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In this issue...

"Leadership to Successfully Navigate the Great Resignation," by Jason Bogart, Deep Customer Connections

The following article, written by Jason Bogart, provides insights into attracting and retaining talent:

https://deepcc.com/2022/05/10/leadership-to-successfully-navigate-the-great-resignation/

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$1 Trillion Surplus

In 2021, according to A.M. Best, the U.S. property & casualty industry grew its surplus to exceed $1 trillion for the first time. That seems like quite a bell weather moment and yet I have not seen any huge headlines touting this landmark achievement.

Now, not all carriers grew their surplus. The insurance industry is an industry of carriers that have plenty of surplus and carriers that really do not have enough from a perspective of a "going concern having much of a future perspective." One carrier by itself possesses about 25% of the entire industry's surplus according to the A.M. Best numbers. The rich get richer and the not so well run...

The headlines that I do see often advertise $100 million in losses, or even a cat causing a $1 billion loss, or even the $3 billion in anticipated aviation losses from the war in Ukraine (those losses are at least partially international). $1 billion is a lot of money, but $1 billion relative to $1 trillion is a little tiny drop in the bucket.

Policyholder surplus grew $100 billion last year. $1 billion in losses is only 1% of the surplus growth!

$1 billion in losses is only 0.1% of all surplus, just in the U.S alone. $1 billion is a rounding error.
If you hear of a carrier whining about surplus issues, keep these numbers in mind.

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E&O Tips

One of the latest innovations in the marketplace are forms provided by wholesale brokers. HOWEVER, it seems some of these brokers are giving the impression that they are the carrier. I see this in cyber, flood, wildland fire, HOA's, and other lines.

As a retail agent, you MUST LIST THE ACTUAL CARRIER on the application. You cannot correctly complete an application stating the broker is the market. The broker does not have a license as a carrier. The carrier must be on the application. For example, I have seen agents make major E&O mistakes by listing the broker as the cyber carrier.

To make things more difficult, one such broker advised they do not disclose the carrier until the policy is written. This is flat out unethical, and I encourage you to avoid doing business with any wholesalers that take this position. Some of these markets are admitted and some are surplus lines. YOU MUST KNOW this point at least before providing a quote because your quote/proposal should identify whether the actual carrier is admitted or surplus lines. Some of these brokers use both admitted and non-admitted markets.

Do your due diligence with these new markets. If something seems too good to be true it usually is too good to be true. Some of these markets are truly providing innovation and others, well, what they are offer is too good to be true. Always list the actual carrier on your applications!

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Are Insurance Rates Legitimate?

I was talking to a friend with extensive insurance industry experience ranging from underwriting to actuarial to system design and he asked this question. "Are insurance rates legitimate?"

Subsequently I was talking to a carrier executive who expressed his frustration with a competitor who lost billions (yes -- literally billions) over the last ten years because his company insisted on pricing that at least makes a modicum of profit, but as a result lost business to another carrier that is willing to lose billions. Out of frustration, his question was "How can the competitor's rates be legitimate when they lose so much money every year?"

Another friend of mine who works outside the industry was offered a homeowners quote of around 40% less than any other quote he received. He called for advice. The carrier primarily writes (now wrote) business along the Gulf Coast and had expanded to the west. My impression was they expanded to show

regulators and rating companies their concentration of risk was being diluted, but also, primarily, to put a bunch of premiums on the books to offset their losses on the Gulf Coast. When a single carrier's rates are 40% less than the market and is new to the market, rarely are they so smart that they can breakeven at such discounted rates.

Another example is when a consumer provides the capital (RRG's and reciprocals) but is insufficiently aware of what this really means. The insurance agreement allows the management team to keep a large percentage of the premium for managing the carrier even if the carrier goes insolvent. The numbers closely resemble the private equity model of 2%/20%.

The insurance industry is extremely competitive. According to A.M. Best, around 950 P&C carriers write business in the U.S. The number seems to fluctuate between 900 and 1,000 as so many new companies are created every year. This does not include all the subsidiary carriers, these are the mother ships so there is a lot of competition. Carriers do not charge 40% extra just because competition is lacking!

One of the most important reasons insurance regulation exists is because in bygone days, or maybe not bygone days, carriers would charge too little. Executives and shareholders might make plenty of money and when claims hit, the carrier would go bust leaving policyholders bare. Over time, consumer regulation has become more prominent whereby regulators have focused on keeping insurance rates down. This has resulted in allowing carriers to charge too little and so far, mainstream insolvency has not occurred, so a sense of confidence has arisen.

