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News Direct

Defining Direct—What Does D2C Mean for Financial Services?

By Patrick T. Leary and Eric T. Sondergeld

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Letter From the Editor

By Ailen Okharedia

Welcome to the May 2017 edition of *NewsDirect*. My name is Ailen Okharedia and I am the new editor of *NewsDirect*. Many thanks to Jill Klibanov, my predecessor for her service to this publication and making it what it is today. I am particularly enthusiastic about the wave of innovation taking place in our industry. Digitization, big data, behavioral economics, all present interesting opportunities to bring positive change to our industry.

Digitization, big data, behavioral economics, all present interesting opportunities to bring positive change to our industry.

In this edition, we have articles that cover a wide range of topics including:

- "Defining Direct—What does Direct-to-Consumer mean for Financial Services?"
- "The Possible Effects of Negative Interest Rates on the U.S. Life Insurance Industry"
- "A New Senior Benefit—Accidental Death"
- "Insurance is Sold, not Bought—But Why? and Lessons Learned from *Nudge*, by Thaler and Sunstein" (Book Review)

The articles in *NewsDirect* come from volunteers, and very often from members of our own Marketing and Distribution (MaD) Section. Have you ever wanted to become a published author? We are always looking for people to with fresh ideas and new perspectives on topics that are relevant to our MaD mission to contribute articles to *NewsDirect*. If you have an idea for an article that you'd like to write, please contact me or any MaD council member.

Also, I would love to get feedback on this edition from anyone who reads any or all of the articles. What did you like? What would you like to see in the next edition? Do you have suggestions for particular authors or subjects? What changes could we make so that you receive the most possible value from reading *NewsDirect*? Please drop me a note to let me know what you think.

I hope you enjoy this edition of *NewsDirect*!

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Defining Direct—What Does D2C Mean for Financial Services?

By Patrick T. Leary and Eric T. Sondergeld

Increasingly, organizations across all industries are leveraging direct-to-consumer (D2C) strategies. This article provides a backdrop for companies seeking to develop a new or expand an existing D2C distribution program.

WHY NOW?

While the financial services industry has always had a "stake in the ground" with D2C distribution, interest in developing expanded D2C capabilities has increased considerably. Several trends contribute to this renewed attention:

- Other industries have raised the bar and created appealing D2C experiences—particularly online. Consumers will increasingly expect (and even demand) the same digital capabilities from financial services organizations.
- Financial services organizations are seeking new outlets for profitable growth.
- Some market segments (e.g., the middle market) have expressed a need and desire for the industry's products and services, but existing distribution methods have not successfully met that need in a cost-effective way.

WHAT IS DIRECT (TO CONSUMER)?

Before exploring D2C in detail, it is important to understand go-to-market strategies that manufacturers—regardless of product or industry—have at their disposal to reach target markets. As financial services organizations take a more consumer-centric perspective of marketing and distribution, the industry must view distribution strategies in a way that is consistent with the distribution framework other consumer-focused industries use to connect with markets.

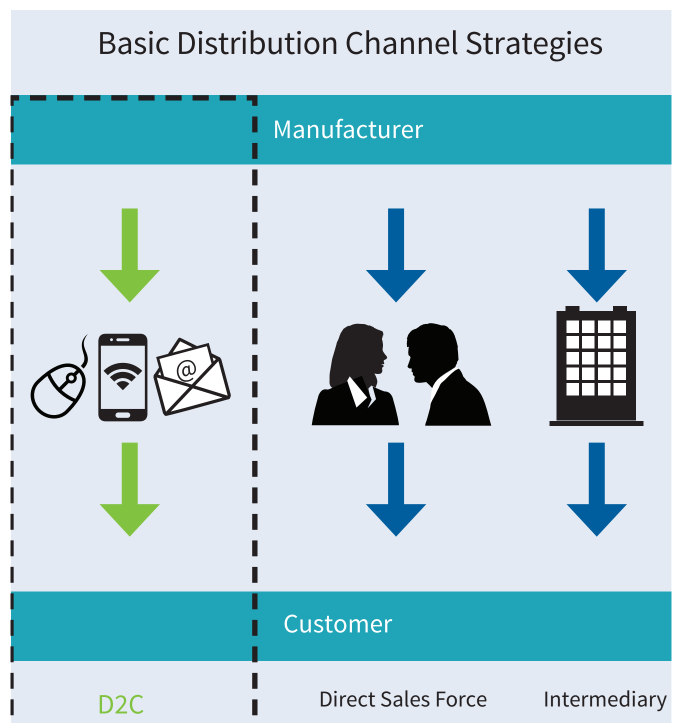
At a fundamental level, distribution is the process of connecting a manufacturer with the market of potential customers. There are essentially two basic strategies (Figure 1). A manufacturer can connect with customers:

- **Directly** through its own distribution channels, including its own stores, outlets, salespeople, and D2C approaches (e.g., online and mail), or
- **Indirectly** through intermediaries, third parties, and other partners that provide access to markets the manufacturer seeks to reach.

Direct distribution channels are those where manufacturers interact directly with the consumers who might purchase their product; they have direct access to them and control of the channel. Thus, direct channels include not only what is traditionally considered direct response, but also direct sales forces. If the manufacturer doesn't direct or control the channel and sells through someone else, then it distributes indirectly using intermediaries (third parties).[1]

As an example, Apple Inc. can distribute its products directly through its offline and online channels (e.g., Apple stores and its website). It also can distribute them indirectly through retail outlets (e.g., Target and Best Buy) and wireless service providers.

Feature 1



Source: LIMRA (2016)

In our industry, investment firms such as Fidelity Investments and Vanguard distribute directly when selling their own mutual funds—yet they also serve as intermediaries for countless other manufacturers. A life insurance manufacturer could sell its products directly through its own sales force or website or indirectly through banks or brokerage general agencies.

D2C can be defined as any non-face-to-face distribution program directed by the manufacturer such that no third party has a financial incentive for the program's success.

