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NON-TRADITIONAL MARKETING: PRODUCTS AND DELIVERY

Moderator:	HARRY PLOSS
Panelists:	JOSEPH FAFIAN, JR.
	JOHN D. LADLEY
	FRANK MINTON*
Recorder:	HOWARD L. STEINBERG

- o Credit card distribution systems
- o Association endorsed marketing
- o Direct response marketing
- o Single premium credit insurance

MR. HARRY PLOSS: Our non-traditional marketing section is sponsoring two panel discussions simultaneously, this and Marketing Arrangements Through Financial Institutions. Interestingly enough we will be talking about selling through banks in both panel discussions, since banks have valuable customer lists.

MR. JOSEPH FAFIAN, JR.: My subject for today is credit cards in the marketing of insurance. I am going to discuss this subject from five different perspectives. The topics to be covered are:

1. What are some ways that credit cards have been used in the sale of life insurance? I will discuss three different ways that I have seen credit cards used successfully as part of the whole overall sales process.

2. What products have been sold successfully when a credit card is part of the sales process?

* Mr. Minton, not a member of the Society, is Vice President of Marketing at American Bankers Insurance Group.

3. Does the use of credit cards really reduce acquisition costs? Stated another way, can credit cards really be a key to a low cost distribution system?

4. What are the proper dynamics of utilizing credit cards to market insurance?

5. What does the future hold?

There are many ways that credit cards have been used in the sale of life insurance, but as I said earlier, I will limit my comments to the three most successful programs that I've seen.

The first is perhaps the most widespread -- the direct solicitation of credit cardholders for insurance.

Examples of this include the solicitations of the Chase and Citibank's Mastercard and VISA card by National Benefit Life; the solicitation of the American Express cardholders by Fireman's Fund Life; the Mobil Oil cardholders by Montgomery Ward; the J C Penney credit cardholder originally by Beneficial Standard and then by J C Penney Life, etc.

Not only have the credit cardholders of financial institutions such as banks been solicited, but credit cardholders of oil companies and department stores have also been solicited.

The process is quite simple. The credit cardholder is mailed an insurance offering in one of two ways:

1. A solo mailing, where the insurance offer goes out as a stand alone mailing; or

2. An insert, where the insurance offering is included as an insert to a billing statement.

The cardholders complete the application and an authorization permitting the company to charge his/her monthly premium to the credit card. Once the application is approved, a policy is mailed to the credit cardholder, and premiums are charged via the credit card.

The bank, oil company or department store typically gets two kinds of compensation; a fee per 1,000 credit cardholders and a service fee, which is equal to a percentage of each premium collected, similar to a commission.

Typically, the average premium generated by this type of sale is about $125 for life insurance, $225 for hospital cash, and usually smaller amounts for other types of coverage. For example, you don't see too many AD&D mailings produce as much as a $100 average premium.

The next way I have seen credit cards used to sell insurance is a variation of the first theme -- the solicitation of direct mail purchasers of other products.

One of the disadvantages of going directly to the credit cardholders is that you have some people who will never buy anything by mail. Some very clever marketers have addressed this challenge. They find lists of people who not only have bought merchandise through the mail but who have charged that merchandise to their credit card. It is a two-step process. Initially, the individual is solicited to join an association of credit cardholders. The association has all the usual benefits -- car rental discounts, travel discounts, etc. By joining the association, you are now eligible to participate in the association's low cost group insurance plan, and that really is the primary benefit of belonging to the association.

These individuals are solicited through the mail in the same manner as a bank's credit cardholders are solicited. Again, after the application is approved, a policy is mailed to the insurer, and the premium payments are charged to his/her charge card. The response rates are typically more favorable than those in the other credit card programs because you have eliminated the person who will never buy anything through the mail.

The third way I've seen credit cards used to sell insurance is totally different. It involves the offering of credit cards to members of an affinity group.

Members of an affinity group or association are contracted by mail and advised that as a member of the association:

1. They are eligible for certain discounts -- travel, car rental, etc.

2. They may be eligible for a VISA or Mastercard.

3. They may be eligible for a supplementary retirement plan.

The mailing includes an application for a credit card. The completed application is returned to the marketing organization which then forwards it to the bank. If the applicant is approved for the credit card, an appointment is made by the agent to deliver the credit card and explain the supplementary retirement plan. The agent can go to the individual's home with an insurance proposal and the new credit card. If he/she makes the sale, the premiums are then charged to the new credit card. I'm aware of one organization that averages about $800 per sale utilizing this technique and closes about 1 out of 2 people to whom it delivers a credit card.

Now what products have been sold successfully when credit cards are involved in the sales process?

In our last example, involving the agent, any product could work since the credit card is really a vehicle for the agent to get an appointment and make a sale in a favorable condition and on an ongoing billing vehicle. However, when direct mail is utilized, there seems to be only six products that have had any kind of success.

The most successful seems to be Hospital Cash, also called Hospital Indemnity, or HIP. A fixed benefit, say $50 per day, is provided for each day you are hospitalized. Benefits may begin immediately, or they may begin in 2 or 3 days.

The second product is sold in a variety of Medicare Supplement policies which, at the risk of oversimplification, basically cover where Medicare leaves off. As an aside, this product has probably challenged more actuaries' pricing skills than any other product in the direct response area.

The third product is AD&D.

The fourth is Term Life. Typically a step rated renewable term to age 70 is utilized.

The fifth is Graded Benefit Whole Life which has been sold to the "senior citizens market" of 50 and over. The product's guaranteed issue provides a benefit equal to return of premium for a few years and then provides the normal death benefits.

The last product is "Birthday Life." It is a traditional whole life product where a specific proposal is sent to the purchaser of one of the other products. The basic pitch is that you'll save some premium dollars if you buy it before your birthday. Obviously you have to price it at age last birthday, or it doesn't work too well.

So these six products account for the lion's share of all direct mail sales to credit cardholders.

We've looked at ways of using credit cards to sell insurance. We've also looked at some of the products that have been sold. Now, let's turn to the question: Does the use of credit cards really reduce acquisition costs? This is really the key to these low cost distribution systems that everybody is talking about.

I am going to limit my comments to the case where credit cardholders are solicited by mail because, like the third example I gave, it depends on what kind of deal you cut with the agent who is out using credit cards as an endorsement but who typically can get full commission. In that example it is not a key.

Let me begin with a definition of terms or "buzz words" that the direct response people like to use.

The first is *response rate* which represents the percentage of people who respond to a mail solicitation. In other words, they send in an application and credit card authorization to an insurance company. These people have expressed a desire to purchase the product being offered.

The second buzz word is *conversion rate*. This represents the percentage of people who respond and are actually approved by underwriting and actually pay their first monthly premium.

Typically, Hospital Cash policies are guaranteed issued. A pre-existing condition is used instead of underwriting so you get virtually 100% conversion rates. For most life applications, simplified underwriting is used. It's an accept/reject type underwriting, and the conversion rate is going to vary dramatically by the group's demographics and by the underwriting goal that you have.

We've defined terms. Now let's examine some possible acquisition costs in the following chart.

