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FIELD COMPENSATION—LIFE INSURANCE AND ANNUITIES

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1. Considering all the players involved in the distribution of individual life and annuity products:

   a. What is the impact on the system of field compensation and related distribution cost of:

      (1) Inflation

      (2) Economic and demographic changes

      (3) Competition

      (4) Consumerism

      (5) Regulations

   b. What changes are occurring or are likely to occur as a result of the above, e.g., revised training allowances/financing methods, flattened or reduced commissions, fees for service, and variations by size?

MR. ROBERT D. LOWDEN: I would like to start by introducing the panel. We are very fortunate to have such a diversified group. We have the West Coast and the East Coast covered; we have stock and mutual representation; we have a field man and an actuary; and we have Tim Leach from LIMRA which will get us started with the formal introductions.

Tim is Second Vice President & Director of Consultation Products, Life Insurance Marketing & Research Association. Tim joined LIMRA in 1959 coming from a field background having served as an agent, supervisor and general agent.

Frank Zaret is an actuary with Metropolitan Life with actuarial responsibilities for designing and costing compensation plans. He is our proof that actuaries are proficient in the area of field compensation.

Don Shellgren is Vice President - Agencies, Planning, and Field Compensation at Occidental Life Insurance Co. Don has been with Occidental for 20 years, and is currently responsibile for all field compensation contracts and benefit programs.

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We hope to cover all the topics listed in the program, but perhaps in a less structured manner than you are used to. Because there is so much material we can do little but scratch the surface and hope to have a thought provoking session that will send you away with some things to think about. We feel it is very hard to treat inflation, competition, consumerism, etc. independently so we are going at it from the standpoint of how all of these things interrelate to affect the players: the new agent, the established agent, the manager, and the general agent. Let's start with inflation. There is little we can talk about these days without inflation being a consideration. When it comes to the life insurance industry and field compensation specifically inflation is no less insidious than in other walks of life. To attract new agents we need to spend more on agent financing. The career agent needs more to live on, but his potential client is hurting and although he may realize that he needs more insurance than ever before he cannot afford it just now so he either goes without or shifts to more term and less whole life. This is generating less commissions. The general agent is clamoring for larger expense allowances and the manager needs more to live on like all the rest. The home office is aware of the problem, but they are feeling the pinch themselves. None of us know quite what to do about this. Competition is serving to exacerbate the problem. Companies are coming out with lower and lower premium rates. It seems to be the trend. Again the agents tell us they need help. Consumerism has only added fuel to this competitive fire with cost disclosure and everything else. So with these opening remarks we will start in with a discussion of new agents and their financing plans.

NEW AGENTS

MR. L.B. "TIM" LEACH: There is no limit to the financial ingenuity that companies are using now to develop new agent financing plans, so classifying them into types is rather difficult. However, we do try to do this based on the subsidy. Either plans have a subsidy or they do not. If they have a subsidy then how do they handle it? Usually it falls into one of three major categories. There is the salary type plan that, as you know, pays the agent a level income. The company retains the commissions. If the agent does better, he may or may not get a bonus. The second type is a fixed decreasing training allowance. Here the agent gets a level income for maybe 2 or 3 months, and then the specified training allowance decreases each month. In addition, the agent gets either the standard agent's contract or an enhanced contract or a reduced contract, and his total income then is the sum of this specified decreasing training allowance and his actual commissions under whatever type of contract he has. The third type is a variable decreasing training allowance. Again the agent is on some kind of a flat allowance for 2 to 3 months, and then from that point on the training allowance is proportional to what the agent produces. If he produces more, he gets a bigger training allowance. If he produces less he gets a smaller training allowance. In any one month his income is a sum of the training allowance and the actual commissions under his contract. Within these three categories, we looked at the plans included in the LIMRA handbook. The handbook contains 33 plans. These plans are representative of the major career building companies. Of the 33, 14 have salary type plans, 14 have fixed decreasing training allowance plans, and 5 have the variable training allowance plan.

MR. FRANK ZARET: Of the 3 types of plans that Tim talks about, we have a cross between two of them. Nothing is pure. We have a fixed salary type in a new agent's first quarter, a combination in the 2nd quarter, and a percentage addition type in the 3rd and later quarters. We set up a plan which did not vary the validation schedule by the level of initial financing. We may change that after a while, but our initial view was that the important thing for a new man is that he produce a certain minimum amount during his first 6 months. During the first quarter we'll support him entirely. During his 2nd quarter he begins to get a fixed percentage of his first year commissions as training allowance; but if he fails to earn at his financing level, we'll support him up to that amount. In other words, suppose we brought in a man for $250 a week. We'll give him $250 a week in his first quarter. In his 2nd quarter he goes on the normal compensation plan plus the training allowance. If he fails to make $250 we'll support him up to the $250. After that he's on a straight percentage training allowance basis. He gets 55% of the first year commissions as a training allowance to start with, and that percentage decreases with time over 3½ years. The purpose is to try to grade the financing plan into what he'll ultimately earn. As the financing decreases, the normal compensation with renewals and other factors begins to take over. How successful has this been? I wonder whether any one plan determines the success of men. It's really the managers and training that determine whether or not a man will be successful, and not the compensation plan itself. The compensation plan is part of it, but not the determining factor.

