**RECORD OF SOCIETY OF ACTUARIES
1986 VOL. 12 NO. 3**

REGULATION OF FINANCIAL SERVICES IN THE UNITED STATES AND CANADA

Moderator: DANIEL J. KUNESH
Panelists: DONALD KURZ*
JOHN C. SWEENEY**
Recorder: STEVE BADER

o This panel will discuss the regulatory environment for banking and insurance, the crossover opportunities and the various types of sales distribution alternatives. Consideration also will be given to the obstacles in such a relationship, including corporate culture and the various risks involved for both the bank and the insurance company.

MR. DANIEL J. KUNESH: The focus of this presentation will be on the regulatory environment for the banking and insurance industries. We will also be discussing crossover opportunities of products and services of these two industries as well as various types of sales and distribution alternatives. Our two panelists will give consideration to the obstacles in such a relationship, including corporate culture, industry culture, and the various risks involved for banking and insurance companies embarking on a program to sell each others' products.

MR. DONALD KURZ: I am going to be focusing on strategy, marketing issues and the implementing and planning insurance diversification efforts for banks.

* Mr. Kurz, not a member of the Society, is Managing Consultant with Cresap, McCormick and Paget in Los Angeles, California.

** Mr. Sweeney, not a member of the Society, is a consultant with Tillinghast/TPF&C in Atlanta, Georgia.

Our firm has done quite a bit of what we call leading edge work in this area, and I will try to flavor my comments with specific examples to give them some credibility and make them come to life.

Banks see an opportunity for the marketing of insurance. It has been an elusive opportunity for banks, and most of my comments are going to be from the perspective of a banking organization to give you an idea of the challenge in trying to successfully implement a program with banks. It is a major opportunity, yet it is an opportunity that heretofore has not been seized with the degree of success that most banks had anticipated when they started planning these programs.

This talk has five major sections. First we will discuss the overall challenge in the market place and some of its key issues including regulations. We will discuss some of the requirements for being successful in these types of programs. We will then go into the strategic alternatives. How can you enter these programs? We will then focus on the specific tasks involved in the planning, design and implementation of such programs along with our work plan for success.

First and foremost what we do with banks is tell them, "This is a major opportunity area." Banks rushed into the discount brokerage business, a market segment believed to have about 5 billion dollars in total revenue potential. Insurance is a business as large as banking, and when a Citicorp looks at it or a major money center bank looks at it, it says, "We cannot find another business that has as big an opportunity for us." It is not an easy opportunity, but it is huge. When banks start to look at their diversification planning activities and realize that their main business is under a lot of competitive pressure, insurance pops out as probably unique due to its size. Therefore, it makes sense for us to explore it in greater detail. The securities business, by contrast, has received a lot of press. This area, including investment banking, mergers, corporate finance and retail securities, is 30 billion dollars in total revenue potential. So just in order of magnitude, insurance becomes quite an attractive segment to be looking at if you are a bank.

Looking at the major components, the lesson we learn is that each segment of the business is quite attractive. It is not just one segment. All major components have large revenue potential. Of the different requirements for success, each has different opportunities for the individual institution. However, when we look at the different elements, we see there is a lot of dollars in each of the major segments. Most of the activity to date has been in the retail property and casualty and life segments. The assumption is that these markets are relatively under served. Accordingly, the current players are more vulnerable than the commercial side because of higher cost distribution systems. An important message in planning is not to get too caught up with regulatory issues. A lot can be done in spite of the regulations because, as we know them, regulations lag behind reality.

We now have a program in place to test these alternatives. For example, there is plenty of direct mail activity going on in the life and accident and health areas. There are programs which involve independent agencies, insurance company representatives, telemarketing, and so forth. In spite of what we call regulations, there is a lot happening right now. There is no right answer as to which program is most effective. Many things are being tested. As far as we know, nobody has the solution, the most effective answer if you will, to a successful program. But many alternatives are being tested, and regulations don't seem to be adversely impacting the programs. The primary roadblocks appear to be implementation and execution, not regulations.

When banks seek entry, they have three fundamental alternatives. First, they can acquire a company, an agency, or a reinsurer. Unfortunately, this is forbidden for most commercial banking institutions. Second, they can build a company, agency or reinsurance organization from scratch. Again, for the most part, this is forbidden by regulations. Third, they can enter through a joint venture. This is the way most programs are going today, other than the 16 or so grandfathered commercial banks and the thrift organizations which are subject to a different regulatory environment wherein they can actually sell products themselves.

The message here is that joint venture programs probably represent the most effective and smartest alternative for a bank. A joint venture allows a bank to take advantage of the expertise of an insurance company. Right now, it minimizes start up costs and the overall risk to the institution. So, forgetting regulations, this is the way we would counsel organizations to get into the business. They shouldn't go out and start acquiring or building firms. They have to get in with a partner that they are very comfortable with.

Why is all this activity happening? From the bank's perspective we have seen five forces driving this action. First, and foremost perhaps, is the search for fee income. Banks as you know have come under real pressure in their main business of lending and the net interest margins that lending has. Fee income is not asset intensive. Accordingly, it can have an unusual impact on the return on assets and return on equity measures, measures which are carefully reviewed by Wall Street. Anything that creates fee income is attractive. Joint ventures generally create fee income without substantial asset accumulation. Therefore, they comprise a very effective enhancement to the bottom line.

Second, banks want to strengthen their current customer relationships. The theory is that if you can increase the number of products you offer to an individual customer, you increase the likelihood that they will remain loyal to your institution, and accordingly you become less vulnerable to competitors.

Third, banks want to attract new customers. It is still fairly novel for a bank to be offering life and property and casualty insurance products. Accordingly, joint ventures can give them a competitive advantage, particularly with the customer who looks for one stop shopping convenience.

Fourth, banks are responding to competitors. More and more banks are starting to get into the insurance business. Some are even looking at it as a defensive measure. They are saying, "If we don't get in soon, we are going to be at a competitive disadvantage."

And finally banks are positioning themselves for deregulation. As I said before, regulation tends to lag behind reality. If banks wait for formal regulations to drop, they are going to be at a disadvantage if they haven't started their planning and implementation activities.

From the insurance company's perspective, we see four fundamental forces driving joint venture activity. First, insurance companies are looking to develop more efficient distribution systems. Traditional means of delivery, as we all know, are very costly and cannot be sustained for many products. Therefore the thought of having captive "hot leads" from a bank and working with a bank partner is very attractive to an insurance company. The goal is to spend less time prospecting and more time selling. The theory is that a bank list and a bank program can do this for you.

Second, insurance companies want to gain sponsored access to new customers. Banks have generally what is considered a higher affinity level than an insurance company. Bank endorsement of a program, which can be made directly or indirectly depending on local regulations, is an attractive element to an insurance company which more or less might have relied on cold calling in the past.