In 2021, by a rough count, the number of P&C insolvencies has increased along the Gulf Coast and West Coast. It is possible those companies charged enough but simply did not have the capital. Charging enough and then leaving the money in the bank, as surplus, is the boring and simple strategy to remaining solvent.

When a carrier does not go insolvent but continually loses money, are the regulators really looking out for the consumer or are they facilitating a marketplace whereby carriers that charge legitimate rates slowly lose market share? In this scenario, does the carrier become too big to fail?

A different angle is why should strong carriers write business in a state when that state allows weak carriers' underpricing accounts to exist? The weak carriers lose business and then when they become insolvent, the admitted carriers are taxed extra to pay for those insolvencies.

Insurance is not like other products where loss leader strategy makes sense for the public. For public safety, rates need to generate enough profit to sustain surplus. When a carrier regularly loses so much money that their surplus deteriorates, are their rates legitimate? If the only thing keeping that carrier in the market is low rates because their products and claims services are marginal, it prevents other carriers with better products and claims services from being more substantive. Is the public really benefiting?

Neither I nor most of my clients can really do much about the regulators' perspective on this point, no matter how important. I know the executives from well capitalized carriers with whom I have spoken are quite frustrated on this point because they feel they are being punished for being prudent -- and they are. But it is what it is.

Many carrier executives express frustration at what can be done when agents and brokers do not even make a legitimate attempt to sell quality. An agent has a choice between two carriers. Carrier A is charging legitimate rates, has higher quality claims service, and better forms. Carrier B's rates are 15% less, claims service is poor, and the forms are average at best. Agents will sell that lower rate almost every time because it is the easier sale, not the better sale.

An old rule of thumb exists that agents should be able to sell a 10% higher price for quality if they are any good at sales. That is a good rule of thumb. 15% is a challenge and 20% may be insurmountable especially if the carriers are all A- rated or better. This is the crux of the matter. Is the job of insurance commissioners to find a way that claims are paid no matter the means or is it their job to ensure carriers' rates are reasonable and not underpriced to the point the carrier cannot establish the surplus required to see it through even moderate catastrophes? The damage to legitimate carriers trying to do right by society is material if that is the case, and ultimately their desire to write business in these states is diminished. They can deploy their capital elsewhere.

If the former is the case, keep allowing new carriers to form without adequate capital and pricing that is materially less than the market without legitimate justification of underwriting prowess that justifies lower rates, while acknowledging and telegraphing to the industry that either the state or the legitimate carriers will pick up the bill. If the latter is the case, regulate rates so that rates are legitimate to a profit.

To head off the argument that rates are legitimate and the carriers' underwriting is just incompetent, which happens too, then how is the public served by such incomparably horrible underwriting? It is not. The carrier must increase rates or otherwise raise capital, or best yet, fix their underwriting. If the rates are 20%-40% less than market, making the case that it is an underwriting problem becomes a difficult proposition bordering on inanity.

To head off the argument that scale is required, force the carrier to define, "scale." Next, establish the surplus. I saw that a few carriers had established $25 million in surplus for fires and floods on homeowners policies. The fires hit California. The average price of a home in California is in excess of $500,000. They have the surplus to insure 50 homes, hopefully geographically spread far and wide.

Surplus includes reinsurance. But $25 million is not scale when 50 or fewer homes can be insured (fewer than 50 homes because adding contents and additional living expenses at Coverage A's of $500,000, means total fire losses are likely close to $1 million and therefore, maybe only 25 houses can legitimately be insured).

Interestingly though, from what I have seen their rates are low.

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Ivory Towers and Reality

A few months prior to initially drafting this article, a semi-famous economist, Janos Kornai, died. He was famous for explaining why socialistic economies, which are heavily planned economies, do not work. He was also famous for making the connection between the failures of planned economies and the failures of businesses with too much capital or political capital protection.

I found his analysis as to why planned economies fail, proven to be correct time and time again, to be at least partially applicable to easy money in capitalistic societies. His analysis showed that companies favored by socialistic economies had no need to fear loss as the state would continue to prop them up.

This lack of risk encouraged lack of financial discipline which enabled massive over building, a focus on the wrong industries, bad products, bad service, and political, but very powerful, idiots running companies all to the injury of their employees, consumers, and ultimately even the state.

No matter what the experts in the Ivory Towers think they can plan, if they do not consider human greed, hubris, incompetency and the need for survival, those plans will not work. The experts never think this

part through as they think they are generally too smart to need to make that consideration.

