THE FIIA BANK INSURANCE WHITE PAPER - 1995

THE CRISIS IN LIFE INSURANCE

How To Solve It With Freedom Of Choice And Free Market Competition

BY

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FIIA

FINANCIAL INSTITUTIONS INSURANCE ASSOCIATION

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THE CRISIS IN LIFE INSURANCE –
HOW TO SOLVE IT WITH FREEDOM OF CHOICE
AND FREE-MARKET COMPETITION

by Michael D. White
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Copies are available from the Financial Institutions Insurance Association, 21 Tamal Vista Boulevard, Corte Madera, California 94925.

"It is to the interest of the private insurance industry to strive to provide adequate insurance protection to the public regardless of the medium of distribution."

\- DR. DAVIS W. GREGG, INSURANCE SCHOLAR AND PRESIDENT OF THE AMERICAN COLLEGE (1954-82)

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ABSTRACT/SUMMARY

The FIIA Bank Insurance White Paper 1995

The Crisis in Life Insurance – How To Solve It With Freedom of Choice and Free-Market Competition

The insurance industry has often claimed that the U.S. life insurance market is mature and saturated. This assertion is simply false. The market is, in fact, sorely under-served, and the United States is dangerously under- insured by the traditional life agency distribution system. Today, 40 percent of all Americans have no life insurance coverage, and 50 percent are under- insured.

The distribution of life insurance policies is heavily skewed to those with incomes over $75,000. Meanwhile, life insurance ownership among the middle and low-income segments of society has decreased substantially. Allowing all banks to sell insurance will provide consumers with greater access to the insurance market and enable them to more adequately meet their life insurance needs--needs which the traditional agency system is unable to meet.

In issuing "The Crisis in Life Insurance – How To Solve It With Freedom of Choice and Free-Market Competition," the Financial Institutions Insurance Association (FIIA) delineates the shortcomings and structural weaknesses of the traditional life insurance agency distribution system and demonstrates its inability to serve the entire consuming public. Section One of this position paper describes and documents the crisis in life insurance coverage and distribution.

Among the deficiencies *The FIIA Bank Insurance White Paper* exposes are:

1) The lack of widespread life insurance coverage among Americans (the crisis in life insurance).
2) The traditional agency system's emphasis on selling to the affluent (the crisis of exclusion).
3) The severe declines in agent recruitment, retention, survival and sales productivity (the crisis in productivity).
4) The inadequacy of agent service and the public's attitude toward it, including the high incidence of orphaned and lapsed policies (the crisis in confidence).

Section Two of *The White Paper* demonstrates that consumers want alternative sources when buying life insurance. New research shows that more than half the American people can legally buy their insurance from banks and that, in 1993, bank customers bought one-third of all individual annuities. Where at liberty, consumers exercise their freedom of choice to buy insurance through banks.

Section Two also sets forth the well-documented fact that bank insurance distribution does not impair bank safety and soundness. It debunks the myth created and proliferated by agent trade associations that the banking industry coerces consumers into buying insurance. And it shows that most big life insurance companies sell insurance through banks and other financial institutions.

Section Three of *The FIIA Bank Insurance White Paper* outlines a solution to the failure of traditional agency distribution to meet the nation's life insurance needs. A free-market system of insurance distribution is shown to offer greater benefits to consumers in terms of real choice in product selection, provider and service. Bank insurance powers produce competition, freedom of choice for consumers,

more insurance protection for Americans, more jobs, and greater economic activity and productivity. *The White Paper* introduces arguments in favor of bank insurance, including the facts that:

1) Effective competition is not “unfair competition,” nor does it constitute “unfair trade practices.”
2) Bank insurance is not unfair competition; it means free-market competition and consumer freedom of choice.
3) Freedom of competition affords opportunity and growth.
4) Competition and consumer choice ensure social and economic security.

The FIIA Bank Insurance White Paper concludes that freeing the insurance marketplace by expanding bank insurance powers will help solve America Is life insurance crisis. With uninsured Americans needing at least $5 trillion in life insurance coverage, there are plenty of sales to be made and many uninsured lives and families to be protected. One agent’s sale is not another agent’s loss. Therefore, competition in insurance distribution is not a zero-sum game. The broader the sale of insurance to the general public, the more capital is invested to create more wealth, expand the economy, and create more jobs and greater need for life insurance.

The life insurance industry’s own data document a crisis situation in life insurance coverage, distribution and agent productivity. Too few sellers result in too few people owning sufficient life insurance protection, proving the dictum that the public is never advantaged when marketplace protections are given to narrow interest groups.

Bank insurance is the reality in the global financial services marketplace, where banks, insurers and agents are free to compete. When the domestic marketplace for insurance products is fully opened to banks, the opportunity for economic growth at home will increase, and the public will be assured a greater and more enduring degree of economic freedom and security.

THE *CRISIS* IN LIFE INSURANCE

How To Solve It With Freedom of Choice and Free-Market Competition

BY

MICHAEL D. WHITE
Ph.D., CLU, ChFC

SECTION ONE:
THE CRISIS IN LIFE INSURANCE

All too frequently, an assertion comes to be understood as a "fact" when it is repeated enough times. Such is the case with the life insurance industry's repeated claim that the U.S. life insurance market is mature and saturated.[1] This assertion is made to open foreign markets and limit distribution outlets within the United States. But the claim is simply false. The U.S. life insurance market is neither mature nor saturated. Indeed, the market is sorely under-served and America is dangerously under-insured by the traditional agency distribution system.

> ***Today, 22 percent of all households and 40 percent of all Americans have no life insurance coverage.***

This white paper documents--with data derived from traditional life insurance industry sources--that too few consumers own life insurance primarily because access to life insurance is largely limited to the legislatively protected traditional insurance agency system. Making life insurance products available through banks and other outlets will expand the distribution of these products and improve consumers' ability to own them. Increased availability will end the crisis in life insurance coverage and enable individuals to be personally responsible for the financial well-being of their families upon their death.

Access to life insurance is critical to our nation's economic and social well-being. Yet more Americans are without any form of life insurance than the 37 million alleged to be without health insurance. Households in which breadwinners have no life insurance protection are in financial jeopardy. When breadwinners die, families with little or no private income too often turn to the government and taxpayers for financial support.

40 Percent of All Americans Have No Life Insurance Coverage

The life insurance industry knows the truth about the crisis in life insurance coverage. In 1990, the former CEO of the Life Insurance Marketing Research Association (LIMRA) admitted, "Life insurance is not a mature industry when it comes to consumers' needs."[2] Today, 22 percent of all households and 40 percent of all Americans have no life insurance coverage.[3] (See Table 1.)

In the last thirty years, individual life insurance coverage has decreased dramatically. In 1960, 72 percent of households owned agent-sold individual life insurance. By 1992, only 47 percent of households were covered by agent-sold individual life policies.[4]

Only 33 percent of all persons own agent-sold individual life insurance, down from 56 percent in 1960 and 43 percent in 1984.[5] In other words, about 1 in 2 households and 2 in 3 persons have no agent-sold life insurance.

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[1] "Fight Harder for NAFTA," *National Underwriter* (*NU*), May 10, 1993, p. 22.

[2] Ernie Cragg quoted in "Cragg: Life Business Is Not 'Mature' Industry," *National Underwriter*, February 5, 1990, pp. 8-9.

[3] LIMRA, *Market Trends 1994*, p. 28.