Third, insurance companies want to segment the market effectively. Banks, particularly larger banks with good customer information files, have a lot of information about products and customer behavior. Good market segmentation measuring customers' buying habits, their income levels, and other demographics will permit an effective program to target new customers with different types of products focused at customer needs rather than going out after old customers with traditional products.

Finally, joint ventures with banks will help insurance companies meet competitor challenges. It is reasonably obvious that the banking industry over time will be allowed to get into the insurance business. The more progressive insurance companies understand this, and they are pursuing joint ventures because they realize that banks are soon going to be on the new competitive playing field. Rather than fight it, they want to participate in it.

Despite these grand opportunities, we are seeing disappointing results from many of the programs to date. We have listed a couple of the possible reasons. First, there has been an inappropriate product distribution and customer fit. There are several variables that you have to look at. For one, you must determine which product is appropriate for which channel and customer segment.

Many programs have not rationalized this and accordingly have had one element of this linkage out of sync.

Second, there has been a lack of proper customer segmentation. We have seen universal life being mass mailed to credit card holders, for example, and those programs have not done well. Why? What sense does it make for customers, who have very little affinity through a credit card, to buy a shelf universal life product when they can get it through their normal channel? Ineffective segmentation of this type has been a key reason why problems have occurred to date.

There is over-reliance on customer affinity. While customer affinity is helpful and is a good start to an effective program, it is certainly not the answer. Just sticking an insurance agent in a bank branch is not the answer to selling a lot of insurance. However, that is exactly what certain programs have done. The Bank of America program, for example, has used insurance agents with shelf products in different branches around California and the program has not been very effective. Why? Because merely placing an agent in a branch does not give a customer a reason to change his buying habits. You must give him more motivation.

There is a lack of bank commitment at the first sign of a problem, such as deposit cannibalization, or a lawsuit by an insurance agent or an independent agent association. At the first sign of trouble, banks have often derailed the program and have abandoned their commitment. They must stay in the program, be committed to it, and spend the dollars that are required to succeed over the long haul. They cannot run at the first sign of a problem.

We have seen some conflict with existing bank activity. When you have an agent superimposed in a branch trying to sell insurance, there is a real danger that you are going to go against the bank's existing work flow by asking somebody to make a referral, by asking somebody to help sell a product. Banks must think through how insurance selling activities are going to mesh with existing branch activities.

Finally, the insurance companies have offered poor compensation structures. They must recognize that a bank is going to abandon its commitment as soon as it sees red ink. If you don't structure the program to allow for some kind of return relatively early in the program, there are going to be problems because the bank is going to run.

Another compensation issue relates to the fact that bank branch personnel who are involved in the program must be motivated to "push" insurance products. A compensation program which is "balance" oriented and which penalizes personnel if bank customers use their balances to pay for insurance premiums creates substantial disincentives to sell insurance. We have seen a lot of contradiction in the message that bank management has been giving its personnel.

In summary, to meet the market place challenge effectively, you must look at a couple of specific issues. First, you must find the specific opportunity areas. That is, which product category, customer segments and distribution methods are most appropriate for your institution? Indeed you must take a good hard rational look at which specific opportunity makes the most sense for your institution.

Learn from the problems encountered by early market entrants. Look at the way you are planning programs. If prior programs have not succeeded, analyze why they haven't succeeded. You have got a wealth of information out there from programs that have had problems. Study why they have had problems.

Enter markets strategically and don't simply react to the unsolicited joint venture proposal. This is a key point. A lot of deals have been entered into between banks and insurance companies on the golf course between chairmen of different firms. That is not the way to enter a program. Both the bank and the insurance company must look specifically at what they are trying to get out of a program. They have to look at what they are particularly good at and then go out and select the company which best fits their criteria for making a program work. It is not simply reacting to whomever comes to them or the kind of deal they can cut. It has been our experience that banks which react to an independent insurance agency's unsolicited proposal end up with a program which does not work at all.

I have listed some of the basic requirements for being successful in joint ventures between a bank and an insurance company. First, have a clear understanding of the program's objective, both short and long term. It is an obvious point, but a point that is violated quite a bit. What are we trying to do in these programs? If you are a bank, are you trying to solidify your customer relationships? Is that your primary goal or is your primary goal to increase short term earnings? Understand that and plan the program accordingly. Whatever your objective is, find it, understand it and then let that guide the program.

A bank must make a commitment to a long term program. Some of the problems encountered early on in a program must be ironed out. Everybody must have a long term perspective. Go into partnership with a company that you will be comfortable with over a 5 to 10 year period. We have seen too many programs stop after a year or two. You can't tell if a program is successful in that short period of time.

Next, carefully plan your contractual agreements. Allow for such things as further deregulation. Be flexible in your planning and get involved with a joint venture partner you can live with.

Effective customer segmentation in target marketing is a truism in any type of program. Find out which customers make sense for which products and hit them with a distribution channel that is both economical and comfortable for the customer.

Choose the distribution system appropriate to the product. Match the complexity of the product with its service and profit requirements and out will come your distribution system that is most appropriate. You can't sell, or at least to date you have not been able to sell, very complex products through the mail or through telemarketing. Should that be retried? Can it be improved? What are the economics of the different products? What are the strengths of your current distribution channels? What are the strengths of the bank as it exists? Is it a technology oriented bank? Is it a branch oriented bank? Understand all these things before designing a distribution system because the fundamental premise is that distribution is the way banks can come in and add value to this business.

Design an innovative, competitive product. Our feeling is that shelf products are a "no go" in this type of a joint venture. Using plain vanilla products that are available through the insurance agent or directly from the insurance company right now should not be sold through a bank. There is no compelling reason for a customer to switch his buying behavior after years of dealing with an insurance company directly and getting the same product. True, the bank product might be lower priced. It might have a product feature like a CD as part of the cash value component in a universal life product, something that makes it unique to the bank. However, you must make a customer want to switch his existing behavior. A shelf product is not going to do that.

Design a program that is complimentary to the existing bank product lines. Make it make sense to the customer. Remember, the customer will still view the organization as a bank. The more you make the transition logical for the customer, the easier the sale is going to be. If a customer is used to dealing with a customer service representative in a branch, then make that representative's work flow fit with the sale of insurance. Don't let it flow against the channel. Design products that make sense to the customer because you are a bank. Use automatic checking account deductions. Invest the cash value in bank oriented investment products. Such things make it easy for the customer to make the transition.

Streamline products and procedures. Banks are poor sellers, and they are poor administrators. If you design a complex program, you will kill it even before it has a chance to start. Banks have limited capacity to sell. They have limited capacity to add additional products. You must make it as simple and turnkey as possible and take as much responsibility away from them as possible. If you rely on their staff too much, you are going to have a lot of problems. They have nowhere near the selling capacity of an insurance company.