MR. DONALD SHELLGREN: Before I get into answering questions it might be helpful if I told the audience that Occidental Life Insurance Co. is not a New York company. We have another company that we own and operate in New York, but Occidental as such is not in New York. Accordingly, we don't have to conform with all of the provisions in Section 213. We do things differently in the areas of compensation, recruiting allowances, etc. So what I'll be saying today probably is going to differ quite a bit from what you're used to. None of our agents are salaried common law employees. Neither at the time they start nor later. They are all independent contractors. We do not have the kinds of development allowances that you're used to. Our financing plans, and there's a number of them, are all based on advances against future commissions. We are simply loaning agents money based on the expected commission income from those sales. That again is probably different than the financing programs you are used to. How good is it? How successful? We feel that we are pretty competitive. We are able to finance at some rather high rates. Certainly, we lose some good prospects to companies who offer a guaranteed salary or an allowance for a period of time. Plans of other companies do not contain a cloud of repayment that overhangs Occidental's financing arrangements.

MR. LOWDEN: We do one thing at the Hancock that might be a little different. We put all the agent's commissions into a fund in order to level out their compensation a bit. We give them 25% of that fund each pay period, so if he does get a big case, he gets a little bigger hit than usual. If he goes for a while without a sale he is not just left dry. Are there changes that can be made that result in cost reductions but still pay more to the successes? What about the general agent's share of the loss in terminated agents? What can we do to encourage the general agent to do a better job of recruiting and to make him bite the bullet? What can be done to encourage terminating the failure rather than just keeping him on for whatever little bit of business he can toss into the system?

MR. SHELLGREN: Again let me comment that our general agents are precisely what that name says. They are true independent contractors. They are general agents in the truest sense. They are not the quasi-branch manager half-the-time, and half-the-time general agents. Except for a period of about seven years in our history, our general agents have always participated in financing losses to some extent. We have had a number of programs and the degree of financial responsibility has varied. Currently we are using a program whereby the general agent uses our pocketbook for the first six months of the agent's contract. During those first six months the general agent has a chance to make a determination if this new agent is going to make it or not. If not and he terminates that agent, he has no financial responsibility. If he wants the agent to continue in his General Agency, he effectively co-signs for the amount of the indebtedness that this agent has incurred since he started. Obviously if the agent turns out to be successful, there will be no financing losses. Also, I think it is obvious that the financing loss is probably the smallest punitive element when an agent goes belly up in the General Agency. The general agent has had to dedicate his own time that he could otherwise be spending more productively. He has had to provide other resources for that agent such as space and other clerical support. So when an agent goes down, the general agent stands to lose quite a bit; just part of it is the financing loss.

What about future trends? I think Occidental is like everybody else. We are trying to do a number of identifiable things to spot the failures, e.g., tougher pre and post selection. I am working on a task force right now that is looking into these matters. We are also trying to design a financing forgiveness program whereby the successful agent, that is the fellow who makes it through the five years with Occidental and he is earning his living selling our products, will be in a position to have this debit balance, that's the difference between the amounts we have advanced and what the agent has earned, pretty much totally expunged at the end of that 5 years. We hope to effect cost recoveries up front through tougher selection, and take that money and plow it back into the successful agent through better facilities, better support, financing forgiveness, and those kinds of things.

MR. ZARET: We have a particular feature in our financing plan in which we don't pay any training allowances to the agent if he earns less than a given amount of first-year commissions. As a simplified example, if the agent earns less than $100 a week in first year commissions, he gets no training allowance. Only when he gets over $100 a week does he get it. If he makes $100 a week after having failed to make it in past weeks, there is no catch up. We don't reimburse for past deficiencies. In that way, we try to encourage the termination of men who are not going to make it. One of the things we believe is that men will get the idea pretty quickly to leave the business if they can't make enough money. Maybe it's a tough attitude, but we find it is very expensive if you are continually hoping for the late bloomer to emerge. We also have some factors in management compensation in which the manager shares in the termination charges. There are different arrangements involving different levels of production of the agent, and different percentages which the managers will share. If the agent produces more, the manager may share in a smaller termination charge should the agent quit. But if the agent is terrible, the manager may pick up a larger charge. We also had one factor which we recently eliminated. We are going to take another look at it. We did not pay any overrides on men who produced below a certain level. This encouraged the manager to terminate people he wasn't making any money on. The attitude of the managers tends to be that the man

is here already, let me keep him, he is producing something, whatever I get is gravy. Now if he is getting nothing, the manager must consider the fact that he is spending time, energy, effort, rent, space, what have you, for somebody from whom he is getting no benefit. I think this is a very, very important factor.

