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ORGANIZING THE PRODUCT DEVELOPMENT FUNCTION

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Panelists will discuss ways in which companies are responding to the need for a reduced product development time cycle:

- Actuarial staffing
- Use of automation aids
- Committee structures
- Coordinating the company commitment
- Market research
- Use of consultants

MR. RICHARD W. KLING: I have responsibility for the basic product development and management function at IDS in Minneapolis. Bob Likins is with Prudential, and Prudential as you know has many different product areas. Bob is responsible for the individual annuity and tax qualified product development functions. Bob Cook is our non-actuary. He is director of marketing with ManuLife, and he is responsible for the marketing of individual products. Our anchor panelist is Dick Schwartz. Dick is responsible for the product marketing function for the agency distribution systems for the Sun Life Group of America.

* Mr. Cook, not a member of the Society, is Director of Marketing with ManuLife in Waterloo, Ontario.

In order to understand our process, it's really helpful to have some background on IDS. IDS is a financial services company. It's a subsidiary of American Express. It's basically a financial planning firm. Its goal is to be the premier financial planning company in the world. A very simple goal and a tough one to reach. IDS Life is a subsidiary of IDS Financial Services, and it's basically a manufacturer of insurance products. The Life company goal is twofold: First it is to provide products that meet the protection, capital accumulation and retirement income needs of the IDS Financial Planner. Second, it is to leverage our manufacturing capability by distributing products through other American Express distributions systems such as Shearson Lehman Brothers.

I believe there are three key factors that contribute to successful product development:

1. One person has to be in charge. I think it's critical that one person be in charge of the entire process.

2. Cost effective distribution systems need to be matched to market segments.

3. Appropriate products need to be matched to these distribution systems.

Each of these is extremely critical. I'd like to concentrate this morning on the third point, which is matching products to distribution systems. Our primary distribution systems, the IDS Financial Planner and the Shearson Financial Consultant, are very different. The IDS Financial Planner does financial planning for a fee. The planner deals personally with every client to gather data, prepare an analysis, make recommendations and then implement those recommendations with product sales. The planner receives not only a fee but a commission for product sales. This distribution system has a relatively high cost. A variety of products, some of them reasonably complex, are needed to meet the clients' needs. In addition, we've got an exclusive arrangement with the IDS distribution system, the IDS planner, for insurance and annuity products. However, that exclusive arrangement is somewhat illusionary since the planner has many other financial products such as Mutual Funds, Limited Partnerships, CDs, and Unit Investment Trusts to help meet the client's financial needs. So we are competing without doubt for a share of the financial planner's business.

Let's move to the Shearson distribution system. That situation is quite different. The Shearson Financial Consultant (FC) operates in a different mode. The FC wants an investment oriented product -- preferably a lump-sum product and one that solves some tax problems. In addition, that product needs to be very simple since the sale is telephone driven. We are dealing with two different distribution systems, and the result is different products that need to be matched to these distribution systems.

In order for a product concept to be considered for development in our organization, it needs to meet three criteria: (1) It must meet an identified need. Sounds simple, but often times it is not that simple to deal with. (2) The product must be capable of generating significant volume. As an example, we won't consider developing a lump-sum product unless we can see annual volume of at least a $1,000,000 within two to three years. We are not going to waste our time on minor irritations. (3) The product needs to balance the needs of the client, the planner and the firm. Today our most significant challenge is meeting our financial objectives, and for us that's Return On Euity (ROE). While we are meeting our objectives for many of our products, some of our insurance products have a way to go to meet our ROE goals.

We have also developed a formal product development process that not only lays out the steps in the process but also spells out who needs to be involved and assigns responsibility at each step. While the process is structured, it is also dynamic and flexible enough to deal with major new products or minor product enhancements. The process has three major phases:

1. research,

2. design, which involves the development and pricing of the product, (We go through this until we are satisfied that our criteria are met.)

3. product implementation, which involves orchestrating a number of steps, many of them simultaneously in order to introduce the product. It involves

steps such as policy form filings, SEC filings, proposals, administrative procedures, and introductory material.

Let's take a closer look at the research phase. That phase involves five separate steps:

1. customer market needs assessment,

2. idea or concept generation,

3. exploration,

4. developing a marketing plan,

5. screening and giving priority to product concepts.

The marketing plan is a critical step often overlooked by people. It's critical to the development process. Here we identify the target market. Who is this product aimed at? We position the product. What needs is it going to meet? We develop some preliminary sales forecast numbers. We determine if we are going to test market it or roll it out all in one shot. Often the marketing plan be a key factor in determining whether we are going to proceed, back track or discard the idea all together.

I'd like to expand on competitor monitoring which I think is a step that we do particularly well in our organization. We have five people who spend all their time monitoring competitors and using this information to support our financial planners. We follow competitors in the insurance industry and other financial services, and regularly communicate emerging developments in the competitive market place. We have access to extensive monitoring done by our parent, American Express. We think we can react pretty quickly. For example, we monitor interest rates credited by major annuity and universal life competitors very, very closely. We update the database on a monthly basis, but when it's necessary, and that is fairly often, we can update that database within four hours. So we have the current information we need to make decisions.

In summary, the product development process is a dynamic process. It's flexible. It doesn't always work smoothly as you might guess and we are far from perfect, but we're making progress. Today we believe we are generally doing the right things and we are doing them more quickly than we useed to.

MR. ROBERT B. LIKINS: I'm glad to and have the chance to talk with you a little bit about how Prudential has organized its product development function.

I'll be talking with you today about how Prudential is responding to the need for faster product development and a closer matching of products to distribution channels. All my comments will be about individual insurance products, not group insurance products. I will provide you with a conclusion first and then some supporting comments to support that conclusion.

Conclusion #1. It is important to consolidate complete product development and distribution responsibility under a single, responsible individual in your organization.

Here is how we consolidated our individual insurance responsibility at the Prudential. Exhibit A shows that in 1980 we had a seven-member executive office and the executive vice president (EVP) of marketing was in charge of most individual product development and distribution responsibility. Property and casualty products and our systems reported to a different executive vice president in administration and finance. But the product development function and distribution reported to the executive vice president of marketing.

Now in 1986, our executive office consists of six members instead of seven, and the executive vice president of marketing is our president. Now that person has all of the responsibility for individual product distribution and development. We think that it has helped us quite a bit to have all of that consolidated under one individual.

Conclusion #2. Make your distribution channels and product lines each responsible for its own bottom lines.

EXHIBIT A

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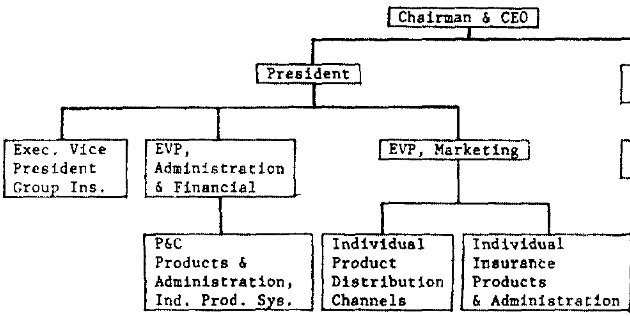
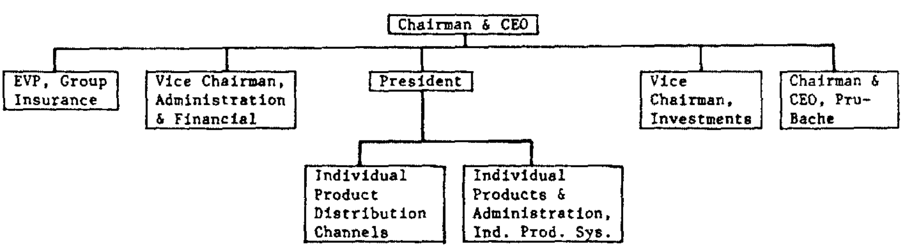
CHANGE IN PRUDENTIAL'S INDIVIDUAL PRODUCT REPORTING LINES

1980



1986



Get each distribution channel to commit to the volume of new and renewal premium it will deliver by product type during your yearly planning process. Exhibit B shows you what we looked like in 1980 and how we changed by 1986. You can see that we have added more product development areas and more distribution channels. In 1980 we had ordinary and district agencies, including some agents in Canada, and at that point they were reporting to our executive vice president of marketing. In the product development areas we had an annuity and tax qualified life insurance unit and a unit that worked on individual life insurance products for the United States and Canada, and we had a health products unit. In 1980, the property and casualty products reported to a different executive vice president as did the systems development area. Matching products and distribution channels wasn't that tough in 1980 because both of our distribution channels sold all of our products.