Finally, build on the bank's strengths such as high customer affinity. Again, that is not enough to close the sale, but it is an important element in prospecting. Have the bank use its name in telemarketing. Have the bank president or a senior executive sign direct mail letters. Make sure that the customer knows the bank is directly endorsing the program. That means a lot to a number of customers out there.

Point of sale access is another strength. This is critical, and it is something that many of the programs have not taken advantage of. When you are closing a mortgage loan, sell the customer mortgage insurance. When you are closing an auto loan, sell the customer auto insurance. Don't wait three weeks because by the customer has already made a decision. Use the information on lapse dates and policy renewal dates. Sell them at that time. Don't make the sale wait. We have seen time and time again that banks haven't taken advantage of this. The trust department is in a perfect position to sell complex life products when updating wills, and so on. There has been little linkage to date in those types of programs.

You need to provide strong marketing and sales support, to emphasize the point made before. Banks don't have exceptionally good marketing and selling capabilities. You must support them extensively, no matter who is doing the actual sales closing. You must train the staff and prepare all sales literature. Indeed, you must take responsibility for the overall selling process.

And finally create a link between program goals and bank personnel performance measures. Make sure that everybody has enough incentive to make a program work. We audited a program for a New York money center bank and were asked to come in and determine why this program hadn't worked effectively. In doing some focus groups with branch managers because it was an in-branch program, we found that the compensation system, the overall way that the branch managers were motivated, was totally contradictory to the success of this program. They were motivated by deposits. They were motivated by sales through their own employees, yet they had an outside insurance agent there. They weren't getting direct fee revenue from the rental of their space. Everything that was in the branch manager's best interest was not in the insurance company's interest. You wonder why the program failed? They might have had the best products and everything else, but the program never had a chance.

When entering the business, a bank and an insurance company looking at selling through banks must make three fundamental choices. First, which customer segments are you targeting, including ways of looking at bank segments, deposit based credit cards, mortgage customers, installment lending, and so on. Second, what product categories are you going to be focusing on and finally, what distribution channels? There is no right or wrong answer as to which strategic alternative is most appropriate. It is going to depend on the characteristics of your customers and the bank's customers, your distribution capabilities, and the specific products you have that have been particularly competitive. There is no formula answer. These are the fundamental choices that you have.

There are a number of steps that we recommend in developing a strategy. First, conduct an internal assessment of the bank. What are its specific objectives? Believe it or not, most banks do not know why they are getting into the business. It has just been something that seems to be a good idea. We make them define what they are trying to get out of the program. What are their unique capabilities and unique strengths to make this type of program work?

Next, *determine the customer's insurance needs and buying preferences.* Understand the customer. How does he buy insurance right now? Is he satisfied? What opportunities might there be in the local market place that are not being well met by the current delivery systems.

Profile the insurance market place. Where are the dollars in the bank's market? Where are the major opportunity areas for the bank?

Analyze existing bank insurance programs. We think this is critical. There is so much to learn from programs that have not been successful. Did the bank pick up on that? Go and interview the people that have been part of prior programs. Understand why they haven't worked. What would they do differently? Then design your own program.

Assess the unique requirements for success in a local market with the local institution.

Finally, develop alternative strategies that have high potential for success. Based on the requirements for success, there might be three or four alternative ways that you might favor. Then evaluate these strategies relative to the bank's objectives and capabilities in relation to those of the insurance company. Consider the unique success requirements for that market place and projected financial results. Then select the preferred alternative. These are the fundamental steps that we suggest you take when entering into a partnership with a bank or insurance company.

Implementation is basically what it is all about. From the bank's perspective we suggest these steps be taken. First, develop a detailed specification document to select the joint venture partner. Outline exactly the types of products you are looking for, the way you want them priced, the way you feel they should be delivered, and so on. Identify which insurance companies might be uniquely qualified to satisfy those requirements. Go out with a formal request for a proposal. Actively solicit appropriate organizations. Make them respond to you and tell you exactly how they would work the program. Identify, evaluate and select the potential partners on the basis of those responses to your inquiry.

Then develop a detailed promotional and marketing implementation plan in conjunction with that organization. We usually set up a task force between the insurance company and the bank to jointly work up an effective sales, marketing and promotional program.

Complete the implementation tests. We try to set up some kind of a scientific test market to look at perhaps two or three different alternative strategies, or two or three different distribution channels before we make a major commitment to a bank's program. A test market will allow you to invest smaller sums of money initially and not alienate a lot of people in the different organizations while you fine tune the test. Then introduce the program and monitor it.

To summarize the implementation tests, there is the internal assessment of the different organizations. What are their unique strengths? What is happening in the market place? Where are the opportunities? Those things combined will give you the unique success factors in that market place. Then select a preferred strategic alternative based on an evaluation of the different ways you can go. Develop the specifications for the joint venture partner, then select the partner. Develop a detailed marketing and promotional plan. Complete the test market and then finally introduce the program and monitor it on an ongoing basis.

Those are the steps that we have gone through with clients over the past year or so in launching a couple of programs. One or two of them have already started up and are running and have been reasonably successful to date. We believe there is still a huge opportunity out there in the market place. We don't think many organizations have found the right formula. However, that is not a suggestion that they should stop looking. Good careful study without rushing into the program will yield some very favorable results.

MR. JOHN C. SWEENEY: If you have been reading the trade press at all recently, you will have come across quotes like this: "The banks have the potential to put a stranglehold on a very wide range of financial services." "We are in a poker game with the banks where we feel the need to be preemptive." "I am not too concerned about other insurers, but the banks could quickly undermine us, if they could only organize their customer base." "Insurers view us as enemies, but we would like to see them as partners." The interesting thing about those four quotes is that you could have read them in the *National Underwriter, Wall Street Journal* or whatever, but they come from European bankers and insurance managers.

The problems that have existed in this connection, this nexus between banking and insurance, have been going on for some time in the European and Australian markets. We were asked to talk about regulation in the United States and Canada. I lump Canada and the United States together and say that the regulations are essentially the same. They are not deregulated yet. They are still controlled. There is something unique to be said about the U.S. and Canada, but there is something also unique about the European and Australian situation in that it is a microcosm for what can go on, and what probably will go on, in three to five years from now in the U.S. So you have a place to look to, if you can get the information on it, to track what is happening and where they are going.

My theme is basically banking and insurance and a view from abroad. Don gave a great overview of the situation. I will try to get you down into the gutter a little bit more and give you some of the nuts and bolts and how you slug it out in the trenches.

This is the one piece of wisdom that you will go away with from my presentation, viewed from either the insurance perspective or the banking perspective. This is the overview of it: "Incredible opportunities." I think it is appropriate.

This is the way I think insurance people and bankers see it when they first approach the topic. The problem is that no one has been able to run up the mountain and make a success of it.

