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In this issue...

It is often easy to avoid reading or hearing from sources who have different agendas, such as plaintiff attorneys. One of the best methods for building proactive discussions though is to listen and read the perspectives of those with different agendas.

In the insurance world, some people look at United Policyholders as an entity with a different, even opposing, agenda because they are an advocate for policyholders, especially it seems to me, homeowners. However, they have one of the best insurance websites I've ever seen.

Much of their website material belongs on the sites of truly professional agencies because the information provided, forms provided, help provided to policyholders is exactly what your clients want from you. Take a look when you have time: https://uphelp.org/.

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Underinsured Concerns

"Majority Of Home And Auto Policyholders Are Concerned They Are Underinsured"

This is the headline based on polling in mid-October 2022. HUB sponsored the research and kudos to them for doing so. I encourage everyone to find the survey results and read them. One key point is that 59% of policyholders are concerned their insurance coverage will not be adequate in the event of a claim. The other 41% are delusional, ignorant of their lack of coverage, or extremely overconfident.

About 100% of policyholders are materially under-insured. I have audited tens of thousands of personal insurance files, conducted hundreds of E&O audits, and taught hundreds of insurance coverage classes. The vast majority of agents do not offer adequate coverage due to some combination of the agent not knowing coverage options well enough to offer their clients the needed coverages and/or because they think (and often know) that their clients will not buy adequate coverage so why waste their breath?

Another reason is the discombobulated use and quality of Replacement Cost Estimates. Another far more nefarious reason, a dirty secret that those who work in the trenches daily know, is that some carriers and agents purposely, quite purposely, sell inadequate coverage because that is how they get to a lower rate. The most common example is, "You only need to insure your home to 80%..."

Rationalize that thought process all you want, but it is bad advice and the number one reason it is used is to convince a homeowner that the agent is looking out for them by finding a way to cut their premium. Premiums are lower because coverage is lower, i.e. inadequate.

A friend asked me recently about the barrier agents encounter when offering better coverage. The barrier is that the insured does not want to pay more for insurance. They do not want to pay more and in fact, they do not want to pay anything because virtually no one but arsonists want to buy insurance. Insureds buy the base amount because they are forced to do so and think that is all they need. No one has ever taken the time to explain to them why and what buying more than the minimum, which is almost always inadequate, will do for them. Consumers will not buy the additional coverage they need if no one ever takes the time to explain the coverage and the benefits of that coverage to them. No magical osmosis will happen. No transcendental thought process exists when it comes to insurance knowledge.

Offer the coverage and if the consumer does not understand it, explain it. Let them make an educated decision. Let them make a decision regarding the trade off between paying more for the coverage they need or self-insuring. Is $50 more in premium worth it to them to avoid becoming their own insurance company?

[Back to Top]

What happens when a Network/Cluster fails?

I have a suspicion that a few networks/clusters are made up of some combination of fraud, Ponzi schemes, and nice people who are incompetent but well-meaning, all of which results in their members losing their shirts.

Other than calling a few agents from a list provided by the network to ask about the existing member's experience, few agency owners, if any, conduct due diligence before joining a network. Has it been a good experience? Have they been treated fairly? Have they gained anything of value? Great questions and there is value in asking such questions. However, those questions are entirely inadequate due diligence questions. A clue as to why comes from within some networks' agreements -- the anti-disparagement clause. In other words, the members CANNOT say anything negative or they will violate their contract!

Therefore, begin your due diligence by reviewing the contract and providing an expert with a copy to read. Give it to a high-quality attorney and someone who knows a lot about clusters/networks to evaluate. This IS NOT a Do-It-Yourself project. With no offense to any reader, most agency owners are not qualified to competently evaluate networks on your own. An expert who has read dozens of these contracts involving dozens of different networks has insight and knowledge you do not possess. They know what should be, but may not be, in the contract you are considering. They know why a franchise agreement is not necessarily the same thing as a regular network agreement. They know the differences between accounting systems and how specific accounting systems will leave members holding the proverbial bag if or when the network goes bankrupt.

Experts understand, even when the contract does not clearly state it, that all liabilities are joint and several. If a small agency signs onto an agreement with joint and several liabilities, that small agency now has responsibility for the liabilities of an agency member 10 times to 100 times larger!