MR. LOWDEN: Perhaps Tim can kind of give us an overall view. He sees a lot of these companies. Some companies I know penalize the agency head more for early terminations figuring that they should do a better job in recruiting. Others penalize them more for late terminations feeling they should have done the weeding out sooner. I've heard both espoused and I do not know which is the most popular.

MR. LEACH: Frequently the percent of loss that the general agent stands may be higher in the later periods, but when you consider the recoveries from deferred first and renewals if the agent terminates the dollar loss may not be as great as it looks. Generally speaking the companies give the general agent 30, 60 or 90 days to make up his mind, and do not penalize him too heavily for terminating at that point. Of course there are exceptions. On the other hand you have to be careful because if you step into a high penalty at the end 30-60-or 90 days, you will see a high termination rate at that point. The general agents panic and often do not keep people that they really should keep. So again you cannot just take one piece and look at it. It must be in the overall relationship. I would like to comment on encouraging managers to do a good job of recruiting, training and developing their men. We frequently see contracts that are so heavily loaded for the general agent with extra allowances for men in the 1st and 2nd year that even in spite of a penalty for financing losses they can make money turning over agents in the first 2 or 3 years. The general agent or manager is going to go where the money is. So if you really are serious about this manpower business look at your contract and put the rewards for bringing men through into the 3rd, 4th or 5th year. I think that will help send a different message. Another comment is on trends. This is one where I feel we may have to rearrange the world because it is not directly related to finance plans. The cost of developing new agents as you know is very, very high. Whatever number you quote someone else has a different number. But the point is that it is going to get higher, and to make career agent development attractive to the companies, somehow or other, we are going to have to make sure that as this agent becomes a going producer we need to get a larger part of his business or virtually all of his business so that it can be a profitable investment for the company.

MR. ZARET: The cost is going higher on training allowances, and a problem that I see coming is one with Section 213 in connection with training allowances and 1st year margins. Inflation is causing the appointment of men at higher and higher initial levels. I do not know that production is keeping up with this increase in the starting salaries, and there is going to be more and more spillage of the training allowances. There is a stipulation in the 1st year margin calculation which says that if you pay training allowances which are greater than 30% of the premiums on men within their first 3 years, the excess spills over into the 1st year margin and reduces it. We are beginning to feel that. In looking over Schedule Q's of other companies, we notice a few other companies are also beginning to experience this. So this is something that could be a problem in the future.

MR. BEN HELPHAND: What is the maximum amount of training allowance on an agent? $1,000 a month? $1,500 a month?

MR. ZARET: We had a $365 per week limit which was in effect for a number of years. It now has been raised to a limit of $500 per week which we do not use very often. The reason we have raised it is so that on rare occasions it can be used. However, the average starting salary in our company is now in the neighborhood of $270-280 a week.

MR. SHELLGREN: Again, as I said before, we don't have a training allowance as such. The average amount to which we will stake an agent is about $1,200 a month. Some start at less, and we do have some that start at larger amounts $2,000, $2,500 a month; but it is not an allowance. As I said before, it is an advance against future commissions. Again that's the difference between Occidental and your typical New York company.

MR. LEACH: New York has been putting a maximum limit on the subsidy for an individual, and they have been raising that number regularly so I am not sure I can remember exactly what the number is, but it is in the neighborhood of around $20-22,000 for the maximum subsidy per individual. This is a financing level of about $2,000 a month, and it is seen in some of your companies; it is certainly not an average, but it is not unusual to see financing at $2,000 a month.

MR. ZARET: I don't know if New York has put out a special regulation on this, but it seems to me they occasionally send a company a letter telling them that there is a limit, and this surprises most of the companies. The company generally reports it to the ACLI.

MR. MARK ABRAHAM: Is there a limitation on the type of agents that a company will hire for this compensation program? In other words, what's to prevent a potential agent from going from company to company collecting allowances?

MR. LEACH: It is not an original thought. We picked up new agents drawing simultaneously on financing plans from 3 companies as a career agent in each one. So it has worked. Now what goes wrong? Well first of all, the manager or general agent that hired him didn't really look into him at all. Second, companies approved it. Third, the companies did not check the fellow's record, and I guess the manager did not really know what the fellow was doing with his time. So it is just a real gap in both field and home office management when that occurs.

MR. ZARET: Let me also add that companies operating in New York must conform to Regulation 50. Regulation 50 restricts your ability to appoint somebody who has already been an agent in another company on a financing plan. If he has worked for another company according to the New York definition he is not to be given financing. However, I don't know how carefully companies check.

MR. SHELLGREN: We have no prohibition, but one of the negative selection indicators we do look at obviously is how many companies an agent has been with in the last few years. If he has been with 5 companies in 7 years he is a bad risk. We do some rather extensive checking as I think most companies do using such tools as inspection reports and a number of other things to make sure that the agent is not on a financing program of 2 or 3 other companies. We are looking much more disdainfully at job movement unless the man is a very successful producer. But chances are if he has bounced around and he has been through several "training allowances", he is not going to do any better with you than he did with the other companies he has been with.