POSSIBLE ACQUISITION COSTS

Cost of Mailing (Per 1,000)	Response Rate	Average Premium	Conversion Rate	Acquisition Cost as a Percent of First Year Premium	
				No Lapses	20%
200	0.5%	250	100%	16%	21%
200	0.5%	90	100%	44%	56%
200	0.3%	90	100%	74%	93%
300	0.35%	125	85%	81%	101%
300	0.45	125	85%	63%	78%
400	0.4%	250	98%	41%	51%
400	0.3%	250	98%	54%	68%
500	0.1%	250	98%	204%	255%

The first column is the cost of mailing per 1,000. This includes the cost of preparing the mailing lists, the design and printing of the solicitation material, postage, the cost of the business reply envelope and any list fees paid to the institution with the credit cardholders to whom you're mailing.

The second column is the response rate -- that is the percentage of people who actually mail in an application.

The third column shows the average premium per sale.

The fourth column shows the conversion rate, i.e., the percent of responders that actually pay that first premium.

The last column shows acquisition costs as a percentage of premium two different ways -- first ignoring lapses and second if the lapse rate is a ballpark 20% (in other words, about 80% of the annualized premium is actually collected in the first year.)

You can form your own conclusion, but before you do, let me state a statistic that Stanford Research Institute published a few years ago. It says 74% of the population of the United States has been solicited for insurance by mail one or more times. Is it any wonder that the response rates have dropped?

As we look at the range of possible acquisition costs, we find that the answer to the question: Does the use of credit cards really reduce acquisition costs is, at best, a loud "maybe."

Before you think I'm totally negative on using credit cards to sell insurance, or on the whole direct response business, let's spend a few minutes on the profit dynamics of the business. How do you really make money in this business?

What makes the profit dynamics of most forms of direct response unique is that acquisition costs are really unknown at the time that the product is being priced. We have seen that response rates to conversion rates will impact acquisition costs as much as mailing costs. So you don't know up front what to build into your pricing. In addition, the impact of testing costs has to be considered. Before you roll out a mailing to a large list, you want to test different approaches to see which one works the best. Do you reflect these test costs as part of your acquisition costs, or do you set up a separate research and development budget to handle tests? I've seen both used. But again, it is something that has to be addressed.

The next item to consider is persistency. When a credit card is involved in the billing of the insurance, persistency is usually better than for comparable socio-economic levels. Credit card billing is painless. You don't have to take any action to pay your insurance premium (just sit at the kitchen table and write a check). In fact, you have to take an action to stop paying your insurance premium. I've seen 13 month persistency on term life of 93-94% with an average face amount of $22,000-$23,000. For a very low socio-economic group, super persistency which is not supposed to happen, really does happen.

Mortality and morbidity are predictable as with any insurance product. However, there is one exception for this type of business -- that is when fraud rings are involved. Let me just comment briefly on these fraud rings.

People have been known to buy a whole bunch of Hospital Cash policies from every company that they could -- via television or mail -- and spend their vacation in the hospital. It's a very good deal. Group insurance pays for the hospital bills, and the hospital cash policies are pure profit.

At least one company, my old one, put in a coordination of benefits clause in Hospital Cash which I told them would never get approved by the state -- but it did, and so at least National Benefit's liability was limited. And after that we didn't seem to have too many problems with fraud rings.

Turning to some of the other dynamics.

Interest is not a major factor compared to what we are used to with universal life, annuities and other interest sensitive products. And other expenses are permissible, just as they are with the other products. The dynamics are no different with respect to expenses or interest in any other product.

The last item on the list is internal marketing. Internal marketing is a phrase used to describe the sale of additional products or riders to people who responded to the initial solicitation. The process begins at time of issue when the buyer is offered an opportunity to purchase additional coverage or add a rider. Typically, internal marketing at issue is done by telephone. Our standard pitch at National Benefit Life was: "Congratulations! You have been approved for your $20,000 that you've applied for and you're such a good risk that you can get $40,000 by just paying double the premium." Once the policies in force had appropriately spaced intervals, the policyholders were offered the opportunity to increase their coverage or add some other additional benefit. Again, this is typically done by mail with a telephone follow-up. The response rates on this presentation are much higher than on your up-front solicitation because these are people who have already bought. For example, at National Benefit Life, one of the things that we did, that as far as I know was the first time in the industry, was to tell all our existing Term Life policyholders: "Look, inflation has really been something the last couple of years, and if you pay twice the premium, you can have twice the coverage." Amazingly, 12% of the people -- not .12% but 12% -- said, "Yes we will pay twice the premium for twice the coverage." So a successful internal marketing program can convert what otherwise would have been an unprofitable mailing into a profitable one. In my mind, internal marketing can be -- and should be -- the key to success or failure, but it sure is nice if that marketing can get it done on a profitable basis up front.

What may the future hold?

We currently see T.V. commercials soliciting insurance. Again, if you respond to the commercials, you will receive a solicitation in the mail, and the process is very similar to any other kind of mail program. With the proliferation of VHS equipment -- a company would send you a tape that you can plug in your T.V. and give you a sales presentation that has been prepared especially for you. That technology is here -- the costs right now are a little prohibitive.

Let's go a step further. I keep hearing that I am not really going to have a television in my family room -- I'm going to have a PC of some kind. I can switch on my "television" and look at a Universal Life proposal. I can play "what if" games. Again, the technology is here. Remember, whatever I bought from my living room would be charged to my credit card.

Let's look on the negative side. What are the potential negatives of this whole direct response credit card related kind of marketing? The major one as I see it is saturation. We all seem to have several credit cards in our wallet. Will we receive at least one insurance solicitation for every credit card that we are carrying? I think so. Particularly in the marketplace that we are dealing with -- when someone has a Hospital Cash product that they really don't understand and now they get another offer which is $1 cheaper -- you might see them drop the old one in place of the new one.

Just before I left National Benefit Life, it was interesting that the term life persistency had not changed one iota over the four years I was there. The Hospital Cash had started to deteriorate. I have no statistics to back it up, but it is very easy to compare Term Life -- I've got so much coverage and I pay this premium. Hospital Income is a little tougher because the benefits can start today or three days from now. You know for actuaries it is very easy to read a policy and understand it, but for the average consumer it is not. The point is, saturation is becoming a problem if it isn't one already.

In closing, let me summarize my comments.

First, insurance has been sold successfully utilizing credit cards in a variety of ways. We talked about three of the approaches that have worked.

Second, the product depends on the distribution system. To date, I haven't seen anyone have great success trying to sell permanent life insurance without an agent.

Third, acquisition costs may or may not be lower because a credit card or mail is involved in the sales process.

Fourth, while profits are not guaranteed because a credit card is involved in the process, persistency is probably better if a credit card is used to bill premiums.

And last but not least, past may not be prologue. Oversaturation can clearly be a problem, but somebody is going to figure out how to use our emerging technology and sell insurance in ways we haven't even thought of.

MR. PLOSS: This business, as Joe pointed out, differs from agency business in that you don't know how much you will pay for it. With an agent, maybe you know you will pay him 55%. Here you could pay 16%, or you could pay 300%. And you have to learn from your successes and, more importantly, failures. Frequently I see people who have had 1/10% response rate, and they just throw it out as a failure without trying to learn from the test. Because acquisition costs are so important, of course you want to sell more business to your existing customers. Your customer list is your most important asset.

MR. JOHN D. LADLEY: Today I would like to speak about a very specific part of the non-traditional marketplace, and that is third party administrators (or TPAs). We are going to discuss them in some detail.