THREE PRINCIPLES

As marketing and distribution strategy has evolved, so have the fundamentals that define D2C channel distribution. Three key principles provide clarity and a contemporary perspective:

1. D2C is more than direct "response."

What was once called direct response typically had some type of stimulus that consumers **responded** to. For example, these included a television or other advertisement with a toll-free number to call, "bangtail" billing envelopes (with a perforated coupon attached to return), or another mailing with a call to action. But with the advent of the internet as a potential sales channel, self-motivated consumers may be responding to their own initiative when seeking information and potential outlets for purchasing financial services products online.

As such, the term "direct response" represents an incomplete picture of the channel. The term "direct to consumer" provides a more contemporary reflection of how organizations engage with consumers on a direct basis with non-face-to-face methods.

2. D2C is non-face-to-face—but not all non-face-to-face is D2C.

If a manufacturer's offer is made through a distribution partner's website, is that D2C or distribution through an intermediary? Does it matter that the manufacturer is making an offer via a third party? The customer experience is similar.

For example, many would consider Amazon.com to be a D2C channel. From a manufacturer's perspective, however, it is selling through an intermediary (i.e., indirectly). In this case, it is through an online retailer versus its own D2C website, where it has direct access to the customer. Here, the distribution channel is indirect: an online retailer. The method is non-face-to-face: online. The fact that it is online does not alone define it as D2C.

3. Marketing and fulfillment do not necessarily determine whether something is D2C.

A third consideration is understanding the distinction between direct marketing and the fulfillment of the product purchase. Working with their chosen distribution channels, manufacturers can encourage the purchase of their products in two ways (Figure 2):

- Using **push marketing,** they push messages through intermediary channels, encouraging them to sell more of their product.

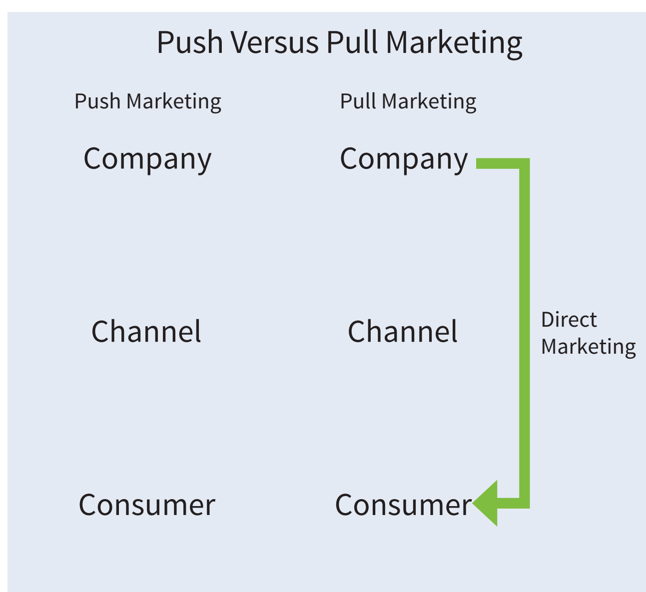
DISTRIBUTION CHANNEL VERSUS DISTRIBUTION METHOD

A distribution channel describes the entire network or path from manufacturer to consumer. The concept of channel is primarily of interest to the manufacturer. A distribution method refers to how the manufacturer, distributor or financial professional engages clients and potential clients. Regardless of channel, multiple distribution methods may be used, such as face-to-face, mail, phone and online.

Historically, direct response methods were limited to mail and phone via contact centers; the customer was purchasing directly from the company without using a local advisor or agent. D2C now includes digital methods such as online, email, social media and online advertising. At the same time, some financial professionals and distribution organizations employ non-face-to-face methods to facilitate sales, rather than simply to generate leads.

- Using **pull marketing,** they market directly to consumers by encouraging them to seek out the company's product, thereby pulling the customer up through a channel to purchase. The channel could be an intermediary, a direct sales force, or D2C. So, while all pull marketing is direct marketing, it does not follow that all direct marketing is D2C.

Feature 2



Source: Innovating in a "Sold Not Bought" Category, Maria Ferrante-Schepis and G. Michael Maddock (2013)

> A D2C strategy can also be integral to an omnichannel strategy for companies that want to offer a variety of access points and seemlessly integrate them.

An important distinction is that financial services product purchases are typically fulfilled by the manufacturer. Unlike most consumer goods, financial services products cannot be purchased by distributors, marked up and then resold. With insurance products, the insurer needs to be involved for order fulfillment, since it must underwrite the risk, issue the policy, and set up an administrative record for the policy. Because of this, it sometimes can be confusing to determine whether something is D2C. This is why the definition of D2C is not tied to the fulfillment process.

Connecting with consumers as part of a D2C strategy requires a direct marketing campaign to advertise and promote the manufacturer's offer through mail, billboards, television, magazines, websites or other media outlets. Often the promotion is calling for an action on behalf of the interested consumers—such as making a phone call, clicking through to the manufacturer's website, or returning a postcard. There is an advertising cost to the manufacturer, but the media outlet has no vested interest in how successful the campaign is; they receive the advertising revenue regardless.

When distributing a product through an intermediary's non-face-to-face methods (such as their online website or membership publication), a similar call to action is often employed. What distinguishes it from a D2C channel is that the intermediary receives more than just advertising revenue. It may receive a contractual sponsorship or branding payment and/or compensation for the success of the program. It gets a "piece of the action" for any leads and/or sales the campaign generates. Unlike with paid advertising, here the intermediary has a vested interest in the result of the campaign.

CHALLENGES AND CONSIDERATIONS

Building a D2C program from the ground up requires marketing muscles that may have atrophied or never existed. To do so, companies will need to develop go-to-market strategies that:

- Identify a market need;
- Define the specific markets that have the need;
- Find the most effective way to reach and engage those markets; and
- Determine what their competitive advantage will be, including the actual product or service offering.

