

Where do Vehicle Service Contracts & Protection Plans Fit in Ally?

Have you seen the Ally Bank television ad called, "[Nothing Stops Us: Ally Team Huddle](#)"? The team is gathered at Ally HQ in a glass enclosed conference room. A manager reminds the team, "Remember, here at Ally nothing stops us from doing right by our customers. Who's with me?" The half-dozen people in the room respond with "I'm in" and reach their hands into the middle of an impromptu huddle. Just then, in her haste to join the huddle, a woman walks (crashes) into the conference room through a glass panel. Outside the room hundreds of more employees are rushing to get into the huddle. Motley Crew's "Kickstart My Heart" is their clarion call. The ad is part of Ally's 2016 enterprise-wide campaign themed "Do It Right."

According to Ally's 2016 Annual Report, "The campaign introduces a broad audience to our full suite of digital financial services and helps crystallize our culture for consumers." Ally Bank is part of [Ally Financial](#), formerly GMAC. Ally is a major player in the Vehicle Service Contract industry. Seeing the ad reminded me of hearing Angie Tuglus, the EVP for Operations at Ally Insurance, speak at the Extended Warranty & Service Contract Innovations Conference last September and then again at The International Conference on Warranty Chain Management in March of this year. The Ally Bank commercial never mentions vehicle service contracts (VSC) or protection plans, none of the Ally Bank commercials ever do, but the enthusiastic commitment to customers depicted in the ad was more than reminiscent of the passion for those products that Angie ascribed to Ally. Angie likes to quote a Federal Reserve Board study that indicated 47% of Americans cannot afford an unexpected \$400 expense in their lives, and she points out that the average car repair is over \$300. As she puts it, "at the end of the day, many consumers need this product, and they need it from a company they can trust to pay claims." I spoke with Angie recently to find out where vehicle service contracts and protection plans fit in the Ally pantheon.

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First, a little background. Ally traces its roots back to 1919 when General Motors Acceptance Corporation (GMAC) was formed as a subsidiary of General Motors to provide financing for dealer new car inventories. A few years later, GMAC extended lending to new car customers by offering retail financing arranged by new car dealers. Jump ahead a few decades and GMAC added Motors Insurance Corporation to provide dealers with physical damage insurance (floorplan exposure) followed by comprehensive auto insurance for their customers. Then, in 1973, GMAC introduced mechanical breakdown coverage for new and used vehicles marking the advent of vehicle service contracts.

Over the years, GM has had its ups and downs but by 2006 it was clear that GM was in trouble. On Wednesday, March 29, 2006, Moody's lowered GM's credit rating to B3 and said the outlook was negative. The downgrade came after GM announced financial restatements for 2002, 2003, and 2004 causing a significant reduction in GM's liquidity. This, at a time when GM was struggling through the Delphi reorganization, declining sales, UAW woes, and negative cash flows. The deal to sell 51% of GMAC, GM's most profitable unit, to Cerberus was announced the following Monday on April 3, 2006.

According to [MarketWatch](#), GM said the sale “would generate some \$14 billion in cash over three years.” Three years later, on May 15, 2009, [USAToday](#) reported that GMAC Bank announced its new name, Ally Bank. Two weeks later, on June 1, 2009, GM filed for bankruptcy. But that’s another story. This article is about Ally, and more specifically Ally Insurance, the business unit within Ally responsible for vehicle service contracts and protection plans.

Your Vehicle Needs an Ally

Finding where vehicle service contracts and protection plans reside at Ally is not nearly so easy as finding the protection products themselves. Google Ally or go to their website, www.ally.com. Click on “Auto”, click on “Vehicle Service Contracts”. You will be greeted by the very friendly, “Your Vehicle Needs an Ally. Our history and commitment to our customers show that we’re dedicated to you and your budget. With an Ally vehicle service contract, you’re protected from the unexpected and prepared for your vehicle’s future.” Read through the list of plans and coverage comparisons. When you find a vehicle service contract you want to buy you will be directed to contact a dealer.

