Personally Speaking

Personal Lines Section Quarterly

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CPCU SOCIETY

Loyalty vs. Distribution

by Aaron J. Stein, CPCU, CFP

Let's start with the fact that I am an independent agent, third generation, and so there will be a perspective to this editorial, although I will try to keep it to a minimum. I should also add that old fashioned ethics and values that I hold will also add a certain slant to my writing. I find that part unfortunate, since it means that some ideas that used to be pretty firmly entrenched in the way people treated each other are no longer considered important.

We have read in the first issue of this newsletter, as well as all over ours and every other business' trade publications, that distribution is king. Of course, in the broad sense, it is, and I embrace that. I firmly believe that I will still be in business in the coming era of financial services reform because I know who my customers are and are not, how to provide them with products they need, and how to keep them satisfied for an extended period. Of course, the independent agency system is not now nor has it ever been the only successful method of distribution and has coexisted with others for years. In addition, the way business is conducted in everything from retail to medical practice is changing rapidly, and nobody can continue as we have in the past.

What concerns me both from a personal ethical perspective as well as a business one is how we will maintain customer loyalty. Our business in particular has always been one where you cannot make a profit if your turnover rate is too high. The cost of acquisition, with necessary inspections, time spent completing applications and following up, and so forth, is such that we need to keep our customers for several years before profitability really sets in.

Unfortunately, this is becoming more and more difficult and in some ways we are creating the problem ourselves. Web-based distribution models such as those used by major booksellers and other retailers have yet to produce a profit—and it is getting more difficult, not less. Things like "shopping bots"—automated programs to find the best price on an item—are keeping them from building loyal customer bases and charging high enough prices to cover costs. Of course this is not directly applicable to us but if we train customers to surf the web and check prices each time their policy renews, at what point will price competition drive the legitimate profit out of the insurance product? Price competition is good for the public in terms of taking excess profit out of any product, but can an industry that depends on adequate reserves for unknown future events really base its sales from year to year on having the absolute lowest prices?

One major carrier who has for years been in both the independent agency as well as direct distribution systems recently signed two deals— one to market directly at point of sale to purchasers of one major brand of cars, another to market on the web to people using one well-known portal. In the meantime, that same car manufacturer announced that it will begin direct marketing on the web, thus competing with its salespeople, who they had just announced had to start selling insurance as well as cars! A large captive writer, who had recently purchased a well-known independent agent carrier, has announced that it will be changing all its captive agents to independent contractors and focusing on web sales. These examples, of course, are only two of many.

Additionally, all the fighting today is only about car insurance. Nobody wants to touch home coverage due to profitability problems in recent years. The notion of "account selling"—building loyalty and retention by taking care of all your clients' needs—has gone out the window. But with the competitiveness in the auto market, whoever is "stuck" writing home coverage is certainly not going to miss the chance to try to sell auto coverage as well. Banks and securities firms are counting on this "account" approach to go to their existing customers and sell additional products. However, what will happen if they tell them that they will gladly sell them car insurance but not home, or some other similar scenario? Leaving doors open invites higher turnover and constant struggles to replace business that leaves. In addition, it shows that only lip service is being paid to the notion of "taking care of the customer."

As you can tell by now, my purpose in writing this was not to answer questions, but rather to raise them. And there is no one right answer; otherwise everybody would drive the same kind of car and read the same books. However, there are some overall considerations here that need to be kept in mind as our industry goes through its biggest changes ever. ■

Aaron J. Stein, CPCU, CFP, is president of Norton & Siegel Inc., an independent insurance agency, in Babylon, NY. He has been with this company since 1978, and prior generations of his family have been principals of the agency since 1927. Stein, editor of this newsletter, is also active in Rotary International and will be a district governor in 2001.

What's the Score —A New Perspective on Risk Evaluation . . . or Who Lives in that House?

by Dale M. Halon, CPCU, CIC

These are all common features of company underwriting guidelines and/or rating criteria for personal property coverage. From my time spent underwriting personal insurance and reviewing claim files, I cannot remember one time when the age of the dwelling, its value, its degree of fire protection, or that it was built out of wood frame or bricks caused homeowners loss. Houses do not take care of themselves, they do not jump out and land on people (only witches), and they do not spontaneously combust.