The order of these steps could vary by company, but it is critical that—before deciding on D2C as a path to market—it is the most (or one of the most) effective means of reaching the desired market. If there is a better way to reach a particular market, then companies should seek that out instead. Once it is decided that D2C is the way to go, companies need to develop a true marketing mindset to understand the needs and attitudes of their target markets and how they want to engage.

A D2C strategy can also be integral to an omnichannel strategy for companies that want to offer a variety of access points and seamlessly integrate them. At the same time, they need to be careful not to inadvertently create conflict between a D2C program and their direct sales force. Conceivably, they could even create friction with other distribution partners, though this is less likely. Another potential risk is spreading marketing mindshare too thin across a growing number of distribution channels/methods.

Finally, one of the biggest challenges many companies face in building a D2C strategy is determining the actual product or service offering. In many cases, existing products just may not work. They may be too complex, not adequately priced for D2C, or otherwise a poor fit for the chosen D2C market(s).

Companies must remember that—unlike most products sold face-to-face—the D2C offering includes not only the product, but also the price, process and experience. And this is where we come full circle to the importance of revisiting and reinventing the customer journey in financial services. ■

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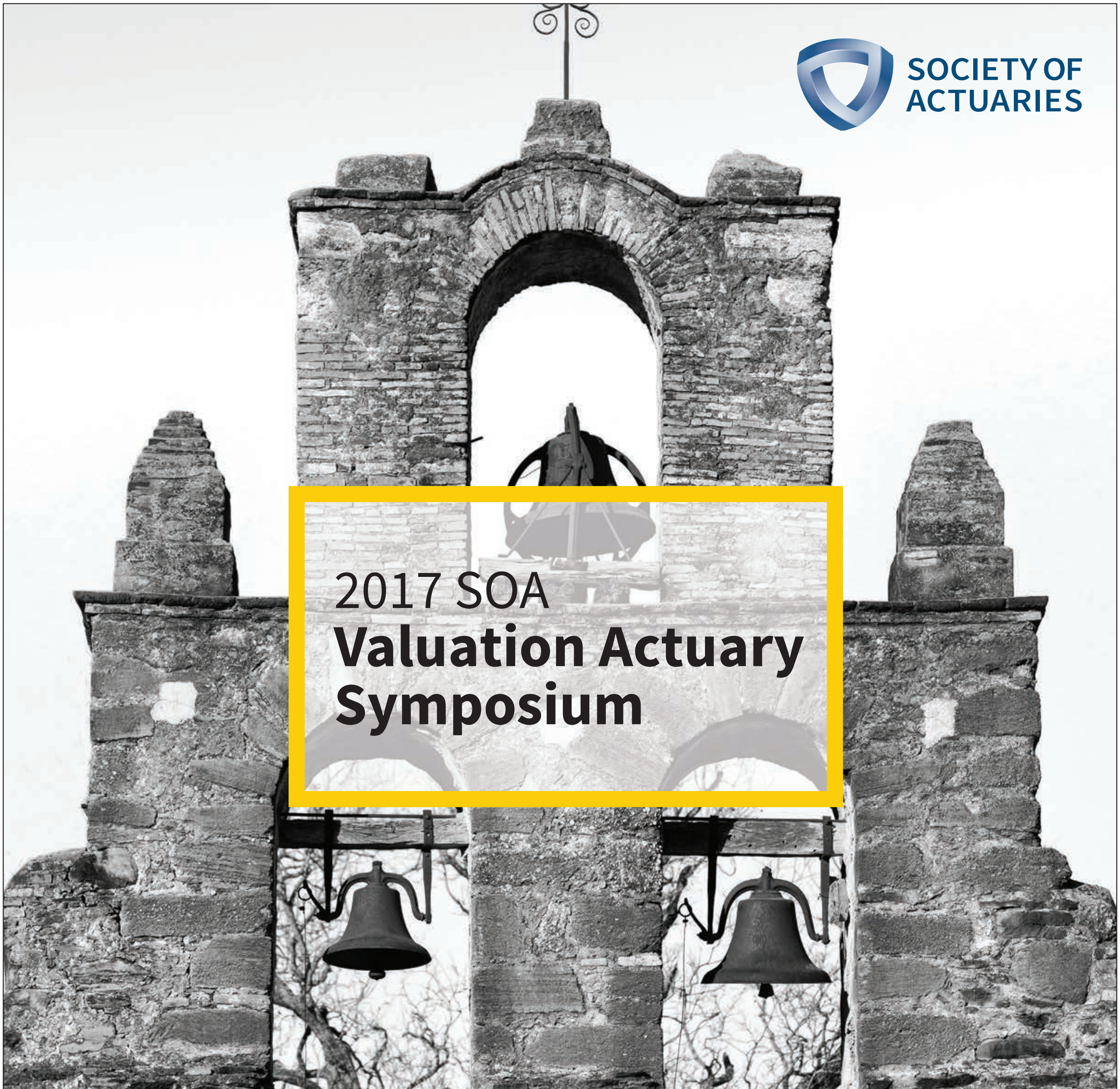
ENDNOTE

1 *Retail Distribution Perspectives,* LIMRA, 2014.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The Possible Effects of Negative Interest Rates on the U.S. Life Insurance Industry

