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AGENCY PROBLEMS

A. To what extent have smaller companies adopted the practice of financing new agents and general agents? How can companies recruit agents today without a financing program? To what extent does annualized commission provide the advantages of a financing plan?

B. To what extent do smaller companies make studies by individual agencies of:
   1. Persistency rates?
   2. Types of policy?
   3. Average size of policies?
   4. Expense rates?
   5. Mortality rates?

MR. MELVIN L. GOLD told of various methods by which very small companies, that is, those characterized by having less than 50 employees, were able to attract new general agents. One company in the metropolitan area offered competitive products and an opening for a general agency in an area which would not be available from the established companies. In other cases known to him businessmen, including a number of general agents, had founded the company and these general agents were able to direct a good proportion of their business to the new company to enhance its value and bring up the value of the stock. He indicated that the standard approach used by small stock companies is to give stock options to general agents, but this would not be permitted in the State of New York.

MR. ELI A. GROSSMAN outlined several aspects of life insurance stock plans for agents as follows:

1. Only a limited amount of stock should be relinquished by the stockholder.
2. If there is no market price for the stock, it is important to establish the purchase price of the stock. Such price may depend on the time the option or stock is granted.
3. If a stock plan is offered, it may be considered to be in lieu of some commission or other benefit.
4. Stock plans must be in accordance with the statutes of the states involved and other regulations such as the SEC.
5. The amount of stock thus issued should benefit the original stockholders as much as possible. Therefore, geographical distribution, timing in granting the stock option, and the amount of stock must be considered. At least part of these items lend themselves to mathematical analysis.
6. Provide a reasonable waiting period before the agent may exercise an option and allow a reasonable time during which he is able to exercise this option, although all the options need not be exercisable at the same time.

7. It is desirable both that the agents keep some of the stock rather than sell it to the general public and that the general public own enough of the stock to create a market for it.
8. The stock should be granted over a period of years to encourage greater persistency of the agent with the company.
9. Rights of the agent as a stockholder, including voting rights and other privileges, must be defined.
10. Amounts of stock granted should follow a formula that is equitable, simple for administration, and understandable.

He also pointed out the advantages and disadvantages of stock plans as follows:

Advantages

1. Agents have tools that many agents of other carriers do not have.
2. Sales personnel should be attracted and held.
3. Sales personnel will be interested in securing sound business.
4. The plan could be used to raise capital and surplus.
5. There are certain tax advantages for sales personnel in stock bonus plans and certain advantages in stock option plans.
6. The very attractive history of many successful life insurance companies makes stock plans attractive especially for new companies.

Disadvantages

1. Too much control might go to sales personnel.
2. An agent might prefer traditional compensation in order to invest in other life companies' stock or other stock.
3. Additional administrative work is thrown on the home office.
4. The program of issuing stock to agents cannot be continued indefinitely.
5. Stock plans can only be used for stock companies.

MR. JOHN A. STEDMAN described the financing plan of the Continental American Life Insurance Company adopted in 1944 to help new men get a start in the business. The satisfaction of both the field force and the home office with the plan's effectiveness is seen in the small change in it since adoption. The plan, an amendment to the regular soliciting agent's contract, provides a minimum monthly salary for 25 months in return for the assignment to the Company of commissions on business produced during that period. This salary is partly training compensation and partly selling compensation, the proportion of the latter increasing with time. At the end of a given month, if the total commissions that would ordinarily have been paid exceed the total selling compensation actually paid by more than one month's salary, in the next succeeding month 20% of first year commissions accruing will be paid in addition to the regular salary. The amount of any credit balance outstanding is paid to the agent in cash at the end of 25 months. All commissions accruing after the training period on business sold during that period are paid to the agent, but these are not vested. Whenever there is a debit balance of as much as one and one-half month's salary, the soliciting agent's contract is terminated. The general agent is required to pay one-half of any debit balance outstanding when the salary amendment is terminated for any reason. The general agent must agree to train the new man in accordance with the training program prescribed by the Company and the agency department checks closely on the progress of trainees through weekly and quarterly reports. Mr. Stedman stated that during 1957 and 1958 they placed 71 men under the salary amendment program at an average monthly salary of $419. Twenty-six of these men failed within 12 months, 20 of them within 6 months, an important cause of failure being the small initial premium collected.

MR. SAUL ROSENTHAL stated that an informal survey of practices of several smaller companies in the metropolitan New York area indicated a general practice of some degree of financing of new general agents but an aversion to the financing of new soliciting agents. He felt that there is general agreement in the industry that financing of agents is extremely expensive and uneconomical, but many companies do it. He found that the larger companies are committeed to the financing of new agents in accordance with the concept of full-time life specialists working under the typical career contract. He doubted that this type of agent and relationship would be possible under today's conditions without initial financing. Smaller companies cannot afford financing and are less committed to the concept of the full-time career man. Thus they approach the recruiting of agents along the following lines:

1. Recruit full-time men on the basis of a special appeal other than financing, such as a well programmed and easily sold standard package, high commissions, stock options, or a good general agent to guide them.
2. A practice considered sinful but popular is that of recruiting effective part-time salesmen.
3. Recruit general insurance brokers, who may have had difficulty with the product customarily sold, may be in the mood to write life business or increase life sales activities, or may have been disturbed by the unilateral action of casualty companies in reducing commissions and canceling coverages. Feeling that he is the captive of one insurance company, the broker is very much open to the appeal of the independent life insurance company which offers him a fully vested contract with lifetime service fees, some fringe benefits, good service and assistance on his sales, and the status of a first class citizen.
4. Solicit surplus business from full-time men of other companies in special areas where this can be done successfully and profitably.