At the very least, if you are going to evaluate one of the contracts on your own, write out how you will get OUT OF the network, per the contract, if you decide you need to get out. Read the contract all the way through for all the hidden clauses that limit your ability more than the exit clause itself limits your options. I recently read a contract that looked like it had an easy exit clause. However, the noncompete portion was an entirely different story.

It is a serious mistake to think all networks are financially solid. I sounded this warning to many of my clients prior to Brooke failing and feel bad about how many small agency owners lost everything when that failure occurred. Doing what I do, I hear rumors and know some are certainly true about other networks that are currently financially problematic.

What happens then when a network fails? A whole lot depends on the contract. If it is a franchise contract, the dominoes will fall in one direction. If it is a joint ownership contract, the dominoes will fall in another direction. The dominoes will fall, but the direction depends on the contract and the exact nature of the failure.

One place to always look is at the ownership of the carrier contracts. If the network owns the carrier contracts and the network fails because it fails to pay the carriers' premiums, then typically the carrier becomes the owner of all the expirations -- yours included. How would that feel to work so hard and lose everything because you did business with "nice" people but failed to read the contract or request audited financial statements?

Audited financial statements should be readily handed to every potential network member. 99.9% of members and prospective members never request audited financial statements before joining a network (and the same goes if you are selling your agency and some of the price is in the buyer's stock). When you join a network, at some level or another, you are putting your future into someone else's hands. If they are not financially solvent, then in the worst case scenario, immediately after signing the contract you have transferred ownership of your expirations to the carriers. Carrier contracts and many state laws make it clear that the failure to abide by state trust measures means the transfer of expiration ownership is automatic. This is true in every state. For those of you who think your state is not a "trust" state -- YOU ARE WRONG. All states are trust states, but a few prohibit commingling of funds. Do not confuse the two laws. Both involve trust monies, but they deal with very different aspects of trust monies.

Another possibility for loss is if the network borrows money using its members as collateral. What are its members' collateral? Expirations and the cash on your balance sheets. Some networks have more than likely borrowed quite a sum.

When the last large franchise failed, dozens of agents who thought they could continue to service their clients discovered they could not because their contracts were with the network that the carriers pulled. If the agent could service the client, they were not going to be paid because the contract was with the network so carriers could not directly pay the agent. The tangled mess just grew larger from there.

From an insurance regulator's perspective and from a carrier's perspective, the goal is the continuation of coverage for the insured. However, if an agent cannot service a client because of difficulties due to a network, then regulators and carriers will seek a fast, immediate, clean solution. This sometimes means they will cut a deal with a high quality, friendly distributor and sign over all the business, without any attached liabilities, on a blanket broker-of-record basis. The local retail agent may or may not be completely cut out and if so, will be left holding an empty bag of promises -- and also some share of the liabilities.

Carriers are not in a position to immediately reappoint 100 agencies overnight, each with their own code, which is what they would need to do if the agencies were to retain the markets. A better solution for the carrier is to turn the entire mess over to a larger network capable of managing the problem. The larger network may not necessarily want the problem because depending on geographies, they may upset their existing members by creating new members who may not meet their qualifications. Also, the potential new members will not be able to review and sign the applicable contracts immediately, and so on and so forth. The agents who signed up for the wrong network are likely stuck.

It is a funny thing about networks. Some of the networks that catch the most grief about being run in a less friendly manner, i.e. members have to meet certain criteria and have tight contracts (as opposed to having tight contracts where it is an open secret that no one pays any attention to enforcement), are the "bad" guys. The looser networks advertise that you can still run your business however you like, and so on and so forth. Those kinds of promises should be red flags because when you join forces under joint contracts and everyone still gets to operate everything any which way they want, someone is going to get hurt. When you operate jointly under any contract, you give up some freedoms and to believe or promise otherwise is idiocy and/or disingenuous.

Quite honestly, the better networks are typically the ones that tell you what freedoms you will lose and what you will gain in return. The better networks are the ones who manage themselves carefully and audit members to be sure they are in compliance. The better networks are run as solid businesses rather than some combination of a good ole boys' network where everyone makes more money without contributing any real value, with everyone pretending a price is not being paid for pretending there is not a cost for everything. I used to ask agency owners which of these two models they preferred and too many answered they preferred to take their chances on incompetency and Ponzi schemes. "They felt lucky!" So I'll ask, do you feel that lucky?

