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In This Issue...

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"The reason most people never reach their goals is that they don't define them, or ever seriously consider them as believable or achievable. Winners can tell you where they are going, what they plan to do along the way, and who will be sharing the adventure with them."

-Dennis Waitley

You Have to Serve Somebody

This title is taken from the most recent Nobel Laureate for Literature, Bob Dylan, and his song, "Gotta Serve Somebody". When the song recently came on the radio after having heard it innumerable times, I was surprised my brain even registered it was playing. I was even more surprised when the lyrics spoke to me as never before. I knew Dylan had written the song during an intense religious period and previously I had always listened with that in mind.

But this time, when he melodiously croaked "that you have to serve somebody," it dawned on me this need not have anything to do with religion and neither is it voluntary. He is right: You have to serve somebody, or more directly, you MUST serve somebody. Serving is not optional behavior. You are going to serve somebody willingly or not. Sometimes that person being served is one's own ego or one's own insecurities. "Someone" is not necessarily someone else. The song, when it finally struck a chord, no pun intended, is about the need for self-awareness. Part of that self-awareness is understanding the world, even if you own your own insurance agency or you are the CEO of an insurance company, does not actually revolve around you. You revolve around something and understanding who it is that you are serving and whether that is the best entity to serve, is the song's aim.

Dylan was again ahead of his time as one of the current management consultant popular themes is servant leadership. Without becoming too esoteric or too far reaching, the idea that serving someone is optional is a key reason so many agents and other executives are struggling. A great many small businesses, including agency owners, are owners because they did not and do not want a boss. This hypothesis has been tested and proven true. It is a fact regardless of whether a person knows this cognitively. From this perspective, the idea is they did not want to serve anyone above them and by owning a business no one would be above them.

To own a business foundationally based upon avoiding oversight means running away. Running away means no goal. Running away, if painted, would picture a man running away from the viewer and running into infinity. No end point exists and no goal exists in infinity.

I have known many agency owners running to infinity. Realizing one is running toward infinity rather than living the dream of being one's own boss is supremely complex and difficult. Dylan's song greatly aids this understanding in that everyone is serving someone and running to infinity is not a solution.

The question to ask is: Who are you working to benefit today, tomorrow, next month, and this year? Are you specifically trying to help them, make them wealthier, smarter, healthier, happier? Even if it is yourself you are trying to make happier, that is who you are serving. That is your reason to be, colloquially, "raison d'etre" as the French say so well. Not having a stated purpose is an abyss, an attempt to not serve. A purpose creates life. Going through the motions of living just because you are your own boss is not a reason to go forward and build life.

A reason to be inherently means serving someone, some purpose and with that purpose comes passion. Agencies are about sales. Insurance sales are about making life safer and better for the agency's clients (assuming the sale is not made by a narcissist). Identifying a purpose then should be easy for many people. State that purpose and build, with all your heart, your agency's culture around who you will serve. Life will become easier. Clarity of your future and the security clarity provides will be yours.

Running infinitely ultimately means running out of energy because a person cannot find enough infinite fuel. Serving a purpose generates infinite fuel. The only question then is this: Who will you serve with a passion?

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Save Money by Insuring Multiple Construction Projects in One Policy, by Chris Harris

Most of us are trained to understand that if we buy in bulk we get a better deal. The same is true with insuring construction projects. This article discusses General Liability Insurance for "for-sale" residential projects as well as more traditional construction projects such as commercial, industrial or government.

There are three primary ways to insured construction projects.

Single entity insurance is where each contractor purchases their own insurance policy; generally primary and excess insurance limits.

This way, each contractor is responsible for it's own insurance choices. Each contractor is able to choose how much risk it wishes to retain, how much policy limits to purchase and how much premium to pay. From a carrier perspective, the insurance company retains the maximum amount of underwriting control over each risk.

With so many insurance policies from different insurance companies on a project, there is the risk of inconsistency in coverage between each contractor's policy and what it may respond to. Also, although a great deal of money is spent by each contractor protecting against risk, an owner or GC still does not have dedicated limits for their project from each contractor. With so many insurance carriers potentially participating in a lawsuit (especially where construction defects are alleged), litigation costs can also quickly escalate from "finger pointing" between the various insurers.

An **OCIP** (Owners Controlled Insurance Policy) involves the owner buying a single insurance policy from a single insurance company covering all contractors general liability exposure on the Owner's project. Many OCIP's involve both general liability and workers compensation, and the benefits are similar, but for this article, we will focus on General Liability only policies.

Owners have the primary legal and operational risk on each project. Under an OCIP, the owner is in control of its insurance needs, including choice of carrier, retentions and quality of coverage. By having a direct relationship with the insurance company at the underwriting stage, the owner can work collaboratively with the insurance company to allocate risk transfer at a price that is acceptable to them as well as maintain a good relationship during the life of the exposure. This is particularly important with for-sale residential insurance which tends to be much more complex with long term exposures.