In 1986, we have ordinary agencies with 4,000 agents and several brokerage offices and district agencies with 17,500 agents. These are the two main distribution systems for the Prudential's product development that I'm talking about. They now report to our president. We also added what we call "other distribution channels" in 1983. I listed three types of other distribution: (1) financial institutions like banks, savings & loans and so on, (2) direct marketing, which could include telemarketing, and securities brokers including the Prudential-Bache account executives and (3) any other securities brokers that we deal with. We have also added a competitive information unit and a marketing research function.

For the product development areas we still have the annuity and tax qualified life area. We have a traditional life insurance area, and that's to be differentiated from our non-traditional life and annuity product development area. What I call the non-traditional life and annuity area, Prudential calls Pruco Life. It's a subsidiary company which we've developed, and it sells variable life insurance, universal life and variable universal life products plus some single pay annuity and single pay life insurance nitch-market products.

We've also consolidated under our president the development of Canadian products which now takes place in our Canadian office. They have a distribution channel of 1,000 district agents. Our health products, property and casualty

EXHIBIT B

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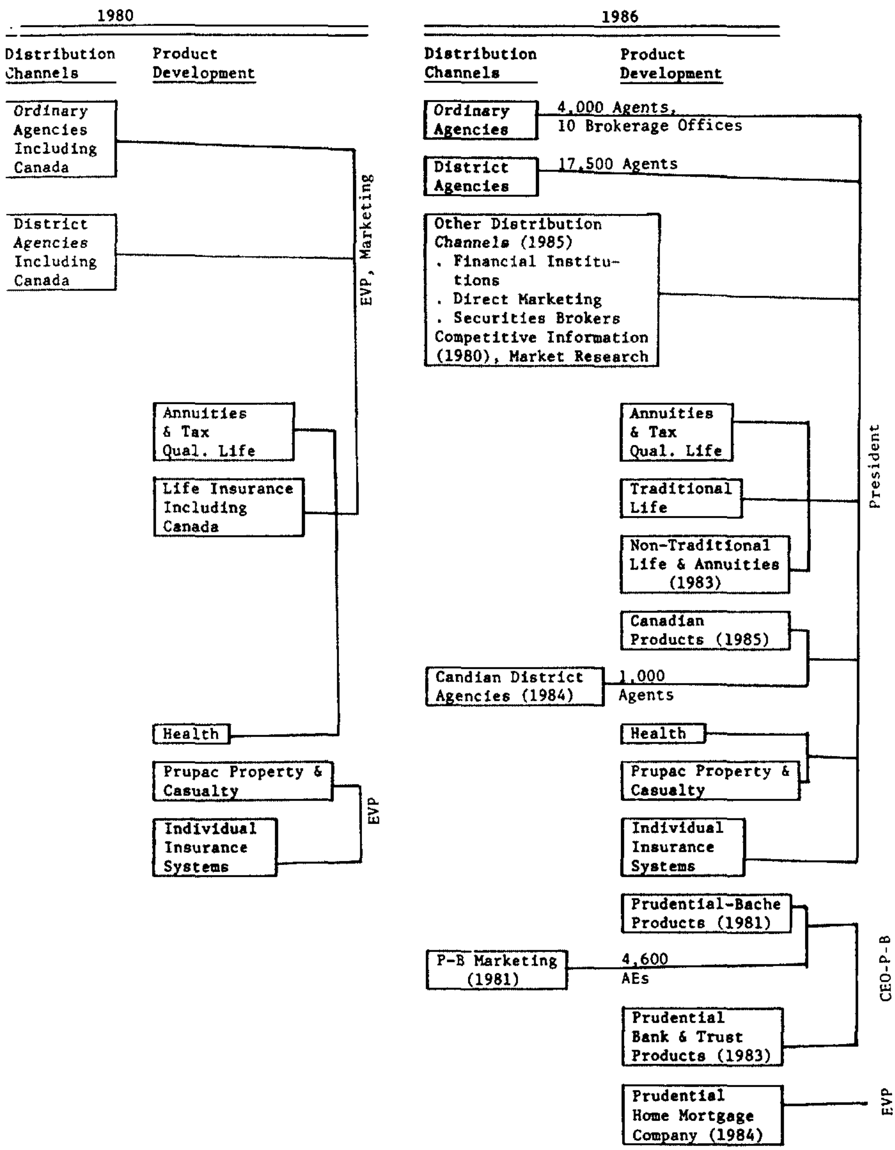
CHANGE IN PRUDENTIAL'S INDIVIDUAL POLICY PRODUCT DEVELOPMENT AND DISTRIBUTION ORGANIZATION



products and individual insurance systems now report to our president. We've added since 1980 the Prudential-Bache organization. It develops its own products. It develops products which our agents can sell also, mutual funds mainly. We also have 4,600 account executives who distribute mostly the Prudential-Bache products but also some Prudential life insurance and annuities. Additionally we have what we call the Prudential Bank & Trust which we added in 1983. It has money market accounts, certificates of deposits and collective trusts, which our agents can sell. And most recently in 1984, we've gone back into the home mortgage market, and our agents can get a small fee for referring a person in need of a mortgage to the Prudential Home Mortgage Company if that mortgage eventually closes.

Matching products and distribution channels has gotten a lot more challenging for us in the last 6 years. We have a lot more distribution channels. We've got a lot more product development areas. Assigning priority to needs is a little more challenging. But the ordinary district agencies do take top priority with us.

Conclusion #3. Establish a way to keep your ear to the ground in order to monitor the competition and know whether you are gaining or losing ground on how state-of-the-art your portfolio is.

Before 1980 we had little in the way of competition monitoring and marketing research. In 1980 we added a market analysis unit whose primary responsibility is to market and monitor our competition. It formally collects and disseminates information throughout the Prudential. We also have a vice president of marketing research who works on more substantial marketing projects and often works with outside research firms. The monitoring function gives us new product ideas both from our competition in the life insurance industry and from competition in the financial services industry in general.

We find that another excellent source of information for product development ideas is our agent advisory council. We try to listen to the council very closely. By paying close attention to it, we have what we think is the best way to match products and distribution channels.

Conclusion #4. As good as your systems probably are, you should evaluate the benefits of at least experimenting with the use of outside systems.

Before the 1980 we relied almost entirely on Prudential systems. We call our main product administration system the advanced ordinary system. It's a very large and very sophisticated system. We've modified this top quality system on several occasions as we've moved from traditional whole life products in about 5 to 6 steps to variable universal life products. With increasing pressure to shorten product development time, we've used outside systems for some products. When we first starting using outside systems, we modified the systems quite a lot to "Prudentialize" the systems. As we've needed to be more and more responsive in product development and have a shorter product development time, we began using and experimenting with outside systems with fewer modifications.

Along the systems line I just want to make two further comments. A few years ago during the product development process we knew that we needed to get a better look at how the client, meaning either the agent or the buyer, would view that product. Several years ago we hooked up our computer prepared product illustration system with our asset shares. The product developer can now look at how the product illustrates as he was developing it. We think that has helped us out quite a bit.

I can also make a lot of comments about using computers, particularly hand held and micro computers for illustrating rates of products, but let me just say that we're starting to move heavily into that area and experiment with our large agency force. I know a lot of other companies are quite a bit ahead of us in that area.

Conclusion #5. To be able to coordinate your current situation and control your outcome, you must have a clear objective.

You must know what your mission is. A well prepared mission statement can help direct a company's energies into or away from potential businesses and products. Here is the current Prudential mission statement:

> The Prudential is to be a leader in the financial services industry. We will be an aggressive market-driven company providing quality insurance and other financial services and products to individuals, businesses and other institutions by using strengths in distribution, investment and administration to achieve superior results for our customers and earn an appropriate rate of return.

As you can tell from that, we plan to be aggressive and market driven. We will be in the insurance and financial services businesses and aim to provide superior products to our customers. This statement really gives us quite a lot to work on, but it does help us to focus. Besides the company level mission statement, we have an overall individual insurance level mission statement, and we have individual department level mission statements within those. And for each we have strategies and development plans to get to those strategies and achieve those results.

Conclusion #6. We need a person or a group of people who have the clear responsibility to make product development decisions and resource allocation decisions.

Three years ago we formed what we call our "Product Planning Group." Members of the group include five senior vice presidents. The senior vice president and actuary is the chairman of the group. We also have on that committee the ordinary agencies' senior vice president, district agencies' senior vice president, the person in charge of other distribution channels and the senior vice president in charge of systems. The Product Planning Group is intentionally small. It discusses product proposals, and at the end of the discussion, it either makes a go or a no go decision on each product that is brought before it. Products that get a go decision also get a commitment for development resources and agency sales support, which is very important. We've had situations before where we've had go decisions but didn't really have the kind of support needed to develop the product and get it sold.

As a side point I might mention at this time that we have a lot of smaller product development areas within the Prudential. We work hard to make these development areas mesh with each other and to keep any competition between these units positive. That is an important aspect of having a lot of smaller units.