MR. WILLIAM HEZZELWOOD: About 1½ or 2 years ago the New York Department sent around a questionnaire asking New York companies to provide suggestions for changes to Schedule Q. Do you recall that? Have you heard anything further on that?

MR. DANIEL CASE: I do not recall that questionnaire, but I do recall a questionnaire that went around about last summer on the question of whether to abolish Section 212 of the New York Insurance Law which sets forth the new business limitation. Also, the Life Insurance Council of New York (LICONY) proposed that New York abolish the requirement in Regulation 49 for vouchering expense reimbursements. LICONY hired Professor Dan McGill to do a study of the problem, and I believe he sent around a questionnaire.

MR. ZARET: There were several questionnaires. One was on Regulation 49. There was also a Section 212 questionnaire. On Section 212, there is a proposal to expand the issue limits which New York now restricts. The new bill proposes to replace the present limit of 115% of the amount of ordinary insurance issued in the "best" of the preceding three years by a limit of 125% of the amount of ordinary insurance as above or 125% of the first year's premiums on ordinary insurance in the "best" of the preceding three years, whichever is greater.

MR. CASE: The New York Insurance Department is supporting the bill to liberalize the Section 212 limits exactly as described. That bill has passed both houses in the New York legislature and we know of no reason why the Governor will not sign it into law.

ESTABLISHED AGENTS

MR. LOWDEN: We will deal next with established agents that are off the financing plan. We will start with the subject of inflation again. The agents cry that there is no money out there and the home office claims it should be easier to sell insurance, etc.

MR. SHELLGREN: It is certainly true that every established agent should be pointing out to his clients what inflation has done in the way of eroding the value of the estate. He should be in there filling that need, and of course insofar as new sales to new prospects, agents are talking in terms of larger dollar amounts of coverage than ever before. However, the fact that the industry is experiencing such a continuing decrease in premium per 1,000, coupled with higher agent operating expenses, certainly has neutralized any advantage of being able to sell larger volume type cases. No, inflation certainly has not helped the agent.

MR. LEACH: Obviously, inflation has pushed up the average size sale. Agents have benefited from a production bonus or production persistency bonus in their contract. Some of the bonuses are based on a company average, but others are based on a specific amount. If you produce so much first year commission you get one bonus. For a higher first year commission, you get a bigger bonus. These are usually designed so that a certain percentage of the field force or a certain percentage of the business will carry this extra loading of a bonus. Of course, if you don't change those bands or thresholds as the average size of new sales goes up due to inflation, you will soon be in a position where virtually the entire field force is getting a bonus which was originally designed only for the outstanding agent. It is therefore important that the company have some system to adjust those bands or thresholds annually and to make sure that the field force clearly understands when and how it will be done. Obviously this is very unpopular with the field force because they feel the company is just making it harder to keep up with inflation. But it is something that most of the companies are doing and have done, and I guess our biggest support comes from the MDRT, the agents' organization, which has consistently raised it's requirements for membership.

MR. LOWDEN: One of the answers to inflation has been a trend away from the regular commission pattern towards the heaped pattern. I am curious as to whether we have any reactions here as to how this has worked. Whether the trend is continuing or if people are backing off.

MR. LEACH: Again looking back at the handbook of compensation and looking at some 68 U.S. and Canadian companies, 58 of the companies already have some pattern of heaped renewals, So heaped renewals have been around for a long time. We've had, obviously, 10 companies that did not go to the heaped renewal pattern. Now whether it's going to solve inflation or not; I really don't think it is. Canada went through two waves of heaping. About 10-12 years ago they had most of their agent's contracts with 7 to 10 year renewals. Then they went to heaping and brought them up to about 5 years of renewal with a big 2nd. Then they went through a 2nd wave of heaping where some contracts only paid one renewal and some only 2 or 3 renewals. They thought that was going to solve the inflation problem and put more money up front to the new agents, and everyone thought they would be happy. Very soon after that was introduced they began to get a lot of static from the older agents. We're on a tread mill. We don't get the stability of the renewal pattern. We came in this business because we wanted to build up that security of renewals. We wanted that annual increase that we get because we pick up another renewal. So now many companies are moving back to a pattern of probably 4 to 6 years of renewals.