Mr. Rosenthal concluded that even the advocates of financing look on it as a necessary evil, although there is a basic contradiction in paying a man a salary to launch him on a career in which he will have to live by his earned commissions without a salary. Evidence of this lies in the alarming rate of failure among financed new agents.

He stated that the device of annualizing commissions clearly provides some of the advantages of a financing plan while avoiding most of the pitfalls. Even a successful new agent's business is likely to include a high proportion of fractional premiums and thus annualizing commissions gives him additional income during his initiation period, the amount advanced being automatically supported by actual production. He said

ILLUSTRATION OF ANNUALIZED COMMISSIONS

Period	Production in Period	Annualized First Year Commission	Conventional First Year Commission
1st Quarter	$30,000	$360	$ 90
2nd Quarter	$40,000	$480	$210
3rd Quarter	$50,000	$600	$360
4th Quarter	$60,000	$720	$540
1st Year	$180,000	$2,160	$1,200
5th Quarter	$70,000	$840	$660
6th Quarter	$80,000	$960	$780
7th Quarter	$90,000	$1,080	$900
8th Quarter	$100,000	$1,200	$1,020
2nd Year	$340,000	$4,080	$3,360

that lapses may be handled either by discounting in advance on an estimated basis or by subsequent charge-back. The accompanying table illustrates the result of annualizing first year commissions for a new agent during his first two contract years, assuming he pays for $30,000 in his first quarter and his production increases by $10,000 in each succeeding quarter until it reaches $100,000 in the eighth quarter. It is also assumed that all premiums are payable quarterly at the rate of $6.00 per $1,000. Lapses are ignored.

Mr. Rosenthal pointed out that on the basis of a 50% commission rate the quarterly first year commission is $3.00 per thousand and the corresponding annualized commission is $12.00 per thousand. The illustration shows that the agent gets $960 more than his conventional earned commissions in the first year and $720 in the second year, although appropriate lapse adjustments would reduce these totals. He suggested that companies wishing to do a modest amount of controlled financing of agents should consider the merits of this system.

He felt that smaller companies cannot justifiably develop statistics merely on the hope that they would be found interesting or useful. He said that the Postal Life of New York and some other small companies make an annual study of the persistency rates by individual general agency. This evaluates the quality of business in the agency and permits discussion of the experience of a specific general agent in terms of the ratio to the over-all company average.

He thought that analysis of the production of individual agencies by type of policy would not be especially illuminating, but the average premium written, which can be derived from the usual monthly production report for the agency, is probably a more satisfactory measure of effectiveness. He remarked that development of agency unit expense rates is unlikely to be useful because results would differ by area, need, and attitudes of a heterogeneous group. He felt that effective agency department supervision rather than additional statistics would be more helpful to a general agent who is unable to live within the expenses provided by formula. With respect to a study of mortality rates by individual general agents he thought this would be indefensible on account of insufficient exposure and number of deaths and that review and post-mortem underwriting of claims is far more effective for both judging the agency and educating the general agent. However, his company is conducting an investigation of mortality by grouping agencies into subdivisions large enough to produce results with some statistical validity in order to analyze differences between agencies operating in metropolitan areas and those operating in smaller communities, agencies specializing in surplus-brokerage business and those with relatively more full-time characteristics. It is intended to develop the mortality experience by class of soliciting agents who are full-time with their company only, agents who are part-time with their company only, general insurance brokers, full-time representatives of other companies who have placed only surplus business with them, and so forth.

MISS GERTRUDE A. SCHLACHTER described the studies of lapse rates by branch office which the Colonial Life has been making for some time. Both Notice Ordinary and Monthly Debit Ordinary lapse rates are calculated by using the two year lapse rate formula adopted by the Life Insurance Agency Management Association. For Weekly Premium business an over-all rate expressed as the number of cents per $100 of debit in force is used. She said that a study of these rates for a number of years gave convincing evidence that local management has a great influence on persistency. Some branches had consistently good records year after year and upon transfer to poor areas managers from branches with good records took their good lapse rates with them. Therefore the company embarked on an educational program, one step being to make part of each manager's compensation depend on his branch lapse rates, thus making the managers lapse conscious. She revealed that the company added to its home office supervisory staff a new position with the title of Conservation Director to devise and carry out this educational program. A man with field experience both as an agent and as an assistant manager filled this post and after the groundwork was completed the job became one of maintaining vigilance, traveling from branch to branch to examine conservation problems peculiar to various areas and concentrating attention on branches with unusually high lapse rates. She stated that a corps of home office inspectors are also used as trouble shooters in branches with poor lapse records. While these inspectors normally do post-issue inspections, in some branches they have been interviewing persons who have lapsed policies in an effort to determine cause of lapse. While lapses remained higher than desirable, the level in other companies made even higher lapse rates seem possible had the steps described not been taken.