Not interested in contacting a dealer? Go to Ally’s other website, <https://allypremierprotection.com>. There you will be greeted by a slightly different but equally friendly introduction, “Your Vehicle Needs an Ally. We know there’s no room in your busy life for complications from unexpected vehicle repair costs. From claims to car rentals, we make it easy for you to get back on the road. It’s easy, it’s affordable and you’ll know we’ve got you covered.” Click on “Get a Quote” and you can buy direct.

There it is, the first revelation. Ally sells vehicle service contracts through dealers and directly to the public. Although the information appears on different websites, the products are the same and so are the people behind them at Ally Insurance. Angie said that by being active in the direct channel Ally can test ideas and learn firsthand how customers respond to different offers and that knowledge informs Ally’s product and pricing decisions and improves their business in all channels.

Protection Plans are the purview of Ally Insurance, part of Ally Dealer Financial Services

Ally reports financial results by business segment. The largest segment is Dealer Financial Services which includes Automotive Finance and Insurance. The other three segments are, Mortgage Finance, Corporate Finance, Corporate and Other.

Ally’s primary customers are automotive dealers, over 18,000 of them. Ally offers a wide range of financial services and insurance products to dealers and their customers. The dealers’ customers are also Ally’s customers. To serve their customers Ally utilizes multiple channels. For example, Ally has commercial accounts with approximately 4,100 dealers for floorplan lending and other commercial loans. In 2016 Ally generated more than 1.3 million retail and lease originations totaling \$36 billion with most coming from GM and Chrysler dealers whose relationships date back to Ally’s days as GMAC. In 2016, 86% of Ally’s new vehicle floorplan financing and 60% of consumer auto financing originations were transacted for GM or Chrysler dealers. GM, Chrysler and the other OEMs and their captive finance companies now compete with Ally. To increase and diversify their dealer relationships Ally launched a “Growth” channel in 2012 to focus on dealers representing brands other than GM and Chrysler. The Growth channel now holds 11,500 of the 18,000 (64%) dealer relationships.

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In 2016 Ally reported pre-tax income from continuing operations of \$1,581 million of which \$1,537 million (97%) from Dealer Financial Services. Insurance is reported as a sub-segment within Dealer Financial Services. In 2016, pre-tax income from Insurance was \$157 million or 10% of Dealer Financial Services. Insurance pre-tax income was down in 2016 primarily due to higher weather-related losses on floorplan exposures attributed to severe hailstorms. Increased dealer reinsurance participation and lower VSC volume were also factors in the decline.

Pre-Tax Income - Dealer Financial Services Segment

Year ended December 31, (<i>\$ in millions</i>)	2016	2015	2014
Automotive Finance	\$ 1,380	\$ 1,335	\$ 1,525
Insurance	157	211	197
Total Dealer Financial Services pre-tax income	\$ 1,537	\$ 1,546	\$ 1,722

Ally reports Insurance sales (written premium) by product line: Vehicle Service Contracts, Other F&I (e.g., GAP, theft, tire & wheel, dent, and appearance) and Wholesale (primarily floorplan). Vehicle Service Contracts and Other F&I contributed \$682 million and \$75 million respectively or a total of \$757 million of \$948 million (80%) net written premium in 2016. Over the last three years the trend in written premium was up for VSC on new retail and down for VSC on used retail. Overall, VSC net written premium was down 8.2% from 2015 to 2016 and down 4.6% from 2014 to 2015. The decrease was due to reduced used retail and increased participation by dealers in third party reinsurance.