Conclusions 7, 8, and 9. Product development time from the point that the idea is received to the point when the product is being sold will be sped up if you do these three things: 1) get a fully developed description from the product suggestor of what is desired at the idea stage, 2) get your system staff involved in the preliminary product specifications so that you don't go too far off the deep end with your complications, and 3) move some of the development work that is not needed until after the product is going to be sold to after the product is going to be sold.

Exhibit C shows that I start with time 0 at the time we receive an idea. Some companies talk about their total product development time, and I tend to think that time 0 for them starts after they have complete specifications for their product. In 1980 from the point when we got an idea to the point where we had a proposal developed was one to six months. It could still take from one to six months, but we are moving toward the lower end of the one to six month timeframe in 1986.

From the time the proposal is prepared, until the time a decision is made, it used to take one or two months, now it takes more like two weeks with the product planning group. These people get together, make a decision, and we either go with it or we don't go with it.

Once we get the go decision, developing the product now takes about four to ten months until the product can actually be sold in the field. It used to take nine to 12 months.

Thus from the time we get an idea until the time the product is sold used to take about a year and a half. Now it takes from a half a year to a year and a quarter. In other words we've shaved about six months off the product development time.

Here is one of the ways we've done that. Note step 4b in Exhibit C "Complete Administrative Systems." It generally took from 0 - 6 months, now it might take

EXHIBIT C

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PRODUCT DEVELOPMENT PROCESS

Step In Process	Area & Staff	Activity	Functions	Elapsed Time 1980	Elapsed Time 1986
1. Idea	Actuarial Agencies/Field Other Distri. Ch. Research	Innovation & Conception	Conceive of an idea for a change	0	0
2. Development of Idea Into Proposal (Preliminary Development) For Product Planning Group Review	Actuarial Agencies/Fld. Advis. Coun. Other Distrib. Ch. Research Law Systems	Coordinator or Study Group Report	. Early Design . Needs to be met . Sales Estimates	1 Month to 6 Mos.	1 Month to 6 Mos.
3. Product Planning Group Review and Decision	Actuarial OA DA Other Distrib. Ch. Systems RHOs Input	Decision of Group	Assessment of . Needs . Priorities . Resources	1 to 2 Months	1/2 Mo.
"Go" Products					
4. Full Development Effort a. To sell: . Basic actuarial design, pricing and administrative systems	Actuarial Agencies/Fld. Advis. Coun. Other Distribution Ch. Systems	Team Effort	. Scheduling & Priority . Actuarial assumption . Design specs. . Pricing . Competitive position	New Product 12 Months or Product Enhancement 9 Months	6 to 10 Mos. or 4 to 9 Mos.
. Sales materials			. Rate Book . Training Material . Promotional Material . CPIs		
			Total	1½ Years	½-1½ Yrs.
b. Complete administrative systems			. Support Systems (Admin., Val, Financial and Accounting)	0 to 6 Mos. after sales begin	0 to 12 Mos.

from 0 - 12 months. That means we moved some of the product development effort for some of the administrative systems from the time before sales begin to the time after sales have started. That's a concern to our policy administration people and that makes it a big concern to Prudential because we have three offices in the U.S. and one office in Canada, each staffed with several hundred people that administer our products. So if we move the development work to after the sales start and we don't fulfill the need to have certain development work ready by, shall we say, the first policy anniversary (which could be as early as six months after the sale), those people in the administrative offices are in deep trouble because they have to take care of these products.

Conclusion #10. You don't have to develop every product your distribution channels sell.

Consider making arrangements to sell a product that has been manufactured or partially manufactured by another company. There are several options from which we can choose.

1. We can form some type of agreement with another company to sell its product.

2. We can use the other company's administration system and do all the rest of the work.

3. We can do it by using the other company's product itself, putting our name on the product and refiling the forms with the Prudential name on them. We can sell that product, and the other company can do all the administration.

4. Another way to bring products to your agency force is to buy a subsidiary. We did that. We bought the Prudential-Bache. We have the Prudential Bank, and we are back in the home mortgage area.

The least amount of work for everybody would be for our agents to sell another company's product under the other company's name. In 1983 the Prudential's ordinary agencies formed a marketing agreement with the Paul Revere Life

Insurance Company to sell Paul Revere's disability income products under the Paul Revere label. That is, Prudential agents were out there selling the Paul Revere disability income products. I've been asked a number of times both inside the Prudential and outside why we couldn't develop our own disability income products. In fact we had our own disability income products at the time, but they really weren't state-of-the-art type products. Our ordinary agencies wanted a product, they wanted it to be state-of-the-art and they wanted it quickly. Our response was to go out and find one from another product manufacturing company. You might be able to think of this a little bit like a major auto maker buying a component part from a component parts maker. That's more or less the way we think about it.

Most of what I've described to you have been changes since the start of the 1980s. The pace of change has been amazingly fast. There is an increasingly sharp focus on financial results for distribution channels and for product development lines. In order to improve your product delivery, I've made 10 suggestions:

1. consolidate responsibility under a single individual,

2. make each distribution and development unit responsible for its own bottom line,

3. monitor the competition,

4. consider using outside systems for non-major products,

5. know what your missions and objectives are,

6. establish a secure decision making group with resource allocation responsibility,

7. get a more fully developed concept at the idea stage,

8. get your systems staff involved early in product design discussion,

9. move post sales development work beyond the sales starting date,

10. consider forming marketing agreements for products you need but don't want to develop and administer.

Matching products and distribution channels requires us to define our customers and communicate and listen to what they have to say. We have to do what we can to satisfy their needs. I see the need for more different types of products in the future and at faster changes. We must continue to look for innovative ways to measure product development and meet these challenges.

MR. ROBERT A. COOK: The 1980s have been described by many people within our industry as the decade of the product and I think that's a pretty apt description. Witness these events:

1. The introduction of several not only new products, but lines of products: Universal Life, Variable Life, Current Assumption Products.

2. A dramatically shortened product life cycle. To give you an example within our own company in October 1983, we introduced a new low cost permanent insurance plan. It was only 11 months later that we introduced the second version of that plan. The third version is going to hit the streets in a couple of weeks and the fourth version is already on the drawing boards.

3. An extraordinary amount of product differentiation. It is very difficult now to beat the competition on price alone. You see many people trying to do it with all kinds of features, you might even call them gimmicks, built into their products.

These phenomena are not unique to any particular marketplace. Manufacturers' Life has had to face this kind of environment in all the markets it operates in around the world.

It was just a little over three years ago that a new general manager took over the Canadian operations of Manufacturers'. He found himself faced with declining sales and an out-of-date product portfolio. It wasn't an old portfolio by any past standards; however, it was a portfolio that had been made quickly obsolete by the action of our competitors. Indeed Manufacturers' believes Canada is right now the most competitive insurance marketplace in the world.

One of the responses to this situation was organizational in nature -- the establishment of a product management structure which was given twin mandates of first quickly developing new products to get the portfolio back in shape, and second ensuring that these new products responded to the needs of both agents and consumers. These objectives were believed to be the source of gaining a competitive edge in our industry. I think many would endorse that belief.

What is this thing I call product management? A textbook definition would start out something like this: Product management is a second or third generation matrix management organizational structure that is generally most useful to companies with a diverse product portfolio.

I think I better start with an example as a better way of explaining what that really means. The Proctor and Gamble Company originated product management many years ago. It has for example, a product manager for Tide laundry detergent. He's responsible for all of the factors affecting the marketing success of Tide where marketing success is defined in terms of both sales and profits. He is not just a sales manager. He decides on the formula of the soap; size, shape and look of the box; the price of the product; the advertising program and the kind of stores it will be sold in. He is not responsible for such things as the actual manufacturing of the soap; the actual execution of the advertising; inventory or distribution.

Another example from outside our industry demonstrates that product management is a growth industry. Coca Cola used to have just one product manager. Like the man from Tide, he made decisions about the formula of his product. Well that guy is just a Federal government statistic right now. His decision last year did open up a lot of opportunities in the product manager ranks of Coke. They now have product managers for New Coke; Coke Classic; Diet Coke; Cherry Coke; Caffeine-free Coke; and the list goes on and on.

With these kinds of examples in mind, I think we can continue the definition of product management. I would define the product manager's role in a four-fold manner. First, create product strategies and plans; second, see that they are implemented; third, monitor the results; and fourth, take corrective action when necessary.

I think the key element in that list is ensuring that the strategies are implemented. The product manager has to be the driving force to ensure that the work is done. He has to balance the input from various functional areas to ensure that the specialized marketing plan for any particular product can be put in place. It is this kind of focused responsibility that allows him to react quickly to any problems that appear in marketing the product.