What is the difference between the socialist planners with their five-year plans and a world where the right salesperson convinces private (and often government because most private equity money comes from government protected pension funds) equity and venture capital that losses do not matter and to just keeping giving them the money? How many firms have you seen that did not try to hide the fact they did not know how to make a profit and did not care?

Take away the decisions of the capital contributor, whether it be the state or a pension fund funneled through private equity and if the receiver has so much capital that financial discipline is unnecessary, why should anyone expect a different outcome from that experienced by socialistic economies? If you flood the economy with so much money that the consequences of bad decisions are mitigated or mooted, why expect any different outcome, much less a good outcome?

The knee jerk reaction of the experts in Ivory Towers is that the free market will fix it through the invisible hand, but that only works if the government does not manipulate the invisible hand. I look at insurance companies that have never made a profit with no indication whatsoever that they will ever make a profit, but their capitalization exceeds that of much better run firms. The main reason they are even allowed to exist is because they have convinced investors to give them so much money they can continue running losses while maintaining adequate surplus to please regulators. The damage to the industry is that well-run companies are damaged and the consumer and economy do not get anything solid in return. The same result happens in socialistic economies when the government favors one company over a completely independent company.

Too much of anything is bad. Just ask your grandmother. Folklore's advantage over Ivory Tower wisdom is that folklore is embedded with reality, including human vices and foibles.

Most grandmothers, at least historically, did not occupy Ivory Towers but they knew more about reality than those residing there. The fact is capitalist governments have decided to sponsor certain industries and even certain companies through their monetary policies. Simply by not stating this is what they are doing does not mean they are not doing it, though they prefer that people not notice. It is what it is.

What does everyone else do to counter these powerful forces? Look at what the opponents possess. They have more capital than you can possibly imagine relative to their actual size. They have incredible salespeople with more charisma than their capital. You, even if you are Travelers Insurance which is a well-run company, are not going to beat them on either count.

Then they have great marketing, although this feature is less equally distributed. Sometimes the marketing consists of slideshows of what they hope to build someday, but nothing works yet. Sometimes they are not quite ethical (you mean I need a license for that?).

In fairness, not every company has boatloads of cash and/or overflowing pockets of charisma.

Competing against those that do have money and charisma is hard. Focus on what the businesses favored by the state do not have. What don't they have? What they may not possess is a viable business or a business built on the need to put enough other businesses out of business to make their business viable. Sometimes with such large balance sheets, they are just going through the motions until they can buy competitors.

What else don't they have? They don't have the ability to make connections at a local, human level. They don't have the ability to educate their clients about the coverages they really need. They usually don't have the ability to connect with clients who care about buying the right coverage. I saw a press release recently from one showing their average premium per personal lines client as about $250. Halfway decent

agents selling to clients who care generate $250 COMMISSION per client. People who care tend to not be as attracted to the seemingly simple answers as those who do not care. People who don't care about quality until after the fact correlate closely to people who seek easy solutions without question. Give them some snake oil and tell them it will cure whatever problem they have, and the odds are good they will drink it, especially if the snake oil has a cache' name related to green, technology, fast money, or is politically correct.

Another key is to not get distracted. Do the basics real world style really, really well. Two straightforward variables make a massive difference. The first is to fix your operations. Carriers in particular seem to have significant operational issues. They simply don't run with enough consistency and cannot adequately track what is happening internally which is increasing their costs unnecessarily. Charismatic leaders, especially those with big balance sheets, never worry about expenses until the last moment. Expenses are beneath their ego. To beat them, you must focus on efficiency to decrease your expenses while not being cheap.

It is a war of attrition. How do you beat someone with a big balance sheet that has a lousy business model? You must make your balance sheet last longer. The only possible ways to do this are to raise capital and/or become more efficient so that your bank account outlasts your opponent's. Period. Lowering costs without sacrificing quality virtually always wins if enough scale exists.

An additional key is to sell to one client at a time and sell the right coverages. I don't think most agents will beat many of the new providers in mass. Slop and slop go well together. To pretend to sell quality while not understanding coverages and exposures is a sham. Therefore, education levels must increase significantly. As a really simple example, I see that 90%+ of experienced producers and CSRs do not understand or appreciate the full scale of how ordinance and law coverage works, and how the throw-in amounts are almost never going to be sufficient in a major loss. Most do not really understand how ITV's work or should work (and this goes for carriers too, maybe even more so). These are quite basic coverage level factors. If the failure rate is this high on basic level coverages, what is the failure rate for complex coverages?