[4] *Ibid.*, p. 25.

Table 1. The Uninsured by Type of Insurance, 1992

	No Life Insurance	No Individual Life Insurance	No Group Life Insurance
Households	22%	45%	47%
All persons	40%	62%	67%

Source: LIMRA

Sixty-two percent of all persons and 45 percent of all households have no individual life insurance coverage.[6] With 40 percent of Americans and 22 percent of households with no life insurance--group or individual--LIMRA's lament that "the insurance industry is meeting the needs of fewer American households than in the past" is an understatement.[7]

> ***"The insurance industry is meeting the needs of fewer American households than in the past."***
>
> \- LIFE INSURANCE MARKETING RESEARCH ASSOCIATION (LIMRA)

A Basic, Unprotected Need of $5 Trillion

At the beginning of 1993, the president of the National Association of Life Underwriters (NALU) described the public's unmet, unprotected life insurance needs this way: "There is a $5 trillion shortfall of consumers with basic life insurance needs that don't have any life insurance at all."[8] According to the American Council of Life Insurance (ACLI), that $5 trillion equaled more than all group life insurance, 78 percent of all ordinary life, and nearly half the total insurance in force at the end of 1993.[9]

> ***"There is a $5 trillion shortfall of consumers with basic life insurance needs that don't have any life insurance at all."***
>
> \- STEPHEN SHAW, PRESIDENT, NALU, 1993

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[5] *Ibid.*, pp. 25-28. During the period 1984-92, group life insurance did not make up the slack in decreased individual coverage. Increasing only slightly, group life insurance covers only 33% of all persons; and median group life coverage has increased only $1,600 since 1976. At that same time, the percentage of persons owning any life insurance continued to decrease. See also LIMRA's *1992 Life Insurance Ownership Study* and "New Study of Life Ownership Covering 1984-1993 Decade Reveals Continuing Decline; Entire Blame Put on Dramatic Drop In Individual Ownership," *Insurance Advocate*, February 26, 1994, p. 27.

[6] *Ibid.*, p. 28.

[7] Cheryl D. Retzloff, "Trends in U.S. Life Insurance Ownership," LIMRA's *Marketfacts*, September/October 1993, pp. 38-41.

[8] Stephen Shaw, president of NALU, cited in Howard Kapiloff, "Life Insurance Sales Remain Flat," *Financial Planning*, May 1993, pp. 101-102, See also, S. Shaw, "Embracing a Multicultural World," NALU's *Life Association News*, March 1993, p. 23.

[9] ACLI's *1994 Life Insurance Fact Book*, p. 5.

Households with life insurance coverage, on average, are under-insured. In 1992, the median amount for all adults was just $30,000 (the mean was $63,000).[10] Thirty-seven percent have less than $25,000 in life insurance coverage.[11] At least 50 percent of all Americans are under-insured.[12]

These statistics should mobilize the insurance industry and alarm legislators who have protected the agency system of insurance distribution. They do not indicate a "mature and saturated" U.S. life insurance market. As the current CEO of LIMRA acknowledged, "the truth is that there are millions of prospects [who] are not getting the opportunity to buy life insurance to meet [their] needs . . . . There are millions of consumers who . . . lack adequate coverage." And he has warned: "These same consumers will seek out alternatives and could be lost as potential customers forever."[13]

THE CRISIS OF EXCLUSION: SERVING THE AFFLUENT, IGNORING THE REST

If so many Americans lack any form of life insurance and many others are woefully underinsured, who's buying all the life insurance that's being sold? If millions of consumers are not getting the opportunity to buy life insurance to meet their needs, where are traditional agents focusing their selling efforts?

Life insurance agents have narrowed their focus to their own return on investment. Despite the great unmet need for life insurance among American families, agents generally serve more upscale clients. They increase their aggregate commissions by selling larger policies for higher premiums to fewer customers. This has given many of those insured better coverage, "but at the expense of other segments of the market that are being ignored."[14]

> ***"The truth is that there are millions of prospects [who] are not getting the opportunity to buy life insurance to meet [their] needs. There are millions of consumers who lack adequate coverage. These same consumers will seek out alternatives and could be lost as potential customers forever."***
>
> \- JOHN C. SCULLY, PRESIDENT AND CEO OF LIMRA

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[10] Burke A. Christensen, General Counsel, American Society of CLU & ChFC, "Selected Statistics and Random Thoughts," *Probe*, February 21, 1994, p. 4; and Christensen, "A Look at the Relationship between Income and Insurance," *Trusts & Estates*, March 1994, pp. 57, 59.

[11] ACLI, *1994 Life Insurance Fact Book*, p. 35.

[12] "...$230,000 [is the] minimum per household average many [life] insurance consultants recommend." See Stephen Advokat, "The Facts of Life," *The Detroit News & Free Press*, July 3, 1994, page J1+. Only 16 percent of all adults have total life insurance coverage of $150,000 or more. See LIMRA, *Market Trends 1994*, p. 28.

[13] John C. Scully, president and CEO of LIMRA, "Increasing Activity: Agents Need to See More Prospects," LIMRA's *Managers Magazine*, September 1993, p. 2.

[14] Cheryl D. Retzloff, "Trends in U.S. Life Insurance Ownership," *Marketfacts*, September/October 1993, p. 41. See also Ernie Cragg, "Agents Have to See and Sell to More People," *Marketfacts*, May/June 1992, p.1.

Traditional Life Insurance Distribution is Inadequate . . . Except for the Affluent

Traditional life insurance distribution appears to adequately serve the affluent. Life insurance ownership by the two highest family income segments has increased, while ownership by the lowest three segments has decreased. Among the 10 percent of households earning more than $75,000 a year, 75 percent own individual life insurance; while in the lowest income segment, the 42 percent of households earning less than $25,000 annually, only 40 percent own individual life insurance.[15]

Traditional life insurance agents ignore less affluent segments of the population, because they make more money with less time and effort selling one big policy than they do selling ten small ones. One agent spokesperson put it this way: "What agent in his or her right mind would try to close four or five $50,000 policies if a $200,000 prospect loomed in the distance?"[16]

Another agent recently wrote: "Almost all we hear and read are tricks to help top executives get more retirement benefits and help the rich avoid estate taxes. . . . Our industry leaders are leading us to higher and higher sales to the rich and eventually to the extinction of our profession. Society will find we are of no use to the majority of people as our function diminishes while CPAs, attorneys, stock-brokers and banks gradually sell more life insurance and insurance companies are selling direct to your customers!"[17]

As LIMRA noted when discussing the "doldrums" in individual life sales, " . . . most companies have targeted upscale markets. A large segment of the population remains unserved, and a clear positive relationship exists between income and ownership. This seems to point to a supply problem, at least in the lower or even middle-income markets--which, incidentally, have always provided the bulk of life insurance purchases."[18] The traditional insurance distribution system of career and independent agents no longer adequately serves the public.

35 Percent of Amounts Are Purchased by Those Who Earn $75,000+

The distribution of life policies is heavily skewed to the upper-income earners. Insurance industry data show how this trend has developed over the last decade.[19]

In 1980, 2 percent of all policies were written for people with incomes over $75,000, constituting 9 percent of total ordinary life amounts. By 1993, those who earned in excess of $75,000 accounted for 13 percent of policies and 35 percent of amounts purchased. (See Table 2.)