Smaller product lines can survive in a big company with product management because the product manager turns into a champion for that line. For example, disability insurance accounts for a very small proportion of Manufacturers' sales. However, by assigning an individual to that product line, I'm able to ensure that it receives the right kind of marketing support.

Product managers report fairly high in an organization, and yet they have no formal authority over most of the people required to develop a new product. Instead they rely on their personal expertise and interpersonal skills to give direction to a team of people that develop the product. They have to use persuasion rather than command to get resources allocated to their projects.

The product management system is not without its problems. Measurement of its results is often quite subjective because of the matrix aspect of the job. Product managers are often too busy managing the line, taking care of the day-to-day problems that crop up, to give serious thought to new products that go much beyond a variation on what exists already. I think another common problem is that the product managers can often be intimidated by the expertise of a functional specialist. Probably the best example with a life insurance company would be the relationship with data processing. How many times have you wanted to bring out a new product only to be told it would take forever to put it on the system?

How have we translated some of these ideas into the context of the life insurance industry? How do we define the rolls of our product managers at Manufacturers'? I think there are four primary areas of responsibility.

The first and most obvious one is competitive and environmental monitoring. The product manager should be the most street wise person in the company about his product. He should define what the relevant competition is, know what it's doing in the way of product development or marketing programs, and be aware of the degree of success that it's having. Plus, he has to go one step further and discern why a competitor is taking some particular action or how it's achieving some particular success. Frankly, I think this part of the product manager's job is fairly easy because there are very few secrets in our industry. I think the second part of the monitoring job is more difficult. Product managers should be major users of research in the company in such things as consumer financial needs, demographics and the changing role of the financial institutions. Only with this kind of information, can product managers develop a total understanding of all of the forces that are affecting this product.

What we do then is take this base of knowledge and analysis and use that as input to the second major responsibility of a product manager, developing marketing strategy. This function includes defining and segmenting target markets, establishing the financial service needs of each of those segments, developing the classic elements of any marketing plan -- product, price, motion, distribution -- and finally, negotiating acceptance of the strategy with senior management.

It is only when a basic strategy has been agreed to that the product manager is ready to execute his third major responsibility and the most interesting one -- product development.

As I noted earlier, a product manager directly owns very few of the resources needed for product development. His role in the process is three-fold. First, he defines the market needs for the new product, where market encompasses both the needs of the agent and the needs of the consumer.

Second, he negotiates the budget, the schedule, and the success measures for the project. Then directly or subversively he acts as the product manager to insure prompt delivery of the finished product in the form required. Most of the product managers at the Manufacturers' are pretty nice and amiable people when they're off the job. On the job we taught them to act like barracudas.

Finally, the product manager is responsible for ensuring that his products are properly supported. This would include some of the traditional marketing functions such as promotion material, advertising, proposal systems and sales contests.

Now these four functions should not be thought of as a series of tasks that are performed in a linear manner, rather they form a closed loop where the results of each function provide feedback to those that precede it.

Remember that competitive monitoring is a relative process. How are we doing compared to competition? Some time after a new product is launched, the product manager should be asking a lot of questions. Questions such as: Have we achieved our objectives? Did we create new demands? Do we take business away from a competitor? Has anyone copied our product or modified an existing one to attack it? In other words, how has the market changed as a result of our action?

There are two other elements of a product manager's job that I think need to be addressed -- financial responsibility and what I call product shopping. A product manager cannot be given bottom-line responsibilities because he does not control all of the elements that affect those results. However, he has to be held responsible for the financial liability of his marketing plan. For example, a new product that will introduce an unacceptably high rate of internal placement is a matter of concern. As a second example, it may be necessary to price a product on a marginal basis, but other products have to be able to pick up overhead and should be priced accordingly. On occasion it may even be desirable to have a loss leader in your portfolio. But the product manager should be forced to demonstrate that having such a product will lead to offsetting increases in margin from other products.

Product shopping or networking is an element that I believe will grow in importance in the future. There are two occasions when networking may be appropriate. Either you have excess distribution capacity but no means to manufacture additional products or you're at less than full capacity in manufacturing but your distribution system is fully utilized. A product manager should be alert to see if either one of these situations turns up in his company and then determine whether or not an opportunity for networking is being created.

So far we've been talking about tasks, but job definition is only part of what's needed to understand how product management works. Equally important is to understand how a product manager's job fits into the organization as a whole. There is no pat answer for this. We have several models in place at Manufacturers', but I would like to discuss some of the common elements that appear to be keys to success.

First, product managers are located in a marketing department. This allows that organization to be established as a co-equal power base with distribution (or the sales function) and operations rather than as a subordinate to sales, which is quite a common organization in our industry. It allows marketing to act as the agent of change for the organization as a whole. If you have just two power bases, you'll find one will always dominate. When sales dominates, you tend to focus too much on short-term issues and neglect strategic planning. This has traditionally been the case in our industry. When operations dominates, you have an administration driven company, and you're totally out of touch of what's going on in the market. With three units, you can have a much more dynamic organization that is responsive to all of the forces affecting its business.

The organizational structure within these major units takes many forms. We have product managers with no one reporting to them, and we have others with small armies of actuaries, lawyers, and advertising specialists. We found though that work tends to get organized in a similar fashion regardless of the reporting relationships.

Marketing strategy and plans drives two teams of people, a product development group and a product application group. Within the product development group, you will find your competition center, product designers, pricing actuaries, communication specialists and some systems coordinators. The product application group is made up of advanced marketing lawyers and accountants, specialists in areas such as financial planning and retirement planning, specialists in marketing to baby boomers and, most recently, microcomputer experts.

I think in an era where more and more agents are operating as independent businessmen it's critical for the product managers in our industry to ensure that this application group focuses not just on educating agents for the sake of educating them but doing so in such a way that furthers the sale of his company's products, not those of his competition.

I would like to review the elements that I believe distinguish product management from other ways of organizing and managing the product development process.

First, the product manager must balance the needs of many clients. The consumer demands good benefits for his premium dollar. The agent wants to be adequately rewarded for his services. The company demands a good return on its investment. If the product manager puts too much emphasis on the first, nobody is going to sell his product. If he puts too much emphasis on the second, nobody is going to buy it. And if he fails to put adequate emphasis on the third client, he will quickly find that his job is in jeopardy.

The second distinguishing element is that a product manager has to contribute to satisfying a wide variety of objectives. Like most marketing people, he has a sales plan to be worried about. However, typically a product manager will have the freedom to control price as well and will be expected to find the balance between volume and margin that maximizes profit.

Finally, if a product manager is responsible for a number of products, he has to be concerned with the product mix. My company has been hurt in the past by becoming too dependent on a single product only to find its market wiped out over night by a change in tax legislation. Also as we noted earlier, the possibility of having marginally priced products or loss leaders in your portfolio forces you to manage the mix as well as the sales of individual products.

A product manager is not a decision-maker, he is a consensus builder. He doesn't have the authority commensurate with his responsibilities. He has to engineer the ongoing support and commitment from the managers of functional areas in order to ensure that there is clarity of direction amongst all the staff that work toward developing products and in order to insure that there is speed in decision-making when you go through the projects. He has to persuade other managers to devote resources to his projects. When this doesn't work, he must be able to get conflicts resolved quickly by escalating them to senior management.

The product management structure was certainly not the only solution we employed to speed up our product development process and make us more market responsive. Certainly a new project management model and approaches to systems were other major factors. However, it was a fundamental strategy that made us a more dynamic and vital organization.

Product management is not the solution for all companies. It must be installed and supported by senior management and not be something that is created from below. It will fail if the role is not well defined and understood. The product manager will use that support from senior management in order to speed up the decision-making process.

Companies that introduce product management will find that there is a period of culture shock. Pricing actuaries and sales support departments will resist the change. I think you have to be prepared to accept an initial and temporary increase in cost until you can adjust the rest of your organization to the change. The biggest obstacle however, is that good product managers are hard to find because the concept is still too new in our industry.

I believe that the product revolution that we are in the middle of is actually a natural situation. It just happens to have surfaced now because technological improvements in Home Office operations and at the point of sale have made it possible.

If I'm right, the product revolution is here to stay. And maintaining or improving our level of expertise in new product development will be the prime source of competitive advantage in the future.

MR. RICHARD SCHWARTZ: I'd like to describe the product marketing process not as we have it at SunLife, but as we'd like to have it. We are on our way there, but we're not there yet.

Product development as we traditionally know it has usually been within the scope of the actuary, but I submit to you that that scope is too narrow and that a more interdisciplinary approach is really necessary, where a continuous spectrum of profitability is looked at and managed towards. Profitability is more than an asset share. It's a continuous monitoring of results and, in the case of our current day products, a continuous redetermination of the product variables. Actuaries can do it, but so can CPAs and so can financially-minded sales executives. We have no province, no monopoly on that function.