From a contractor's point of view, an OCIP allows smaller general contractors and subcontractors to work on larger and more diverse projects where either they don't have coverage under their single entity policy or the insurance costs make it prohibitive to do so.

A CCIP (Contractors Controlled Insurance Policy) is very similar to an OCIP in that it covers all the contractors on a project in a single policy. The difference is the general contractor is in control of the purchasing of insurance.

The major benefit of a CCIP is that the general contractor usually has a larger volume of work, may have a better risk profile to present to underwriters and in turn maybe rewarded by better insurance premiums, terms and conditions.

Other CCIP benefits include:

- CCIP's lower the overall cost of insurance on a project by aggregating all the risk in one policy, usually with higher limits. This cost savings is ultimately passed along to the owner.
- General contractor cannot shield their financial and hard assets from a lawsuit by using an LLC (as project owners can), therefore, they tend to have a bigger internal infrastructure to manage risk. GC's tend to be more sensitive to the quality of an insurance program.
- With one carrier insuring all contractors there is a unified defense that can drastically reduce litigation costs and improve a GC's overall loss experience.

However, owners have a broader and longer liability exposure than general contractors; therefore if the owner is named on a CCIP, the CCIP and thus the general contractor's loss records are exposed to broader liabilities.

There is one additional nuance to the above, the **Rolling Program**.

Rolling Programs (or Master Programs) involve combining several projects into a single master insurance policy. This can be done as either an OCIP or CCIP and depending upon the type of construction can either be shared limits for all projects or per project limits.

There are two main benefits of a Rolling program:

- Insurance carriers will generally give a far better insurance rate for larger volumes of construction values; therefore, the greater the volume being committed to a program, the better the premium.

- It is significantly less expensive to combine projects by purchasing more vertical insurance rather than buying several insurance policies at primary insurance rates. By purchasing excess insurance, the buyer is purchasing a single "tower" of insurance at less expensive rates. For example, instead of buying three primary policies at $4 million each and paying a premium for each, the buyer purchases $12 million in vertical limits in a single insurance tower. The rates per thousand of construction value for $8 million in excess over the primary $4 million can be as little as half of the primary rates.

However, there are also several challenges:

- One has to have a good understanding of how many projects/total construction costs will be going into the policy and will start and finish within the construction period of the insurance policy. In order to give a lower premium per thousand of construction values, the insurance carrier must have a guarantee of how much premium will be earned. While there are cash flow devices possible, by the end of the policy, a certain amount of premium must be paid. If a buyer is unrealistic in their project projection, they could end up paying a minimum premium for something that they do not build.
- Although there are benefits to all participants for all the projects sharing the limits of the single tower of insurance, all owners and contractors, as well as lenders and investors, must be comfortable with the other exposures under the rolling program and their consistency of risk management efforts. Of course if per project limits are provided this is a non-issue.
- Combining all of the exposure under the control of the owner or general contractor through the contracting process is a difficult task in practice even if strong risk management processes are present.

The benefits and challenges of the above type of insurance program(s) require a relationship with an insurance carrier that has the ability to understand and underwrite a more complex product. There are only a few insurance carriers that understand these complexities and will be able to help the buyer make

the right structural decisions. Although written submissions are a useful tool for certain types of business, at Cove Programs, we meet in person with each insured and their retail insurance broker to fully explore these factors and find a program structure that works best for each buyer The best structure for the buyer will generally result in a better risk for the insurance carrier.

About the Author:
Chris Harris joined Cove Programs in 2014 and has over 20 years US Casualty and A&H experience in the Lloyd's insurance market. He was Divisional Director for Pioneer Wholesale where he managed the in-house binder/delegated authority facilities, including Professional Liability and AD&D. Prior to Pioneer, Chris worked for Jansen & Hastings Intermediaries, a Lloyd's cover holder and program manager underwriting a variety of products including construction liability, AD&D and property. Chris has broking and underwriting experience within the Lloyd's and London Company marketplace and also held underwriting and management positions at several MGAs in the US.

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Carrier Commoditization

Much, much ink or more accurately, bits and bytes, have been expended lamenting the commoditization of insurance from a sales perspective, i.e., at the retail level. Mostly overlooked is another commoditization: Carrier Contracts. It used to be that many companies' contracts, and the products, pricing, underwriting, and claims services inherent to possessing such a contract, were prized. These contracts conveyed true competitive advantages. But with only a couple of general exceptions and slightly more niche carriers, companies have blown it. Their contracts convey no extra value. On any given day a producer many value one company over another but tomorrow will be another story.