A major point and a pivotal point in the presentation is deregulation, and in this particular case I'm talking about bank deregulation. The deregulation of the banks has intensified pressures on spread margins. For those of you who don't know what a spread margin is, it's the difference between bringing in deposits and making loans. The bank basically tries to earn a positive spread, and that's how it makes its profit. Deregulation has increased the pressure on its spread margins, reduced them considerably and accelerated the trend to fee income that Don has already alluded to. That's the primary focus, from a bank's perspective, on why it wants to diversify. The way it does it is by seeking more stable fee income. Incidentally as the interest rates and inflation interest rates have come down, the fee income still hasn't fallen onto the back burner, but the idea of making a spread has become a little easier for the banks.

The banks have, however, gravitated to a strategy that includes four components, some of which they can do and some of which they can't right now. And there are elusive ways in running around the regulations to get to them. Insurance is the primary focus, in my belief at any rate. Banks would like to get in and earn fee income on insurance.

They've all tried brokerage, or I should say a massive group of them have tried brokerage, and they found it unappealing. They haven't been able to make a profit in it yet. And I think Don has already alluded to some of the reasons why.

Investment management is a normal activity for a bank in the trust division as well as in its own operational investment activities. Banks are trying to offer this as a fee service now. You'll see more of the private banking and the fee for service type of activities that a lot of the insurance agents are trying to sell going on in the bank.

The final on mutual funds is that because of the Glass-Steigel Act, banks are not really allowed to do that. But there has been some lessening in the power of that particular piece of legislation. As I understand it right now, with some skirting of the laws, there has been some movement in that particular direction. So you'll see banks moving in that area trying to sell their mutual funds. These are the four sources of fee income that you'll see banks gravitating to over the next couple of years.

Why are insurance services the primary focus of a bank? Don's already alluded to a number of them. Banks can provide multiple services to a target market. Australia has taken to the idea of life cycle marketing, and it has managed to combine the life cycle marketing relationship with multiple services. In fact a couple of Australian banks package products using a life cycle strategy. They start out with the young, up and coming married couples, the middle class achiever as it were, and the Yuppie group of course, and then finally the retirees, and there is probably one more in between. They package the various types of bank products with insurance products so that they actually stratify and segment the market and put these things together. When you buy the bank's package of services, you knowingly or unknowingly buy the insurance package as well. It's an interesting way to approach it. While it's illegal here, you'll find that with deregulation or no regulation, some interesting things may happen. The Australians have been fairly successful at it.

The Australians can spread the basic distribution cost. What we're really talking about here is by having "the bricks and mortar in place" with their extensive branch network, the more products they can push through the system out there, the more money they make, the more they spread the distribution cost and pull in a better return on their assets.

Capturing more discretionary spending and saving is basically what they are in the market to do. They see universal life, term products, annuities and so forth as being a way for them to capture some of the savings and, of course, some of the necessary spending on the property and casualty side.

All of you are in the life industry, at least I believe you are, but P&C is viewed as a necessary commodity and banks are skilled at selling commodities. So I'll include in my presentation references to the P&C insurance area. It's a no-brainer for a bank. It sells P&C the way it sells bank services. Somebody happens to walk in the door, sit down at a desk and asks for it. That's the most elaborate concept of marketing in a bank, not quite what we're used to in the insurance industry.

Entering into home banking in the electronic store may sound a little flukey and maybe even flaky, but if you're on Compuserve or a home electronic system, you'll find that you can buy insurance directly from a number of insurance carriers. You can also do your banking from more banks than you can buy insurance from insurance companies. The banks have caught on to this in a big way. A little later on, I'll tell you about probably the leading country in home banking and electronic purchasing, and I think you'll be surprised to find out which one it is.

What is the scope of banks in the insurance market place? With the exception of the New York City money center banks which have some things going on in the insurance area, the real movement in insurance right now is in the regional banks. The larger regional banks (in the $1.5-2.0 billion asset range on up) have a client base somewhere in the vicinity of 200,000 customers. If the bank manages to penetrate just 20% of its client base, the net result on an annual basis is that it can get $2 million in P&C commissions without even trying. If it hires some really talented young bankers and makes them into insurance agents, it will get $14 million in life insurance commissions each year. Now there's obviously a fallacious element to this line of reasoning. It is that you cannot make a bright young banker into an aggressive insurance agent.

In fact, I think it is impossible to make a bright young banker into anything aggressive.

What does the customer want from the financial services industry? A number of surveys have been done and I am quoting a Stamford Research Institute study of about 2 or 3 years ago. When it asked the question, "What's the customer looking for in the financial service industry?", the answer was "expert and trusted advice."

I see that the government is trying to regulate the financial planners and with some degree of success. Probably it has a right to do that. From the same survey, this is what the customer said he thinks he gets from the various purveyors and providers of financial services. From the banker he gets trusted but not expert advice. From the stockbroker he feels he gets expert but not trusted advice. From the insurance agent he feels he gets neither. So if you are a banker looking at this sort of survey and realizing that in the view of the consumer that you have integrity and they have trust in you, then the opportunity is to go after the stockbroker's business and the insurance agent's business and the insurance agent in particular is quite obvious. I think these are some of the motivations behind why the banks are moving in that direction.

Australia, in particular, is a microcosm of where we'll be in 2 to 3 years, maybe 5 years. I am making my subtle forecast of deregulation of the banking and insurance industry in the U.S. The reason why I choose Australia is I spent some time down there in September and October of 1985. Australia is about a year or two into deregulation. In fact, the week that I was there, the Australian Mutual National AMP, the largest life insurance company in Australia joined forces with a bank, and they decided to call themselves CHAMP. That was their acronym, CHAMP, AMP being Australian Mutual, the CH was Chase Manhattan. An American bank moved into Australia and teamed up with the largest Australian insurance company. It's a powerful force. It owns 50% of the market and it's going to try to provide banking and insurance services through both media, through the bank as well as through the insurance company. And its got a real tie on the market.

A week later, interestingly enough, the National Mutual Life Insurance Company, the second largest insurance company in Australia, owning 30% of the life insurance business in Australia, joined up with Royal Bank of Canada. You note the lack of Australian banks in it. I was down there to put together an Australian bank strategy for entering the insurance industry. I think Australia is headed in a direction that will basically replicate, probably in the next year or two, because it had some regulations that were done away with and now it is in the process of joining banking and insurance. So I think if you can keep your eye on it, and it's difficult to do because the information is skimpy, you'll see the way we'll probably progress.

I've just spent some time over in France. A very major insurance company in that country is owned by a major bank. Three of the top 10 banks in the world are French banks. Some of the larger French banks, as well as some smaller ones, all own insurance companies and provide insurance services to their customers as though they were common every day banking products.