By Richard de Haan and Simpa Baiye

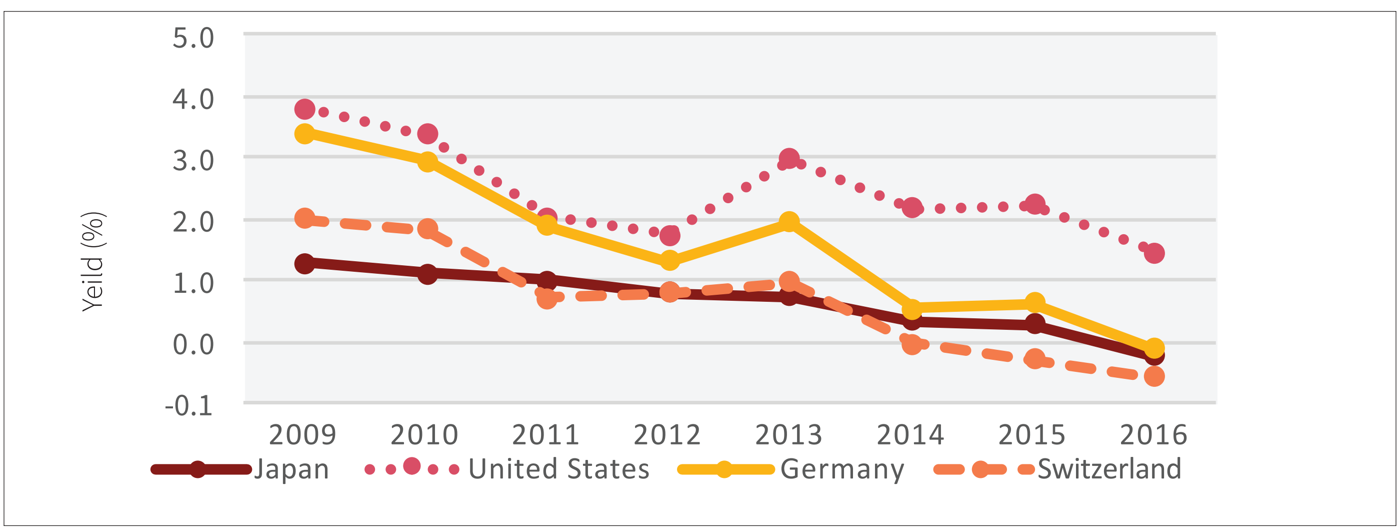
The persistent low interest rate environment in the U.S. has impacted life insurers for far longer than many expected. However, with potentially rising economic headwinds, negative nominal interest rates, as experienced in some developed economies, are more than merely a hypothetical possibility for the U.S. Negative interest rates challenge life insurers' value, profitability, and solvency and affect their product strategy and pricing, product portfolio management, financial reporting and investment management and asset adequacy.

BACKGROUND

Eight years after the great financial crisis of 2008, U.S. treasury rates remain at multi-generational lows. Federal Reserve Bank and Treasury programs of various types have kept rates at levels intended to spur lending and overall economic growth. Central banks in much of the developed world have kept rates at even lower levels. Low rates have driven down anticipated returns on fixed income investments for both life and P&C insurers in a number of developed economies and have even resulted in the need to rehabilitate some life insurers. In Germany, for example, near zero or negative yields on sovereign bonds have put German insurers with significant exposure to fixed-income intensive, guaranteed-return insurance products under significant pressure. Moreover, investors' flight to safety in the wake of Britain's recently announced plans to exit the European Union has put further pressure on U.S. treasury rates.

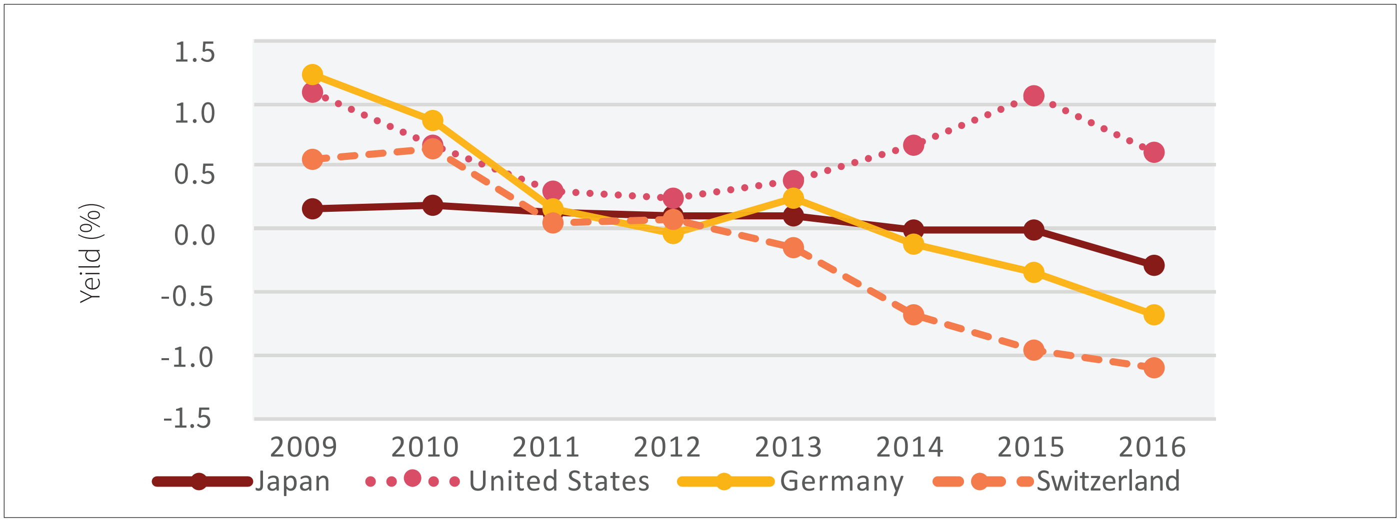
Sovereign interest rates in many developed economies have shown little sign of rising. In fact, charts 1 and 2 show that rates in a number of developed economies are already in, or are headed toward negative territory. For the U.S., the future direction is less certain, although there are mounting pressures that increase the possibility that sovereign rates in the U.S. might go negative, particularly in the first 10 years of the yield curve. Pressures include the flow of capital from developed economies with near zero or negative rates seeking greater positive yields and more attractive credits in the U.S. (increasing demand increases price, lowering fixed income yields). Also, as waves of retiring baby boomers seek guaranteed returns, and as pension plans increase their allocations to fixed income in order to manage pension-funding risks, the demand for guaranteed yield is also likely to suppress and even drive yields on debt into negative territory.