MR. SHELLGREN: I just might mention a little bit about our experience at Occidental. We did our research and development work in 1971-72 and in January 1973 we introduced a new, very high heaped schedule. On most of our plans, we paid 25% the first renewal year, then 15-10-10. So we paid 60% commissions in 4 renewal years, which was pretty heavy. Prior to 1973, we did not have a formalized pension plan. As part of our new Agent's compensation package, we installed one. In 1972, when we did all this, we were operating in a 1% or 2% or 3% inflation environment. Much of our business is concentrated in term insurance and brokerage. At that time there were far fewer companies that were seriously into the term and brokerage market. We introduced this heaped renewal compensation while still maintaining a very high 1st year commission rate. And we paid nearly

the same commission rates on term as on whole life. In 1974 and 1975 inflation, of course, started getting very uncomfortable. Our concerns were compounded by the fact that in the last 4 or 5 years everybody got into the term insurance market. So by 1976 and 1977 we found that for our new products which were extremely price sensitive, we no longer could sustain that heaped renewal schedule. So while we still have a number of products that pay the higher renewals, our newer more competitive policies pay the lower, lifetime renewals. We try to maintain a large, 25% renewal commission in the first renewal year on our par and non-par whole life, while maintaining a pretty decent first year rate. In summary, we simply couldn't afford to keep that very rich renewal schedule and at the same time stay as tough as we wanted to be in particularly the brokerage market place.

MR. LOWDEN: Everybody is curious about what everyone else is doing. Competition is driving down the premium rates and inflation is driving people to lower premium forms. We hear that agents might be willing to accept different forms of compensation to get a more competitive product. Some of the things that have been talked about are lower commissions, first year or overall, more level commissions, commissions that vary by size of policy, no commission products, use of fees, salary for agents, pay for policyholder service, etc. We hear about these things, but I for one am not sure if it is just talk or if some of these things are happening.

MR. ZARET: I think agents would like salaries, commissions, heaped renewals and bonuses all at once, if they could get them, and all at a very high level. The fact of the matter is that the quality of your agent will determine what he really wants. I have found that the better agents are willing to take a more level commission scale. They look at the job as a career one, and want to flatten out their income so as to know what is coming. The less productive ones want it all up front. In my opinion, I think in the majority of cases, agents will not want level commissions. They will want high first year commissions, and as much heaping as they can get. It's really a short sighted view, but that is a fact of life. I also think that a problem with leveling of commissions in that if it comes it will have a very serious impact on the entire compensation plan and on Schedule Q again. Level commissions will mean higher training allowances. Remember, if a new man comes into the business and you pay him a high first year commission and a high heaped renewal scale, it gives him some front end money. If you level it out there is less up front. Training allowances have to go up then. You may level commissions, i.e, cut first year commissions and raise renewals compensatingly, but you may also have problems with your "renewal demonstration" in New York State. New York State doesn't recognize that you lowered the first year commission to make up the renewal difference, unfortunately. So this is another problem. I don't know of any plan with salaries that is a good one. Our experience is that every time we add a flat to the plan, production goes down. It seems that the agent establishes in his own mind some level of income he wants to live by. If you increase the flat, it makes it easier for the agent to live with a lower production.

MR. LOWDEN: I think we all agree that the normal everyday agent is hurting in this economy. This brings up something I wasn't sure whether we'd get into. Some companies have gone the route of trying to find other ways of putting a dollar in the agent's pocket, the multi-line concept, casualty, mutual funds, etc. Giving them other products. I am curious as to the pros and cons of this approach. For example, can the field force adequately digest even the basics of all these different products they have in their kit?

MR. SHELLGREN: I have always been amazed at what we have asked our agents to do, and I am sure it is true in many of your companies. Our same field force sells group insurance, pension products, and health insurance (when we were in that business). Of course, today we have been talking strictly about life products, but our agents do realize a fair amount of their income from the sale of group and pension products. About 15 years ago, we started a "department store of finance." One of our sister companies is the Transamerica Insurance Group which is a very large casualty carrier. Working with them we had a great number of our agents go through all the requirements to get their casualty license.

We also started two mutual funds, and many agents got their NASD licenses. The idea was to create additional markets for our agents. The sale of pension and group has poured an awful lot of commission dollars into the pockets of our agents and managers. Our casualty experiment really didn't work out very well. While the fund market was good, our agents did fairly well. However, activity from our funds has slowed down materially. That was our approach, which is a little different than some others such as Prudential, Hancock, and a number of others that are into the casualty business and promoting it pretty heavily. The casualty and funds experiment, on balance, did not do much for our agents. Group and pension does contribute substantially to agents' incomes, however.

MR. ZARET: The experience that I found is that when you introduce a new line of business like property and casualty (P&C) it tends to draw on the life business. P&C doesn't supplement life fully, but it does shift energies from one line to the other. I think P&C is a much easier sale. The agent begins to concentrate on that, and the life business tends to suffer. I don't know about the other lines.

MR. LEACH: On this one, I am perplexed because I can talk to two people in the same company and get entirely different stories. So it all depends on whom you talk to.

MR. LOWDEN: We are (John Hancock) one of the companies that are doing it, and I think it is just as you say. Some people are convinced of its merits and, in fact, our casualty people have a slogan, "there's a lot of life in casualty," but there are a few of us that are not sure that is correct.