Spain has a unique situation in that tie-in sales, which are illegal here, are legal in Spain. When I was running an insurance operation in a bank in North Carolina, I was sued by the entire life insurance agency force in North Carolina for promoting tie-in sales, taken to court, and we won. It was thrown out on procedural reasons. We were taken to the legislature over the same issue, tie-in sales. By way of definition, tie-in sales result when we "twisted the client's arm" so that, whenever we make him a loan, we make sure he also buys insurance. In Spain, banks do that. In fact, it's totally legal. Tie-in sales are the norm there. If you go to a bank in Spain and you want an automobile and take a loan out, the bank immediately makes you collateralize the car with its property insurance, and it will also collateralize your life as well with a life insurance policy. It's standard business practice.

Interestingly enough, Spain is the country that I would suggest is probably the most developed in electronic banking and home banking. Ninety-nine percent of all adult Spaniards have checking accounts, a figure that is no where near replicated here in the U.S. From 60-70% of all bills are paid directly through wire transfer. You never write a check. It's basically a checkless society in Spain. About 80-90% of all adults get paid directly through wire transfers into their account. Banco De Santander, a bank we've never heard of but which is well known in Central and South America, is probably the leader in home banking. It is giving free computers away to its clients to use to get into its system, and it's providing services that no one here in the U.S. has even seen. So I suggest that if you watch these developments, you'll see the direction in which marketing techniques may move in the U.S.

And in the United Kingdom, a final note. The U.K. has been doing banking and insurance for about 20 or 30 years, and it has been doing it in a splendid English fashion. It's failed utterly. The best bank over there, Lloyds Bank, owns a company called Black Horse Life, and it has never let Black Horse Life penetrate its customer base in the last 20 years. Lloyds was afraid the agents would upset the relationship with the bank. Therefore, it wouldn't let them use this relationship. That's the sort of English mentality that still exists.

However, if you were to ask for a demonstrable case of the success between banking and insurance, meshing the two together, it would also be in England. Typical of the English, a bank by the name of Trustee Savings Bank (which we've never heard of, it's a regional bank over there) raised the average production of its agents. It has an agency force of about 450 men covering the entire island. Very much like here, the average production for a typical agent is one policy per week. Trustee Savings raised that up to 17 policies per week per man. It's an incredible increase in productivity.

The four major considerations that we're going to be looking at here will be regulatory considerations, methods of bank entry into insurance, insurance operations within a bank, and some marketing ideas on insurance. Keep in mind again, I want to make this fairly eclectic. What I'm saying here is going to be somewhat specific to the U.S., but it's basically the way we're working throughout the world. There is really no difference.

I'm going to go through some of the regulatory aspects, since the theme is regulation, to give you an idea of what's been happening in the U.S. and why we're having some problems. The 1956 Bank Holding Company Act basically prohibited a bank holding company from providing general insurance agency services. But the statute contained certain exemptions. In a town of 5,000 people or less, the bank could provide insurance. If you had $50 million in assets or less, you could provide insurance services. There were certain very large institutions, most of them in the mid-west, which were selling insurance, and they had a special exemption. They became the grandfathered banks later on.

In 1982 Garn-St. Germain affirmed the 1956 bank holding regulations with exemption "G" for the grandfathered companies.

You generally don't know if you ask what a grandfathered bank is. In fact, when I go into the various banks that are interested in doing insurance, they all tell me they're grandfathered. And I now have a list so I know which ones I'm talking to and whether or not they know whether they're grandfathered. Basically they're regional banks. Some of them are fair sized banks. You won't see any major money center banks on the list.

First Bank System in Minneapolis is I believe the 7th or 8th largest bank in the country. It has in the vicinity of $30 billion in assets. It is also the 7th leading insurance brokerage firm in the country. It is primarily property and casualty oriented. It is 90% P&C and 10% life. It is a major success story, but it's an exception. It's not one that I would point to and say this is the way you should do banking and insurance, and for one reason. The insurance operation developed independent of the bank. It just happened to have an insurance agency that went out and bought other agencies and had no relationship to what was going on with the bank. It is trying to pull it together today and make it even more successful. Basically First Bank System runs five states in the upper mid-west, and it controls the insurance operation on the P&C side, mainly in the commercial area, coincidentally.

First Wisconsin is moving very rapidly. Norwest has also got a big operation. The rest of them are nascent right now. Basically you would find that insurance operations in most of the banks are in a state of desuetude. They have all the mechanical operations in place, but they're cobwebbed. Nothing has been used in 60 years, so getting this started again is an opportunity for people like myself. However, it's not an easy opportunity.

When you get into the regulation of banks, there are two levels of regulation. If you are a nationally chartered bank, you're run by the Federal Reserve and the Treasury Department and they basically charter you. As a result you've got to live under their particular rules and regulations, including the Bank Holding Company Act.

If you're a state chartered bank, which most of the 14,500 banks in the country are, you aren't totally controlled by the national regulations, but you do have state regulators, state banking commissions and you have to live by their regulations. So if you're a state chartered bank, and you don't have N.A. after your name, you can do some different things. I happened to work for a state charter bank, and that's why they thought they were grandfathered. And if you ask the chairman of my bank that I worked for why we were doing insurance, he'd tell you they were grandfathered. They weren't grandfathered; they were a state chartered bank. The state of North Carolina was one of the states that had no prohibitions about state banks selling insurance.

Twenty states ban the sale of insurance right now. This is a very dynamic number because it changes from year to year. Thirty banks have no regulation. They don't affirm the idea of selling insurance through banks, they just don't say anything about it. North Carolina was one of those particular states. So you have to find out when you get into banking with a state organization, whether the state permits it.

We've already heard from Don about the methods of entry into insurance, so I'll just run through it quickly.

You can rent space for an agent in the lobby. So far you've seen a number of these types of programs, and they're failing utterly.

You can buy an agency. Again this is a less popular approach than buying an insurance company. It's a difficult approach and I'll get into that a little bit later on. Incidentally, of the thirty states that allow insurance, about 1,000 state banks are active in insurance in one way or another. However, this involvement is minimal, and you probably wouldn't even know that they're involved in it. They buy a little agency in the town that they're located in.

So there are probably somewhere in the vicinity of 1,000 agencies around the country that belong to state chartered banks.

You can invest in a third party marketing organization. These things have cropped up all over the country. They're growing in acceptance, and they may well be a good approach. This will be a joint venture approach with buy out arrangements later on when deregulation is assumed to occur. The third party sets up the organization, hires the agents, sets up the entire insurance operation and gives the bank the option to buy them out if and when deregulation comes along.

You can buy an insurance company. Nobody has done that to date with the exception of Citibank and which has done that in Europe. In fact, in every country I visited in the last 4 or 5 months, it seems like Citibank was in there buying an insurance company.

You can be bought by an insurance company. That's an interesting approach. There are some examples but these are minor right now.

The final approach is do it yourself. Start up an agency or start up an insurance company. A number of banks have started up agencies. I know of no company in the U.S. that's starting up an insurance company as such, but that is happening elsewhere in the world.