To those of you who are not familiar with them, I hope this will be informative. It will lead you through the reasons why they fit into the direct response business; why they have made sense for carriers and even non-insurance carriers to look at; some of their basic characteristics and their customer characteristics; and, what is going on in this business today and how you might get into it (and evaluate it). That is how we are going to course through this topic.

For those of you who have had some involvement with TPAs, which may have been negative, see if you can shed some of the thoughts you may have had in the traditional ways of doing business with third party administrators, and maybe we can come away with something positive on TPAs for you.

First I would like to discuss the subject area and how it fits into this mass marketing/direct response business. Third party administrators are organizations specializing in marketing and/or administering insurance and benefit programs on a mass basis. In their most common form, third party administrators control large blocks of life, health and other insurance businesses, pension and benefits included.

Third party administrators have survival instincts and the kind of protection that they need in a difficult environment. As we know, the insurance business is changing. Much of the third party administrator business is changing even more rapidly with health insurance/health care changing so very rapidly. These organizations will be survivors. They are going to survive no matter what. They are very close to their market, they are adaptable, and they are very experienced in their business. They will probably survive longer than many insurance companies will survive.

They have substantial market experience. In a sense, they are not non-traditional. Many of the TPAs have been around for a couple of decades, and they have considerable experience in the direct response business. To summarize, I see them as a very significant, high potential market for insurers and, of course, non-insurers too, including banks and other financial institutions.

How might a third party administrator be attractive to an insurance company? Maybe there are some bank representatives here, too, and many of these points would also apply to you.

The first way would be in administering business. That would include processing of claims which is a major function, and there have been some trends in that business lately towards some carriers purchasing third party administrators just to process claims. Frequently they are more cost efficient than insurers. That is claimed to be the case by many third party administrators, and it seems to be confirmed by some of the major insurers in the business. Many third party administrators, despite a relatively small size, have quite efficient, high quality systems which include claim systems but which might also be performing benefits processing -- 401(k) and the like.

Some third party administrators have been looked at as providing a different level of service for the carrier, so there could be a series of qualities or levels of service which could be offered by the insurer, a very difficult undertaking for an insurer to accomplish internally.

And in a lot of ways, through their administrative capability, TPAs may be the only way an insurer or non-insurer can easily enter this business. It seems relatively clear to me that direct response has numerous peculiarities and systems demands. That is not always recognized, but specialized systems are certainly required to handle the various aspects of direct response.

A second way a third party administrator would be of value to an insurer or non-insurer would be simply to sell business -- a pretty conventional view of them as sort of a super agency of the company.

A third way would be to provide a customer base for the insurer, and there are a variety of ways to look at that.

There may be prospects within a third party administrator which are not customers -- potential lists, for example. If the third party administrator controls a large association, or through its marketing methods develops a lot of potential customers, but not actual customers, that may be a huge base.

Another opportunity would be to add products or sell more of the same products to actual customers of the third party administrator. Of course, you always have to look at the endorsement, and we will talk about the endorsement that the third party administrator can deliver in a little while.

Third party administrators may have agents. Many TPAs have a substantial relationship with agents who may number in the thousands, although it may not be a close relationship in the terms of numerous sales and lots of commission -- nevertheless, they do have a relationship that has some value.

The third party administrator may provide an entry for an insurer into certain markets, either that they are not now in or they are not far enough into to meet their objectives. This might include small group, older age people, alumni, unions or some other specialized area of the business.

Another reason for considering TPAs would be that it might afford an insurer or non-insurer the opportunity to learn certain marketing methods. And some of these people are very clever and certainly have a very diverse approach to the business -- almost a "no two alike" kind of situation.

As a business, third party administrators are generally quite profitable in their own right. That is something that can be looked at.

And all this assumes that there are third party administrators established out there you can work with, but of course, an insurer can start its own third party administrator or accomplish the same thing in other ways.

We are now going to cover some of the TPA *characteristics*: the customers; the products; and generalized size and market share of TPAs.

For purposes of this session, I categorize TPA customers into three general segments, by emphasizing that TPAs deal largely with groups which have memberships.

The *high affinity group* -- this would include employers, organizations which demand high dues, and causes with strong feelings attached to them. These would generally be associated with the strongest, most valuable endorsement, but also the one usually with the largest political ramifications to its use.

A second category would be *lower affinity groups* -- clubs, low dues paying groups, and, in some cases, credit cardholders or customers.

A third segment would be *non-affinity groups*. These are non-groups, often developed by the TPA themselves. These groups sometimes take on a life of their own. They may be created for insurance purposes, but can easily move into the low affinity or high affinity status themselves. That may be by design or by accident. Often when it is by accident, there is a control issue involved with the TPA and perhaps the carrier.

Where are these customers and TPAs located?

Generally, since TPAs use direct response techniques and want to spread costs, they tend to operate nationwide. Infrequently, they are regional, but there are examples of TPAs which are regional. That is speaking to the customer base of the TPA -- where they find their customers.

Most third party administrators *themselves* are in New York, Illinois, D.C., California, and Florida. There is some concentration in Pennsylvania and in a few other states. Traditionally, they are close to the headquarters of the associations they serve and, of course, population centers.

How many customers would a TPA typically have?

Generally, they would be in a super agency category for most companies. There would be customers numbering typically in the thousands; 20,000 or 30,000 is not uncommon for a reasonably sized TPA in the small group market. Customers could also be the agents, who may number in the thousands. And *potential* customers to an insurer, including current non-customers, have to be looked at very carefully. There could be virtually no non-customers with a relationship, or there could be as many as 100 prospects for every existing customer. That could be highly valuable.

Endorsement? Again, it depends on the strength -- the affinity -- of that group as we mentioned before. Its strength and extendibility is very important. The endorsement has to be looked at very carefully and analyzed very carefully in terms of limits on its use, timing, wording, frequency, true control over the endorsement and a number of other factors. It is often something loosely treated in negotiations and discussions, but it has a lot of aspects to it.

There is a control element to third party administrators that tends not to exist in insurance generally, but may exist in some circumstances in other business. That is, a few insurers and non-insurers can frequently get a close contractual non-product relationship with a third party administrator that they certainly cannot obtain with brokers, and perhaps not even with their own "captive agents" these days. It frequently makes TPAs attractive in terms of enabling insurers to get control of at least one of their customer bases.

What are the products of the third party administrators?

First, perhaps the key, would be *service* (but not always). They virtually always do some sort of administration and usually do the claims processing as well and, as mentioned, pension and benefits processing. There are some specialists in claims processing only. Often overlooked -- a good way to develop a third party administrator and keep one going -- is *membership* processing, usually involving superior data processing facilities for the customer organizations. Many small organizations can be joined into a single large one through effective membership processing. And that might include membership promotion and creation, as well as maintenance.

A second product or area where TPAs offer value is in marketing. I won't go into that in a lot of depth. That is worthy of several panel discussions in itself.

TPAs frequently do creative work: the production work of advertising, media buying, participate in product development, manage media and product campaigns, and monitor results.

The lines of business that TPAs are typically involved in include most frequently group accident and health package plans for under 50 lives (a business that is under a lot of pressure, especially in certain TPAs as it is in the rest of the industry -- but they have done very well of late in that business) and pension and 401(k) business. There are Life-only TPAs, and there are those that are involved in supplemental coverages. It is my experience that most third party administrators still think and sell along a single product track -- and they have not been very good at adding additional products or supplemental products to an existing product base. That may change. That may be an outgrowth of the fact that I think that a lot of third party administrator organizations are controlled by aggressive, top-notch former agents who perhaps have an individual sales approach to the market more than a true direct response approach.