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15 John C. Scully, "Selling More Policies: Industry Needs to Extend Its Reach," *Managers Magazine*, August 1993, p. 2. See also LIMRA's *1992 Life Insurance Ownership Study* and "New Study of Life Ownership Covering 1984-1993 Decade Reveals Continuing Decline; Entire Blame Put on Dramatic Drop In Individual Ownership," *Insurance Advocate*, February 26, 1994, p. 27.

16 Don Barnes, "The Gentle Art of Losing," *National Underwriter*, November 29, 1993, p. 19. The average premiums paid by the highest and lowest income classes are, respectively, $1,425 and $267 (see John C. Scully, "Selling More Policies," *Managers Magazine*, August 1993, p. 2). See also, for more examples, Steve Moeller, president of Sell to the Rich, Inc., "Searching for Success," *Managers Magazine*, October 1993, pp. 22-23, and Dennis H. Pillsbury, "Target: The Affluent Market," *Life & Health Insurance Sales*, September 1993, pp. 14-15.

17 Yi-Cheng Chang, "Don't Forget the Middle Class," *Life Association News*, February 1995, p. 9.

18 LIMRA, *The Individual Life Sales Doldrums*, 1990, p. 12.

19 ACLI, *1991 Life Insurance Fact Book Update*, p.7; ACLI, *1993 Life Insurance Fact Book Update*, p. 7. and ACLI, *1994 Life Insurance Fact Book*, pp. 12, 36.

Table 2. Distribution of Ordinary Life Insurance Policies by Income

	Incomes Less than $20,000			Incomes Greater than $75,000		
Year	Percent of Policies	Percent of Amounts	Mean Individual Insurance Coverage	Percent of Policies	Percent of Amounts	Mean Individual Insurance Coverage
1980	65%	42%	N/A	2%	9%	N/A
1993	24%	9%	$29,900*	13%	35%	$231,200

** For incomes under $25,000*

Source: ACLI and LIMRA

The Underclass of Life Insurance

In contrast, in 1980, 65 percent of all policies were written for people with incomes below $20,000, constituting 42 percent of total ordinary amounts. By 1992, only 26 percent of all policies and 10 percent of amounts sold were written for this income class. Adjusting for higher incomes, standards of living, and inflation does not account for this shift, for approximately one-third of all households still have incomes of less than $20,000.[20] Only 4 percent of life policies and 1 percent of face amount insure individuals with incomes of less than $10,000, a level of income earned by 15 percent of all households. (See Table 3 to learn that only a few--the affluent--receive half the beneficiary payments made.)

Table 3. Ordinary Life Insurance Beneficiary Payments

Face Amounts under $15,000 as a Percent of		Face Amounts over $100,000 as a Percent of	
Total Number of Policies	Total Beneficiary Payments	Total Number of Policies	Total Beneficiary Payments
85.7%	15.2%	3%	47.4%

Source: ACLI

The high cost of traditional life insurance distribution has encouraged the agency system to focus on the affluent class of insurance consumers. While it is important to meet the insurance needs of upper-income earners, it is also important to offer life insurance products to all economic classes of Americans. Life insurance agents are ignoring middle and lower-income earners and, according to LIMRA, are "missing the chance to fulfill our mission of bringing financial security to every family . . . [and are] creating a situation that allows other providers to fill the void."[21]

[20] U.S. Department of Commerce, Table No. 711, "Money Income of Households--Percent Distribution, by Income Level, in Constant (1991) Dollars," *Statistical Abstract of the United States 1993*, p. 457.

[21] John C. Scully, "Selling More Policies: Industry Needs to Extend Its Reach," *Managers Magazine*, August 1993, p. 2. See also John C. Scully, "Life Insurance: Another Victim," *Marketfacts*, September/October 1994, p.1.

THE CRISIS IN PRODUCTIVITY: DECLINING LIFE INSURANCE SALES

LIMRA regards the number of policies sold as the most accurate measure of how the life insurance industry is doing.[22] By its own criterion, the industry is in decline.

New Sales Have Been Falling Steadily Since 1983

The number of new policies sold annually reached its peak in 1983 with 17.74 million policies sold and has declined steadily since. New policies sold in 1993 totaled 13.57 million, a decline of 23.5 percent since the 1983 peak.[23] As of August 1994, policies sold were down 6 percent compared to the same period in 1993.[24] If that rate of decline continued, the number of policies sold in 1994 will have been the lowest in 20 years.[25] (See Table 4.)

Table 4. Number of New Ordinary Life Policies Purchased by Year

Year	Ordinary Policies (Millions)
1983	17.737
1988	15.579
1993	13.574
1994	12.760 est.

Source: ACLI and LIMRA

The declining number of agents and decreasing number of new policies sold indicate that the average sales productivity of agents is falling. The average number of life policies sold annually by ordinary agents with 5+ years of experience dropped from 54 in 1987 to 47 in 1992.[26] This declining level of sales productivity does not keep pace with lapsing policies. Unfortunately, productivity is projected to decline to 39 policies sold in 1997.[27] (See Table 5.)

Table 5. The Decline in Average Number of Annual Sales per Agent

Year	1987	1992	1997 est.
Average Annual Sales per Agent	54	47	39

Source: LIMRA

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22 *Ibid*.

23 ACLI, *1994 Life Insurance Fact Book*, p. 10. See also LIMRA, *Market Trends 1994*, p. 34; and Brendan Noonan, "Average Policy Size Resumes Growth," *Best's Review* (L/H), December 1993, p. 14, 16.

24 "LIMRA: More Declines in Sales Figures in August," *National Underwriter*, November 7, 1994, p. 23.

25 ACLI, *1986 Life Insurance Fact Book*, p. 10.

26 LIMRA, *1991 U.S. Ordinary Agent Production and Survival Survey*, p.7; and LIMRA, *1992 U.S. Ordinary Agent Production and Survival Survey* cited in "LANSTAT: Commissions Up, Policies Sold, Down," *Life Association News*, February 1994, p. 28.

27 James O. Mitchel, "Turning It Around," *Managers*, October 1993, pp. 11-12.

Tens of Millions of Policies Have Lapsed in the Last Decade

In the thirteen years for which data is available starting with 1981, the number of in-force ordinary policies in the United States fell by 9 million to 140 million in 1993.[28] (See Table 6.)

In the same period (1981-93), almost 202 million new ordinary life policies were written, over 35 percent more than the total number of policies in force in 1981.[29] With 149 million policies in force in 1981 and 202 million new policies written since, 351 million policies existed at some time during those 13 years. Yet, less than 32 percent of that number--140 million--were in force at the end of 1993.[30] Tens of millions have lapsed in the last decade!

Table 6. Number of Ordinary Life Insurance Policies In Force by Year

Year	Ordinary Policies (Millions)
1981	149
1983	146
1989	144
1993	140

Source: ACLI

Traditional Agency Distribution – Insurers' Greatest Expense

The traditional agent distribution system is a life insurance company's greatest single expense. Two-thirds of insurers' expenses go to maintaining this legislatively protected distribution system.[31] Life insurance company CEOs are increasingly concerned about the excessive cost of distribution and low sales force productivity.[32] Their companies are under pressure "to aggressively control expenses, particularly distribution expenses [and] to increase unit productivity (such as agent productivity) to spread costs . . . . CEOs have launched some serious reviews of marketing strategies in general and of various distribution strategies in particular, looking for lower costs and higher productivity."[33]

In its recent study of life insurance comparative expense performance, Tillinghast/Towers Perrin, the insurance management consulting firm, concluded that "Significant improvements in agency distribution

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[28] ACLI, *1994 Life Insurance Fact Book*, p. 16.