In discussing bank strategies and insurance, you've got two ways of approaching the insurance issue. You can produce and distribute or you can distribute only. When I say produce, I'm talking about underwriting. Many foreign banks underwrite life insurance. In Europe, and particularly in Australia, that was basically their motivation. They saw the underwriting profits as a major motivator. You'll find that if you go over and look at any of the operations over there, since you don't have restrictive regulations, banks have been very happy with the underwriting results of most of their insurance company affiliates. There is one catch to this. Life insurance in Europe or Australia is synonymous with investing. Bankers consequently are very happy and content with this because what they're really doing is selling things like insurance bonds and annuity type investments with hardly any protection. This is the sort of thing that banks does naturally anyway, and they're very comfortable with it.

The reason for it relates to the breakdown of the public social security system throughout Europe and Australia. It's something called "the 2005 syndrome." The increase in reliance on private pension schemes is being pushed. The federal government pension schemes are failing all over the place, and as a result in the last year or so, the federal governments of those countries have been pushing the banks and insurance companies to offer private pension plans to their people because they know they're going to run out of money in around the year 2005 to 2010.

What are the cons of underwriting? I believe the underwriting of insurance by banks hasn't happened in the U.S. for a number of good reasons. Banking is capital intensive, and banks are buying each other. In fact, I noticed this morning, First Union Bank in North Carolina has just purchased First Railroad Bank in Atlanta, and they have now become, overnight, the largest bank in the southeast. There's an explosion in this regional banking, and it's using up all the money the banks have to buy each other up. Bankers are not really sure what it's all about, but as they get into it and they find out that there really is a capital commitment to insurance, they back off from underwriting in a quick way.

There is the issue of an exposure to adverse risk. This is more P&C oriented, although I've had some experiences on the life side. The adverse risk exposure is that you have your bankers passing over to your insurance agents on the P&C side bad loans by trying to have their collateral covered by property insurance. It becomes a real problem within the bank. You wind up taking on things that you wouldn't normally take on as an insurance agency because you've made a loan to that particular group.

There are regulatory inconsistencies. Regulations between the banking and insurance operations in the states are very difficult to sort out. When I was sued and taken to court, there was a lot of press about who was to try the case, the banking commissioner or the insurance commissioner in the state of

North Carolina. It was never resolved. The case was dismissed before they ever resolved their issues. So you do have those problems and they're real.

If you're in property and casualty, you know about the cyclical nature of earnings. That's not what banks want. However, this is obviously not the case on the life insurance side.

I can't understate the importance of differing cultures. These differences in the cultures of an insurance operation and a banking operation are like night and day. Different compensation schemes are part of the culture. It's significant. One is driven by commissions, the other is driven by salary, and it's hard to make the two work.

There is tax uncertainty. The banks just don't know where they are on some of this.

The technological incompatibility issue means that you can get an insurance operation up, but you will not be able to connect it to its mainframe easily. In fact, when we went to Europe to put these strategies together, the biggest hangup in implementation was trying to get the insurance systems to mesh with the banking systems. If you do it yourself, internally, it's a two year lag. It takes that long to get it started. And we're no where near putting anything like this together here.

And finally there are back office problems. Although banks are great at shuffling paperwork around, the paperwork that an insurance company produces is considerably different than that known and understood by a bank. The net of it is you've got to have another back up system, and you wind up doubling your back office personnel. So those are the cons.

I'll go through the pros quickly. You leverage the distribution system by running more products through the branches. Next, you have greater control. This is probably the most important reason why banks would want to underwrite insurance. In the European setting, it really has been the motivation. Other pros are as follows:

- Product design. Innovative new products can be used.

- Integration of banking products and insurance products.

- Marketing. Banks can gain control over marketing and pricing strategies. All that comes out of underwriting obviously.

- Favorable risk selection. Through knowledge of the customers and knowledge of the market, banks feel that they have control over risk selection. As a result, they believe they are going to get better clients. They believe they are going to be able to underwrite better than some other people because they know the details of their client base.

- Establishing alternative uses of capital. While capital resources are now limited because banks are buying each other up, many banks believe insurance underwriting is a viable means of obtaining a substantial return on capital investment.

- Providing protection against disintermediation. This means trying to keep dollars in the bank through insurance products in the event that interest rates go bad again. They see that, as people invest in insurance products which offer the build up of tax deferred cash value, such as annuities and universal life, banks can control that piece of the business as well.

- Cost spreading over a wide product base. All we're saying here is it's costly to keep the "brick and mortar" out there for the bank. By increasing the number of products for their customers, banks can lower the basic cost of existing delivery systems.

- Multiple distribution systems. Banks have branch networking which is their primary approach. Insurance companies are looking at this carefully today. Branch networking represents an alternative distribution system to insurance companies. Therefore, you are hearing so much about it in the insurance press today.

- Corresponding network. The corresponding bank network is extensive. Being in the insurance industry, we don't know very much about it. Of these 14,000 banks, the top 100-150 banks have correspondent relationships with the remaining banks where they work together and provide services back and forth. First Wisconsin bought an agency and started up its insurance operation to provide liability insurance to its correspondent banks -- not to its client base but to its corresponding banks as its clients. So there is a huge client base out there that the banks think they can capitalize on and probably can.

Finally, banks are putting a heavy emphasis on electronics through credit card mailings, direct mailings on credit cards and automatic teller machines (ATM). To use one example, I recently wrote an article. In it, I mentioned that Australia introduced ATMs. There are television screens in the front of each bank. A lady will come on the screen and by merely pressing "insurance," she'll show you how to get term insurance, automobile insurance, homeowners, and so on. You plug in the information, it is underwritten it through a computer that supports the ATM, you get a binder. The bank doesn't really give you a policy, I understand. You can also buy mutual funds and investments that way. So they've taken the idea of ATMs one step further.

When I published the article, I had about 15 phone calls from Australia decrying this as a bunch of nonsense; they'd never seen it. So I've been circulating the October 6th edition of the *Australian Times* front page where they had pictures of all this and a large story about it. Whether or not they're selling much, I can't tell you. However, that's what's coming. In fact, I believe there are some seminars being held around the country now on this particular issue.

There are a number of advantages to marketing insurance company products by a bank. Here are some examples:

- It creates desirable fee income.

- It requires a small capital commitment. You don't have to go out and worry about surplus drain. You just put an agency into effect, which really means putting some people into your branch or some regional location.

- o It affords cross-selling opportunities. This is another one of the major key items that bankers look at and stress and talk about their ability to cross-sell bank and insurance products.

- o It produces cost effectiveness of the sale. Banks see selling two or three products as being very cost effective, which of course it can be. If they can do it, it enhances the full service concept which they have been trying to promote.

The problem with cross-selling is that banks are notoriously poor at it. Yet it's the sort of thing that makes bankers salivate. It gets them excited. They see connections between insurance and banking.