To look at them by size -- the comparison is a little simplistic but I think it describes them rather well -- we have small, medium and large.

The small third party administrator may be a specialty administrator (about $5 million in premium revenue generating little over $1 million, typically, in commission revenues, writing frequently a single case, and usually not a heavy user of direct response).

The mid-range third party administrator, which I have identified as acquisition or venture "targets" (which I think probably make for the best opportunities for venture, purchase and other activities by insurers) would generally sell in the small group market. It either sells through true direct response, or direct to agents who then sell the product, or it perhaps uses telemarketing. These are significant organizations with anywhere from 50 to 150 employees. (There are some averages that have been developed from some surveys.) They will tend to have, even at this size level, some fairly sophisticated and sometimes integrated systems. Systems would include: claim systems, administrative and also agent systems (tracking agents both as to experience, payment of commissions and those kind of financial matters relating to agents), and marketing systems.

We then move into the "very large" category -- Planned Services, or Consolidated Group here in the Boston area, and a number of others. Very sizeable organizations, sometimes with a few hundred employees. These TPAs may use a variety of marketing methods but frequently will have some sort of agency or group representative field force.

The market share of third party administrators -- I'm not sure anybody knows the market share of carriers and other players active in the health insurance market -- has been variously estimated at about 15-25% which they are controlling, doing processing for and selling to. In general there seems to have been some growth in the number of percentage points of market share for TPAs in the past 5 to 10 years. They have apparently done that at the expense of the Blue plans. Now TPA growth is slowing somewhat -- the impact elsewhere in the industry from HMOs and other prepaid plans is being felt by the third party administrators. Although some are doing quite nicely, it is an individual situation.

What is the current situation that TPAs find themselves in?

Most are in need of carriers. They do not represent enough carriers -- sometimes only one. My experience would be that very few third party administrators are looking for carriers so that they can play them off against one another as an individual salesperson might. I have not found much evidence of that. Of course, very few have the opportunity to do it too with so few carriers represented. They may have more than one carrier for additional product lines -- some of their product lines are fairly unique, such as dental insurance, and it is not easy to find someone to write even small group medical in many cases.

Much effort within a third party administrator -- in fact one of the primary functions of a top person in the third party administrator -- is finding carriers and developing relationships with carriers. Maintaining good relations means working through all kinds of things like rate increases, product changes, new product development and so forth. That is, one of the key marketing functions that the top person has is simply working with the carrier, and the TPAs that perform very well are naturally very good at that.

Some are desperate for a single carrier, and that can frequently be an opportunity but might also be a huge warning signal about that third party administrator. But many times that is not due to bad business that has been written or improper marketing methods. It is just that carriers are entering in and pulling out of that business frequently and that the TPA probably has only one or two prime carriers.

Inadequate capitalization is becoming an issue for a lot of third party administrators, and therefore a lot of them are seeking arrangements with insurers and others who will help them through this period.

There are *prejudices about third party administrators* and their businesses. Certainly there has been a small minority with serious financial problems; some have had poor management; and some have driven a few insurers into insolvency. But some insurers have been driven into insolvency other ways as well. TPAs frequently sell small group health insurance, and that is an area of concern for probably the majority of life insurers. These are sources of major prejudices about them.

TPAs tend to be very profitable entities and have sizeable margins. They control $15-20 million of premium on average. They have had a high growth rate, at least through 1984 and the beginning of 1985 although that is now slowing. There is some consolidation taking place right now in that business. There is quite a bit of merger and acquisition activity taking place among TPAs. It is an easy way for non-insurers to enter the insurance business, and a number of insurers are looking at them also.

Is this a business for you?

As I mentioned, insurers have been working with and purchasing TPAs recently. The structure of the transactions depends on the utilization of the TPA. Banks are establishing or buying TPAs as well.

TPAs can certainly write specialized products or broad based product lines (either one). One of the questions to ask yourself is how flexible are you if you would get involved in this market? How fast moving in terms of products and systems and how accommodating will your existing systems and people be regarding growth and concentrations of business at certain points in time?

A major consideration in any arrangement is who is going to take the marketing risk and what exactly that marketing risk is -- considerable time can be spent discussing that and getting it defined. There are many buzz words (as I'm sure the rest of the panel will agree) used in direct response such as "conversion rates" and "send no money" and "response rates" and so on. A very clear definition of all the marketing functions that are taking place and exactly what these terms mean is essential in order to understand exactly what it is costing you and exactly what you are agreeing to.

How would you evaluate a third party administrator?

I have just a few suggestions. I would say an on-site business evaluation with preparation is critical but not always the easiest process to arrange. However, it is very important to see the TPA operation you would be involved with.

Careful examination of the claims function is certainly an important process to undertake. Procedures have to be audited from beginning to end, and the claims information and what is done with that information has to be reviewed. A positive sign that you will see on occasion, but not frequently, is when an actuary has been involved in the third party administrator's management. That will be very helpful to you, and I think a real indication of the commitment that the third party administrator has to understanding the business, as opposed to just processing it.

You can look for financial statements. You often won't find them in the third party administrator. It would be preferable if the statement was audited, but by far the most prevalent type of statement, when it is available, seems to be a compiled financial statement. The TPA may or may not have instituted GAAP. They are permitted to use GAAP but most do not, so you may have to generate the GAAP effects of their operations. You might also ask yourself who has done some of these financial statements -- a small firm down the hall from the third party administrator or a Big 8 firm? This can make a large difference in statement credibility.

Actual product forms and carrier arrangements must be studied when there are any and there frequently are, and the process of selection (or underwriting) has to be carefully reviewed -- almost as closely as the claims function.

To summarize, I feel that third party administrators are a significant factor in non-traditional insurance marketing and administration. Insurers and non-insurers alike may not want to overlook them since they can act in a variety of ways to increase insurer capacity and effectiveness. But since you're dealing with small businesses -- a cottage industry -- you therefore have to evaluate your options very carefully if you plan to get into this market.

MR. PLOSS: Third party administrators are frequently staffed with insurance people, and perhaps the biggest thing that TPAs lack is the capital to be an insurance company themselves. They are an interesting opportunity. My company has kind of grown their own third party administrator, and it has a separate marketing organization with branches all over the country. Perhaps control and understanding how TPAs work is the key to making a profit through them.

MR. FRANK MINTON: In order to put my presentation in the proper context, permit me to give you a quick overview of American Bankers. Some of the audience may not be familiar with the organization, and as American Bankers typifies a modern multi-media credit insurance marketer, some background information on the company would be helpful to the presentation.