MR. BARRY SCHILMEISTER: Is anybody getting into some kind of innovative marketing concepts where they would throw a lot of these different products together. In other words, to stress to the agent how one feeds off of the other.

MR. LEACH: This is what State Farm has been doing. It is what your Farm Bureau companies have been doing, and I think it is fair to say that companies like the John Hancock, Metropolitan and others that have gone into the P&C business tried to do exactly that same thing. They tried to package an overall one stop service with a coordinated effort to build multi-line clients. Unfortunately, with a few exceptions, there is a big gap, and we find that the people buy different products, and they are not always as successful in selling the one family all products as they had hoped they would be. However, I think most of the companies tried that approach.

MR. SHELLGREN: That's basically the story even if you are not licensed in the general lines of business. I think the good career agent tries to stay with his clients and his changing needs and provide a full program of coverages. If you are not in the casualty business or general lines obviously you can not complete that part. State Farm particularly has been tremendously successful in developing a substantial amount of life insurance from their house of casualty clients. Most everyone looks to his agent for all insurance needs, and I think it is typical that you start out with our casualty agent and after about 15 years and 15 claims you build some faith and trust in him, and then you want to look to him for all your insurance needs. So it is ideal when you have an agent who is licensed in all these fields, and does a good, continuous, estate planning job for the client.

MR. PHILLIP SCHORR: More and more we are running into cases of selling either very large individual policies or a large group of policies to a business. Obviously the more you do this the more you run the risk of an individual lapse really hurting you financially. I wonder what the company's experience is in possibly setting some rules for spreading commissions on those very large type cases. If you are doing that, what sort of rules or break points are you using for that sort of thing?

MR. CLEMENT PENROSE: We have had some of these situations where there are very large individual life sales in some cases involving a group of lives on deferred compensation or something like that. There have been a number of instances in which we have had our agency officers have discussions with the agent and his manager about possibly escrowing those commissions and not releasing them all right up front. Particularly since we annualize first year commissions, and we have done that once or twice. But generally even though there are discussions, the decision is: well this is a big producer who has a big renewal account with us. Even if there are chargebacks we will be able to recover eventually, and we end up after discussing not doing anything special on those big cases. Our only chargebacks would be on a lapse in the first year.

MR. NORMAN MARTIN: Our agents are primarily property/casualty agents. I think we would readily admit to that. We have had a little bit of success in selling life insurance also. Our experience has been that basically the sale of one line does in fact lead to the sale of another. And this is precisely the way we have trained our agents. Because they are property casualty agents I would have to say they are suffering somewhat from economic conditions, from the number of automobiles being purchased, and the number of homes being built. We find that the property/casualty market basically is down from what it was, and as a consequence our life insurance sales are perhaps somewhat suffering at this point. I suspect those life companies that are going into property/casualty are probably just finding the reverse

situation that we had about 20 years ago when we really got into the life insurance business - the matter of convincing agents to get out and actually sell all lines. They have their pride in the one line they are selling and they think the others are for the birds.

We have been talking about compensation to agents. To this point in time in the life insurance arena at least, the writing agent of our life insurance contracts has got the compensation so long as he stays a writing agent. Now this has been contrary to what we do in the property and casualty area. If the policyholder moves away, he gets a new servicing agent in the property casualty business. We are wondering about the possibility of changing some of the compensation in the later renewal years on a policy to the so-called servicing agent rather than the writing agent. I am wondering what the trend might be or what anybody else's thinking might be about compensation when the client moves away from the original agent.

MR. SHELLGREN: I would like to comment on a couple things that Norm said. It sounds very good theoretically and some agents successfully wear those many mantles and service all your needs. More realistically, however, is that one tends to spend most of his time doing what he is good at. If you have been brought up in the casualty business and you are spending 12 hours a day with all that crazy paper work, it's hard to learn something else. A few years ago, several insurance companies rushed into the security dealers market. They told the account reps, "Look, here's how you can make some money." But, by and large, the account executive didn't feel comfortable talking life insurance to his clients. Plus the security dealer puts in long hours, and it is not that easy to follow up your normal day with life insurance appointments. It is not easy to take a casualty man and say, now on top of everything else, and after 60 hours a week in general lines business, you are going to sell life insurance. You can do it, and some do it very, very well. At least State Farm has sold it. They are one of the leading writers in life today. But, individually, it is very hard for a securities man or a casualty man to become a life man. It is very difficult. Some do it well, but many do not. I will comment also on Norm's question about the service. What we are doing we have been doing for a long time. Again, what we are doing is probably a little bit different from most other companies because we have been so heavily in brokerage. One of the big incentives that we offer a broker to place a piece of business with Occidental is that the broker will be protected on that piece of business as long as it is on the books, and that includes any subsequent options that are exercised on that policy: conversions, renewals, all our various go-backs and jump-around options. The broker will always receive commissions and will be protected. That even includes situations where the insured moves out of the area. For example, a policyholder moves from Los Angeles to Philadelphia. Occidental assigns an office to service that policyholder. They call on the policyholder, and offer to provide help. However, Norm still gets those commissions back in Los Angeles. If that case is converted, Norm will get half of the new commissions. If the policyholder stays here locally and somebody else gets in and converts it, Norm will get all the commissions. Those rules have served us very well in the brokerage market. You get a certain amount of mileage from the agent as well. That's your client and we assume you are servicing it. From time to time, our protection rules have come under a lot of pressure, particularly when we went to the 4 years of renewals; 5 years of commissions. Then you get into the question of whether or not to pay service fees to somebody beyond that commission paying period for making these calls. We are doing that at the