The biggest problem that you have, a problem that is understated, is that if you have an insurance operation in a bank and it's an aggressive insurance operation, you wind up replacing the bank in most situations. You don't cross-sell. You wind up selling 401ks and IRAs and doing estate planning on the insurance side. The bankers get mad at you, and they immediately close you down because you're competing with their products. It's not quite clear that you can cross- sell some of these products and make a good dollar at it, but you do have opportunities.

There are also a number of disadvantages to marketing insurance company products by a bank:

- o Poor insurance service. It could mean the loss of a bank account. Take the example of a customer who has a large commercial account. He's got millions of dollars of CDs, a large checking account, he does all kinds of cash management services through you and is worth a lot of money to you as a bank customer. What happens if he has a major claim on a fire and the insurance company through which you sold him a policy refuses to pay? Guess what? You lose. You don't lose the client as an insurance client. You lose him as a banking client and there go the CDs, his bank account, and the cash management services. It's a risky business in that area. The banks are understating it and they're saying it's controllable but it's probably the biggest threat to the banking and insurance relationship. My own view of it is any bank that gets into insurance, especially P&C insurance, and tries to go the commercial route, is suicide.

- Good banking client, poor insurance risk. This is another interesting phenomenon where you have a guy who has tons of money with you and does all kinds of activities and he wants a large life insurance policy. However, he's just had a cardiac arrest and a couple of by-passes, and there's no way you can insure him for that million dollar policy that he wants. The same thing happens. You've got a great bank client, but you can't provide the service that he wants through you. If you think that these are exceptions, let me say that in the year or two that I was doing this, they were common occurrences, probably once a week.

- Legal problems. The difficulty with tie-in programs is that they will basically guarantee some sort of legal problems. One of the larger Georgia banks has just gone out and done some direct mailing and is getting into the business. Already this bank is receiving legal advice because agents are starting to mass together and threatening to sue. It happens.

- Cultural problems. There is a big difference between running an insurance agency and running a bank.

The origin of the cultural problem comes from the fact that a bank is consumer driven and an insurance company is distribution driven. Banks have a captive client base. The identity and affinity of the bank's client to the bank are very strong. When you capture his business, you capture all of his business. He generally doesn't have two or three accounts. This is the average bank client. You sell him commodity products, all of which are easy and convenient to use. By definition a commodity means he wants it, he needs it, and therefore he comes to you for that particular service.

What determines whether or not you get him as a customer is convenience, location and personal service. These are the things that really win over bank customers. Since banking is a commodity business and is really service oriented, bank products are not price sensitive. You will find most bank products are essentially priced the same. There is a marginal difference, but not that much. Basically, the consumer drives the bank's strategy in terms of pricing services and the type of products that a bank offers.

When you move over to the insurance company, the contrast here is that you have a distribution driven system because the products are complex and difficult to sell. You need somebody who knows a little bit about the product itself. When I say a little bit, that is probably what most agents know. Nonetheless you do have to have more than just direct mail. You can't sell universal life very effectively through the mail. When a complex problem comes your way, you need somebody to explain it to you. It is an independent distributorship system, and as a result, the insurance company has very little control over it as such.

Insurance is very price sensitive. When I talk about price here, I am talking about commissions. This is obvious to you, but just to make the point relative to banks, the intermediary here, an agent or PPGA, is more visible to the customer than the insurer. Surveys indicate that the person buying insurance identifies with the agent, not the company from which he is buying insurance.

Finally, the distributor controls the client base, not the insurance company. This clash in cultures between the insurance company and the insurance agency in the bank is such that bankers are not quite sure which direction they want to move in or how they want to do it. As a result, the banks try to modify the distribution driven system. To date they have not done so very effectively.

THE COMPENSATION SYSTEM

If you work for a bank, you are salaried. You may have a bonus, but you must be one of the top guys in the bank to get a bonus. There is one absolute rule -- you are never paid higher than the CEO. In the insurance industry you have commission driven production incentives and no caps. How many top salesmen make more than the CEO in the insurance industry? It is a common occurrence in virtually every company. Those sort of problems preclude one from hiring a really good agent to work in a bank. He is not going to stand for that.

There are ways of doing it, however. Let's say that my top agent in the life area ranks high on the Million Dollar Round Table, which would put him in the top five hundred producers. In my bank he would probably make under $40,000 which would put his compensation in the bottom third of those producers. This is because he is on a salary. Because he performs so well, we make him a vice-president and gave him no increase in salary. That's a bank's attitude towards compensation.

It will work when you take the type of people that we had, failed agents. We gave them leads and made them a success. But they knew as soon as they walked outside the bank they wouldn't be "top of the table" any more. They are the kind of captives you can get within a bank agency and make them successful. However, you can only find a handful of those kind of people.

ORGANIZATIONAL FACTORS

Banks are relatively well organized, formally structured, quiet and orderly. Move into the insurance agency. It's small and informal, less structured, less organized (if it is organized at all), flexible and less rigid, especially in terms of procedures and accounting, and it's busy and active. This contrast in the culture right here is most striking. I remember when the top management of the bank would come over and see my operation, these managers thought it was pandemonium. Chaos reigned. It was obviously a poorly managed operation because people were really doing things, answering phones, running around pulling out policies, doing all kinds of things that the bank management wasn't familiar with. It scared those managers to death. I don't want to overstate it, but I don't want to downplay it either. It is something that the bankers aren't use to.

OPERATIONAL FACTORS

You have trust and integrity in the bank. You have a professional image that banks try to portray. On the other hand, the insurance company has an aggressive sales orientation. Agents give advice which scares the bankers to death. On the P&C side the agent gives out advice on coverages, and the bank is liable for that. There is a real responsibility there. The bank doesn't ever want to be accused of coercive selling, but when you throw insurance in on top of a loan or whatever, there is a coercive aspect to it.

ADVERSE SELECTION PROBLEMS

I've already talked about the good bank client who is a bad insurance risk. There is also the loan risk transfer, where the bank makes bad loans and then transfers them over to the insurance operation. There goes your bonus for the year because of your loss ratio.

What drives the whole thing? The key strategic issue in my mind is people. Who do you have to run the operation, either on the insurance side or the banking side, particularly the banking side? What are their abilities? I can answer quite generally for the banks. When they try to start up an insurance operation, they keep it a banking operation. They don't have anybody that knows anything about insurance. The bankers' abilities are zero in insurance management, sales, or whatever. The net of it is you must to go outside of the banking industry and hire qualified insurance people. A lot of banks have started up insurance organizations. One of the reasons why they failed is that they didn't get the right people with the needed expertise in house, and it took too long to "grow" expertise. Banks may well grow expertise in the future, but not right now. In starting up an operation, you must get experienced insurance people. Banks haven't done that to date.