Product marketing in total puts a good product in the field, and it also manages to the bottom line so that the profit built into the asset share is realized, not just presumed to occur.

There are two parts to the product marketing function: product development and product management. It's a continuous process. Product development creates the goods while product management manages the growth and fulfills the profit realization. Product development knowledge is necessary to bring forth the profit emergents on the product management side. Product management knowledge, a knowledge of what's happening out in the marketplace, is necessary to better design your products.

There are obstacles to a good product marketing function. Often corporate commitment to change is lacking. In many companies there seems to be a perceived commitment to the status quo. Objectives are set at 15% over last year. Not in terms of how that 15% will be achieved, but rather in terms of

"Here's what we want to do." I submit to you that there needs to be more definition of how that change is going to occur in the product, in the market and in the systems necessary to bring it about. The product marketing function needs to be perceived as a purveyor of change and a leader in changing directions. Too often the Board of Directors and management are perceived as 18th century thinkers in 20th century clothing. We hope at SunLife we're more into the 21st century.

Another major problem or obstacle is clarity in design objective. We often define ourselves as marketing through a distribution channel, and we say that we will provide whatever product is required. We chase after product for product sake. Purely because the competition has the product, we have to have that product. I think that is pretty fuzzy thinking. We are perceived by our employees too often as trying to satisfy too many diverse groups. Product for product sake is the goal. Not with the prior idea of how we are going to market that product and what new niche we're going to emphasize.

The next normal obstacle is multi-tiered responsibility for products. Too many people have their hands in the process. There needs to be a single person. You have heard this from each speaker. We really found that it is necessary. There needs to be a single person in the corporation who can be looked to to move the process along for coordination, for updating, and for making sure that all the product departments are involved. At SunLife, he is a gun slinger, and he needs to cut through the bureaucracy that is found too often in companies.

A major problem that I also heard today is commitment by the sales department to its final set of specifications, and it must be the sales department's set of specifications as well as yours. Your new product cannot be the actuary's product alone. The sales vice-president must be just as firmly committed as the research and development team which physically prepares the product. A formal sign-off process is needed. The set of specifications must be taken to the agency department with "Hey, are you with us or are you not with us?" Besides that agency department, the senior pricing individual, the administration, Management Information Systems (MIS), sales, legal and sales promotion areas all need to sign-off on that set of specifications. Make sure that there is nothing that slips through the cracks.

Do you know who your competition is? At SunLife we have an ongoing competitive analysis system both in rates and values. Each month we look at new interest rates declared by our competition to see what the trend is. Unfortunately the trend hasn't been downward enough. Somebody is playing chicken.

The companies which are your competition need to be defined well in advance of when you need the product. That definition of competition also includes the amount of compensation that they're paying to the field force. Too often we find that we develop a product, and at the last minute, the sales vice-president comes in and says here are my 22 companies which I want to use for this competition analysis.

The companies on the list are those that he just heard of in the last 10 days on his last trip to the field. Make him commit to what his marketplace is so that you can analyze it well in advance. Keep the list to ten companies or less. And don't have your competition defined as everybody under the sun.

Often we think that MIS, which is our data processing department, and our administration people are incapable of change. Really they just don't want to change. They have more projects than they have resources, and very infrequently does a product marketing function have its own dedicated MIS team which it directs. Usually you have to queue up for the project availability or resource availability. The MIS people seem to have an unending system of red tape, and it's your job to get through that red tape.

We need to organize for success. If there's one thing that we've mentioned, and it needs to be repeated, all the functions, the sales promotion function, the data processing microcomputer support function, and the product actuary function need to be under one roof. That's extremely necessary. There has to be an on-going analysis of your competition. Even more important than those functions, there has to be a momentum that's established by the product marketing function. That momentum says during the initial phases, we write up the minutes, we prepare an agenda, and we set objectives. Too often we go into meetings where we just sit around and look. The sales guy and the marketing guy just sit around and look at each other and say, "What did we decide last time?" That momentum has to be created by the product marketing function, implementing positively.

There are various phases in product development. There is an initial, very critical phase, with a weekly progress evaluation, to get the product off dead center. Sales, marketing, pricing and MIS must get together. We call this time the critical period. You have the minutes, you set the agenda, you work that agenda, and you do it very frequently during the initial period. You meet your agenda; you meet your timetable. That gets the ball rolling and that, to me, is the biggest function of the product marketing person.

Firm target dates must be set. This is almost just plain old common sense. Do what you can do best. We can set definite dates for pricing completion and filing completion. Unfortunately the states tell us we can't set definite dates to introduce the product. I don't think we're unique, either, in the fact that we have problems with various states. So when we get enough approvals in various parts of the country, we then set our seminar dates. We have 30 to 45 days before the seminar date to go out and blitz the area, to make sure we get people there, both recruiting and our existing agents.

Lastly, make MIS a part of the process from day one. Those people have to be involved. They have to get their frustrations out from the very beginning and tell you it can't be done. Then you tell them, go ahead and do it anyway. Don't keep them in the closet until the last minute. It just doesn't work.

Let's look at some of the keys to good product design. You have to define the sale size. What do we mean by that? It sounds obvious. One product can't cover the whole spectrum. One product can't be used effectively at the 10 to 25,000 dollar sales size and at the quarter of a million and over sales size. The competition is different, the compensation that you need to pay to your agent is different.

Let's define what goodness is. It seems obvious, but goodness is not the same to all people. To some people, goodness is the target premium level on a universal life product. It's the vanishing year on an interest sensitive product. It used to be the 20th year values. But more often now, the agency departments are looking at the 5th and 10th year values. But make sure before you get into the process, you have clearly defined what you're going to be measured on.

Don't tinker with products. Tinkering in my mind leads to false expectations by your sales department. It thinks you're working on something grand and all you are going to do is change the risk rates by 2%. It doesn't work. Small changes are usually misuses of time and resources. Make the change worth the announcement and make it worth the expectation that you've created on the part of the rest of the company.

Definitely have visible points of difference between you and the competition. All too often we've said, "Go design a product just like ManuLife. They're a real good company. We'll take the product just as they have it." I feel like saying, "Well go sell for ManuLife." Where's the creative point of difference, such that when your marketing people go in the field, they can say that here is where we're different; here's where we're better? Give them something to talk about. We have found in development, for instance, of a universal life product, that the ability to pay first year compensation in the second and all future renewal years, depending on the premium flow, was something that really motivated our agency department. It also drove our product developers crazy. But we managed to do it.

Product management is the other half for the product marketing function. Product development, as we have said, is bringing new products which have sales potential and profit potential to the agents. Product management is making that potential into a reality. Part of management is defining what is important, what are the key variables that are going to make this product work. Traditional concerns, such as mortality, lapse and expenses are still there. But more important, the product management function must talk about the new concerns, such as investment segmentation, the declared rates relative to what your competition is doing, and the trade-offs that might be necessary (in other words, providing more interest than maybe you can afford in the first 25 months, which crosses the critical point of the product.) If we get that product to pay any part of the third year, we've made an initial profit and we're out of a loss position. We need to do whatever is necessary to get it through, including perhaps slight misallocations of pure interest to get it where we need to go. In our universal life products, we need to find that critical point, or what is as important, what is the best level of premium relative to the target premium. You don't want all target premiums. In fact, the lower the premium is, the closer to the minimum premium, the happier we are. How do we communicate that to our agency people?

Once you define what is important and what is going to be measured, make sure you communicate that and have everybody agree that it's important. Not only agree verbally, but emotionally from the heart, agree that it's important and understand why it is important. You have got to measure it as part of the product marketing function. Part of the product implementation has to be set up with controls that will be used to measure the profitability of that product.

We also give the product management function responsibility for setting the compensation formula for our sales people. That is a wonderful thing. It gets their attention if you put in their sales plan what they're going to be paid on, their variable factors. They really listen to you when their dollars are dependent upon it. It's a total function, a total integration and we feel it works.

As we have said, product development is getting the right equipment to work with. Product management is doing the right job. There is nothing more frustrating than doing the right job with the wrong equipment. In many cases, this has been likened to trying to make the desert bloom, a truly noble cause. However, not having the right equipment to make that desert bloom can be extremely frustrating. And certainly we recognize that our clients are special, and we try to provide the right product for the agent and the client.

MR. DONALD A. BLUE: First I have a question for Dick Kling. When you established the need to define a marketing plan, you didn't make plain which departments are involved in this. Presumably the technical staff is involved. Of course the marketing staff has to be involved. How does that involvement work?

MR. KLING: We have a product marketing/product management function in our distribution channel as well as a product management function within our life insurance organization. Our product management people in the life insurance organization are responsible for the overall process. They work very closely with that product manager in the distribution system to develop that marketing plan, to make sure we know how we're going to position it, what kind of a sales forecast we can expect. So it's a joint effort, but the person on my staff has the responsibility for seeing that it gets done.