[29] ACLI, *1994 Life Insurance Fact Book*, p. 10.

[30] From 1981-93, the number of payments to ordinary life insurance beneficiaries was 17.116 million. Considering the 17 million policies paying benefits in respect of an insured's death and the 140 million policies still in force, as many as 194 million ordinary policies lapsed during the years 1981-93. ACLI, *1994 Life Insurance Fact Book*, p. 45.

[31] Carole King, "Consultant Predicts Radical Distribution Changes," *National Underwriter*, January 25, 1993, p. 7; "CEOs Rank Distribution Management as Top Concern," *Marketfacts*, May/June 1994, p. 12; Thomas H. Kelly, Senior Vice President, LIMRA, and Ram S. Gopalan, Program Director, Cost Research, LIMRA, "Managing for Profit," *Marketfacts*, November/December 1992, pp. 47-50.

[32] Michael B. Petersen, Director, LIMRA Editorial Services, "CEO's Focus on Finances in LIMRA Study," *Life Association News*, April 1994, pp. 38, 40.

[33] "A View from the Top," *Managers Magazine*, July 1994, p. 5.

are needed--and the only way to achieve them is to fundamentally rethink the distribution function."[34] In its "U.S. Industrial Outlook--1993," the U.S. Department of Commerce declared that, to reduce the high costs of their traditional distribution system, "insurers will look for cost-efficient marketing alternatives, such as direct mail and alliances with other financial institutions."[35]

> ***"The business of selling individual life insurance through career agency systems is dying . . . . Remnants of the career agency system will survive, but single source distribution as the primary delivery system of the insurance industry is no longer viable. Its problems go beyond changes in the marketplace, competition and economic reality. They are at its very core."***
>
> \- DONALD W. MEYERS, "THE REVOLUTION IS OVER; SINGLE-SOURCE IS DYING," *BEST'S REVIEW* (L/H), FEBRUARY 1994

As many analysts have concluded, "The business of selling individual life insurance through career agency systems is dying . . . . Remnants of the career agency system will survive, but single source distribution as the primary delivery system of the insurance industry is no longer viable. Its problems go beyond changes in the marketplace, competition and economic reality. They are at its very core."[36]

> ***"The same basic method of marketing [life] products is still in existence. We don't seem to want to try anything else. It seems to me that if something hasn't worked for 50 years, it is about time some changes were made.... [But] we seem to have the faculty for looking down our noses at anyone who tries other methods of marketing."***
>
> \- PRESIDENT OF JOHN HANCOCK LIFE INSURANCE COMPANY, SPEAKING 24 YEARS AGO

Though their magnitude and long-term effects are greater than ever, "the ills of the agency system have been recounted before."[37] At a conference for life insurance executives held in 1971, a former president of John Hancock similarly declared, "The same basic method of marketing [life] products is still in existence. We don't seem to want to try anything else. It seems to me that if something hasn't worked for 50 years, it is about time some changes were made . . . . [But] we seem to have the faculty for looking down our noses at anyone who tries other methods of marketing."

Also at that 1971 conference, noted management consultant and professor Peter F. Drucker said, "You have among the highest selling costs of any industry, and they are going up . . . . You have built up a

[34] Roger Heath, principal, Towers Perrin Insurance General Management Consulting practice, quoted in "Life Insurance Productivity Continues to Decline Despite Expense Reduction Programs," *Marketfacts*, September/October 1994, pp. 14-15.

[35] Steven Brostoff, " '93 Outlook: Modest Sales Growth," *National Underwriter*, January 18, 1993, pp. 1, 22. See also "CEOs Rank Distribution Management as Top Concern," *Marketfacts*, May/June 1994, p. 12; and *Insurance Times*, January 12, 1993, p.1.

[36] Donald W. Meyers, "The Revolution is Over; Single-source is Dying," *Best's Review* (L/H), February 1994, pp. 58, 60.

[37] Janet Corrado, "Agency System is Millstone of Life Marketing Strategy," *National Underwriter*, October 9, 1971, pp. 1, 7, 8.

huge selling staff, and you are getting marginal results . . . . If it sounds like I'm not impressed with the agency system, I am not impressed."[38]

Ernst & Young published its 1995 annual insurance executive report on *The State of the Industry* warned: "The [life] insurance industry will never be able to move beyond its current performance levels without addressing the cost and inefficiencies of its main distribution systems. Agent productivity has changed little in decades, and average acquisition costs are estimated at a whopping 175 to 200 percent of each dollar of new life premium. How long

> ***"You have among the highest selling costs of any industry, and they are going up.... You have built up a huge selling staff, and you are getting marginal results.... If it sounds like I'm not impressed with the agency system, I am not impressed."***
>
> - MANAGEMENT CONSULTANT AND PROFESSOR PETER F. DRUCKER

consumers will accept such costs and their effect on product performance isn't clear, but there are signs that a more knowledgeable marketplace is beginning to demand change. And, " Ernst & Young continues, "change won't come easily. In the industry's most successful effort to deal with these issues, it has turned to banks and other financial institutions for the sale of its savings products. Fully 20 percent of individual annuities are now sold through banks"[39]

THE CRISIS IN THE TRADITIONAL AGENCY SYSTEM: LOW ENROLLMENT, HIGH DROP-OUT RATES

The life insurance industry uses several key measurements to assess the performance, health and potential of agents and the agency system: agent recruitment rates, four-year agent retention rates, incumbent sales force survival rates, and agent productivity. LIMRA, which tracks these data, describes these bellwethers as "either flat or heading south, " indicating "a continued slow and painful decline."[40]

> ***"Present levels of recruiting will not maintain the sales force at its current size, and so sales will continue to decline."***
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> - LIMRA, *THE INDIVIDUAL LIFE SALES DOLDRUMS*

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38 *Ibid*.

39 Bob Stein, National Director of Insurance Industry Services, Ernst & Young, "Financial Forecast," *Insurance Executive Report: The State of the Industry*, Winter 1994/1995, pp. 2-5, 7.

40 Walter H. Zultowski, SVP of Research, LIMRA, quoted in Amy S. Friedman, "Agencies and Companies Told to Realign to Suit Market Needs," *National Underwriter*, November 22, 1993, p. 7. See also Richard K. Berry and Roger R. Heath, "Reinviting Agency Distribution," *Best's Review* (L/H), August 1993, pp. 33-36, 110.

Record Declines in New Agent Recruitment

According to LIMRA, the decline in recruiting new agents is the most disturbing trend. 1993 marked the fifth year in the last six to record substantial declines in ordinary agent recruiting. The greatest annual decline in agent recruiting history--14 percent--occurred in 1992. Ominously, the number of ordinary agent recruits for 1993 was down 5% from 1992.[41]

1994 will not be better. The number of new agent recruits dropped for the twelfth consecutive quarter in the third quarter of 1994, down by 13 percent year-to-date.[42] 1994 will be the sixth year in the last seven in which new agent recruitment declined.

