Agency Perpetuation—A Company's Perspective
by Chris Burand

An independent insurance agency, from a company's perspective, is a salesperson. The agency is the person selling their product. The company needs and wants to know then, whether that salesperson is likely to still be selling insurance in one year, two, or ten. Whether an agency has a perpetuation plan largely determines whether the agency will still be selling insurance in five to ten years. Therefore, companies want their agencies to have perpetuation plans so they know who is most likely to still be selling insurance and with whom they should be contracting.

Some might argue that whether or not an agency has a perpetuation plan is the least important issue about whether an agency continues to sell the company's products. Indeed, over ten years, many problems can erupt to change relationships. However, two major changes are occurring in our industry today that make perpetuation plans extremely critical to companies. Both factors have caused many companies to make their contracts conditional upon agencies having perpetuation plans. Those factors are the average agency owner's age and the consolidation of independent insurance agencies.

First, the average independent insurance agency owner is approximately 58 years of age. The median age is not available but it is a fair assumption that approximately half of all owners are more than 58 years old. Therefore, approximately half of all agency owners are going to retire, try to retire or begin initiating their retirement in the next five years. As an agency owner, if you knew you were going to lose half your sales force in five years, would you start planning to strengthen your future? That is what companies are doing.

The companies realize most of their agencies will be changing ownership in the next five years and they are taking precautions to make those transactions as smooth as possible. By making sure agencies plan for their perpetuation, the companies can get to know the future owners, work with them, and build relationships. The company gains some certainty that upon the sale, their contract will not be severed and the agency's new owners will not ruin the agency. As an analogy, think about what happens when an insurance company gets a new CEO. Sometimes, the company suddenly changes direction leaving agents hanging. Insurance companies are trying to avoid having this happen to them.

Companies also know that agencies with perpetuation plans are more likely to survive. Without a plan, a great agency can waste to nothing in no time if an owner dies. I have seen this happen many times and as recently as last month. An agency owner dies without a perpetuation plan and by the time the agency is sold, nothing is left. The agency's companies have lost the business and the agency owner's family is left with nothing.

The second critical factor is agency consolidation. It is clear the number of independent insurance agencies is shrinking and will continue to do so. Since the number of people employed in the industry is not shrinking, most of the shrinkage is clearly due to agencies and banks buying other agencies. Hardly a week goes by where I am not involved with an agency valuation, calls from agents looking to buy other agencies, and agency perpetuation. The effect such shrinkage has on companies is twofold. First, they will want to contract with the buyers rather than the sellers of agencies. By contracting with the buyers, they are less likely to lose their contract. They are also more likely to write more business because they will have an opportunity to write the business of those companies that do lose their contracts.

For example, often when a large buyer who already represents plenty of companies buys an agency, they do not need the seller's company contracts. They can roll all the business to their current companies and desert the seller's companies.

Second, because fewer agencies will exist in the future, companies will become more dependent upon those agencies. Other distribution channels such as the Internet and toll-free phone numbers will also become more critical but agencies, in the foreseeable future, will remain companies' number one salesperson. Because companies will be more dependent on fewer agencies, they will work more closely with those agents. They will have more at risk and they will invest more in those agencies. Therefore, they will want to be sure those agencies are strong, stable, and will still be selling insurance in five or ten years.

These two forces: the huge proportion of agency owners that will be selling or preparing to sell in the next five years and the fewer agencies that will exist in the future make it extremely important for companies to contract only with those agencies with the most secure future. Otherwise, they may lose half their sales force and find themselves unable to get enough new quality appointments.

The industry is changing so fast that writing a perpetuation plan today when you are not planning to retire for five years may seem irrational. However, it takes five years to completely create and carry out an internal perpetuation plan! New people usually have to be hired and/or people have to be groomed to take on additional responsibilities. Future owners need to be prepared for ownership because ownership and management is very different from producing as an employee. Sometimes, there are no employees capable or desirable for buying the agency and an outside person must be hired and then prepared to become an owner. Employees also need to get used to having new people running the agency. Furthermore, financing will probably have to be arranged for the buyers and tax planning is a necessity for the sellers. Otherwise, a seller could pay half their proceeds in taxes depending on the situation. By beginning a perpetuation plan now, agency owners can make sure a buyer is in place with ability, experience, and money when they retire. Sure things can change over five years but if they do, the plan can be changed. Having started a plan, even if it must be changed, will always better situate the owner than not having a plan at all.

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