In the first quarter of 1986 American Bankers reached $1 billion in assets. Now this may not be particularly large in terms of the size of our client institutions, or large as it relates to major full line insurance companies, but when one considers that most of our business, as a matter of fact almost all of our business, is related to credit transactions, a billion dollars in assets really is substantial. The collected premiums of the year run around $800 million -- about which 3/4 is related to credit transactions and is driven by sales conducted through financial institutions such as commercial banks, thrift institutions, consumer finance companies and mortgage bankers. In fact, we have structured our company according to various financial markets. Consequently, American Bankers group is divided up into a number of businesses that do business only with one type of financial institution. As an example, we have a business that does business only with consumer finance companies. We have a business that does business only with thrift institutions around the country. We have another one that does business only with credit unions. And, lastly, we have a business that does business only with commercial banks. Each one of these organizations incidentally has its own P&L statement, its own balance sheet, and is held accountable for profits. We feel that dividing ourself up along market lines truly makes us very sensitive to our customer needs. And being in an extremely competitive environment, I assure you this division is particularly important. Most of our employees have come from the institutions they serve. As an example, most of the people in the commercial bank business at one time were employees of commercial banks, so they are extremely familiar with all the insurance opportunities that are available in a commercial bank environment. We market almost all of our products using the financial institution as an intermediary, and our sales message is presented to the consumer through a variety of methods: direct mail, statement stuffers, such as through a credit card or a monthly checking account statement, telemarketing, or face-to-face sales with the institution's loan officers being the customer interface.

My talk today will be addressing credit life and disability insurance, of which almost all is sold in a face-to-face, one-on-one situation between the institution's loan officer and his customer. Almost all credit life and disability premiums sold in the United States today are single premium insurances. The key loan products that drive credit insurance sales are installment loans on automobiles and home improvement loans. The average loan may be in the range of around $8,000 with a typical term of three to four years, and the corresponding premium would be in the area of $200 to $300 of sales. Now the premium rates for credit life and disability are regulated by each state, hence, they can vary significantly from one state to another. As an example, the single life rate in Louisiana is $1.00, while in Ohio the same coverage is only $0.52. The final premium cost to the consumer, however, will depend upon a number of factors: the insurance rate in each particular state, the term of the loan (obviously, the longer the term of the loan -- the more expensive the insurance is going to be), the loan APR or the interest rate and, of course, the size of the loan. Very often the amount of the insurance coverage will be based upon the customer's original total indebtedness or, in other words, the sum of the customer's monthly payments. Credit life insurance, with its relatively stable earnings, became a national product with which to put the additional marketing emphasis.

A typical sales-oriented bank today will sell in the area of $2.50 of credit life and disability insurance for every $100 of installment loan volume. At a 40% commission, that adds another percentage point to gross margins. And again, for a banker in an extremely competitive environment, credit life insurance then does represent a major opportunity which he has to capitalize on. Incidentally, the commissions can range anywhere between 20-60% depending on the rate in the state, the size of the bank, and special servicing needs of the bank, such as sales training.

Now there are basically two methods with which a bank can receive income from marketing credit life and disability insurance. One method, as we have already stated, is from a basic commission income plan where the bank will receive a percentage of the premium. The second, being a bit more lucrative for the bank, is an income stream generated if the bank owns its own captive. The captive route usually tends to produce a smaller tax liability than the basic commission income plan which would be taxed at the standard corporate rate of 46%. As indicated earlier, the premiums are usually single premiums paid in advance with the premium being paid by the bank, to the insurance company, on behalf of the customer for the full term of the loan. In actual fact, the amount of the customer's loan will usually be increased to pay for the insurance premium. The bank then receives an advance commission from the insurance company. If the customer pays off his loan early, the unearned premiums are refunded to the customer. Very often the insurance company is willing to share the profits with the bank in the form of a contingent commission. This form of commission is contingent on the insurance company earning its full retention.

Depending on how the contract was structured between the bank and the insurance company, if the losses exceeded 46%, the insurance company's retention would be reduced or eliminated. The bank then would have to reduce its advanced commissions the following year, or the losses would be carried forward and subtracted from subsequent year's contingent commission. Obviously, the lower the advance commission the more secure the insurance company's retention and the more willing the insurance company will be to pay the bank a contingent commission. However, the forces of the marketplace very often require the payment of large advance commissions to the bank as well as contingent commissions.

As an example:

Earned Premium		100%
Deductions		
Advance Commissions	40%	
Insurance Company Retention	12%	
Premium Tax	2%	
Losses	43%	
Total Deductions		97%
Contingent Commission		3%
Total Bank Commission		43%

Many of the larger banks have opted to assume all the credit life and accident and health risks themselves, and they have formed their own reinsurance company. The Federal Reserve Board has long permitted banks to own their own reinsurance companies, provided the coverage is limited to credit risks generated by the bank or, in the case of a bank holding company, any of their subsidiaries. Usually the bank will choose to form the captive in Arizona where the capital and surplus requirements are a minimal $150,000. The bank then will typically negotiate a fronting fee with an insurance company that is licensed to do business in the state where the loans are being made. The ceding fee charged by the fronting company to the reinsurance company is very often volume based.

6.0%	Up to $2,000,000 of net written premium
5.6%	next $500,000
5.2%	next $500,000
4.8%	next $500,000
4.4%	next $500,000
4.0%	remaining premium

There are a few insurance companies that front business for bank captives that have fairly extensive sales training programs for the bank's loan officer personnel. In making a proposal to a bank, the insurance company that has insurance sales training facilities will very often detail a twelve month marketing and sales training program it would put in place. In those cases where the insurance company is offering high levels of service delivery such as sales training, the company's retention is based not only on the expected premium size but also on the ratio between the written credit premium and the new loan volume. The fronting company's retention will usually increase if, through sales training programs, it can increase the ratio of premium to loan volume. In summary, the insurance company's retention will decrease when premiums are driven up by loan volume but will increase when premiums are driven up by the ratio. We put all this into a matrix format.

RETENTION MATRIX

Credit Premium Per $100 of New Loans	Net Written Premium $(000) 2,000	2,500	3,000	3,500	4,000	4,500
Up to - 1.70	6.0%	5.6%	5.2%	4.8%	4.4%	4.0%
1.701 - 1.78	6.5	6.1	5.7	5.3	4.9	4.5
1.781 - 1.86	7.0	6.6	6.2	5.8	5.4	5.0
1.861 - 1.94	7.5	7.1	6.7	6.3	5.9	5.5
1.941 - Over	8.0	7.6	7.2	6.8	6.4	6.0

What we said then is that, when a contract is written (and we've made an example here that the bank is writing $1.70 of premium for every $100 of loan volume), and the written premium is expected to be $2 million -- then the retention is going to be 6%. But if the bank starts to market more and more loans and the premium increases to $2+ million, then your bank can expect to pay the insurance company a lower retention rate. Meanwhile, however, the insurance company is out there calling on the bank branches, teaching the loan officers how to sell insurance, and that ratio of premium starts to creep up to $1.78 or to $1.86 for every $100 of loan -- then the insurance company is going to want a larger and increasingly larger retention. So you have the retention rate going down while the loan volume is driving up the aggregate premiums. On the other hand, you have the retention rate going up while the insurance company is out hustling the bankers.

I think any overview of the business would be incomplete without addressing a major problem facing the industry today. The problem concerns itself with the issue of adverse selection. In a group life and disability contract where the only requirement for coverage is that one be within certain age limitations, naturally there will be a certain amount of adverse selection. Remember, the rates are level regardless of one's age. However, where the amount and duration of loans are fixed and with a predetermined amortization schedule, the insurance rate can be adjusted to take care of the adverse selection problem. However, many banks made the strategic decision several years ago to de-emphasize the traditional installment loan in favor of a revolving line of credit.

As the interest on the balance is often pegged as some short-term barometer, such as the prime rate, it becomes very easy for the bank to match its assets and liabilities. Now with the emphasis on the automobile manufacturers to be a major influence in the financing of new automobiles really starting the second quarter of 1985, the banks have increased their emphasis on revolving lines of credit and have basically surrendered the new automobile installment loan business to the automobile manufacturers.