Why does loss experience differ from one home to the next with similar property characteristics? How can a hailstorm do so much damage to one house and little to the house next door? How can one family own a German shepherd that's sweeter than its grandmother while another family has one that eats mail delivery persons for lunch? Why does the loss experience differ in each of these situations? How do agents know potentially profitable business from less profitable business? The fact is, people cause losses, not the property itself. Why don't we consider who is living in the house as a risk variable?

Well, okay, we do look at loss history. While that information is good, valuable underwriting information, there are many homes that have had no losses during the experience period in loss history databases. Or, the loss information does not give the details behind why and how the loss occurred. A property could reflect one loss with a weather-related loss— a good piece of underwriting background to consider. But what does that tell us about the likelihood of future losses.

The credit history gives us the only look we have into the inner fabric of the only individual that has control over that property. The credit report is a track record of a person's willingness to accept the responsibility he or she signed up for when agreeing to accept the obligation. There are similar obligations an insured has on his or her end of the bargain of the insurance policy. If a person is consistent at upholding the level of assumed obligations in one area, would it not make sense that he or she would do likewise for an insurance relationship?

It is that very thought that has allowed me to make the intuitive connection between one's credit history and one's insurance behavior. We all have control of our own loss potential of our personal property. We either chose to spend the money to fix or maintain a part of our property or use the resources on something else. We either keep our premises safe for visitors or we have a lax attitude. We either report losses with absolute truth of the items damaged and their value, or we try to make a profit. We either take personal responsibility for a problem or we try to pawn it off on a third party.

Those using credit or credit scoring for underwriting or pricing, including agents, should try to use this added information to help them get a better understanding of the risk presented to them. The effect credit has on insurance performance is not hocus-pocus, as some might say. If it were hocus-pocus, would actuaries and product managers be so adamant about using it?

> *"The fact is, people cause losses, not the property itself."*

Credit scoring models, because of their mathematical derivation, are above the heads of most of us (most notably the author). Is that a reason to dispute their value? How many people can explain how a microwave oven works? Do you not use one because of this lack of understanding? What about how e-mail works? The key to remember about the models is that they are built to predict insurance performance and not whether or not someone will pay his or her bills. The scores are a simple rank ordering of a potential loss ratio and not necessarily a view of credit worthiness.

It is with these ideas for which we need to have an open mind on credit and credit scoring. There is a value here that can help us as underwriters and insurance professionals who price insurance to achieve the most accurate segmentation of risk.

We have so few tools in personal property underwriting to understand what might really affect the outcome of whether we make a profit or not. This new one has proven itself over and over and does have a logical place in the risk analysis process. ■

Dale M. Halon, CPCU, CIC, is associate vice president at Doubleclick Inc. He recently joined Doubleclick from ChoicePoint, a leading provider and integrator of intelligent information used in business acquisition, underwriting, and claims handling. His Doubleclick responsibilities include marketing, direct sales, and consultation to insurance companies for focused customer acquisition programs.

Halon is a graduate of the University of Massachusetts at Amherst (1977), majoring in communication studies. Prior to joining Doubleclick and ChoicePoint, he was with Fair, Isaac and Company, working with insurance companies to implement predictive models and credit data into their insurance processes. He had previously worked in the insurance industry in key underwriting and product development positions for 17 years.

He has addressed numerous industry groups on predictive models, databases, and underwriting tools and marketing data. He has published articles for insurance trade publications and industry groups on predictive modeling and the use of consumer credit in insurance.

SYMPOSIUM

Road Rage, Aggressive Drivers, and Teen Drivers:

Impact on the Insurance Industry and Tips for Avoiding Disaster

Date and Location

February 23, 2000
USAA
9800 Fredericksburg Road
San Antonio, TX 78288
(210) 498-2211

Registration Information

Fee: **$60 for nonmembers**
$55 for CPCU Society members
$50 for Society section members

- **Registration Fee**
  The registration fee includes a refreshment break, one CE certificate, and all handout materials.
- **Cancellations**
  Your registration fee will be refunded if notification is received at the Society two weeks prior to the symposium. After that date, registrations are transferable, upon request, to other programs for one year following this symposium.
  A non-refundable processing fee of $20 will be deducted from all refunds and requests for symposium changes.
- **Tax Deductions**
  Tax deductions for educational expenses are permitted in accordance with current U.S. Treasury regulations.

Symposium Speaker

Clyde "Clint" Gillespie, CPCU, LUTCF, state manager for product and pricing for Virginia, Maryland, and Delaware, Keystone Insurance Companies, Philadelphia, PA.