[Back to Top]

Why Complex is Better

The property insurance situation in some coastal states is in a crisis. With another big hail season and/or fire season, much of the South and Intermountain West may see the property market freeze. For those in more northern climates, the property market is comparatively much better.

Many of these problems are self-inflicted and the solutions can be provided by the industry. The self-inflicted part is that the industry has made too much insurance look easy, and appearances in this case are absolutely deceiving. If anyone thinks anything about insurance coverage is easy, they should not be trusted.

A Business Owners Policy (BOP) is a great example of making insurance coverage seem easy. The net result is agents don't think they need to understand what they are selling because the BOP has made thinking irrelevant and has placed the focus on the price. Just focus on the price. One simple example of why hard thinking is mandatory when selling even BOPS involves the business income portion. Somewhere between 98% and 99% of the producers I meet think the Actual Loss Sustained (ALS) clause is perfect because it pays for the actual loss sustained. This thought process simply proves they don't know what they are selling.

ALS does not unconditionally pay for the actual loss sustained. It has many limitations. A quite pertinent limitation is the time factor. With all the supply chain disruptions we're experiencing, many businesses will exceed the time factors built into the ALS coverage. ALS only provides coverage for actual losses sustained within specific parameters. Failure to understand those limitations is a major failure of professional advice.

Homeowners is another example. Insurance people are not at a high enough percentage thinking through the coverage issues. I once completed a study of the basic ISO homeowners endorsements (25 or so <u>basic</u> ISO endorsements exist) to calculate how many combinations of coverage exist at a most basic level. The number was around 33.5 million. Nothing simple exists when 33.5 million coverage combinations exist, but insureds do not know this, and I find most agency people don't either. To slap a commodity label on an HO-3 with the same set of endorsements and treat every homeowner to the same coverage, only differentiating the Coverage A amounts, is to neglect the actual coverages most homeowners actually need. This also fails to provide many homeowners with options provided by more robust policies.

A client told me we should go back to the days of professionalism when agents had to build the policy. A history lesson is that agents literally had to find different coverages and build a complete homeowners policy. They had to integrate the coverages. All the ease and packaging taken for granted today did not exist.

Going back to that model, without going backwards, is probably the solution to many of the property insurance issues that exist today. People that do not know what they are selling and don't stop to think through the coverages people actually need, will not understand the following. For all the others, a solution is to split property coverages apart into different policies. Many aspects of property are not difficult to insure. Fire coverage is a major issue in California, but it is not an issue in Little Rock. In Little Rock, wind and hail are the major issues, and these are not that important in California. So split the policies into two. One policy is for the easy coverages in that geography and the hard coverages are placed on another policy. These are Difference in Condition (DIC) policies. These policies have been in existence forever, but I find few people with less than twenty years of experience know anything about them. They've never seen anything but package this and package that.

A newer form of insurance is an elaborate DIC in many ways, and this is parametric insurance. Parametric insurance is in its infancy and many limits being offered are too small to be relevant, but large limits are being written for governmental entities.

The benefit is that to do this, agents must become more professional because they must know what they are doing. They must understand insurance and they must understand their clients' specific needs, not generic needs.

Is it more complicated? Absolutely. A homeowner might need a policy excluding wind/hail, a wind/hail policy, and a flood policy (or maybe an earthquake policy or both). They would need three policies and intuitively one would think this should all be wrapped into one. But that makes an inaccurate assumption because insurance carriers don't want to insure all the perils for which the insured needs coverage. What the insured needs and the market is willing to provide are two different things. Pretending to make insurance simple, with one policy where carriers are not interested in covering specific perils, is a huge mistake. Even now where wind/hail deductibles may be 10%+ in places and ACV on roofs over seven years, pretending to sell a simple policy only for the insured to discover a huge deductible after the fact, is a huge mistake. When carriers put those deductibles on property, they are not interested in insuring the peril/property. It is impressive in some cases they even try to find a meet-in-the-middle solution by offering limited coverage.

The property problem is unlikely to fix itself soon. Smart people willing to invest in complex solutions that are specific to their clients and their carriers, and other alternative markets, even DICs, is how an agent takes control of the situation. This is how you protect yourself and your clients, gaining a competitive advantage in the process.