More than 5,000 agencies new to the independent agency system have been formed in the last seven or eight years. 90% have access to every contract they need. The only requirement is they have a license (and frankly, I'm not sure some companies even check this based on the Zenefits debacle). Agencies with $200,000 - $300,000 PREMIUM have more carriers than traditional agencies with a million dollars plus commissions have. Carriers are handing out contracts like politicians handing out promises. Many pretend not to be doing so, some have convinced themselves they are not doing so and others do not flinch from admitting they do. By some estimates, 38,000 independent agencies exist. I saw one company had appointed 30,000. It is hard to imagine why the other 8,000 don't have a contract too.

Companies may say they give out contracts easily because agents always want more just like any addict. If no true exclusivity exists, no extra, if any, value in a particular carrier's contract exists. A commodity has been created. One agency is replaceable with another agency because they are offering the same product. They are interchangeable. Maybe not risk for risk, but they are overall interchangeable. The companies

then have commoditized their contracts so they might just be better off at this point going ahead and giving a contract to every agency. Just get it over with it.

This leads to the second phenomenal mistake carriers have made (assuming they want to create proprietary value): A few carriers who tried to remain more exclusive remained too loyal to their agents. Too many of their agents made too much money without doing enough work. They took advantage of the exclusivity of the contract and began taking life easy. They quit working hard to grow. When newer, hungrier agencies called the company for a contract, the company declined saying they already had an agency in that area. The company remained loyal to a lazy agency instead of appointing a hungry new agency. Loyalty is a two-way street and companies have mistakenly allowed many of their agencies to take advantage of them with no return loyalty in the form of actually continuing to grow.

These companies' problems are exacerbated when their incumbent agents sell to serial acquirers or join an aggregator. The company is no longer protecting a select agent. It is no longer working with a particular agency owner possessing limited resources. Suddenly other agents see the bigger shop or aggregator with the same contract they have cherished for years endangering their livelihoods. (I know rules are in place with some companies to protect a location and the contract cannot be used by other branches/related entities of the serial acquirer/aggregator but even IF this works, which is questionable, perception is reality.)

So now we have a situation where every Tom, Dick, Harry, Sally, Rita and Joan have every carrier contract their hearts' desire. What is left? Now comes the hammer or 2X4: The large players ask for, nay – demand, more money. I have read several articles recently where interviewed carrier CEO's subtly, but strongly, allude to these demands. Their points boil down to, "We can't afford, in this low interest rate environment, to pay higher commission without an offset. More volume is not an offset in this environment."

A commodity is a commodity. Carriers have made their beds. Now comes the time to lie in them. The solution they should have chosen (again assuming they don't want to be a commodity), and time exists for a few still, is that rather than letting middlemen foster new small agencies into existence with every contract and staying true to lazy agents living off rich contingencies and high quality contracts, carriers should foster new agents. Instead of demanding $X or not even returning inquiries from new agents, companies should have made new agencies a strategic focal point.

The strategy keeps agents from acquiring too much power while simultaneously increasing growth. These 5,000+ agents have effectively written all new business in the last five years. Look at it this way. If these agents average $1,000,000 premium in total (which is the bare minimum since this is only approximately $120,000 in commission which in turn is the bare minimum for an agency to keep its doors open), then 5,000 times $1,000,000 equals $5 billion. Total net premium written growth, excluding reinsurance, has increased, per A.M. Best, $74.1 billion. At an average annual rate increase of 3%, $70.4 billion of the increase is nothing but rate increases.

Companies have to make a decision whether they want to pay extra to powerful and large consolidators and aggregators possibly for no extra growth or better loss ratios, or invest in new agencies that are hungry to grow. If you want my services to develop a strategy to defeat commoditization of carrier contracts, whether by determining how to develop new agencies or build other key value propositions, contact me today.

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Clusters are Not All the Same

I've been asked many times to assist in creating "cluster" agreements. Mostly, agents want to learn to do it right but a large enough proportion of agency owners, company people, and agent association personnel seem to refuse to acknowledge more than one kind of "cluster" exists. When they ask me to help or even discuss the subject, and I ask them to first advise what kind of cluster they want or want to discuss, some get so mad or frustrated they fire me or hang up. It is as though they think I'm trying to get more money from them or something.

Companies also do not understand the true differences either (or don't care) or the implications to the agencies and themselves.

Given this environment, a short synopsis of the major "cluster" structures is worthwhile. This is not all encompassing because more forms of clusters exist than Baskin-Robbins has ice cream flavors. What follows are common "cluster" structures.

First though a caveat: Not all clusters are clusters and not all aggregators are aggregators and not all agencies are truly agencies. Some agencies are really aggregators and clusters.

1. Partial ownership organizations. Several forms exist but in general, a central "ship" owns some portion of all the other ships. For example, the central organization owns 40% each of ten other agencies. The ownership is supported by the correct kinds of legal agreements (hopefully). The percentages may be majority or minority positions. The "other" ships cannot sell themselves, typically, without offering the first right of refusal to the central ship. The central ship owns the company contracts and receives the contingency bonuses directly.