MR. BLUE: Now, I have a couple of questions for Bob Cook. Perhaps I misunderstood a point you made initially. I understood you to say that there should be joint responsibility for sales and profits vested in a single person. You then said later on in your presentation that in the area of financial responsibility you did not give bottom line responsibility to the product manager. Is that so? It sounds like a contradiction.

MR. COOK: I'd like to clarify that remark. The product managers essentially are responsible for putting together a marketing plan. The marketing plan will have financial measures in it that go beyond sales and do include profit measures. The organization as a whole is responsible for delivering on that, and the product manager can influence some of those things. Obviously he cannot influence the cost of maintaining a policy over time. He should, however, draw it to the organization's attention if an assumption is being made in the pricing of a product that we're not meeting.

MR. BLUE: That clarifies the point. Now on the subject of new product teams and product managers at ManuLife, is there a single manager for all new products?

MR. COOK: I can give you some examples from various divisions. I am responsible, for example, for all individual insurance, disability and annuity lines. I have working for me, associates who are responsible separately for insurance, for annuities, for disability To take a slightly different example from our U.S. Division, we have a product manager for individual insurance who then has associates working for him, one responsible for universal life, one for variable life, one for traditional products. How you break these things up depends primarily on the number of different products that you have in every area and the degree of risk involved because of the volume of sales you may have in the specific area.

MR. ROBERT K. BOLTON: I think each of the panelists talked somewhat about consolidating the product development responsibility under one person. I'd like to ask each of you what problems you have had with that. I assume there are plenty.

MR. KLING: We found the need to make sure that one person was responsible. We have three primary areas with a "product manager" who has either a marketing or a technical background, but has overall responsibility for that process. We have a manager for our annuity business, which is a huge business for us. We have another manager for life insurance and disability insurance. Finally we have a third manager for distribution of the interest sensitive products through other channels than our own sales force. Each of the product managers is responsible for bringing all those things together. This has been functioning for about a year in the fashion where everybody knows that these people are supposed to be responsible for things. It's starting to work reasonably well. We're having better success in keeping things from falling through the cracks, and we can really point to one person to lead the project in that way. So it's starting to work for us.

MR. LIKINS: I think the question was how we coordinate our overall development of a product and how we sort and sift priorities between different products. The way we do it at Prudential is when the product planning group gets together, it has representatives from all the key areas-sales -- systems, actuarial. They make the decision and then it goes to one of about a half a dozen different units. Each unit works on different types of products. It might be health products, annuity products, traditional life products or non-traditional life products. The product planning group steers it to one of the units. Once it gets to that unit, the unit is responsible for coordinating the overall development of the product, including the systems development work, the accounting and everything.

MR. COOK: I will address one aspect of stressing the importance of just one person. 5 or 6 years ago our method of product development was to have a product development committee. It had representatives from marketing and from sales and from administration and from the field. It got together 2 - 4 times a year and made recommendations. The head office would take those recommendations and proceed to work on some of them and forget about others. The world is changing too rapidly now to have that kind of system. We heard Bob talk earlier about the need to cut half a year, or three quarters of a year out of the time it takes to develop new products. That's one of the things that we are trying to do to be more responsive to what is needed today. I think another factor that has influenced the Manufacturers is that, in our Canadian operation at least, we don't make any particular attempt to have innovative products out on the street. We try to take the General Electric approach of being a fast second in the marketplace. Let somebody else take the risks and prove that something works, and then we'll come along with something a little bit better afterwords. If you're going to take that kind of approach to the marketplace, you have to be able to develop products quickly, and you have to have somebody who is responsible for watching what's going on, watching what is working, and what is not working.

MR. SCHWARTZ: At Sun Life we have an agency system, and we have a direct marketing system. We have product marketing people in charge of each of those functions. It used to be that we took 6 - 12 months to develop a product, and we still do on a larger product, such as Universal Life. We did that in about 8 months, including all the systems. On short products and modifications to products, which I define as slightly above tinkering, we usually take something like 2 - 4 months. This would be for something such as a salaries savings product where we have the framework established and all we're going to do is put in new variables and a little bit of different marketing material. We still have product administration meetings controlled by the product marketing person to disseminate information. But the responsibility for getting products from conception to birth and then to profitable sales is centered within that one person.

MR. KLING: I would echo the need to be able to move quickly if your strategy is a fast follower, rather than cutting edge leader, which happens to be our strategy as well. We're similar to Bob Cook's operation in that way. We can move quickly on many products. What will usually hold us up is a securities product, where we need to have the SEC approval. With other types of products, for example universal life products, we can move quickly and be in half the states in four months after we decide we want to do something, even if it's a build from scratch, now that the systems are in place. That's real important to us.

MR. ALAN F. HINKLE: This is primarily directed to Mr. Schwartz and Mr. Cook. It seemed like in your presentations, you said you had one person in charge. What you said was you had one person in charge of each product, and therefore you could have 5 - 6, however many, people in charge of different products that are being developed at the same time. And at least in some of these instances, I believe, these are people that have no one directly reporting to them. How do you reconcile the allocation of scarce resources when you may have more than one product going on at the same time and more than one person in charge?

MR. SCHWARTZ: At the Sun Life, each of the product marketing functions have their own support teams. Within those teams, allocations of resources have to take place, but they take place within one agency function, if you will. So the agency sales person, the president, and the product marketing people basically set the priorities. Once those priorities are set, the product marketing people have to achieve those priorities.

MR. COOK: I think I'd like to answer that question two ways. One would be to follow up on examples I used in my presentation. Take a look at the packaged goods industry. If you took a company that was manufacturing a bunch of cereals, it would have and somebody in charge of cereals and then it would also have one person in charge of Cheerios and one for Fruit Loops, etc. So, there several tiers of product managers so that you can resolve some conflicts.

The other approach is very similar to the approach used at Sun Life of America. Our operations areas tend to be organized along product lines as well so that there is a set of systems resources allocated to the annuity line, to traditional life and to nontraditional life products. So there isn't as much competition for resources as you might think there would be with multiple people in charge of products.

MR. HINKLE: I'd like to expand that question a little bit. We're not as large as the Prudential or a lot of the companies that are being described. If we want to come out with a major new product -- for example, to enter the variable market -- it would be all well and good to say we have systems resources allocated along different lines. But we would to re-allocate the resources. Does your system permit such re-allocations and, if so, how do you do that?

MR. COOK: Well I think that if you found yourself short of resources in the systems area, because you were going to pursue a major project, you would probably find yourself strapped for resources in every other area of the company that also had to contribute to the development of the new product. So I doubt, for example, that your sales training area could cope with anything other than developing the materials for the variable life plan at the same time. Your agency compensation area probably couldn't cope with much more than figuring out how to compensate for the new product, so that even if you had resource competition in one area, I don't think you would have any options in terms of transferring resources from another area because you'd probably find that the whole company was strapped for the same thing. We have faced some problems over the last few years where we have taken on projects that were very large, even from a large company's standpoint. We entered the group life and health small business marketing in Canada three or four years ago, and that was an enormous undertaking for us. In order for us to do that, we had to go out and hire a small army of people, and pull a core of experts away from other areas, and, in effect, build a new business unit to handle this major project because it wasn't a one-time demand on resources. It was so big that it was going to be an on-going utilization of resources and, in effect, forced us to reorganize part of the company in order to accommodate the demands.

MR. SCHWARTZ: I think when we're faced with a problem like that, we'll try to isolate one person from our existing staff who knows the company and knows the interfaces. We'll put him in charge and then go out and hire a series of contractors, perhaps MIS, perhaps actuarial. We'll have one internal person in control so the product interfaces well within the rest of the company. When these hired guns leave, we have somebody on the staff who knows what went on.

MR. KLING: Let me follow up on that as well. With the three major product managers that we have in our organization, we're continually running into resource problems in our systems areas. There's no question that is our bottle neck, and it may be for others of you as well. The senior management of the life company, the operations area, the systems people and I will sit down once a month to see where we are. We are continually reviewing our priorities on products and other projects and will reset priorities. We think this works better than it used to.

MR. MURRAY J. TAYLOR: I think all of the statements that have been made by our panelists are certainly telling us of a new direction to this whole process and I applaud you for your comments. I find our company is going in the same direction, and I would like to give one more response to the last question. We see ourselves as that number one company that ManuLife is trying to chase in Canada (it is a very aggressive market in Canada), we have tried to come up with very innovative products. That usually means nightmares for systems people. We've just gone the route of having a full-time senior person -- by senior I don't mean management necessarily, but a full-time person working for me -- whose entire job is sorting out all those allocations of resources within the marketing area. That person keeps track of all 60 projects, or whatever they are, from the annuity, disability, insurance lines, traditional, universal, and so on. He keeps track of all the critical paths on all those projects, sees where they integrate, sees where the problems are, sees where things could be speeded up or slowed down. That process is reviewed by the senior management of each area at least two or three times a month. So what we're seeing is a real dynamic shifting of priorities as we move along, so that we hit all the important things all the time and respond to where the marketplace is going all the time.