Chart 1
10-year Sovereign Yields (Rates through June 30, 2016)



Sources: CNBC Finance, Investing.com

Chart 2
Two-year Sovereign Yields (Rates through June 30, 2016)



Sources: CNBC Finance, Investing.com

The possible impacts of negative nominal treasury rates on 1) product development and pricing, 2) product portfolio management, 3) asset adequacy, 4) financial reporting and 5) investment management in the U.S. life insurance industry are as follows:

- **Product Development—**U.S. standard non-forfeiture laws largely put a floor on interest rate guarantees. In the absence of substantial revisions of the law to account for the possibility of negative interest rates, insurers would likely need to manage this regulatory constraint by offering longer rate guarantee terms (where state insurance laws or interstate product compacts allow) or by simply taking or lengthening portfolio yield terms relative to rate guarantee terms. Taking on more asset-liability risk in itself is bound to make rate guarantees less capital efficient and thus more expensive to offer from an economic standpoint. More expensive rate guarantees may result in insurers offering policies with less guaranteed rate elements. Insurers also would likely seek the option to reset rate guarantees much more frequently than they have historically.

  Low interest rates in the U.S., coupled with the rising equity markets that have been punctuated by periodic market crashes, have made and will continue to make equity-indexed life insurance and annuities an attractive proposition for policyholders. As sovereign rates fall and go into negative territory, insurers will look to find ways to offer insured products without making substantive interest rate guarantees. As a result, structured equity participation products that offer participation in the equity markets while limiting downside losses may increase in popularity.

  As insurers reach for yield in order to avoid the impact of negative benchmark rates at the short end of the yield curve, it is likely that they will limit their long-dated guarantee offerings to payout annuities and whole life insurance in order to meet non-forfeiture requirements and still earn sufficient interest margins.

  Insurers also may choose to offer more credit risk guarantees as they reduce their exposure to interest-rate guarantees. Institutional products such as stable-value wraps, for example, allow insurers to make credit risk guarantees with little rate guarantee risk. Insurers may look for ways to offer such products on a retail basis.

- **Product Pricing**—Public companies typically price products to earn an internal rate of return of 10 percent or more. The equity investor community implicitly sets this rate based on its broader expectations about risks and rewards for financial services companies relative to lower return and lower risk opportunities. Negative interest rates could lower investor expectations about the risk premium for financial services companies and hence result in a realignment of expectations of product and, ultimately, sector returns. Mid single-digit risk-adjusted return targets may not be an uncommon pricing target for insurance products in a negative interest rate environment.

Recent deals activity by certain Asian investors confirms this. The desire for positive returns in the U.S. insurance market relative to near-zero or negative rates in Japan has served as motivation to make acquisitions. This activity also has raised the valuations of life insurance companies (at the margin) relative to the unchanged or lower profitability expectations for their in-force businesses.

- **Product Portfolio Management**—Insurers will face much greater pressure on margins earned from legacy blocks of annuity and insurance premiums with high minimum rate guarantees. Negative rates may encourage insurers to offer buyouts on products (e.g. fixed annuities) with larger rate guarantees than they currently offer or can offer in at least the near-term future. In order to do this successfully, insurers would need to conclusively show policyholders the value of taking upfront gains in lieu of holding onto their attractive rate guarantees.
    - **Product risk disaggregation**—The process of unbundling product risks on a component by component basis may play a more prominent role in helping companies manage their businesses. Reinsuring or transferring interest rate risks to parties willing and able to assume such risks may present new opportunities for insurers to manage the risks of their legacy businesses. They will need to evaluate and minimize risk-transfer counterparty risks in this process. They likewise will need to weigh the benefits of these potential opportunities both for formulaic regulatory reserves and asset-adequacy reserves.
    - **Product-line disaggregation**—Divestitures or spin-offs of underperforming closed blocks of business or specific lines of business could become the favored approach to dealing with interest-rate sensitive lines of business that drag down insurer earnings and capitalization ratios as rates fall. This could present a new wave of opportunity for private-equity buyers of insurance business and for public-equity investors who can set an appropriate bid for prospective returns on interest-sensitive products.
- Asset Adequacy and Capital Requirements—U.S. life insurers periodically assess the adequacy of assets backing reserves under moderately adverse interest rate scenarios in order to

identify possible gaps between assets on hand and liabilities as they come due. They typically evaluate anticipated cost of minimum interest rate guarantees on life insurance, long-term care, and annuities via the assessment process' rate scenarios. The possibility of negative interest rates could lead regulators to change asset-adequacy testing scenarios and effectively place additional surplus strain on insurance companies. The Federal Reserve's increased focus on stress testing also could drive companies to consider and model the impact of negative rate outcomes.

Another impact to consider is the valuation and credit rating of underlying investments. Write-downs of book value and credit downgrades will reduce available statutory capital and increase risk-based capital requirements, and also will place additional pressure on insurer capitalizations. This could lead to insurer credit rating downgrades and result in scaling back or shutting down ratings-sensitive lines of business. Insurer ratings downgrades also may make it more expensive for insurers to refinance their debt. And, while negative rates may offset higher debt refinancing costs resulting from downgrades, such offsets will be less meaningful for insurers that are more exposed to rate guarantees.

- **Financial Reporting**—Negative rate scenarios have statutory asset adequacy and capital implications that could result in additional reserves needing to be held in respect of minimum rate guarantees. Public companies also would need to re-evaluate their GAAP Reserving and DAC investment yield assumptions and loss-recognition/recoverability testing processes under US GAAP to account for the possibility of negative interest rates. Insurers would need to review and retool interest-rate scenario generators that support these testing processes in order to account for negative interest rates along the yield curve. Insurers also would need to review their enterprise reporting, valuation, and administration systems for both assets and liabilities to ensure consistent reflection and reporting of negative interest rates and their financial impact.