Gillespie is the founder and chairman of the pilot Personal Lines Section of the CPCU Society and secretary of the CPCU Society's Philadelphia Chapter. He holds undergraduate degrees from California State University (public administration) and Los Angeles Harbor College (business administration/accounting). With more than 20 years of experience in both law enforcement and the insurance industry, Gillespie brings a unique perspective to the subject of traffic safety and the impact of "problem drivers."

The views and opinions of the speaker are his own and not necessarily shared by the officers, members, or staff of the CPCU Society.

Continuing Education Credits and Certificates

The CPCU Society has filed this symposium for the following continuing education credits:

- CPD—3
- CE credits in the following state:
  - TX (3)

This course may be rejected and no credit given.

Registration fee includes one CE certificate. Additional certificates are available as follows:

$4 each .....CPCU member ***and*** CPD Qualified
$8 each .....CPCU member ***not*** CPD Qualified
$12 each .....Nonmember

To Register
Call the CPCU Society's Member Resource Center at (800) 932-2728.

Auto Injuries Less Severe, IRC Study Reveals

Study Also Shows Fewer Claimants Are Hiring Attorneys

by Karen Burger, CPCU, CPIW

Editor's Note:

This information was reprinted from a press release issued by the American Institute for CPCU and the Insurance Institute of America.

The Insurance Research Council (IRC) is a division of the American Institute for CPCU and the Insurance Institute of America. The Institutes are independent, nonprofit organizations dedicated to providing educational programs, professional certification, and research for the property and casualty insurance business. The IRC provides timely and reliable research to all parties involved in public policy issues affecting insurance companies and their customers. The IRC does not lobby or advocate legislative positions. It is supported by leading property and casualty organizations.

Good news for America's drivers: auto crashes are resulting in fewer severe injuries. At the same time, a lower proportion of injury claims involve lawyer representation.

These conclusions are based on the analysis of more than 87,000 auto injury claims by the Insurance Research Council (IRC) in its new study, Injuries in Auto Accidents: An Analysis of Auto Insurance Claims. The IRC conducted similar studies in 1977, 1987, and 1992.

The new IRC study (based on 1997 claim information, the most recent available) shows fewer severe injuries, along with a decrease in hospitalization and disabilities associated with auto injuries compared to 1992 and earlier levels.

More good news: average claim payouts under bodily injury liability and personal injury protection declined, reversing a 15-year trend of increases in the major injury coverages.

These findings help explain why auto insurance rates have reversed their upward trend and are actually lower (based on U.S. Bureau of Labor Statistics data), according to Elizabeth A. Sprinkel, senior vice president of IRC.

The study also tracked the level of attorney involvement and its impact on auto injury claims. It found:

- The percentage of injury claims with attorney representation decreased from 46 to 41 percent nationally. It was down significantly in several states, including California, Maryland, Virginia, and Ohio.
- Claimants without attorneys netted more dollars than claimants with attorneys, a major shift since 1992. Although claimants with attorneys received substantially higher gross payments, they lost an average of 32 percent to legal fees. They also had higher economic losses, primarily medical expenses, to be covered by their claim settlement.
- Bodily injury claimants with attorney representation averaged a net payment of $708 compared to an average net payment of $1,449 to claimants without attorneys. This is a major change from 1992, when claimants with attorney representation netted $101 more than did claimants without attorneys.
- Claimants without attorney representation received payments more quickly than did claimants with attorneys.

Commenting on the results of the IRC's new study, Sprinkel said, "After years of escalating injury claim frequency and costs and increasing attorney involvement in the injury claim settlement process, these trends have stabilized and, in some cases, reversed. Efforts by insurers, state and federal legislators, consumer groups, auto manufacturers, and others to reduce injuries and costs associated with auto crashes seem to be having a positive effect."