   In this sense, this form is not that different from a regular agency with multiple shareholders except that a key shareholder of the other ships is a corporation that owns assets (company contracts) upon which the other ships are highly dependent. When done well, this form offers much more stability than other "cluster" forms but it obviously comes at a price of some ownership. When it is done poorly, and some of these have horrendous legal agreements, the result is a huge legal payday for multiple attorneys.

   Agencies may pay a fee to the central ship but most don't charge a fee unless they are providing additional services such as training, IT services, staffing, etc. Depending on the structure, the central ship may provide E&O or E&O may be the responsibility of the other ships. Usually these programs are designed well, but definitely not always, so that responsibility for E&O is clear. Additionally, accounting for trust monies is usually crystal clear.

   A key point though is this is not a cluster, nor an aggregator, nor a franchisor. This is a separate category.

2. Franchises. Historically, insurance agency franchises have been a complete disaster. The Brooke fiasco is possibly the best example (Google "Brooke Corp FBI" for an interesting read if you're not familiar). A few new franchisors have begun doing business and they are true franchisors. They use franchising agreements and have to (or are supposed to) comply with franchiser regulations in each state. Franchise agreements have their pluses and minuses.

   Franchise organizations are not aggregators or clusters either. The franchisor typically owns the company agreements. The franchisees typically access carriers through their franchisor but they own their own business 100%. Restrictions may exist on the sale of their agencies but the franchisee owns 100%. These organizations may share branding and a franchise fee is typical. E&O responsibility and accounting for trust monies, when the franchise agreement is

well written, are usually clear but often no accountability for the franchisor exists (Google Brooke again).

3. Cluster That Owns Company Contracts. A key issue with so many cluster contracts is they are written by attorneys who have no idea how to write a cluster contract assisted by agents who have no idea what needs to be included in cluster contracts. The blind leading the blind is a valid judgment.

   Assuming the contract is written well, the cluster owns the company contracts, and the members give up the right and the value of owning their own individual company contracts, then the cluster is responsible for collecting all trust monies and verifying that all members are consistently in trust. The other members accept joint and several liability for all members' trust monies. One cannot truly get around this key point and yet almost no cluster contracts I've read address it appropriately. The cluster does not own any portion of their members' agencies. They may or may not have a first right of refusal on the sale of member agencies. The cluster must vote to accept or eject members. The cluster may share contingency income in any manner they desire, preferably though by a prearranged memorialized formula.

4. Cluster That Does Not Own Company Contracts. Some clusters decide to aggregate their volume but individual members continue to own their own contracts. This requires permission from the companies to aggregate volume and in situations where members do not represent the same company, that company must give permission for "sharing" their contract.

   Assuming the companies give permission to combine volumes and share contracts while leaving the contracts in the individual agency names, the same risks exists as with clusters that own company contracts except the risks are much higher because this structure is inherently less stable. The "flexibility" this form provides is really just extra instability. A member can pick up and leave, taking a key contract with them. A member "owning" a particular contract might decide to keep the entire contingency. The member owning the contract almost definitely becomes responsible for all other agencies "sharing" their contract relative to trust monies. Rarely do these organizations ever have any kind of coherent carrier relationship strategy creating considerable frustration for companies.

5. Aggregators. Aggregators are really just a larger form of the latter cluster form with central administration for which they charge a fee. Sometimes agencies access contracts the aggregator owns and sometimes they own their own depending on the specific aggregator. Sometimes it is a combination of both. How contingencies are addressed varies. Aggregators and clusters, particularly unstable clusters, are particularly good for agencies that have no real plans to grow. They just want a place to hide and not lose company contracts for too little volume and no growth.

In my experience, the more formal and restrictive the form, the better the results. This is like anything else. When accountability exists, people perform. When accountability does not exist, people get lazy and take advantage of others. The performance disparity is so significant that it is time to not generalize. People tend to make mistakes and overlook opportunities when they generalize. Many agencies also underestimate their risks when they generalize and get sloppy by not understanding the differences and by accepting poor legal documents (among others, Google Brooke again but they are not alone, just the most headlines). Joining one of these organizations is definitely a caveat emptor situation.

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Chris Burand is president and owner of Burand & Associates, LLC, a management consulting firm that has been specializing in the property/casualty insurance industry since 1992. Burand is recognized as a leading

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Burand has more than 25 years' experience. He is a featured speaker across the continent at more than 300 conventions and educational programs. He has written for numerous industry publications including *Insurance Journal*, *American Agent & Broker*, and *National Underwriter*. He also publishes *Burand's Insurance Agency Adviser* for independent insurance agents.

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