> ***"We already have too few agents. Sales have not stagnated because there is no longer a need for life insurance or because the public doesn't want to buy life insurance, but because we are not giving the public the opportunity to buy it.... And that is not the mission of the life insurance business—the mission to insure every family adequately."***
>
> - JOHN C. SCULLY, PRESIDENT AND CEO LIMRA

In 1993, the number of inexperienced ordinary agent recruits was down 56% from 1982.[43] LIMRA's reaction to this data is pessimistic: (1) "Present levels of recruiting will not maintain the sales force at its current size, and so sales will continue to decline."[44] (2) "The industry will continue to experience a relatively permanent 'structural change,' of which a continued decline in agent recruiting is one of the elements."[45]

This response to these record declines in agent recruiting is nothing new. For years, LIMRA has warned: "We already have too few agents. Sales have not stagnated because there is no longer a need for life insurance or because the public doesn't want to buy life insurance, but because we are not giving the public the opportunity to buy it." In 1975 every 200 households had one career agent. Today, there is one career agent for every 400 households. What sales increases the industry sees in total face amount and premiums are the result of selling bigger policies to fewer people. And that, complains LIMRA's CEO, "is not the mission of the life insurance business--the mission to insure every family adequately."[46]

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[41] Steven F. Sullivan, "Can the Recruiting Tailspin Be Reversed?" *Life Association News*, February 1994, pp. 40-42, 44; Michael B. Petersen, "Recruiting of Inexperienced Life Agents Continues to Slide," *Society Page*, October 1993, p. 18; Walter H. Zultowski, "The Recruiting Downslide: Temporary or Permanent," *Marketfacts*, March/April 1993, pp. 19-23; D. Layne Rich, "Field Management: On Its Way Out?", *Marketfacts*, November/December 1993, p. 26; Michael B. Petersen, "Recruitment Drops," *Life Association News*, October 1994, p. 37; and LIMRA, *Recruiting Trends, Fourth Quarter 1993 Report.*

[42] "U.S. New Career Agent Recruiting Still Weak...." *National Underwriter*, December 12, 1994, p. 7.

[43] Inexperienced ordinary agent recruits declined from 42,129 in 1982 (LIMRA, *The Individual Life Sales Doldrums*, 1990, p. 8) to 18,630 in 1993 (LIMRA, *Recruiting Trends, Fourth Quarter 1993*, p. 1.). Through the third quarter of 1994, inexperienced ordinary agent recruits are down 17 percent year-to-date, a rate that would put the total for 1994 at 15,463 or a decline of 63 percent since 1982. See Carole King, "U.S. New Career Agent Recruiting Still Weak...." *National Underwriter*, December 12, 1994, p. 7.

[44] LIMRA, *The Individual Life Sales Doldrums*, 1990, p. 13.

[45] Walter H. Zultowski, "The Recruiting Downslide: Temporary or Permanent?," *Marketfacts*, March/April 1993, p. 21.

[46] John C. Scully, "How Are You Doing? Industrywide, Recruiting Is Down," *Managers Magazine*, May 1993, p. 2.

The 84 Percent New Agent Drop-Out Rate

It is harder than ever to bring new agents into the insurance business, and LIMRA believes the recruiting downturn is permanent. Worse, once new agents are recruited to the life business, few last long. The average 4-year agent retention rate is 16 percent. In other words, for every 100 new agents recruited, only 16 remain in the business 4 years later.[47]

Moreover, survival rates for all agents declined from 1990 and 1989. "Seventy-two percent of the incumbent sales force at the start of 1991 survived to the end of the year, a two-percentage-point decrease from 1990."[48] For every 100 agents with 2+ years of service selling on January 1, 1991, twenty-eight dropped out, leaving only 72 in the business by December 31st. Overall, the number of full-time life agents has dropped 18,000 from 248,000 in 1978 to 230,000 in 1991.[49]

The average 4-year new agent retention rate is 16 percent. In other words, for every 100 new agents recruited, only 16 remain in the business 4 years later. And 22 percent of experienced agents drop-out of the insurance business annually.

Why are new recruits and agents leaving and why are sales down? What explains the 22 percent annual drop-out rate for experienced agents? Why have 84 percent of all new agents left the insurance business four years after they began? The answer is generally tied to the difficulty of prospecting. Prospecting for new customers is the toughest part of the life insurance business, and "the old methods of prospecting just aren't working."[50] The industry's leading publications repeat the same plaintive cry: "Agents don't fail for lack of technical knowledge. They fail because of poor prospecting skills and a lack of training in this vital area."[51]

The Expensive Costs of the High Agent Drop-Out Rate

The high agent drop-out rate frames a story of disappointment for the individuals who began with hope but "failed" in the business. The high drop-out rate also creates an expensive and inefficient treadmill for the life insurance industry. The average company invests $120,000 in selecting, recruiting and

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47 William T. Quinn, "Selling Life Insurance Takes Toll on Today's Agents," *The Newark Star Ledger*, August 21, 1994, Section 3, page 5+; and "Market*stat*: Ordinary Agent Production and Survival," *Marketfacts*, September/October 1993, p. 48.

48 "Agent Production and Survival in 1991," *Marketfacts*, January/Februrary 1993, p. 15; and "Market*stat*: Ordinary Agent Production and Survival," *Marketfacts*, September/ October 1993, p. 48.

49 LIMRA, *Census of Life Insurance Sales Personnel, Research Report 1980-3*, p.1; and Michael B. Petersen, "LIMRA Surveys Provide Look into Future of Life Sales," *Society Page*, April 1994, p. 25.

50 Carole King, "Seminar Selling Has Its Place and Its Dangers for Industry," *National Underwriter*, May 17, 1993, p. 7. See also John H. Melchinger, "Avoid the Depths of Prospecting Hell," *Managers Magazine*, May 1993, p. 12-15, who writes: "Producers at all production levels often claim that prospecting for qualified buyers is the most difficult aspect of selling insurance and investments" (p. 13).

51 Pamela Yellen, "Profitable Prospecting," *Managers Magazine*, August 1993, pp. 9-11. See also John H. Melchinger, "Avoid the Depths of Prospecting Hell," *Managers Magazine*, May 1993, p. 12; Michael B. Petersen, "Learning from Agents Who Terminate in First Year," *Society Page*, August 1994, p. 23; and Todd A. Silverhart, "Recycling Agents: Waste Not, Want Not?", *Marketfacts*, September/October 1994, pp. 19-22.

training an agent.[52] It takes insurance companies 9 to 21 years to recoup the time and money they invest in a new agent.[53] When agents fail and leave the business, the insurance company loses as well.

This investment exceeds the revenue generated by agents during their first three years. "It isn't until the fourth year that agents produce more than they cost, and it takes several more years for a company to recoup its investment."[54] To further compound an insurance company's problem of recovering its costs for agent recruitment, retention and survival, only 1 in 6 agents stays with a company for four years.[55]

> ***"The smaller agency force has decreased the public's chance of being approached by a life insurance agent."***
>
> - LIFE INSURANCE MARKETING RESEARCH ASSOCIATION (LIMRA)

As the ranks of insurance agents have thinned and competition among them has lessened, consumer access to life insurance products has declined. Since 1984, the U.S. population has grown by about eight million people while the size of the traditional agency field force has fallen. "It is as if a new state the size of New Jersey had been created and there were no life insurance agents to service it."[56] Thus, although each agent now has a potentially larger market that goes untapped, "the smaller agency force has decreased the public's chance of being approached by a life insurance agent."[57]

THE CRISIS IN CONFIDENCE: AGENT SERVICE AND THE PUBLIC'S ATTITUDE

Because insurance agent trade associations have long insisted they are the servants of existing policyholders and the defenders of consumer interests, we need to evaluate their performance in order to verify their claims. How well are consumers served by the traditional agency system? Data compiled by the insurance industry indicate that consumers, in general, are not well-served by the existing agency system and that traditional life insurance agents have not earned the trust of the consuming public.