With the major retail lending emphasis by banks on revolving lines of credit and credit insurance, revolving lines of credit represent a major adverse selection problem for the insurance carrier. Consider the individual who has a line of credit of $50,000. He has credit insurance and his outstanding balance is $5,000. He has just received some bad news from his doctor -- he has a terminal illness. He pulls down his remaining line of $45,000 and his insurance now automatically increases to $50,000. Shortly thereafter he dies. Now the insurance company has collected premium for $5,000 of risk but is now forced to pay for the losses on $50,000 -- obviously not the way to prosper in business. A great deal of the problem we feel could be alleviated if State Regulators permitted a pre-existing clause to be put into the credit life contract. Ideally, the pre-existing clause would be employed not only at the time the loan was applied for, but just as importantly -- perhaps even more importantly, every time the credit line was drawn down, and the insurance company's exposure was increased. Because of this situation very few companies now are offering credit life insurance on lines of credit. And particularly as the lines become increasingly larger, the companies are backing away from it. Many people who would normally purchase this coverage are really left going uninsured. It is a major problem facing the industry today and is being accented particularly as the banks pull away from the traditional installment loan business and start to put more and more of their assets in revolving lines.

MR. PLOSS: Frank described how a credit company with an effective but experienced credit insurance training program for loan officers can compete against low retention quotes from other carriers. The matrix retention schedule is a performance agreement -- the insurance company will only profit if it can deliver better sales penetration, which creates a bigger pie with more profits for both the bank and the insurance company.

MR. MICHAEL DON HOPKOVITZ*: I was wondering if anyone has had any experience with direct mail products in the United Kingdom. What kind of responses have they got? Are they comparable to the United States?

MR. MINTON: I've had a little experience in the direct mail business overseas, and let me share with you my very first effort at it. I was living in Sydney at the time, and we had just concluded a program with Carte Blanche. Corresponding back to my superiors in New York, I suggested a program that was really quite complex. It had different limits for different sorts of situations. If you were flying in an airplane one way, you got something -- if it was going another way, you got something else. I really didn't know what I was doing. We made up our marketing piece and much to my superiors' chagrin back in New York, I sent it out, and the results were overwhelming. The responses just came in -- no one could believe it. In following years I thought back upon it and tried to figure out why, and the net of it is I think that in some places of the world you can literally do anything in the mass marketing area and be successful. Unfortunately, the United States is not one of those. And the United Kingdom is something like the United States. I've done a number of different marketing programs around the country, and it seems that the more sophisticated the country is at it relates to the mass marketing sort of thing -- the lower the penetration rates are going to be.

Again, focusing back to my experience in Australia, I think we had 14 or 15% of the customers respond. Today I am familiar with some of the activity going on in Australia, and maybe it's 1 or 2%. We do an awful lot of business today with Barclay's Bank in United Kingdom. and we are looking at maybe 1 or 2% response. Marketing those same products in the United States today will get maybe 3/4 of 1%. And so, I think a lot has to do with the state of technology in the country, as well as the level of mass marketing of all sorts of things in the particular country.

* Mr. Hopkovitz, not a member of the Society, is an Assistant Vice President/Actuary at Associates Insurance Group.

MR. LADLEY: I'm aware of a couple of programs that have used return of premium health insurance, some health insurance of the hospital indemnity type, and savings oriented life insurance. My impression is that the response rate has been more favorable in the U.K. than in the United States, but it has been sort of a fledgling industry to them -- a fledgling approach to marketing. It is not really very well developed. They don't really have the kinds of media available that we do here with the kind of liberality of use and "the reach" that we have in the U.S. So it is not really directly comparable. I think there was some feeling that national health insurance would eliminate any kind of direct response type of selling, but I think it is tending to enhance it right now. I think the experience has been fairly favorable there from what I understand.

MR. PLOSS: The United Kingdom is a less developed market, perhaps 20 years behind the United States. Most marketing attempts have been quite successful since their mailboxes are not as saturated with direct mail pieces as in the United States. Also, England has had very high interest rates and inflation and so you see a lot of return of premium products that will work in their environment, and we can't achieve quite the same pricing.

MR. E. PERRY KUPFERMAN: I've got a three part question for Mr. Fafian: What are you doing with list segmentation to work on penetration? Second, what specifically has been your persistency experience? And, third, I take from your thoughts that your hospital income product has not done well. Do you feel that in fact there is a good future for that product or not?

MR. FAFIAN: As far as segmentation, the banks were a disaster. Surprisingly, the banks have very little information about their customer in terms of what they get on an application for a credit card. They get the world of information, but they don't put it in machinable form. What you basically have is all the stuff that you need for billing, some indication of activity, credit lines and that kind of thing. So the bank is the only segmentation in which you are able to sort out the folks that didn't use their credit card and didn't respond. We had super success segmenting the lists when National Benefit was acquired by American Can. American Can has a mass marketing company called Fingerhut that sells all kinds of merchandise through the mail. Because they were a sister/brother kind of relationship, they have done a tremendous job of segmenting for their own business and never looked at insurance because when you start paying folks so much per thousand mailed -- there is no real motivation to not mail to the folks who don't respond. But because we were of the affiliation, they broke down the list every which way and improved the response rates dramatically. If I look at hospital cash, the information I'm giving you is about two years old because I left National Benefit Life in 1984. But at that point the 13 month persistency in hospital cash had gone from something like 85% to closer to 70%. I have no statistics to back it, but if you look there are a couple of phenomena that went on with the banks. You cut a deal with let's say Chase Manhattan to mail to its credit cardholders. It now starts a new program of some kind, and guess who it starts as its firsts set of customers -- its credit cardholders who it now cuts a deal with. Somebody mentioned AIG. So you will find that within a bank, it is not inconceivable that the same folks are getting more than one "Chase mailing" from more than one insurance company. You are not dealing with a very sophisticated buyer. I think intuitively that is what has impacted persistency. What will the future hold? It is really a fundamental pricing thing. One of the things that was going on at National Benefit Life before I left was that we were going to re-examine the whole pricing because things have changed. It is no different in the agency business.

MR. PLOSS: You had mentioned that 3/4 of your business was credit business. I was wondering if you would describe some of the casualty coverages that arise from automobile loans.

MR. MINTON: Well basically the principal product that is driven from an automobile loan is the automobile physical damage dropping coverage. We are basically not into writing that. It has been disastrous for everyone around the country, and we have no intention of repeating anyone else's mistakes. I think that the principal casualty product that we are writing today is unemployment insurance. We do it on credit cards. We have been immensely successful with it. The first quarter this year we mailed out around 10 million pieces. The response rate is fantastic. We have just done a program with Chase Manhattan, and typically with a bank like Chase, the response rates will tend to be smaller than with say a bank like Southeast, simply because Chase will send out literally four and five times as much different sorts of insurance material as a local regional bank, so the responses will tend to decrease. But unemployment insurance is the principal casualty product we are writing today through commercial banks, and we are experiencing a loss ratio probably in the area of 30% or something like that. The perception of unemployment is high today, but obviously the probable would be when it turns around and starts to go up again. So, we are reaping the rewards, and I'm sure we will have a price to pay sometime down the line but not right now.

