parts before the repairs are made. They also require the consumer to be informed that any warranties applicable to those replacement parts are provided by the manufacturer of the parts rather than by the original manufacturer of the car.

While these provisions may require disclosure prior to the repairs that non-OEM parts are to be used, they do not address the lack of disclosure in the actual insurance contract. They also do not address the hobson's choice the insured must face of having to accept the non-OEM part or pay the difference for the use of an OEM part. This bill would ensure that consumers are notified that insurers may require the



use of aftermarket parts at the time they enter into an insurance contract, before a collision has occurred. If the policy specifically requires the use of aftermarket parts, then the insurer would subsequently provide additional disclosures prior to making repairs that are already required by existing law.

d) Federal law already prohibits the voiding of a warranty when aftermarket parts are used

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The Magnusson-Moss Warranty Act (Act) is the federal law that governs consumer warranties. (15 U.S.C. 2301 et seq.) The Act generally prohibits "tie-in" provisions, which would require a purchaser of the warranted product to buy an item or service from a particular company to use with the warranted product in order to be eligible to receive a remedy under the warranty. (15 U.S.C. 2302.) However, manufacturers are not required to cover the use of replacement parts, repairs, or maintenance that will cause the product to function improperly. (Id.) Thus, vehicle manufacturers may include provisions in their warranties which state that the warranties do not cover vehicle or part failures caused by the use of non-OEM parts.

The California Automotive Wholesalers' Association and the Automotive Aftermarket Industry Association state that this bill is aimed in the wrong direction and should instead be directed at warrantors' to ensure that their practices are in compliance with federal warranty law. They assert that vehicle manufacturers are not allowed to deny warranty coverage simply because an aftermarket part is used in the vehicle's repair and that the pro-consumer approach is to target

the bad-actor warranty provider, not the insurance and the automotive aftermarket industries.

Technically, federal law does place the burden on the manufacturer to demonstrate to the Federal Trade Commission that a product will not work properly with aftermarket parts before a product's warranty may be voided. In this sense, the enforcement of federal warranty law may, in and of itself, be a problem. However, this bill is seeking to address a different problem, namely whether consumers should have a choice

in whether or not to purchase insurance policies that will cover OEM or aftermarket parts.

Support: Advanced Auto Body Center; California Autobody Association; California Motor Car Dealers Association; California Peace Officers Association; Consumers for Auto Reliability and Safety; DJ's Auto Body; Haddick's Auto Body and Towing; Motor City Body Shop; Poway Valley Collision; Pro Tomes Automotive Refinishing & Body Repair; Rich's Auto Body, Inc.; San Luis Autobody; 41 individuals

Opposition :(Submitted prior to recent amendments) Allstate Insurance Company; Association of California Insurance Companies; Automotive Body Parts Association; Certified Automotive Parts Association; Keystone Automotive Industries, Inc.; Personal Insurance Federation of California; 18 individual employees of Keystone Automotive  
(Submitted after recent amendments) State Farm Insurance; Automotive Aftermarket Industry Association; California Automotive Wholesalers' Association

#### HISTORY

Source:Collision Repair Association of California

Related Pending Legislation:SB 1167 (Wiggins) would require an insurer, when a claimant first reports the vehicle damage to the insurer, to ask the claimant if he

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or she has selected an auto repair facility, and if the claimant has so selected, would prohibit the insurer from engaging in any discussions about an insurer repair program or facility until after the claimant's repairs are completed. This bill is currently in the Senate Banking, Finance and Insurance Committee.  
SB 1371 (Correa) would prohibit insurers from applying any arbitrary limit, cap or threshold

when adjusting labor, parts, or any other material on a written automobile repair estimate. This bill is currently in the Senate Banking, Finance and Insurance Committee.

AB 2825 (Carter) would require an automotive repair dealer, when doing auto body or collision repairs, to provide the customer a certification upon completion of the crash parts installed on the motor vehicle. This bill is currently in the Assembly Business and Professions Committee.

Prior Legislation: AB 1163 (Yee, 2005) would have established that a "certified aftermarket crash part," not manufactured by the OEM, is of "like kind and quality" to an OEM aftermarket crash part, and would have required the non-OEM manufacturer and the insurer to warrant that part. This bill was held in the Assembly Business and Professions Committee.

Prior Vote: Senate Banking, Finance and Insurance Committee  
(6 Ayes, 3 Noes)

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