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52 John C. Scully, "The Value of a Good Manager," *Marketfacts*, July/August 1993, p. 1. Insurance company investment in a new agent can range from $90,000 to $190,000. See Todd A. Silverhart, "Recycling Agents: Waste Not, Want Not?", Marketfacts, September/October 1994, p. 19; see LIMRA, *Investing in New Agents: A Cost Blueprint*.

53 Todd A. Silverhart, "Recycling Agents: Waste Not, Want Not?", Marketfacts, September/October 1994, p. 19; see LIMRA, *Investing in New Agents: A Cost Blueprint*.

54 Raymond H. Hinchcliffe, "Ordinary Agents: The Retention Factor," *Marketfacts*, November/ December, 1992, p. 35. See also Ian Mackenzie, "Lapsing Agents," *Life Association News*, October 1993, p. 6; and Walter H. Zultowski, "Distribution in the '90s: '*Deja Vu* All Over Again?'," *Marketfacts*, September/October 1990, pp. 32-35, 57-58.

55 Todd A. Silverhart, "Recycling Agents: Waste Not, Want Not?", *Marketfacts*, September/October 1994, p. 19; and Raymond H. Hinchcliffe, "Ordinary Agents: The Retention Factor," *Marketfacts*, November/ December 1992, p. 35.

56 Walter H. Zultowski, "The Recruiting Downslide," *Marketfacts*, March/April 1993, p. 23.

57 Cheryl D. Retzloff, "Trends in U.S. Life Insurance Ownership," *Marketfacts*, September/October 1993, p. 39.

One-third of ordinary whole life policies lapse in their first 5 years. Furthermore, 38 percent of policyholders have no active servicing agent and are designated "orphan" policyholders. Some claim orphaned customers outnumber clients with agents.

The Public's Low Level of Confidence

The American Council of Life Insurance's 1991 MAP Survey, which monitors attitudes of the public, revealed that 28 percent of consumers believe life agents do not tell the whole truth about what they are selling; only 15 percent believe them to be fully honest.[58] Thirty-four percent believe agents are more interested in big commissions than selling the right product; only 13 percent think they are more interested in selling the right product.[59] A mere 25 percent believe agents do a good job of keeping in touch after the policy is issued.[60]

Fewer Consumers Deal with Agents

In 1993, only 31 percent of consumers had a personal life insurance agent, down from 44 percent in 1967.[61] Of those households with less than $25,000 in annual income (a market segment representing 40 percent of all households), only 22 percent have an insurance agent.[62]

Of policy owners, 36 percent bought their most recent policy before 1984; 16 percent could not remember when they bought their most recent policy.[63] Between 1991 and 1993, one-fourth purchased their most recent policy directly from the insurance company or through some source other than a traditional agent.[64] ACLI surveys have shown that, of those who plan to buy a policy, one-fourth to one-fifth indicate a preference to buy insurance directly from a company or an agent at a bank or other retail establishment.[65]

Dissatisfaction, Lapses and Orphans – Agent Service Leaves Much to be Desired

Insurance industry data reveal that customers believe there is "significant room for improvement" in the service performances of their agents. Thirty-seven percent of policyowners rated the quality of agent service no better than satisfactory, nearly twice the lower-category rating agents gave themselves. And policyholder service by traditional life agents is not likely to improve. "Agents believe their clients are

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58 ACLI, *1991 Monitoring Attitudes of the Public (MAP) Survey*, pp. 10, 48.

59 *Ibid.*, pp. 11, 50.

60 *Ibid.*, pp. 11, 50-51.

61 "Individual Life Sales Declining, Study Finds," *BestWeek* (L/H), March 7, 1994, pp. 5-6; and ACLI, *1993 Monitoring Attitudes of the Public (MAP) Survey*, pp. 35, 74.

62 "LAMP '93: Reaffirming the Qualities of Life," *GAMA News Journal*, March/April 1993, p. 43.

63 ACLI, *1993 Monitoring Attitudes of the Public (MAP) Survey*, p. 49. More than one-quarter (28 percent) bought their most recent policy between 1985 and 1990.

64 *Ibid.*, p. 50.

65 *Ibid.*, p. 32, and ACLI, *1991 Monitoring Attitudes of the Public (MAP) Survey*, p. 73.

substantially more satisfied than they actually are."[66] Even when facts and consumer assessments contradict them, agents continue to make claims that their client service is top-notch. Meantime, agents are encouraged to improve their sales productivity by "cutting the time and effort spent developing [their] client relationships and improving [their] results with [their] present level of activity."[67]

> ***"This large percentage of orphaned policyholders...dramatically illustrates the lack of follow-up contact in the life insurance industry.... [Moreover,] producers need to do a better job in providing quality financial advice and in making recommendations with their clients' best interests in mind."***
>
> - LYNN MERRITT, PRESIDENT AND CEO, LIFE OFFICE MANAGEMENT ASSOCIATION (LOMA)

Related to the quality of service is the high lapse rate of life insurance policies. One-third of ordinary whole life policies lapse in their first 5 years,[68] largely because the agents who sold policies are no longer in the business. Furthermore, 38 percent of policyholders have no active servicing agent and are designated "orphan" policyholders.[69] Some claim orphaned customers outnumber clients with agents.[70]

According to the president and CEO of the Life Office Management Association (LOMA), "This large percentage of orphaned policyholders . . . dramatically illustrates the lack of follow-up contact in the life insurance industry . . . . [Moreover,] producers need to do a better job in providing quality financial advice and in making recommendations with their clients' best interests in mind."[71]

THE CRISIS IN LIFE INSURANCE SUMMARIZED

A large portion of U.S. households and individuals have no life insurance. Most of those with coverage are severely underinsured. A few own substantial amounts because agents have targeted upper-income earners as customers. Agents like the higher premiums and larger commissions they can earn selling big-ticket policies to affluent customers.

Agent focus on wealthier customers has resulted in a substantial decline in agent sales productivity, since agents are prospecting in the same limited market segment. Other income-segments are ignored or neglected. "It seems quite clear that . . . there is a large, diverse and generally untapped market for insurance and other financial services awaiting those who have the will to approach it."[72]

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66 Carole King, "Agents/Policyholders Split on Service," *National Underwriter*, October 12, 1992, pp. 7, 12.

67 Andrea R. Gaedeke, "Is Your Agency Focused on Productivity?" *Managers*, January 1994, pp. 25-26.

68 LIMRA, *Long-Term Ordinary Lapse Survey, 1992*, p. 9.

69 *Quality Service in the Life Insurance Industry*, A Cooperative Research Project of ACLI, LIMRA, LOMA, and NALU, 1993, p. 31; John C. Scully, "Another Look At 'Verities,'" *Probe*, July [15], 1994, p. 4. See also "Agents Falling Down on Follow-up," *Life Association News*, February 1993, pp. 24, 30.

70 Donald W. Meyers, "The Revolution is Over; Single-source is Dying," *Best's Review* (L/H), February 1994, p. 62; and Thomas H. Kelly, "$10 Trillion Market," *Marketfacts*, May/June 1992, p. 34.

71 Lynn Merritt, president and CEO of LOMA, "There's Room to Improve the Quality of Service," *Best's Review* (L/H), March 1994, p. 42.