Complex is better. Excessive simplification does not benefit clients. If all this is new to you and you are interested in learning more, I applaud you. Considerable resources, some dating back decades exist that you can read and study. The newer solutions are exciting and given how new the solutions are, quick search engine searches will generate tens of thousands of hits. The material exists from which to learn.

[Back to Top]

Property Loss: Climate Change or Building Codes?

I saw a headline stating that Florida building codes are at the root of Florida's property insurance problems. I doubt that building codes are the root of the problem, but are they a contributing factor?

Prior to Hurricane Andrew that wiped buildings clean of their foundations for miles, Florida's building codes were weak. Considerable angst was expressed among all concerned parties regarding the inadequacy of Florida's building codes. The state's politicians, to their credit then, worked with knowledgeable construction and engineering experts to develop much tougher building codes which, of course, increased building costs. From what I see and hear and based on the claims incurred, while no hurricane as destructive as Andrew has since struck Florida, the homes built to those new codes have generally withstood the storms.

Instituting even tougher building codes now could also help, but frankly, fixing the litigation issues in Florida are far more important.

Building codes, however, should not be ignored relative to climate change. A good portion of Miami is in visible danger as a consequence of rising waters. Tougher building codes could address the problem. However, a different coding issue is perhaps more important. Waters are rising because some of the land is sinking due to the over pumping of ground water which is a regulatory issue and a building code issue regarding the regulation of water sources. It is not a climate change issue.

In California, wildfires are not necessarily or even primarily a climate issue. Building codes are the issue. California acquiesced to builders who wanted to build homes close together. When the wildfires struck, the fire spread from home to home to home. The loss of so many homes is an apt illustration of not learning the lesson of the Great Chicago fire of 1871 and Mrs. O'Leary's cow. Build wood buildings next to each other, too closely, and when one goes up in flames, the others go too. The adequate spacing of buildings is important and fixing that issue does not require the population to stop burning fossil fuels.

Another example of a building code issue is that wood fences provide a trail for a fire to spread. That fix is simple enough. Override the homeowners association's rules and force metal fencing by outlawing wood fences. Leave the wood and save some trees in order to further mitigate climate change if that is of concern to insurance commissioners who worry about how climate change is a danger to the insurance industry.

Around 25 years ago in Colorado, shake shingles and cedar siding were banned in new construction within many wildfire zones. That code makes complete sense. It is a commonsense solution regardless of whether climate change is a factor in the wildfires.

Another wildfire issue is allowing grass to grow too tall in urban parks. When fire hits, it spreads rapidly through the tall, dry grass. Tall dry grass has always existed west of the Mississippi and has always caught fire. Historically, the grass was knocked down by grazing animals, whether buffalo or cows or both. Also, Indigenous people set fires to protect and cultivate the land. To pretend that tall grass fueled fires are a climate change issue is baloney. Mow or graze the grass.

Climate change is such a convenient excuse for incompetency and now COVID is being used as an excuse in the same way. I saw a report from a carrier stating their numbers were wrong because of COVID. I don't think people understand how ridiculous they sound when they use climate change or COVID as an excuse for the failure to use simple math and logic.

From an insurance coverage perspective, if regulators use common sense to address these problems, agents had better be aware of how inadequate most ordinance and law throw-in coverage is today. Rebuilding to new codes will cost far more than the 10% most carriers give away. In fact, if your local building codes have materially changed already, 10% is likely inadequate. Have this discussion with your insureds and offer them increased limits as they almost certainly need more coverage.

While it may take forever to address weak building codes and perhaps even longer to convince those who religiously believe that reversing climate change, rather than learning how to mitigate the impact of the inevitable, is the solution, you can build your organization and better protect your clients through basic risk management recommendations.

Suggest that your insureds use metal to build their fence, if allowed, install an underground electric fence, or use fire resistant materials. Or, clear ground around the house. Perhaps they should live where the municipality is not causing the land to sink or at least not allowing it to sink. They could move to a place where some space exists between buildings. If your insureds are planning upgrades to their homes, suggest that they use more fire resistant materials such as replacing their roof with metal roofing material. Metal may not be the homeowner's ideal material but at least you gave them great advice. If they live next to tall grass, and are not allowed to cut it, suggest they move or take extra precautions.