manager level but not at the agent level. Again how effective that is depends upon whom you talk with. If you talk to agents and their associations, they tell you that if you pay a service fee they will service the hell out of the policyholder. But when you talk to the insurers, and LIMRA has conducted surveys on this subject, they say we never used to do it, we do it now, we haven't experienced any improvement in policyholder service or persistency. So it depends whom you talk to.

MR. ZARET: I would say that we are very similar to you. We instituted a compensation plan which pays renewal commissions only to the writing agent on life business. Now, if the client moves or the agent moves, we still pay the writing agent the renewal commissions. On transfers, that same writing agent gets the renewals. Our own observations indicated that you wouldn't improve service by paying service fees. It just does not happen. How much can you pay to make it worthwhile for a man to go out and make a long trip? We also found that it was better to pay renewals to the writing agent only because we could pay higher amounts. Remember, there is big turnover in the industry. If you spread the commissions to everybody, the renewal commissions are lower. For the man who remains, you can pay him more. Why pay it to the potential terminator was one of our considerations. It was the career aspect we wanted to emphasize. We tell the agent - if you stay with us here is what you can make.

I also want to go back a moment to the P&C question asked. It reminded me of a study LIMRA did recently which I thought was very interesting, in case you haven't seen it. It studies the production of people by the percentage of P&C they sold. The effect of an additional line of business seems to be dependent on the direction you are coming from. If you are a P&C company and moving into life you seem to gain an addition to the amount of business you are selling. But if you are going from life to P&C the effect is not the same. It seems that the higher the proportion of P&C the better you will do as a multi-line company. That is just an observation. I do not know the reasons for it.

MR. LEACH: First of all, some of the Canadian companies have gone to a very complex system of policyholder service. We identify policyholder service as the type that the home office always does, changing addresses, etc. That's not what we are talking about. We are talking consultation type service where they want to talk to somebody that can give them advice. One company dropped its 2% so-called service fee, took that pot of money and hired salaried service representatives. The Canadians have gone quite extensively in different ways of trying to do this. In the States we have had this so-called service fee which is really non-vested renewal because it does not really relate to service. A few of the companies have made that now a transferable service fee. Again the question - so we spend that money what evidence do we have that service was rendered? You still don't, but it is an attempt to at least say to an agent you are paid $420 to service this block of business, and it does give the company and the manager a little more leverage to lean on the agent. The strings alone with that though is that they do not assign orphan policyholders to new agents. It must not be used as a dodge to try to finance a new agent. Be very careful in sending a new agent out to service a particluar piece of business.

MR. LOWDEN: There have been questions asked about experimenting with preferential agents' contracts for the really big hitters, and what would be included in such a contract: preferential underwriting treatment, special bonuses, improved office facilities, etc. Has anybody had any experience with special contracts for the big producers?

MR. LEACH: More and more we are seeing in the normal career agent contract built-in production persistency bonuses and quite frequently built-in expense allowances. So you automatically are doing this. Of course what is this? This is an anti-PPGA competitive device. If you are going to keep career agents you are in competition with PPGA Companies. So that type of expense allowance and the bonuses are kind of automatic. I would say they are quite prevalent. Now the other things, such as the ego recognition type things, and special underwriting privilege are important. Some of the companies do them. I don't have any feel for how many, but I would say the more of those things you can do the better it would be. These fellows have been with you a long time. You know them. These are the people you can afford to make some concessions to.

MANAGER, GENERAL AGENT, ETC.

MR. ZARET: Following are some of the major elements of compensation of branch managers that at one time or another we either instituted or considered: normal overrides, first year and renewal, and training allowance type overrides; if you are trying to encourage building an agency, you build up the training allowance feature. Perhaps a recruiting override on the number of people that you recruit where you pay some sort of bonus. You may have a salary, a flat amount that you might want to give to your manager, although in an incentive compensation plan this is a controversial item. There is a persistency factor which may be on a grid tied to production or it can be just a straight persistency item. An expense element may be used; you can structure this in several ways, to measure what the manager has control over or what the agency should be spending. There is always the controllable, non-controllable question which comes into play, and you get into a lot of arguments, I guess in every company, as to what should or should not be in the formula. You might even have an element which is based on the number of leaders conference qualifiers, a bonus based on the number of men who make a minimum standard. A termination charge for training allowance or recruiting costs is a possibility. Growth is another element; you might measure the amount of premium growth, say over the last year, or over the average of 3 years. You can also restrict payments on low producers; don't pay if somebody produces less than a certain amount. A length of service factor can be thrown in if you want to encourage a career type of position. There is one other element that I can think of and that's minimums. If you feel that a manager should not live with less than a certain amount of money, then after everything is said and done if he makes less than a certain amount you pay him a supplement, a minimum supplement. That's about the list I can think of.