72 Burke A. Christensen, "A Look at the Relationship Between Income and Insurance," *Trusts & Estates*, March 1994, p. 59.

Meanwhile, it has become more difficult to recruit and retain agents. Many insurance companies never recover their costs of recruiting and training agents. With the number of new policies sold annually reaching a 20-year low, a declining sales force means that sales will continue to decline. Thus, the public has even less opportunity to buy life insurance, and a large portion of existing policyholders continue to endure unsatisfactory service.

> ***"When you deify one [distribution system] to the exclusion of all others, you're asking for trouble.... With fewer and fewer agents selling fewer and fewer policies, how are we going to bring the benefits of life insurance to every level of society?... You can never have too many distribution systems."***
>
> - JOHN C. SCULLY, PRESIDENT AND CEO, LIMRA

If the traditional agency system retains its lock on the insurance industry, public confidence in insurance agents will continue to decline. As fewer consumers deal with an ever-smaller number of agents, more insureds will join the millions of orphaned policyholders. Others will simply let their policies and coverage lapse, adding to the tens of millions of policies that have lapsed in the last ten years.

The whole process is a vicious cycle that is itself created and repeated by the expensive and inefficient system of traditional agency distribution. The cycle follows this course:

- An ever-increasing population of uninsured and under-insured Americans;
- Focus on sales to the affluent market, where policies and commissions are bigger;
- Continued decline in overall agent productivity;
- Neglected lower and middle-income markets;
- Fewer agent recruits and long-term survivors;
- Fewer sales of policies;
- Large numbers of poorly serviced, dissatisfied consumers and a distrustful, skeptical public;
- Lapsed and orphaned policies;
- An ever-larger population of uninsured and under-insured Americans.

These disappointing outgrowths of the protected agency system have caused more life insurance companies to look for new distribution strategies that better serve the public, lower distribution costs and raise productivity. Banks are a part of the distribution solution to this crisis in life insurance. Banks can perform a greater service for the public if all consumers are allowed the freedom of choice to make their own decisions in a marketplace freed to maximize competition.

Despite its need to be cautious about discussing bank insurance distribution in order not to offend traditional agent associations and career agency insurance companies, LIMRA has recognized the need to develop alternative methods of life insurance distribution: "When you deify one [distribution system] to the exclusion of all others, you're asking for trouble . . . . With fewer and fewer agents selling fewer and fewer policies, how are we going to bring the benefits of life insurance to every level of society? . . . You can never have too many distribution systems."[73]

[73] John C. Scully, "Another Look At 'Verities,'" *Probe*, July [15] 1994, p. 4.

Banks are a part of the distribution solution to this crisis in life insurance. Banks can perform a greater service for the public if all consumers are allowed the freedom of choice to make their own decisions in a marketplace freed to maximize competition.

SECTION TWO:
WHERE AT LIBERTY, CONSUMERS EXERCISE THEIR FREEDOM OF CHOICE

Following the one-year federal moratorium of 1987 on expansion of bank insurance powers, the U.S. Senate and House each passed banking bills that affirmed the right of states to permit state-chartered banks within bank holding companies (BHCs) to engage in insurance agency activities. This action occurred after a coalition of consumer groups wrote the Senate Banking Committee to "strongly oppose" any amendment that would restrict authorization of insurance sales activities for BHC-controlled state-chartered banks.

> ***"Insurance competition from banking organizations with appropriate safeguards could benefit consumers.... Any further [prohibitions on bank insurance sales].... would be an ill-advised step detrimental to the interests of millions of Americans."***
>
> \- LETTER FROM 24 NATIONAL AND STATE CONSUMER ORGANIZATIONS TO SENATE BANKING COMMITTEE MEMBERS, FEBRUARY 22, 1988

That coalition of twenty-four national and state consumer groups included the Consumer Federation of America, National Insurance Consumer Organization, Consumers Union, Bank Watch, National Association of Neighborhoods, Public Citizen's Congress Watch, and the American Council on Consumer Awareness, and groups from Alaska, Idaho, Kansas, Louisiana, Massachusetts, Michigan, New York, North Carolina, Ohio, Oregon, Pennsylvania, Texas, Virginia and Wisconsin.

Many Consumers Want Alternative Choices When Buying Insurance

In their letter, the consumer organizations argued that "allowing banks to engage in insurance activities could bring much needed competition to the insurance industry . . . , reduce the cost of insurance and force the insurance industry to become more efficient." They declared that "insurance competition from banking organizations with appropriate safeguards could benefit consumers." More importantly, they stressed the importance of "exploring inadequacies in the present distribution and underwriting system" and proclaimed that "any further [prohibitions on bank insurance sales] . . . would be an ill-advised step detrimental to the interests of millions of Americans."[74]

For some time, many consumer groups have supported bank insurance sales activities. This support is consistent with the findings of numerous consumer research surveys. A 1990 survey found that 10 percent of consumers had already bought insurance from banks and another 30 percent were willing to

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74 Letter to Senate Banking Committee Members, February 22, 1988. See also, for example, "Banks and Insurance: Time for a New Policy," *The Miami Herald*, February 11, 1990, p. 2V: "This prohibition's consequences have grown from mere inconvenience to potential injury--to consumers and to banks.... Removing this prohibition [against bank insurance activities] is widely supported by leading consumer groups precisely because it would enhance competition, convenience, and choice. Florida thus ought to join the growing number of states repealing this anachronistic ban."

buy.[75] The ACLI's own *MAP Survey* showed a plurality of consumer respondents favor expanded bank insurance powers.[76]

The Consumer Federation of America (CFA) determined in its 1987 survey that bank-based agents provide more product-related information and offer fuller purchase-disclosure than do traditional agents. Indeed, the CFA concluded, "The potential benefits [of bank sale of insurance] are large enough for policy-makers to work very hard at striking the proper [regulatory] balance. There is no reason to prohibit states from carefully expanding bank sale of insurance or for federal authorities to dismiss bank sale of insurance out of hand."[77]

Many major metropolitan newspapers have also endorsed bank-based insurance sales. *The Detroit News and Free Press* recently echoed the sentiment of consumer groups: "The move [to allow banks to sell insurance] is opposed by life insurance agents, but with proper safeguards, there is no reason why banks should be prevented from becoming one-stop financial shopping institutions . . . . A competitive market can only be created by allowing marketing . . . . When more people are selling a product, there is more variety and price competition. Let the financial institutions sell insurance."[78] Thanks to a state Supreme Court decision and action in the Michigan legislature in 1994, Michigan financial institutions can now sell insurance.

"The potential benefits [of bank sale of insurance] are large enough for policy-makers to work very hard at striking the proper [regulatory] balance. There is no reason to prohibit states from carefully expanding bank sale of insurance or for federal authorities to dismiss bank sale of insurance out of hand."

- CONSUMER FEDERATION OF AMERICA, *THE POTENTIAL COSTS AND BENEFITS OF ALLOWING BANKS TO SELL INSURANCE, 1987*

In December 1993, a month following the *Free Press* editorial, *The New York Times* decried "antiquated laws that prohibit banks from . . . selling new products." *The Times* called for additional reform of the banking industry, noting how previous attempts to expand bank insurance powers have been stymied by anti-competitive forces: "The insurance industry blocked President Bush's proposals to give banks the right to sell insurance. Congress buckled under, even though banks would have served merely as sales agents for policies and would not have incurred risk."[79] In the wake of a 1994 decision by the state's highest court, New York State banks can now sell annuities. Still, at both the national and state levels, bank insurance laws and regulations remain a confusing patchwork of permissible and impermissible powers and activities.