- **Investment Management**—As we previously noted, negative interest rates will put more pressure on insurers who take on more credit, equity and duration risk in search of yield. State regulations on insurer asset allocation and the impending reduction in risk-capital requirements for below-investment-grade securities will help temper credit risk pressure. However, structured equity participation products—many of which pay equity-linked coupon income and come with a principal guarantee—may take on a more significant place in insurer portfolios despite their higher surplus-volatility implications relative to traditional fixed income.

- Insurers may look to take on more duration risk, but most likely with the option to shorten portfolio durations if the need arises. They may obtain this option through the trading of interest rate options; accordingly, they would need to carefully evaluate derivatives trades of this nature to determine their fit with investment portfolios.

CONCLUSIONS

The consequences of possible negative U.S. treasury rates pose a significant threat to life insurer value, profitability, financial reporting and solvency. Negative rates require a thoughtful reevaluation of insurer product strategies in order to offer meaningful value to current and future customers. In particular:

- Insurers may have to earn the margins they hitherto earned on interest rates by taking more traditional insurance risks, deemphasizing interest rate guarantees, and taking more credit risk.

- Negative interest rates would effectively lower capitalization ratios more significantly for insurers that offer long-dated interest rate guarantees.

- Insurers may need to manage their capital in respect of in-force business via reinsurance, by modifying their investment management strategy, through product buyback offers, and/or product portfolio sales.

Even though the possibility of negative interest rates may be somewhat remote, life insurers should determine the range and severity of potential impacts on their business, and develop strategies and plans to execute should negative interest rates ever become a reality. ■

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A New Senior Benefit: Accidental Death

By Jay M. Jaffe

Accidental death benefit (ADB) life insurance has been offered by insurance companies for 100+ years. The benefit has been offered as a rider to, or automatically incorporated in, life insurance, as the main or one of several benefits provided by accident & health policies, etc. It can also be issued by life insurance, accident & health, or P&C insurance companies. There is also the option to use individual or group policy forms. Sometimes ADB includes dismemberment benefits or multiple times benefits for specific causes of death such as automobile or common carrier losses. In other words, ADB is a very popular and adaptable benefit.

There have been two notable ADB mortality tables developed by actuaries in the United States based on ADB insured life experience: The 1926–33 Intercompany Double Indemnity Table and the 1959 Accidental Death Benefits Table. These tables have been used as the basis for ADB reserves and pricing ADB insurance. The 1959 ADB Mortality Table is probably the table used for reserving ADB issued by U.S. companies even though it is based on 1951–1956 experience (which either makes the table absolutely or optically a dinosaur.)

ADB coverages are usually subject to a termination age of around 70, may not be issued above a certain age such as 60, and/or use reductions in ADB benefits past an attained age to offset what is perceived to be almost escalating claim rates at the older ages. Another reason ADB amounts often decline by attained age is that it can also be problematic to adjudicate ADB claims at older ages because accidents often result in deaths where the insured first has an accident and then dies of complications that follow. For example, an older person may break a hip, then become ill with pneumonia and die. Was it the broken hip or the pneumonia that caused the death?

Actuaries utilize non-actuarial produced experience to price ADB products. There are many public sources of accidental death experience in the U.S. One of the best is the National Safety Council (NSC). Each year this organization publishes a summary of accident related data titled Injury Facts. Several of the tables in this publication cover data relating to deaths from unintentional injuries. Broadly speaking, the causes of death included in unintentional injury related deaths are those that would be covered under ADB's. Another valuable source is the National Vital Statistics Report (Deaths) that is also published annually.

NSC data reports experience as far back as the early 1900s, but it is the death rates post-World War II that are probably of greatest interest for today's actuaries. Unintentional injury related death rates over the past 70 years among the adult population (ages 25+) have declined at all ages, but noticeably have been the reductions starting at age 45+. In particular, the precipitous drop in population death rates for ages 65+ is the reason that ADB can become a more important benefit for seniors. Compared to death rates during 1950–1954, recent unintentional injury death rates for 65+ year olds are now just 40 percent of the rates from 60 years ago.

Another observation from the NSC data is that death rates from unintentional injuries for age groups 45–64 and 65–75 are now about the same whereas a generation or two ago, the 65+ year crowd had much higher death rates than the next younger group.

The dramatic reduction in senior unintentional death rates and the similarity of these rates throughout ages 45–75 presents a significant opportunity for insurance companies to rethink the design and marketing of ADB insurance. Why should ADB only be offered up to age 60 or benefit reductions occur at age 70? Could ADB be issued through age 75 and now terminate at age 80? Not only might ADB sales be expanded, but there is a massive opportunity to automatically amend current ADB programs to incorporate the more recent reported NSC experience. For examples, ADB riders on existing individual life policies could be continued (keeping the same premium) to a later termination date. Voluntarily extending coverage would also be an opportunity to market additional coverage to insureds under favorable conditions.

The decision to revise ADB products must include analyzing any changes in terms of the exact product involved, the composition of the insureds (by age and sex) and any other pertinent risk factors.

Expanding ADB to more seniors would require some internal administrative changes to accommodate new coverage periods, notices to insureds and agents describing what is being done, and some actuarial considerations. The last mentioned item, actuarial concerns, might necessitate recalculating reserves for ADB using an out-of-date table (1959 ADB). But the good will generated by continuing and expanding ADB coverages should more than offset any cost concerns.

Because of the new patterns of unintentional deaths and the potential for an expanding ADB product line, it would be helpful for the SOA do an analysis of insured life ADB that reflects current mortality and related benefit experience. Valuation and pricing actuaries would greatly appreciate having more current data on which to base premiums and reserves. The 1959 ADB table reflects experience from more than a half century ago and was restricted to only a specific type of ADB exposures. If possible, the analysis should separately cover both group and individual ADB insurance, A&H policy claims, claims for benefits often included with ADB (e.g., dismemberment or multiple times claims for auto or common carrier accidents), catastrophes involving multiple deaths, and any other ADB areas of interest to actuaries.