My experience in terms of segmentation has probably been somewhat akin to Joe's. Segmentation is a word that all bankers will use today, but for all practical purposes, they really don't segment their customers effectively. Consider yourself the last time when you went in to apply for an automobile loan at the bank. You sat down there next to the banker, and he asks you all sorts of information, and then he filed that away in hard copy. The only thing he puts on tape is your name, address, account number and the amount of the loan. Because he can only give you that level of information, there are only a few ways you can segment it, perhaps by zip code and by the amount of the loan, but it is very difficult. We have a telemarketing program running now with a number of banks where, after we speak to the customer about an insurance program, we ask the customer to participate in a survey where we ask him salary information, we ask him information about whether he has children of college age and all sorts of things which we put on tape and give back to the bank as part of the package for giving us an opportunity to sell insurance to its customers. And so we are in the business of helping the bank update its customer information files, but banks are really light years behind what their talk says they are.

MR. PLOSS: An expensive bank segmentation process would involve address/census tracking data enhancement. This is more viable on large unendorsed merged lists.

MR. THOMAS M. MARRA: In the introduction of Mr. Ladley, it was mentioned that he has had an affiliation with the American Association of Retired Persons (AARP) organization. I would like him to expand on that and also to comment on the prospects for a potential endeavor with AARP in the life insurance area.

MR. LADLEY: I was first employed with Prudential, then Colonial Penn. Both carriers are now or were involved in AARP programs. I had no affiliation with AARP itself directly.

My understanding is that AARP was started by someone who would have met my definition of a third party administrator. This individual felt he saw a need for insurance products among older persons and started with teachers and worked that into a much larger association of retired persons. Generally, AARP was created. It was one of those associations that took on a life of its own very quickly. Not the least of one of its activities became extensive lobbying and representation of the senior citizen market. Broadly speaking, there are actually several major subsegments which comprise that.

In the earlier days, AARP programs involved largely indemnity-type health insurance products and small amount life insurance. The endorsement was very important to AARP members. It is a very strong endorsement despite the fact that it was a relatively low dues organization. You might call it something between a cause and an high identifier type of association.

Property/casualty was added and, in the past five or ten years, much more in the way of medical expense coverages have been added, including some experimentation with long-term care and perhaps medical expense coverages.

MR. MARRA: How are senior citizen products changing?

MR. LADLEY: I do not see a lot of change there. There is some change, but it will not have a significant impact. I will just talk about older age people generically, and I won't even define older age here for various reasons.

To simplify, the senior citizen market is really bi-modal. The first mode is the average middle and lower middle socio-economic class which has a fairly modest means, a large portion of the retirees are in that segment and that is the majority. Most of the products that are sold to that segment fill modest protection and savings needs pretty well. They have some very desirable features. For one, they generally don't involve underwriting. They also may not involve an agent -- a positive from both the customer's perspective and also, from the agent's point of view. The incentives for an agent to make a small sale are really not very great because the potential commission is so small, and there are few add-on possibilities. Agents are backing away more and more from that business with few exceptions. So, for those reasons, I do not see it changing much frankly.

The second mode is the upscale market, and there more conventional products and distribution work well. Health insurance needs, including long-term care, are shared across segments and a variety of distribution systems apply.

MR. LADLEY: I'm curious as to what extent you feel there is added risk in many direct response offers, and to what extent, theoretically and practically, that demands additional returns to the insurer?

MR. FAFIAN: Think of all the folks in direct response, like those old numbers that we looked at as acquisition costs, that we always use to price our direct response products with, in the hope of getting a much bigger profit and a much bigger return on investment than we did in our agency products because that is a very big unknown -- who you have out there. And even when Chase, a classic one, started out as being a super account for National Benefit Life, by the time I left, it was, at best, borderline. So, I think the insurance company deserves a high return for taking that added risk on.

MR. PLOSS: I think if the company finds a niche and it can test, it can determine whether or not it can get that high of a return. Most often, it won't get any return at all. It will simply have to write off its testing as just that. Fortunately, when you do find an opportunity, if the list is large enough, you are able to increase your mailings so that you will achieve not only a good return on equity, but also have a significant block of business.

The return on equity of direct response versus agency corresponds to the level of excess competition. Direct response marketing cost risk is similar to the agency risk of successful product development.

MR. FAFIAN: If I could just add one comment using the Chase example, I know after I left National Benefit Life that Chase went to another carrier who was, I'm sure, panting to get something as prestigious as Chase Manhattan Bank. I would be shocked if anybody made money with the traditional products, something like that was described earlier as a whole different approach. Sure you've got a shot, but the people who wanted the term life and wanted the hospital cash -- they are basically important. So the likelihood of the new boy in town going to that list and getting super responses is zero to none, and insurers really haven't been aggressively marketing credit cards since Jimmy Carter's days, compared to what they did prior to that.

MR. MINTON: I would support the idea, obviously, being employed by the insurance company, that the margins should be greater through mass marketing than through an agency system, particularly since we do not do a great deal of business with agents. Just to relay an experience we had recently with a bank, which had around 300,000 credit cards, we did a solicitation for a product which we have had mild success with in other parts of the country. It cost us around $30 each, ballparking at close to $100,000. Anyhow, we did the program and we received responses back, perhaps maybe 100-150 people replied back for it, and that can be very, very disheartening. And obviously, the losses you incur in an operation like that, you have to put back into another product and hopefully, recoup. So it is in many ways like Las Vegas where you roll your dice and hope that the central numbers come in, and when they don't, you have to look around for somewhere else to pick it up. And the responses will vary greatly from one bank to another. In this particular case, the fellow who was managing the credit card operation was the new fellow in town, and he was unfamiliar with the past solicitations and the records weren't kept up-to-date. So the net of it is -- we solicited an insurance product that had been duplicated around three or four months before we rolled ours out. So everyone who is going to buy had already bought, and we are out $100,000. Those things do happen in the business.

MR. PLOSS: Could you compare soliciting bank credit cards with retail organizations?

MR. FAFIAN: At least at National Benefit Life we tried a couple of the department store kind of ventures where, at the risk of sounding like a male chauvinist pig, the wife is apt to have her credit card. The husband never sees the mail-in. We had no real successes with the retail stores. I'm sure somebody must have success because everybody keeps trying it, right? I personally haven't seen it.

MR. MINTON: We have had some successes. As an example, we market insurance where banks have specialty credit cards, as an example, through Firestone Tire. We are on its credit application, and I would think probably of everyone who now gets a credit application through one of the Firestone stores, which as most of us may know, sell appliances and so forth, I would say probably 30% of them are signing up for our credit insurance program.

MR. FAFIAN: Were the successes where the head of household would be apt to be the credit cardholder?

MR. MINTON: Yes. Without question. The head of the household goes in there to buy a tire or to buy a T.V. set or whatever.

MR. FAFIAN: Unfortunately, all our accounts at National Benefit were not with the head-of-household since they were all disastrous.

MR. MINTON: Retail balances tend to be smaller than the credit card balances also. And so, particularly when you are marketing credit insurance, the premiums tend to be appropriately small in a retail environment as opposed to a VISA or Mastercard environment (unless you are going to a Lord & Taylor's or something in that nature).