The Ivory Tower experts are betting billions of pension fund monies that not caring about customers and not building quality operations is a winning bet. They have put all their money on black. Too much money with too little care for expenses is dangerous. Will you take advantage of them?

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What Insurtech is Really About

Much Insurtech is about data that enables cross-sales. The example that follows is from ANT, the ginormous Chinese financial company/insurance company that, for those unfamiliar with ANT, is also a payment system. They (and all big data users) are constantly checking data for correlations. With massive computing power, one does not have to be a statistical genius anymore to theorize about relationships.

Just dump the data into sophisticated (and expensive) analytical software run by powerful computers, and let the software find the correlations. ANT discovered that women who wore skinny jeans broke their phones more often. Whether this was from their jeans being too tight or the pockets not actually being designed to hold phones was a moot point. They discovered this because the data showed a high correlation between skinny jean purchases and new phone purchases/phone repair charges. So, ANT began selling these women phone insurance.

I am not sure how many different Insurtech press releases I have read that promised that this firm or that firm now had software that could time the sale of ancillary insurance purchases perfectly based on some factors discovered by that firm's algorithms. This may be one reason Pet Insurance is catching fire.

I have no doubt some of this will work. Such technology provides great solutions to consumers who are not sophisticated, educated, or bright enough to realize their pockets are not designed to hold phones.

Making consumers think they need a product when they do not or creating a financial service of convenience that does not really fit the consumer's need is an exciting trick. The sellers get to think they are doing a great service and the consumer thinks they are getting a great service. This is what happens when consumers lack education -- something the industry has failed miserably to provide.

The industry for that matter is not emphasizing education for people selling insurance either. Uneducated agents are relics, expensive relics, because the computing systems are more powerful and with scale, far cheaper and they don't complain to their employers.

If one is ethical, and ethical is defined as working with clients to sell them the coverage they need for their exposures rather than opportunistic selling (i.e., specific, but definitely not all algorithm selling), which means educating clients as to what their exposures really are, then this technology is not the central point of your future. As an agent, how you sell and how you are paid will definitely change and you will need far better data than you have collected in the past, but your future will be bright.

The reason is that a conversation with a client regarding what their exposures really are and helping them discover their exposures, remains the best method for assisting clients to buy the coverages they truly need. You get more data in a conversation. People need better pockets, not insurance for their phones. They need the right coverage for their lives because one cannot create any other pocket to hold them securely.

Mike Edwards, a retired coverage guru with whom I had the opportunity to travel for a full week once, would say, "Selling insurance isn't the same as the clerk at a drive-up window asking, 'Would you like fries with that?'" ANT has shown that cross-selling today really is more like cross-selling French fries and hamburgers -- but only relative to small insurance policies. The proof does not exist that cross-selling in this manner for large sales exists. The best way to do this is by analogue, by talking to your client and learning their needs.

Insurtech is currently mostly focused on very small commercial and low limit personal lines accounts. Another advantage this target market possesses from the sellers' perspective is that the buyers have even less insurance knowledge than normal. Agents have heard small contractors say they only want insurance so they can provide a certificate a quadrillion times. These contractors truly, at least when buying, do not care about the insurance itself. They could not care less about the coverage. Agents trying to help, trying to educate clients as to why they should care eventually just give up. They give the client the best policy they can or they tell them to buy from the agent down the road. However, for Insurtech, these are good candidates because the buyers do not care and do not know the difference. This makes them even better candidates for cross-selling.

Again, large scale cross-selling insurance works when taking advantage of uneducated consumers and/or uncaring consumers. Scaling cross-selling, even personal lines, at a high-quality level remains problematic for many reasons. One simple reason is a carrier may have a great form for one line but not the other line.

The differences in cell phone forms is not likely to be important. The difference in a quality commercial auto form and a GL form, that is totally different. Even the difference between a carrier's homeowners form and auto coverage is often too wide. Even if the forms are close, are the rates for both close?

If the rates are good and the forms are good, are the underwriters onboard?

The best way for agents to cross-sell is to sit down with their clients, learn about their clients' needs and exposures, and then offer them good coverage solutions. The best tool is a coverage checklist or an exposure checklist. These tools are usually recommended for E&O protection but my clients who use them well also happen to cross-sell much more insurance. Competition is less for agents using this tool because it requires solid coverage knowledge, and most agents will never make the effort to learn coverages deeply. Furthermore, this is not massively scalable, so it is not of interest to Insurtechs.