Sprinkel credited the following factors for helping reverse the trends of more serious injuries and higher claim costs during the 1980s and early 1990s:

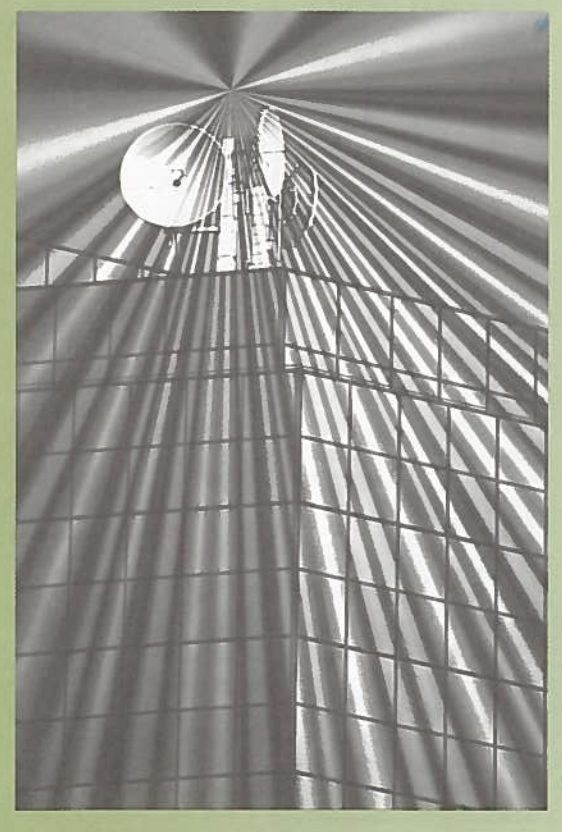
- seat belt use laws
- better seat belt, air bag, and passenger compartment design
- campaigns against drinking and driving
- intensified fraud investigation
- insurer investment in technology to streamline claims review

The improvement in claims costs has contributed to lower auto insurance rates, according to Sprinkel.

"Statistics from the government (U.S. Bureau of Labor Statistics) show that auto insurance rates declined in 1998 for the first time in 25 years," Sprinkel said. "Nationally, auto insurance rates dropped less than one percent. But some major markets such as California, New York, Florida, and Massachusetts had more dramatic decreases."

The IRC study, Injuries in Auto Accidents: An Analysis of Auto Insurance Claims, is based primarily on an in-depth review of 87,193 private passenger auto injury claims that closed during the spring and summer of 1997. The study focuses on claims paid under the five principal injury coverages: bodily injury liability, personal injury protection, uninsured motorist, underinsured motorist, and medical payments. Forty leading insurers, representing 67 percent of the private passenger automobile market in the United States, participated in the study.

For more detailed information on the study's methodology and findings, contact Elizabeth Sprinkel by phone at (610) 644-2212, ext. 7568; by fax at (610) 640-5388; or by e-mail at sprinkel@cpcuiia.org. Or visit the IRC's web site at www.ircweb.org. Copies of the study are available at $35 each in the United States ($50 elsewhere) postpaid from the Insurance Research Council, 718 Providence Rd., Malvern, PA 19355-0725. Phone: (610) 644-2212, ext. 7569, fax: (610) 640-5388. ■



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a live satellite broadcast on

Financial Services Modernization
May 25, 2000

Details will be available soon.
Please watch your mail.

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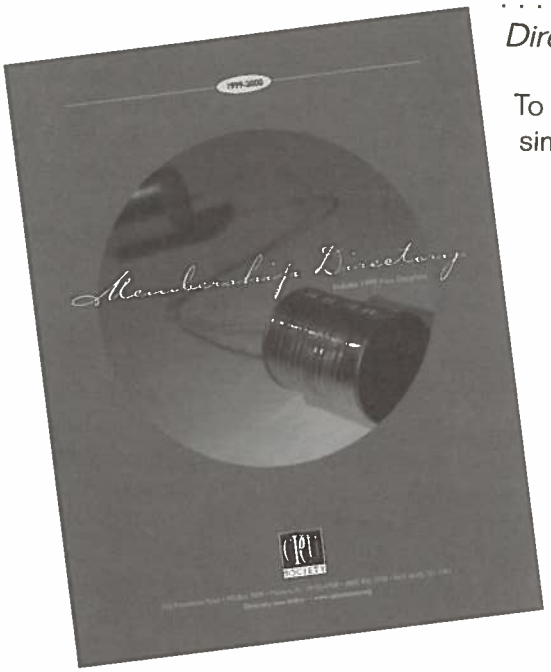
Good News . . .



. . . the CPCU Society's *Membership Directory* is now online!

To access this interactive directory, simply

- visit the Society's web site at www.cpcusociety.org
- enter through "Member and Chapter Services," and
- follow instructions for "Membership Online"

If you would like to receive a paper copy of the directory, which includes a listing of section members by individual section, please contact the Member Resource Center at (800) 932-2728.

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