There is a house in southern California that survived a wildfire about 30 years ago. Dozens of homes all around that home burned to the ground, but not that house. The owner had taken precautions because he knew he could not control his neighbors' actions and his voice was not going to be heard by the local politicians or building department. I will bet that no one, upon rebuilding, followed his example.

You can lead a horse to water but you can't make it drink.

[Back to Top]

Practice, Practice, Practice

As a producer, do you practice?

I was in a situation the other day that I thought I could handle, but something unexpected happened and I was caught off guard. I now know what I would do differently going forward even though that particular situation will likely never occur again. I would practice.

This experience got me thinking about producers and how little they practice sales techniques. I have had the opportunity to work with quite a few ex-college athletes who transitioned into insurance. I always enjoy asking them how much work they put into their college performances. Then I like to ask how much work they put into their sales efforts. The differences are stark.

The two preparatory factors I focus upon are education and practice. Almost no material education occurs whereas when they were athletes, they were studying the sport, and other teams if applicable, for hours upon hours. As an athlete, they might spend as much time in one week studying as producers spend in an entire year on their education (and much more than some producers). Producers are selling extremely complex legal contracts designed to protect clients against life-changing financial losses. There are millions of these contracts given all the carriers and different versions and different endorsements, and so forth. To only spend the state minimum, even triple the state minimum, learning coverages is inadequate. It just makes sense that a professional practicing their art relative to selling a product with serious life affecting contracts would study more than a person who is an amateur playing a game.

The second factor is practice. I find almost no producers practice sales techniques. Practicing sales techniques mostly means role playing. I suppose some producers practice by going through the motions of one unsuccessful sale after another, because the failure to make the sale is at best, a practice session. Would it not make more sense to role play in a safe environment with people who can provide immediate constructive criticism, just like athletes have with their coaches?

The value of practice is significant, but what occurred to me in my case was that with practice I would have had muscle memory. In the middle of an intense sale process, having muscle memory is invaluable. Otherwise, the client will say something or do something unexpected and you will be thrown off-kilter. You will lose your momentum. The probability of losing the sale increases. In this industry people have always figured this was the value of experience.

Experience is in many ways, an elongated form of practice. A person can gain the benefits of decades of experience in less than half the time, maybe a tenth of the time, with enough practice. In other words, a person can learn what they need to know over a long period of time or they can accelerate their success by true practice. Having someone else throw out stupid questions which you would never have thought possible or sharing a key data point at the last second or advising that their goals have changed is great practice and results in being seamlessly prepared. It can make the difference between winning the sale and losing the sale and feeling horrible for weeks afterward.

Finding practice partners is really difficult for most producers. Most producers will not have people within the agency who have the ability and/or time to practice with them. This requires a third-party.

When you put the three parts together, you have professional level preparation. Traditional training in the insurance world is like reading a playbook the first day you are employed and expected to execute on the court immediately. Or if you are lucky, you at least get the playbook and time watching the equivalent of film before being expected to execute. No coach in their right mind would ever do this in sports. But we do it every day in this industry. It is a waste of time and money.

If you are interested in professional level preparation, our Three Dimensional Training® program creates practice during the education process on multiple levels so that when you go out to the real world, you are prepared and confident. To learn more, please visit BurandEducation.com.

[Back to Top]

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 consultant for agency valuations and helping agents increase profits and reduce the cost of sales. His services include: agency valuations/due diligence, producer compensation plans, expert witness services, E&O carrier approved E&O procedure reviews, and agency operation enhancement reviews. He also provides the acclaimed Contingency Contract Analysis® Service and has the largest database and knowledge of contingency contracts in the insurance industry.

Burand has more than 35 years' experience in the insurance industry. 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.

Burand is a member of the Institute of Business Appraisers and NACVA, a department head for the Independent Insurance Agents and Brokers of America's Virtual University, an instructor for Insurance Journal's Academy of Insurance, and a volunteer counselor for the Small Business Administration's SCORE program. Chris Burand is also a Certified Business Appraiser and certified E&O Auditor.

Burand & Associates, LLC is an advocate of agencies which constructively manage and improve their contingency contracts by learning how to negotiate and use their contingency contracts more effectively. We maintain that agents can achieve considerably better results without *ever* taking actions that are detrimental or disadvantageous to the insureds. We have ***never*** and would not ever recommend an agent or agency implement a policy or otherwise advocate increasing its contingency income ahead of the insureds' interests.