Another competitive advantage and reason why it is not scalable is because the clients who want the right coverage and who will simultaneously give agents the time to offer the right coverages are not likely to be the same consumers who insist on putting their phones in jean pockets not designed to hold phones.

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When You're Wrong Even When You're Just Asking a Question

Everyone has likely heard the saying, "Damned if you do and damned if you don't." Insurance agents who try to do the right thing (not the sloppy, incompetent agents who are only interested in making a sale, even if it is the wrong sale) are so often caught between these rocks and hard places. They try to advise their client they truly need additional coverage and lose the sale because that is not what the client wanted to hear and some other agent offered them a lower price without mentioning the coverage was inadequate.

Conscientious agents cannot bring themselves to offer inadequate coverage, but they need to eat too. Life is hard for do-gooders.

One of the plagues of the industry is the decades long effort to make insurance "simple" by ignoring the "coverage" aspects. The commoditization of a complex product that technically cannot be commoditized happens because the people selling insurance and the people buying insurance do not understand its complexity. The result is a pretend dumbing down that only serves those entities who sell insurance by cutting corners.

Just how hard it is to sell insurance effectively is exemplified when a client protests not only against good recommendations, but even when the agent asks deep questions. An extremely common situation involves insurable interests. An agent friend of mine was asked by his family to insure a vacation home owned by different members of his extended family. The question was, "Who has an insurable interest in this home?" The response was, "What difference does that make? The whole extended family owns it and we're all good people so there will never be a problem." It is my understanding that the family then told their own family member-agent that if he would not sell them the policy as requested, they would find an agent who would.

If your own family does not appreciate a perfectly reasonable question from a family member they supposedly trust (who knows -- maybe they don't trust him), what are you going to do? I had the same issue happen in my own family when I asked a family member why they were insuring another family member's vehicle when they had no insurable interest in that vehicle. Their response was, "My agent told me it was cheaper that way." When I asked for their agent's name so I could turn the agent in to the insurance department, I became *persona non grata* rather than the incompetent agent.

No wonder so many people just give in and sell clients whatever they ask for, even if it is wrong, and then hope for the best relative to E&O claims. Sometimes ignorance is indeed bliss.

But what if you are one of those people who just cannot bring yourself to just give in to harmful client demands? First, we should eliminate mind altering drugs and alcohol as potential solutions to the pain you will bear. Next you will need to find the daily fortitude required when you buck the system of clients, peers, competitors, and sometimes carriers who will nudge and push you to go along with the flow. Where you find that fortitude will vary by person, maybe daily.

One consistent solution I have seen agents discover is deep coverage knowledge shared in the form of questions rather than statements. Rather than asking about insurable interests, begin by asking more oblique open-ended questions designed to gauge how much someone wants solid coverage. Then play along with whichever path they choose relative to the strength of the coverage they want versus the time and money they are willing to spend with you. The deeper your coverage knowledge, the better you will be able to ask the right questions.

Then as you are closing the sale, give them three options. Give them a high-quality coverage option, a medium quality option, and a low quality option with a cheap price tag (not to the point of deception or saying insurable interest does not matter). If they choose low quality, have them sign off in writing that they are knowingly choosing a low-quality solution.

This takes the burden off your back to convince clients to buy the right coverage and when they don't, you feel bad that you failed to get them to make the right decision. They may still not make the right decision, but they are signing off on it. Your responsibility ends and you have the client's signature to prove it. You can sleep well and move on to the next client who will make a better decision.

Many of my clients have also discovered that by requiring a client to sign off and willingly walking away from a sale if it comes to that, causes clients to respect the agent's recommendations to a greater extent resulting in the client buying more coverage. These are truly win-win situations for both parties.

Otherwise, trying to convince people you are attempting to help who get upset with you just for asking totally reasonable questions, much less offering only one quote with really good coverages (coverages other agents are at least quietly suggesting are unnecessary), is one tough road to travel. The messaging in the industry is that insurance is a commodity and is simply too much to overcome with the vast majority of clients and prospects.

The commoditization of insurance really amounts to, "Buy insurance from us and then just trust us that your claim will be paid." Then, when a claim occurs that is not covered, carriers and agents both hide behind the legal castle wall of, "The insured has a duty to read and understand their policy." It is a system that benefits those people who truly do not care about their clients more than they care about making the next sale.

Rise above the cacophony by knowing your coverages, learn how to ask the right questions that do not send people running to competitors, and offer multiple quotes with sign-offs. I am confident this is a better solution than beating your head against a wall, having family members resent you, and even drinking too much.

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