MR. STEVE P. COOPERSTEIN: I haven't heard much talk about permanent insurance. I've heard talk about saturation. I'm wondering, particularly with Jack, whether the strong marketing orientation of these third party administrators gets them into not only mail order, but follows up with telemarketing and even agent follow-up type of mass marketing campaigns where the target is permanent life insurance as opposed to not necessarily selling it through the mail since there is a saturation using that lead generation to go and sell permanent insurance?

MR. LADLEY: I've seen not very much sale, strangely enough, of permanent insurance within the third party administrator business. That is a problem in a way, but it is also an opportunity for a lot of people I think, in that they haven't done much with that. One would think with the TPAs individual agent's background that in many cases they would be more heavily involved in individual permanent insurance, but in fact they don't seem to be. There are, however, right now, many examples of successful sales of Universal Life and telemarketing of other types of permanent coverages, generally in modest amounts. Also benefits, including IRAs and annuities are being sold direct. Considering that many of the third party administrators are into small businesses that have some means and are paying very substantial health insurance premiums in a lot of cases, I think it is a good, logical market for carriers to be looking at.

MR. LADLEY: Looking at credit cards as a business entity unto themselves, how do you look at the dynamics or the value of having a "credit card business"? Several carriers have been establishing credit cards of their own. How advisable would you say or what factors might be involved in an insurer thinking about establishing a credit card business -- not *selling insurance* through credit cards (at least initially) but just the credit card aspects of it.

MR. FAFIAN: In my own mind, unless they want to be in the credit card business for the sake of being in the credit card business, there is enough credit card things (like the example I gave you in my formal comments of the chap who buys lists of people who buy through credit cards), you can set up a merchant account and use the credit card mechanisms to bill; you can do that on your agency business. One of the things we have talked about at Maine Fidelity but haven't quite gotten off the ground is the deal with one of the problems of payroll deduction business when the employee leaves the job. How do you catch up with him before he owes you so much back money that it is not practical? I've toyed around with the notion of getting a credit card authorization as part of the application. We are now looking into whether or not enough of these folks really have credit cards. All the experts tell me they don't. Somebody has got to have them because the ultimate consumer in payroll seems to be the same multiple consumer you get in direct response business.

MR. MINTON: Actually, in terms of the value of owning a credit card operation, I would think historically there has been no better time than today (banks typically are marketing their loans through credit cards at 18%, 19%, 20% and 21%). Cost of funds ranges around 8%. I mean the margins are absolutely fantastic. Also, in regard to doing a response to marketplace soliciting new credit cards with pre-approved lines of credit, typically a bank today will get maybe 2-2+% response rate, and each one of those customers are charging $25 or $30. So just in terms of acquisition alone, it costs maybe $30 to solicit 100 people, and you are going to get $50 in fees back just like that. It is a pretty darn good business. The problem I would say with getting into this immediately now is that there is an immense amount of consumerism pressure building up against the marketers of credit cards to reduce the rates. As an example, there is a small bank in Arkansas right now that started marketing VISA cards several months ago at 12%, and I think they are bringing in around 20,000 new cards a month unsolicited. Recently, it was the general thought that the elasticities of demand for interest rates on credit cards was fairly vertical. But recently Manufacturers Hanover reduced its credit card interest rate 2% to 16%, and it is overwhelmed with the responses of people who are leaving their current card where they are being charged 18 and 19% and taking out a Manny Hanny card. I suspect in the very near future that credit card rates could come tumbling down both from a consumers' pressure prospective, competition prospective as well as from a regulatory point of view.

MR. PLOSS: Frank, would you recommend you go with a VISA card or start your own? I noticed only the big guys, Citicorp started their new card CHOICE, and Sears recently started Discover; it would seem difficult to compete with that league.

MR. MINTON: Absolutely. You are far better off getting a VISA. All the banks have VISA or Mastercard franchises and to my mind, in terms of the banks anyhow, Citibank is the only one who has a viable credit card program going on now both through CHOICE and through, to some extent, Carte Blanche.

MR. PLOSS: Any thoughts about building your own list through buying lists and combining them or starting your own little association with some kind of benefits, like a travel association? Would anybody comment on that?

MR. FAFIAN: If you look at an awful lot of the successes that come from that kind of mechanism, for some reason we seem to see the home office thought process being quite different than the entrepreneur in the field. We had one direct response operation that had nothing to do with credit cards at National Benefit where these fellows brought lists of students, and they mailed twice a year, just before Labor Day and some time after Christmas, and were super successful. It was just term life on the kid. And again, the office has got to be the biggest success I would think in terms of sheer size.

MR. MINTON: But then again, it is becoming increasingly more difficult to make money in the direct response business, and if you don't have a supporting organization where there is already a built-in customer affinity such as through a bank to its customers, you can really expect to have typically very small, very disappointing sales performances and penetrations.

MR. LADLEY: There are many very good people that know how to get lists, how to get them cheaply, and how to evaluate their quality. You are competing against a lot of them in many cases (not all) when you try to do direct response on a fairly large scale. The best successes are examples I've seen where people have put together units of small lists and made them into a previously non-existent large list. And also where they have combined, as I might have alluded to, some sort of membership services along with some of the other things that they are doing which is a way of initially adding value to the organizations. Very few of the significant insurers in the direct market are very interested in other than a large list; many of them have fairly substantial minimums of 100,000 customers and up. I think that is an opportunity area.

MR. OWEN J. GARFIELD: We are all talking about introducing a fourth party into the traditional insurance arrangement -- some sort of premium collection/ claim paying agent. In regard to this question of using names that you generate from one source, who owns those names? Who owns the process? What kind of contract do you have? Is the contract between the TPA and the insurance company? If you have a bank arrangement, who owns that list of names that is coming out of the bank? Does the bank continue to hold that ownership or does the insurance company have it after it uses it? What is going on?

MR. MINTON: That is really a highly debatable issue, particularly when the insurance company has spent money to gather the business and they have their insureds, for the bank to say that the insureds are its customers and not the insurance company's and the bank has the right in essence to give those insureds over to another insurance company. That does happen in the business. I think the contract defines who owns the list. The contract with the insurance company and the bank is established before the solicitations are done. Typically, the way most insurance companies have set it up is that they will have a right to the list for a period of 2, 3, or 4 years or whatever, and by that time, hopefully, they will not only recoup their costs, but will have made somewhat of a modest profit; then the bank can go out and sell them again to someone else if they want. There is a lot of horse trading going on in the field as it relates to who owns lists.

MR. LADLEY: In the case of third party administrators -- generally, the TPA owns, and if they don't own, they control, all the means of getting at the list, and that might include the insured people, the non-insured people, agents and any other person you might conceive of as involved there. However, if the TPAs themselves are owned or have some other form of very close relationship with an insurer, then the insurer effectively owns the lists. This is probably a happier situation for the insurer. In many cases even in an insurer who has "captive agents," the agency force has a position that it owns the insurer's customers, including orphan policyholders and other categories, paid up policies, every kind of thing. I am not sure anybody has guaranteed control if there is a fairly strong distribution network out there. Again, it has got to be negotiated at the front end of any arrangement. That is a very important point, Owen, about negotiating and setting up contracts that define ownership, depending on your objectives.

MR. FAFIAN: In my experience the list is the bank's or whoever has created the list, not the insurance company's.

MR. LADLEY: I should have also mentioned the impact of a fifth party. City and county organizations have an awful lot to say about mailbox management and a lot of other things concerning how members are solicited. So that is very important and has to be considered as well.