My question is to Mr. Likins. You mentioned that the major way you were able to shorten your time frame was by deferring many processes and development with regard to administration beyond the introduction date. Now in my view and work in product development, that was one of the oldest tricks in the book. It was something that always made people mad and frustrated. It seems to me to be quite counter to the general session speech on excellence in terms of being able to treat our policyholders effectively and promptly and accurately. It seems to me that we're moving into an environment of realignment on time processing, where it's actually impossible to do things manually for a while.

Is that really the way to do it or what are the other ways? I'd also like the other panelists to address that question. We see the need for shortening times; we're doing a lot of things organizationally, I think, to try to move that way, but what are the tangible things that are allowing us to do that?

MR. LIKINS: This gives me an opportunity to clarify what I tried to say when I said we cut about six months off of our development time. Actually that wasn't the major source of improvement in our total product development time. That was an important source however. If we agree among ourselves that the pressure is too great, we will allow a product to start to be sold before we have all the administrative systems in place. We have three U.S. Regional Home Offices and one in Canada, and each of them have literally hundreds of people that do administrative work. That's when the systems work. There would be thousands if the systems didn't work.

But what did we do to cut the approximately six months off? We are getting better at shortening the time to go from idea stage to proposal stage. That still takes one to six months, but we're getting closer to one to three months than we were six years ago. We're getting better at making a decision quickly, once the specifications are set, so it can go to the product planning group. They take a couple of weeks to make the decision rather than floating it all over the company and the regional home offices in all the different marketing areas and taking up to two months. We're also getting somewhat faster in the actual systems work that we do before product development time. We're getting better at some of it, and we're moving some of it to the post sales date.

So, in response to your question, our systems are big and they're pretty sophisticated, and they do a lot for the clerical staff that administer the product. And we think they're on-line kinds of systems in the sense that I think you mean it. But we do develop a product and release it figuring that within six or eight months we'll have the system pretty well completed. We had a universal life product that didn't actually have a guarantee in it that said you could increase the face amount, but we indicated pretty heavily that you would be able to increase the face amount. When it came to be the first anniversary, we told the field force, "Don't go out and get any of those because they're still completely manual. We haven't put that in the systems yet. We're still working on it." It has taken more like a year and a half to get that built in to the system, and fortunately we didn't have any number to speak of on the first anniversary. But we do run that risk. I hope that responds to your question.

MR. SCHWARTZ: We have had two generations of interest reflective products. On interest sensitive life where we do annual accounting, we said, "Let's wait a full year. We're going to wait until after the product is introduced to get all our systems up. We have a full year until we have to do the interest sensitive type processing. Until that time we treat it as a traditional product." That product was introduced in 1983; and we still have bugs in the system. It's still not fully automated. I think you build time bombs when you do it that way. Our administrative people tell us we can't do it, and when we do it, we find out that they were usually right. On universal life, the flexible premium monthly administration system, we did a little better. It was only a month after our initial sales that we had the ability to administer it. I think we're much happier with that process.

MR. KLING: That was an excellent question. That's an issue that we've struggled with. We've gone through the process of introducing, for example, the universal life type products, not having everything ready on the theory that you can't make any changes in the product for the first year. We did that three or four years ago. We were able to get the product out extremely quickly. We wouldn't do that today. One of the things that has happened, particularly since our acquisition by American Express, is that we've taken a much closer look at our corporate values. Our main value now is service to clients. So we would not do the same thing. We would still defer statutory reserves and things like that. But anything that needs to be done that affects the customer must be done in a way that will provide top notch service before we introduce that product. We've taken a step back, primarily, because to us the customer counts an awful lot.

MR. COOK: Our systems people often complain that we start selling the product before they have the administration system ready, but they get even more upset when I change the design of a product after we start to sell it. There are a lot of things that you don't have to have done when you start selling the product, not withstanding the remarks that were made in the general session. There is a three to six week period after you start selling a product before an agent will really wonder why you haven't been able to issue a case yet. So you don't really have to have an issue system set up the day you start to sell the product. You don't have to have the annual statement for a universal life type plan done for 13 or 14 months after you start to sell. We are continually mortgaging our future in that way, but you have to get the product out on the street fast. You do tend to cut some corners in order to do it, in order to keep up with the Great Wests of the world.

MR. TAYLOR: Let's pull ourselves back a little bit and look at our whole operations, both new products and things we would want to do to enhance our responsiveness on our existing products. Now by that I don't mean tinkering with features or anything else. I just mean improving the administrative approach, the computerization and the way we can relate to our agents with information. All of those types of things I'll call maintenance. Do you find that there is a strong pull, particularly with the type of organization we talked about (and quite frankly I agree with it) to not do enough of that maintenance type of thing, which is going to maintain our customers, keep our clients, make them happy, because there is such an attraction to building up sales and bringing in new products? I mention this, because as there is pressure to cut down that time frame, it would tend to pull off resources from those other things that in the long run are going to be what keeps us in business.

MR. LIKINS: At Prudential, we do have a very wide sophisticated system that we put all of our expected high volume products on. Part of the procedure for this system is to fully implement the product in each one of its individual pieces, including all the way out to the part that is handled in the field office which has the screen and which can input the applications on receipt and get policy statuses. While we do that for all of our major products, there are some short cuts we take on what we call our niche products -- the single pay life, single pay deferred annuity kind of things. We have actually gone out and bought some vendor systems to handle those products. When you get a vendor system, it isn't hooked into all those things. 'Making the bridges from the vendor system to the Prudential systems is a big complicated job in itself. For the major products we have all the steps involved. For some of the minor products, perhaps some of the products which don't require as much policyholder service, we do take some short cuts and then eventually will bring them into the fold and put them on the regular Prudential systems. Some we may never bring in to the fold.

MR. KLING: In line with the issue of 'Clients Come First', when you are acquired by another company, there's a little magic involved known as a merger reserve. You can use that and do a lot of the things that you wished you'd done and never had a chance to do, especially if you're doing something really different. One of the things that we did immediately after the acquisition was focus heavily on clients being able to tie all of our products into one client system. Our focus is heavily on clients, a client management system and a quarterly client statement, so our client gets to see all the products on one statement. We've spent many millions of dollars on a client system. Our whole focus today is on managing clients, rather than acquiring products or managing products. But it's been extremely expensive, and the payoff is still down the road.

MS. B. DALE MATHEWS: In how many stages of the process do you have a go/no go decision? For instance, when the initial decision is made to proceed with the product, what level of research has been done? Have you actually done some preliminary pricing to see that the original design makes sense? Has the systems area said it's at least possible or do you find that out later, after the resources have been allocated and more investigation has been done? If that's the case, do you still have a chance to turn back?

MR. LIKINS: I was recently involved in trying to develop a universal life product for the tax qualified markets. We had done a lot of marketing research, development of specifications and so on. The field force definitely wanted this product from the Prudential, on Prudential's paper. We talked to the field force about giving it a product on another company's paper. We said we could do that quickly. We did not think it would sell in that high of volume. The agents said, "No, we really need this one on Prudential's paper." The product planning group got together and gave the product a go decision. We started to develop it. The systems people were concerned. They said, "You're going to have to build in the flexibility for this product to change the face amounts because we know on every anniversary there are going to be a lot of face amount changes. That's the nature of a pension plan. People are going to get more contributions, their salaries are going to go up and so on." We were going on our way, and we were running into some obstacles. It was getting complicated to develop. We were working very hard at it. We were about halfway through the process of developing the product, but weren't halfway through the systems development part of it. We re-evaluated the cost of following through for the product and re-evaluated the sales we expected to get from it. The product planning group got together again and the agency force which wanted the product the most got together again. The agents had a bottom line. They knew they had to commit to certain sales to make that particular product pay off with that kind of a price tag. They said they'd changed their mind. They reviewed it again and said they didn't want it quite that bad. I think that responds to your question.

MR. SCHWARTZ: At Sun, we often take a competitors product and put it into our asset share system, just to see if we're in the ballpark, to see if we can do it with the compensation that our salespeople tell us they want and with the numbers that are out there. After that we factor in the amount of MIS resources that is going to be necessary. Based on that information, we decide whether or not we have a go/no go situation. We don't do it in very fine detail. We'll sometimes be more aggressive if we see a big marketplace than if there's a very small marketplace.

MR. KLING: There are two or three points in our process that may have a no go or a go decision. It's usually go, go, go. But that's assuming you have something that's rational to deal with. You've sorted it out. If it meets a need, we'll go ahead to the next step. The marketing/planning part of the process is critical. Oftentimes we'll start something that's just not going to make it for one reason or another. The final point is the screening and assigning priority process. Once it reaches priority status, it more than likely will go and more than likely will go according to schedule.