Insured ADB experience is different than population data and needs to be studied by itself. Insured ADB products exclude deaths from many causes that are otherwise included in unintentional deaths (e.g., participation in a speed contest).

Even though ADB is a limited benefit life insurance product, for many seniors who cannot qualify for life insurance or for whom the premiums at the higher issue ages become burdensome, ADB may offer some life insurance coverage.

The change over the past several years in unintentional death rates at the older ages provides an interesting opportunity to revisit and expand ADB coverage for the senior market. ■

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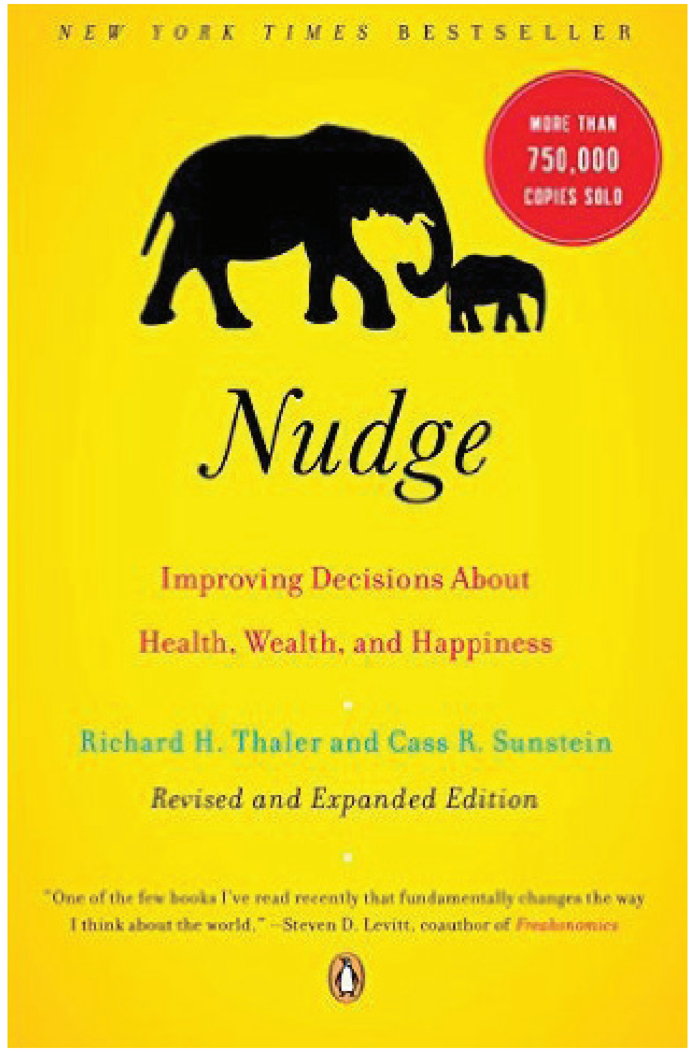
Insurance is Sold, not Bought—But Why? Some Lessons Learned From *Nudge* by Thaler And Sunstein

By Ailen Okharedia



Those familiar with the field of Behavioral Economics will have no doubt come across some of Richard Thaler's work and other interesting books written by him. He is arguably the most prominent mind in the field of Behavioral Economics today. *Nudge (Improving Decisions About Health, Wealth, and Happiness)* by Richard H. Thaler and Cass R. Sunstein is a book about the direct application of Behavioral Economics to tackle real world problems. Proponents of Behavioral Economics support the notion that it is possible to help humans make better decisions for themselves and their loved ones through seemingly small interventions—nudges.

Nudge starts off by identifying human tendencies and biases that make us susceptible to making decisions that are not always in our best interest. It then explores the world of nudges and provides examples of successful interventions that have been used in the world of Finance, Health and other social issues.

Here are a few notable examples of seemingly small but impactful interventions (nudges) from the book:

- **The power of continuous feedback (Thaler & Sunstein (2008, p. 196)):** "Thompson (2007) has explored the efforts of Southern California Edison to encourage its consumers to conserve energy—and its creative, nudge like solution. Past attempts to notify people of their energy use with emails or text messages did no good, but what worked was to give people an Ambient Orb, a little ball that glows red when a customer is using lots of energy but green when energy use is modest. In a period of weeks, users of the Orb reduced their use of energy, in peak periods, by 40 percent. That flashing red ball really gets people's attention and makes them want to use less energy."
- **The power of social norms (Thaler & Sunstein (2008, p. 69))**: "... consider a study of the power of social norms, involving nearly three hundred households in San Marcos, Calif. All of the households were informed about how much energy they had used in previous weeks; they were also given (accurate) information about the average consumption of energy by households in their neighborhood. The effects on behavior were both clear and striking. In the following weeks, the above-average energy users significantly decreased their energy use; ... But here is an even more interesting finding. About half of the households were given not merely descriptive information but also a small, non-verbal signal that their energy consumption was socially approved or socially disapproved. More specifically those households that consumed more than the norm received an unhappy emoticon, whereas those that consumed less than the norm received a happy emoticon. Unsurprisingly, but significantly, the big energy users showed an even larger decrease when they received the unhappy emoticon. ..."