Premium and Service Revenue Written

Year ended December 31, (<i>\$ in millions</i>)	2016	2015	2014
Vehicle Service Contracts (VSC)			
New retail	\$ 444	\$ 436	\$ 422
Used retail	427	485	509
Reinsurance (ceded to 3rd parties)	(189)	(178)	(152)
Total Vehicle Service Contracts	682	743	779
Other Finance and Insurance	75	65	58
Wholesale	191	169	186
Total	\$ 948	\$ 977	\$ 1,023

Transforming Service Contract Operations

When Angie spoke in Nashville at the [Extended Warranty & Service Contract Innovations Conference](#) she highlighted the transformation of Ally from the staid, if not stodgy, captive finance and insurance arm of General Motors (GMAC) to a leading independent finance and insurance company with a culture of innovation and superior customer service. Angie said that the transformation at Ally is in direct response to the changing needs and expectations of Ally's customers. "Consumers want to purchase cars and related products in a fast, digital and transparent way. They want to feel in control and get everything on demand. Whether you are a digital VC-backed auto startup, a publicly-owned dealer group or a family-owned dealership, you know this and Ally is working to deliver that experience."

Over the last couple of years, the transition from captive to independent included a new focus on the used vehicle segment, revamped and modernized pricing platforms, targeted "Growth" channel, and revised Ally Dealer Rewards (to incentivize dealer loyalty and cross-sales). Angie revisited the topic of transformation in Tucson at [The International Conference on Warranty Chain Management](#) where she spoke on "Transforming Service Contract Operations". In one portion of her presentation, Angie described the process her team followed to map the contract-to-claim lifecycle and the resulting discovery of over 50 potential leakage points.

Unlike third-party administrators (TPAs) Ally Insurance is vertically integrated. Ally controls the entire value chain from underwriting (developing the terms and conditions of coverage), to pricing, to issuing coverage and serving as obligor, to distribution through an inhouse team of sales agents, to training retail dealers at point-of-sale, to customer service centers and claims administration, and profit sharing. Placing protection plans under Ally Insurance assures alignment of financial interests. That's important on many levels. For example, if the terms and conditions of coverage are too generous losses can quickly mount, on the other hand, if they are too restrictive dealers and customers will complain, or worse, defect. The same is true with claims adjudication, too loose and losses escalate, too tight and complaints or even litigation follow. Ally works to make sure that dealers and their customers know exactly what they are getting by sending in their own specialists to counsel dealers and train their sale representatives. Ally helps dealers comply with myriad consumer regulations and effectively sell the benefits of vehicle service contracts and protection plans.

Ally works to make sure that dealers and their customers know exactly what they are getting

Specialization is key. The Ally Insurance field staff who call on dealers for Wholesale insurance are property and casualty (P&C) experts. They sell floorplan and other commercials insurance policies. A completely different group calls on the same dealers for vehicle service contracts and protection plans. And, yet another group, representing Ally Bank, call on the same dealers for floorplan financing and installment and lease lending agreements. Ally does not use independent agents. It's a similar story on the claims side of the house. Ally owns and operates its own customer service centers and runs its own proprietary insurance platform and IT systems. Ally employees interact with repair facilities and customers alike. Certified auto technicians review and approve claims. By treating vehicle service contracts and protection plans like insurance, even when they are not insured, Ally controls the end-to-end process in a disciplined and methodical manner that protects the interests of all parties. A unified platform helps drive efficiencies and a cohesive management structure helps align goals and objectives.

There are some downsides to doing everything internally. It takes more time and effort to scale (up or down) and it is more difficult to enter new channels and markets. A few of Ally's competitors are also vertically integrated. Companies like [Allstate Dealer Services](#) and [The Warranty Group](#), but they have taken different routes and actively engage TPAs and independent agents. Other competitors, like [APCO](#) and [Interstate](#), are themselves TPAs. The industry is highly fragmented. [Personal Safeguards](#) estimates that OEMs control 40% of the market for automotive vehicle service contracts. Another 40% is controlled by large vertically integrated providers like Ally, Allstate, and The Warranty Group. The remaining 20% is controlled by TPAs like APCO and Interstate. Given its heritage, Ally's position is unique and, to be sure, its market presence in vehicle service contracts and protection plans is enhanced by its legacy relationships and ongoing lending operations for dealers and indirect auto financing for their customers.

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