What are the attitudes of the people manning the operation, based on their culture? I just had an opportunity to observe this the other day. A fellow was hired to run a bank's insurance operation and he was excited. He is brand new at this and probably making a pretty good salary. He is going to be disillusioned in about six months. He thinks he has the secret to it all. He has the formulas. Six months from now he will be back saying he did something wrong. He doesn't know what it is, but it's not working. He did all the right things. It's because he's a banker, and he thinks he's going to run this operation like a bank. He has already laid out all of those issues I have just outlined. He is going to have a salary structure that is going to meet the bank's structure. Getting over that particular hurdle is going to be difficult if banks stay with people from within the banking environment.

How do you motivate them? You have to change the salary structure somehow. You have got to put a bonus in there for production. It's the only way to get, I think, aggressive sales out of an insurance operation.

How do you compensate them? If you are not going to motivate them with compensation, which is questionable, you have to start throwing in trips and prizes, the sort of things that are normal in the life insurance industry. At the banks they don't do this. They give them titles. That's why there are so many titles in a bank. You compensate with titles and that is generally not a good motivator for an insurance service organization.

So the net of all of this is, if you don't change the cultural attitude, the ambience of the organization you are involved in, you are going to have a difficult time putting it together. And I think that is why you are reading about these failures that we have seen in the *National Underwriter* over the last couple of months or so.

MR. KUNESH: I was most intrigued by the wave of activity that has been occurring in Australia, Europe, and of course, England. Do you think this wave of activity, whether it be in underwriting, cross marketing opportunities or joint ventures, will actually cross the oceans and reach our shores, or will they fizzle over the lobbying efforts in Washington, and if so when?

MR. SWEENEY: I think the only thing that is preventing the sort of activity that is taking place in Europe and in Australia, is the regulatory environment here. Until the regulatory barriers come down, you are just going to be too constrained. It is awfully difficult and very costly, and it takes a lot of creative effort to work around these. You have the Citibanks doing it. You have some of the large regionals doing it. However, they have to have the manpower and be out there spending money on lawyers and so forth trying to figure out ways to circumvent the laws. This makes it a little difficult to do. When deregulation comes into effect, I think you are going to see the banks come out in a big way, pull the plans off the shelf and go right after insurance. I do think they present a threat to the insurance industry if we don't get our act together about how we are going to work with them.

As to when it is going to happen, I used to say it's always two years off in the future. If you asked me two years ago, when I went with a bank, it was two years away. It's probably another two years, maybe more like three or four. I'm getting the feeling right now from Congress that after Continental Illinois and some of the other bank problems of the last year or two, and then the departure of Bill Isaacs from the FDIC, who was a major deregulation promoter in the Reagan administration, deregulation went on the back burner, and nothing is happening right now. So it seems to me that we are probably two to three years away, bare minimum, and as many as five, which isn't terribly exciting from the bank's perspective.

MR. KURZ: I think I mentioned before that the thrift industry is currently allowed to directly sell insurance, and there are a couple of thousand savings and loans and mutual savings banks out there. Some of them are reasonably successful. If they are a sample of what will happen when commercial banking is legally allowed to enter into the business full force, we might be able to have a preview of what specific opportunities there might be. A couple of thrifts like Gold Dome and H. F. Ahmundsen on the West Coast have large operations and have made significant incursions to the local market places. They have already faced some of the problems that I think the commercial banks will once they are legally allowed to have their own employees sell insurance. Those are the cultural issues and many of the things that John mentioned. But the one message is that thrifts are currently allowed to be in the business, and through investments and through other different types of programs that are currently out there, they are muddling through right now. Thrifts are not commercial banks, they generally don't have the management talent that commercial banks have, but they do have the captive customer bases. They do have a lot of capital, and so forth.

MR. WILLIAM P. SAKEL: Are the banks looking for fee income up front, basically, experience refund types, or captive insurance company types, in other words profit sharing? Where do you see them ultimately going?

MR. SWEENEY: Actually the banks really don't know what they want. They want fee income. They don't have a well defined plan. If you were to promote any one of the three or four things you were just talking about, depending on the bank you were talking to they would say yes we want all of those things, or some of them. It doesn't make any difference. They really don't have that finely tuned. If you are trying to hone in on a strategy on how to approach the bank on fee income, I don't think it is a matter of getting very sophisticated. One thing the banks tend to be somewhat positive about that will help an insurance company pay them, is that they are willing to pass on value to the consumer by cutting, up front, the commissions. You can get a bank to go to levelized commissions and take it as an annuity because he feels he is going to be able to sell that product and keep it on the books much better than the standard agent and some of the figures indicate that that's true. The 13 month persistency tends to run in the 95 to 96% range. So levelized commissions are a way to go.

If the banks do any kind of an analysis on it, they will wind up saying I can get a lot of money up front. I would like to have that right away. Picking it up a little later on in a reinsurance agreement is a little technical for them right now. I don't think it has a lot of pizzaz except for one or two of the banks which might have some sophistication, like Chase or Citibank. I think it is probably a concept way ahead of itself for the bankers right now.

MR. KURZ: Generally the more sophisticated and the larger the bank, the more sources of revenue it is going to look for. We encourage Citibank and Chase, as clients of ours, to look at reinsurance revenue through whatever legal means they can get it, through all kinds of profit sharing and volume based compensation systems as well as traditional commission streams. The larger the organization you're thinking of going with partnership with, the much more likely it is going to squeeze you for every possible dollar of revenue that it possibly can. The banks perceive themselves as having the bargaining power and the customer base to try to squeeze you from all the sources that you have mentioned.

MR. SAKEL: Would you then say that from what I have seen in savings and loans, is that banks want the money up front?

MR. KURZ: Yes, because they are less sophisticated, and they have a much shorter term orientation to this. They have no stomach for red ink, even in the first year.

MR. SAKEL: But the larger banks are more receptive to the risks?

MR. KURZ: They have a whole insurance department that they have set up. They are taking this as a long term major business effort for them, and in fact, their plans call for assumption of risk the first possible moment that they can.

MR. SWEENEY: Bear in mind that those large banks are a handful as opposed to the thousands that are out there. Also, the S&Ls have a different perspective they banks do on insurance for a couple of different reasons. I think one of the primary reasons is the bank is transaction driven every week. You see the client, he comes in, he makes a deposit, he makes a withdrawal from the bank, or he uses checks, whatever. In the case of S&Ls, he sees the client on one-half of that balance sheet and just once, if a guy pulls a loan out and then makes a thirty year mortgage or whatever and leaves, you never see him again. He probably never enters the S&L. The S&L is really trying to sell insurance to the depositors who they see on a frequent basis, but their motivations are different from the people who take out loans, and therefore they are different from the retail bank customers as well. It's not a transaction driven type of environment in an S&L. Consequently that leads up to what Don just said -- one shot deals, up front money, that sort of thing. They try to get it as quickly and fast as they can.