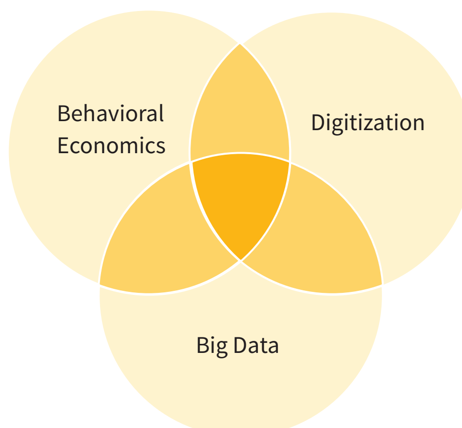
- **The power of ratings and disclosure (Thaler & Sunstein (2008, p. 192)):** "… A paper by Ginger Zhe Jin and Phillip Leslie (2003) documents a similar finding for restaurants. In 1998, Los Angeles County introduced hygiene quality grade cards that had to be displayed in restaurant windows. The researchers found that the grade cards caused the restaurant health inspection scores to improve, consumers' sensitivity to hygiene in restaurants to increase and hospitalizations for food-borne illnesses to decline." Thaler, Sunstein, Nudge.
- **The power of seemingly small financial incentives (Thaler & Sunstein (2008, p. 236)):** "Dollar a day: Teenage pregnancy is a serious problem for many girls and for those who have one child, at (say) eighteen, often become pregnant again within a year or two. Several cities, including Greensboro, N.C., have experimented with a "dollar a day" program, by which teenage girls with a baby receive a dollar for each day in which they are not pregnant. Thus far the results have been extremely promising. A dollar a day is a trivial cost to the city, even for a year or two, so the plan's total cost is extremely low, but the small recurring payment is salient enough to encourage teenage mothers to take steps to avoid getting pregnant again. And because taxpayers end up paying a significant amount for many children born to teenagers, the costs appear to be far less than the benefits."

The book makes it clear that nudges are most impactful where decisions are difficult and rare, where people do not get prompt feedback for their decisions and when they have trouble translating aspects of the situation into terms that they can easily understand (Page 74, Nudge by Thaler & Sunstein). There are many similarities between the situation described above and the products offered by the life insurance companies. Specifically, **"the benefits of holding the insurance are delayed, the probability of having a claim is hard to analyze, consumers do not get useful feedback on whether they are getting a good return on their insurance purchases, and the mapping from what they are buying to what they are getting can be ambiguous."** (Page 79, Nudge by Thaler & Sunstein).

"the benefits of holding the insurance are delayed,the probability of having a claim is hard to analyze, consumers do not get useful feedback on whether they are getting a good return on their insurance purchases, andthe mapping from what they are buying to what they are getting can be ambiguous."

A well-defined problem is critical to finding an appropriate solution to the problem. The better we are at identifying the underlying traits that make the current paradigm of "insurance is sold, not bought" a reality, the closer we are to finding solutions to this age-old problem and the better positioned we are to explore innovative ideas that will help consumers appreciate the future benefits of their insurance products, help consumers to become better at mapping what they are buying to what they are getting. But it all begins with focusing on defining the problem. Are there nudges that can make the probability of a claim less difficult to analyze? Are there ways we can provide consumers with useful feedback on whether their insurance purchase is giving them a good return? Are there ways we can make the process of buying less ambiguous? Behavioral Economics digitization and big data are tools we can use to engage with consumers in ways that was previously not possible. We are able to engage with them in a way that can breakdown some of the barriers/challenges we described above. (See chart 1)

Chart 1



A holistic approach to tackling these well-defined problems is required which will ultimately impact all aspects of the life insurance value chain: marketing, distribution, sales, product design, pricing, underwriting. I recommend reading this book and allowing your creative juices to flow as you explore the many examples of other successful interventions in the book and think about appropriate applications to the life insurance industry. In future publications we will seek ways to explore ideas and opportunities that exists right across the life insurance value chain to breakdown some of the barriers described above, particularly through engaging the tools of digitization and big data. ■

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MaD Happenings

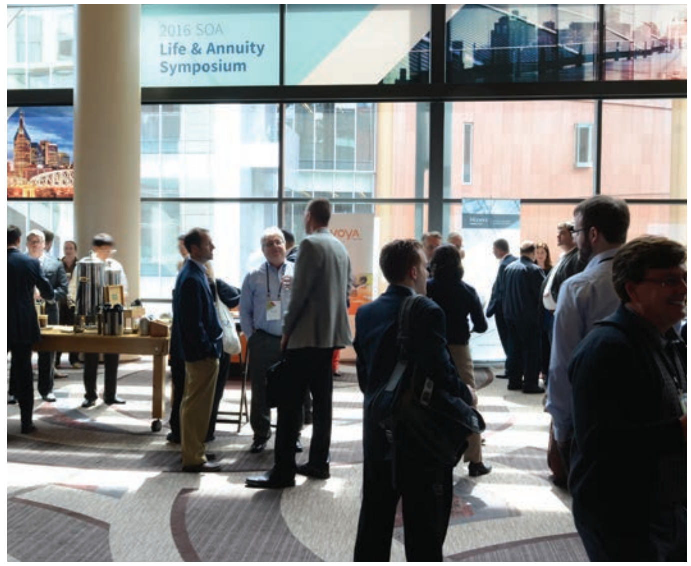
By Marketing and Distribution Section

MaD will be sponsoring or co-sponsoring the following sessions at the SOA Life and Annuity Symposium in Seattle, May 8–9. Please see the meeting program and registration page for more details. [https://www.soa.org/prof-dev/events/2017-Life---Annuity-Symposium/]

- Session 2 Networking Event: Dinner and Seattle Underground Tour
- Session 13 Panel Discussion: Improve Client Acquisition via Analytics … And Actuaries!
- Session 38 Panel Discussion: Shifting Gears to Accelerate Life Insurance Ownership
- Sessions 49 and 59 Panel Discussion: InsureTech Startups: Insider Perspectives
- Session 70 Lecture: Beg, Borrow, and Steal—Innovations Around the World

WEBPAGE

The Marketing and Distribution Section is pleased to introduce our newly designed section webpage. The section home page will be updated consistently throughout the year with the activities and offerings of the section. You will note that there



are now tabs at the top of each section's home page, including a "newsletter" tab. You can quickly access the section newsletters by clicking on this tab.

Visit the Marketing and Distribution Section webpage to see what is new and while you are there check out the new SOA Engage website to find communities and discussion topics that may interest you.

MEMBER INVOLVEMENT

For anyone interested in getting involved with MaD, a great way to get started is by becoming a friend of the council. By doing so, you can join in on monthly conference calls with the council and find additional opportunities to participate in section activities. To become a friend, simply contact any member of the council. ■

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