MR. SHELLGREN: First of all, like most companies we have the same laundry list of things we try to hit, just like Frank explained. Again, we are a little bit different. We have about 700 sales outlets in the United States and Canada. 600 of those are general agencies and 100 are branches. Up until 1979, we had very little expense accountability, as least as compared with most other companies. One comment I might make. I think that the compensation of company-operated branch offices and general agencies is coming very, very close together. They used to be very far apart and now they are moving together. So that basically, I think the only realy difference is the vested equity build-up after the termination of the branch manager or general agent. Branch managers, by and large, when they terminate get a final pay check and that is it. The general agent has been working for vested renewal overrides that will continue, depending upon the terms of his contract, for many years following termination. At Occidental, we only recently started to get branch managers more involved in the expense accountability in branches. Prior to 1979, they had no real monetary interest in the expenses and expenses did not enter the formulas of any of their bonuses. So we are kind of a Johnny-come-lately in this cost control. It is a good idea. We designed a profit indexed or profit center type of bonus where now essentially the manager, in his principal bonus, is responsible for every nickel of running that office right down to the depreciation of the furniture and equipment. Expenses are measured against the new first year life premium produced in that office, and the manager participates in the differential, on kind of a profit sharing arrangement. We do not pay our managers large salaries. Salary is a small piece of their total income. We have allowed our managers to continue in personal production also which a number of companies do not.

MR. LEACH: From an industry standpoint we see the merging together more and more of general agent and manager compensation. You have to get very picky to find out really what is a general agent and what is a manager. We see managers with general agent's contracts and we see general agents with managerial contracts. Don't get hung up on the name. Look at the job, and particularly look at the real issue that separates general agents and managers - that of vested renewal overrides - ownership. Who put up the front money? Who gets the back money? With money goes control. So I think that is basically the difference. What elements do we want in a general agent's or manager's contract? We want an element for new sales, we want an element for manpower development both new and established. I am looking at the various elements within the job of the general agent or manager that we want to pay for. Again the job is what dictates the structure, and then the relation between the agency head and the company, and the financial relationship really is what sets the general agent's pattern.

MR. LOWDEN: From time to time with some of our contracts we have problems with agency heads who have built up a big book of business. Their kids get out of school. They are 40 to 55 years old, and they are living well. There is no incentive to hire, develop, and keep building the agency. This is a weakness. There is a flaw in the contract which allows this guy to sit there, live comfortably until his retirement date, and now the fellow you put in just doesn't have the kind of shop left that there was 10 years ago. Has anybody here run into that kind of problem and tried to make corrections in the contract to do something about it?

MR. SHELLGREN: I think first of all we should distinguish between a general agency and a branch office. Let's talk about a branch office where the manager is salaried. The general agent is paying his own expenses so he has to keep working. It is probably human nature if you start off as a typical branch manager, a fellow 27-28 years old; you can talk to an awful lot of prospective agents about that same age, and go through all the craziness and have your heart broken a million times. But by the time you are 50-55, you can't look another 26 year old agent in the face. You are burned out. Hopefully, you have developed some good staff people. However, we pay our branch managers only on new first year premium. Our branch managers virtually get nothing from the book of inforce business. All that renewal premium gets them very little. This fact alone tends to tug the manager along year after year. If you are compensated only on first year premium, you better have first year premium coming in or you are out of business. But slowing down at age 50-55 is a very natural thing that happens.

MR. LEACH: This is one of the basic weaknesses of the general agent concept because we made it that way. We built ourselves into that box. So in designing general agent's contracts now, we try to consider this pre-retirement general agent. Recognizing that what Don says is absolutely natural, that the general agent or manager is going to burn out. However, in the case of a general agent with a big block of renewal overrides, the pressure is off for new sales. If you look carefully at most general agent's contracts, financially, in most cases, he would be very foolish to spend much time or effort trying to develop new agents that he is not going to stay around to collect on. So we try to get companies to consider this, to be realistic, and there are a number of things you can do. For example, waive any charge for financing losses for agents in the last 5 years of the general agent's tenure. In this way he can continue to recruit and not be stuck with the losses when he is not going to be around to make the gains. Waive any share of pay that the manager or the general agent has to make on 2nd line people to encourage him to bring in someone to become an understudy and take over the agency. So there are many things including adjustments in pensions, etc., that you can do to overcome this, but it takes a lot of careful thought. If you don't push, you just get back into the same box every time.