MR. MARTIN J. THOMAS: To what extent is the product manager's personal compensation tied to product success? I don't mean a somewhat typical annual performance evaluation of the product manager. I mean at the outset of product development, the manager being given a target sales level at a point in the future, and if that target is met, the product manager can expect a bonus of a certain amount. It would be a motivational tool to induce the product manager to speed up the process and to increase the sales. I'd like to know to what extent it is used and to what extent you think it could be used.

MR. COOK: I believe in it. We're not using it. However, we are thinking about it and trying to figure out how to introduce such a system into a head office environment that just doesn't have a bonus right now. I think the biggest hurdle to overcome is that you've got 1,500 people working in a head office. All of them are on salary and all of a sudden you want to put a variable component in somebody's salary. It's a big psychological hurdle to overcome.

MR. SCHWARTZ: We have thought about it from time to time, and we usually find that there are so many functions the individual has to do that to try to measure a couple is usually counter productive. What we do is have the individuals participate in the bottom line profitability of the company as a whole. If it makes the company more profitable, they will prosper. But it's not on a one for one basis with every function that they do.

MR. KLING: We do use a bonus system for our people. It's tied not to any one particular product, because we know we're going to have some successes and some failures. But it is tied to overall sales results, it is tied to earnings for that product line. It is tied to product penetration, client penetration, and distribution system penetration. For example, the number of people making X sales or the number of clients that have a product of this particular type. Each product manager has that tie-in for his particular line of business and he gets a bonus on that. It seems to work reasonably well. I often wonder if we couldn't do more on particular projects, much like the question that was raised, but we're not there yet.

MR. LIKINS: At Prudential, the decision to develop a product in the setting of the sales and the sales commitment is not a decision that the product manager gets to make. But there is some relationship between compensation and the product manager's ability to bring the project in within the kind of time frame that's been committed to and expected of that person. It's more indirect and not related to the bottom line of the product as much as the development of the product.

There's also the second phase which is managing the products after they are sold. I would say there is some relationship to the these people's compensation, but not a particularly direct one.

MR. JOSEPH F. KOLODNY*: Some of you alluded to a measure of return on equity in your product pricing. Could I get a comment if possible of what your current hurdle rates are and how close you are coming to them in your product pricing?

MR. SCHWARTZ: We will get a return on equity after 5 years on a pure cash basis, not including reserves but including cash values. We also look at more traditional profit and percentage of premium measures after 10 or 20 years, but we have to achieve our cash return on equity over a very short period of time.

MR. KLING: Our hurdle rate is 20%. That's a hurdle. I haven't got over it yet.

MR. BLUE: Two central themes running behind what each of the presenters have said I think, are communication and commitment. The most important aspect of commitment in a new product is a commitment of the distribution force to the

* Mr. Kolodny, not a member of the Society, is with Presidental Life.

product itself. Have you ever been in a position where despite your best efforts or the product manager's best efforts at communication of ideas and in gaining an initial commitment, a product that you feel is good has not moved because the distribution force just doesn't believe in it? And if you have had this problem, what did you end up doing?

MR. SCHWARTZ: We withdrew the product.

MR. COOK: We changed it. Essentially the problem materializes if you misjudge that balance I was talking about between the needs of the agent, the needs of the client, the needs of the company. For example, we brought out a product that didn't pay enough to make it worthwhile for the agent to sell it. We had to rethink that one.

MR. KLING: This is an example. We developed in the early 1980's a variable annuity that had no 'fixed' side to it on the theory that we wanted to transfer the investment risk to the customer. It was a great technical theoretical idea, but it was dog food and the dogs wouldn't eat it. It's finally catching on a bit but we've just recently changed the whole concept and put in what people wanted, which was a fixed side to the product, so the client has a safety valve. We tried and we tried hard, and we never got over 20 - 25 million dollars a year in sales, so it really wasn't worth it. We needed to change.

MR. LIKINS: We have a pretty big portfolio of life and annuity products and are changing and adding products all the time. We revise our entire portfolio every couple of years. We establish our dividend formula and look at any product which has sales of less than about 5,000 contracts a year, and we consider withdrawing any of those. We do withdraw and add new ones all the time.

MR. ISADORE JERMYN: Mass Mutual has experimented with different types of product manager arrangements, and has encountered some of the problems that you've described which gives me some comfort. One I haven't heard you talk about is what you might call actuarial integrity, in terms of the actuarial decisions that get into the pricing of the products. We've had some concern as to whether we've had the same quality of decisions being made from an actuarial standpoint. We've had to wrestle with those and come up with some solutions. I would be interested to hear what sort of problems any of your areas have had. I get the impression that with the different arrangements the decision-making is moving away from where it was traditionally. If so, how has that occurred and how do you handle it?

Let me state an assumption that I am making in the question. I'm assuming that with the realignment of the product manager function, the pricing is coming out of what was traditionally the actuarial division and is being handled in marketing or some other such arrangement, and that the decisions about design and maybe even the assumptions, and some other pricing decisions are being made in a marketing environment rather than an actuarial environment. Is that a correct assumption?

MR. SCHWARTZ: I think we have actuaries very well integrated into our process. We do not believe in loss leaders. We have assumptions and in order to change them, they have to be reviewed. While the actuary puts out the initial set of assumptions, those assumptions are subject to review. If he's not comfortable, he has plenty of opportunity to say that, and so far we haven't had a problem.

MR. JERMYN: Do the actuaries report to the product managers or marketing managers rather than, say, the corporate actuarial area?

MR. SCHWARTZ: In our function the individual product actuaries report to the product marketing person, but that product marketing person happens to be an actuary.

MR. JERMYN: Separate from the corporate actuary or chief actuary?

MR. KLING: We have a corporate actuarial function that's separate. We don't have a chief actuary per se. That actuary's responsible for the basic financial soundness of the organization in terms of valuing liabilities, making sure we've got adequate capital and surplus and things like that. I happen to have actuarial training, and I run the product side of the house. I think we do a pretty good job of maintaining integrity. One thing I would say is that at one time in our organization, and maybe in some of yours, there was one actuary someplace or other who was kind of king of the hill and called all the shots. It doesn't happen anymore in our organization. It probably never will. I don't think that was necessarily the right way. Nobody is that good or that important that they know everything. So we tended to disseminate the responsibility a bit but the integrity is still there.

MR. COOK: We have two kinds of actuaries in the company. Essentially there's a pricing or marketing actuary who works with the product managers and may or may not report to them. Then there's sort of a chief financial officer for the operating division whose responsibility is to review all the assumptions that go into the pricing of a product. We are working towards -- but haven't quite gotten to the point -- where one of the jobs of the pricing actuary would be to demonstrate how any particular product fits into the business plan for an entire portfolio of products.

MR. JERMYN: This could become much more sensitive of course if the compensation of not only the product manager but also some of the people reporting to him, including the actuaries, depended upon the sales.

MR. LIKINS: I might just add that at Prudential I would say that the marketing people over the last 5 years have gotten about 3 to 5 times better in their ability to go in and ask questions about actuarial assumptions. They are getting good at finding out where the soft spots are if we try to be too conservative in product development. If we try to assume too high a lapse rate, too low an interest rate, too high mortality, expenses, or what have you they'll quiz us , and they're getting good at cross-examining us. But I would say the actuarial product developers in our corporate actuarial department, particularly the actuarial product developers, still have a good hand on the controls.

MR. KLING: That's a good point. I would certainly echo that. The marketing people are more financially aware. Sometimes they're compensated from the point of view of financial results. There's a lot more questioning, a lot more taking issue with assumptions, a lot more understanding of what the basic leverage points in the product might be. Some of that is that we've done an educational project with a lot of our people. Maybe we've done it too well in some ways. It's almost scary how much some people understand right now.

MR. DAN R. SPAFFORD: The whole direction of product development is through product development teams, as we heard from the panelists. This creates a number of interest groups which have a big stake in any given project. We've heard about compensation being directed to the results of these projects. I was wondering if any of the panelists would have any comments about competition between these interest groups in terms of developing the right kind of advertising and pushing their projects to the detriment of other projects in the field.

MR. LIKINS: One of the things our group of senior vice presidents does for us in that regard is to sort priorities. We have had situations where the different groups compete a little bit too much, but they're caught at a fairly early stage. Decisions are made at a level above these teams. They do sort the priorities and say, "Okay, this is number one, and these other ones are two, three and four." That must happen or you could have somebody on team A who maybe has more ability than somebody on team B. But as far as your distribution system is concerned, team B has the product that it needs more than the team A product. Things could get a little bit out of kilter, so I think that's a valid concern.