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75 Ellen Memmelaar, "Public Willing To Shop Banks for A Range of Products," *American Banker Consumer Survey*, 1990, pp. 20-21; and E. Memmelaar, "Banking Public Favors One-Stop Concept," *American Banker*, October 2, 1990, pp. 1, 6..

76 ACLI, *1991 Monitoring Attitudes of the Public (MAP) Survey*, p. 94.

77 Consumer Federation of America, *The Potential Costs and Benefits of Allowing Banks to Sell Insurance*, February 10, 1987, p.7.

78 "Let Banks Sell Insurance," *The Detroit New and Free Press*, November 6, 1993, p. 12C.

79 "Unfinished Bank Reform," *The New York Times*, December 29, 1993, p. A10. See also "Banks and Insurance: Time for a New Policy," *The Miami Herald*, February 11, 1990, p. 2V.

Many National Banks and Bank Holding Companies Already Possess Insurance Powers

Even so, many of the country's national banks and BHCs already have legislative and regulatory authority to engage in a range of insurance agency or brokerage activities that are far broader than popularly recognized.

Title VI of the Garn-St. Germain Act of 1982 stipulates that BHCs under $50 million in assets may engage in any insurance activity except, generally, the sale of life insurance and annuities.[80] When enacted, this provision applied to some 2,300 of 3,500 federally regulated bank holding companies. It also grandfathered approximately 1,000 BHC subsidiaries whose insurance activities were approved by the Federal Reserve on or before May 1, 1982.[81] National banks and BHCs may operate insurance agencies in towns of 5,000 or fewer inhabitants or in a place where the community can be demonstrated to have "inadequate insurance agency facilities."[82] National banks may sell annuities, as affirmed by the swift, unanimous decision of the U.S. Supreme Court on January 18, 1995.[83] BHCs are permitted to sell, purchase or underwrite insurance for the holding company, or its subsidiaries, or its employees.[84] Moreover, U.S. bank holding companies are permitted to sell all types of insurance overseas.

> ***"The move [to allow banks to sell insurance] is opposed by life insurance agents, but with proper safeguards, there is no reason why banks should be prevented from becoming one-stop financial shopping institutions.... A competitive market can only be created by allowing marketing.... When more people are selling a product, there is more variety and price competition. Let the financial institutions sell insurance."***
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> - *THE DETROIT NEW AND FREE PRESS*, 1993

80 Richard M. Whiting and James E. Scott, *A Guide to Federal Law of Banking and Insurance,* Prentice Hall Law & Business, 1992, p. 62.

81 Edgar W. Armstrong, Jr., "Overview of Permissible Activities," *The Banker's Guide to Income Producing Insurance*, American Bankers Association, 1989, pp. 33-34.

82 Richard M. Whiting and James E. Scott, *A Guide to Federal Law of Banking and Insurance,* Prentice Hall Law & Business, 1992, pp. 45, 81.

83 *NationsBank of North Carolina v. VALIC* (S. Ct. Nos. 93-1612; 93-1613), January 18, 1995.

84 Edgar W. Armstrong, Jr., "Overview of Permissible Activities," *The Banker's Guide to Income Producing Insurance*, American Bankers Association, 1989, pp. 33-34.

More Than Half the American People May Buy Their Insurance From Banks

Insurance powers are widely permitted at the state level, where state-chartered bank experience in insurance activities is extensive. In fact, more than half the American people live in states and demographically-prescribed areas of states where broad bank insurance powers are permissible. Approximately 134 million Americans, almost 53 percent of the population, can legally meet all their insurance needs through bank insurance agencies. Another 25 million, nearly 10 percent of the population, live in states that permit them to buy annuities from state banks.

The number of states that permit banks broad insurance agency or brokerage powers has grown dramatically in recent years. A recently completed survey of state banking and insurance regulators found that nearly half the states (22) now grant banks these broad powers. These states include Alaska, Alabama, Arizona, California, Delaware, Idaho, Indiana (limited to insurance products other than life insurance), Iowa, Maryland, Michigan, Minnesota, New Jersey, North Carolina, Ohio, Oregon, South Carolina, South Dakota, Utah, Virginia, Washington, Wisconsin and Wyoming.[85] These states with broad insurance powers are home to 120,215,000 residents, or over 47 percent of the population of the United States.[86]

At least eleven states grant broad insurance agency and brokerage powers to banks on a geographical basis limited to towns of a particular maximum size. Arkansas, Colorado, Georgia, Kansas, Missouri, New Mexico, North Dakota, Oklahoma and Tennessee limit insurance activities to towns of 5,000 or fewer residents. Mississippi limits insurance activities to towns of 7,000 or fewer people. And, Nebraska limits insurance activities to towns of 200,000 or fewer inhabitants, effectively preventing bank insurance only in Omaha.[87] Of the 35 million people who live in these states, approximately 14 million live in non-metropolitan or rural areas that are permitted to be served by bank insurance agencies. That 14 million constitutes 5.5 percent of the nation's population.[88]

Approximately 134 million Americans, almost 53 percent of the population, can legally meet all their insurance needs through bank insurance agencies. Another 25 million, nearly 10 percent of the people, live in states that permit them to buy annuities from state banks.

Five other states grant state banks annuity sales powers--Colorado, Louisiana (in towns of 5,000), Maine, Nevada and New York. States permitting their banks to sell only annuities are home to an

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85 Michael D. White, "Some Key Findings from FIIA's Survey of State Banking and Insurance Regulators," *The FIIA Survey of State Bank Insurance Laws*, 1995, p. 1.

86 "Resident Population" based on statistics from the U.S. Bureau of the Census, *Statistical Abstract of the United States 1993*, p. xii.

87 Michael D. White, "Some Key Findings from FIIA's Survey of State Banking and Insurance Regulators," *The FIIA Survey of State Bank Insurance Laws*, 1995, pp. 1-2.

88 "Resident Population in Metro. Areas" based on statistics from the U.S. Bureau of the Census, *Statistical Abstract of the United States 1993*, p. xiii; "Table No. 37. Urban and Rural Population--States: 1990," based on statistics from U.S Bureau of the Census, *1990 Census of Population*, in *Statistical Abstract of the United States 1993*, p. 34..

additional 24.6 million residents--almost 10 percent of the U.S. population. When these "annuity-only" states are combined with states that permit state banks to sell all insurance products including annuities, approximately 159 million Americans--almost two-thirds of the nation's population--already possess the right to buy annuities from state-chartered banks.

In addition, at least 45 states permit banks to lease lobby or office space to third-party insurance agencies and agents, and numerous states permit rental of bank customer lists for third-party insurance selling.[89] Several restrictive states previously permitted banks to have broader insurance agency powers, because grandfathering provisions were granted to bank agencies when the laws were changed to restrict bank insurance powers. Among these states with license-grandfathering provisions are Arkansas, Colorado, Connecticut, Georgia, Louisiana, Massachusetts, New Mexico, Tennessee and Texas.[90]

Many state banks have historically sold a wide range of insurance. For instance, Indiana state banks have had insurance powers for a century. Almost a third of them currently engage in some form of insurance agency activities; yet Indiana's banking industry "has not dislocated local insurance agents, " but it "has provided a very fine level of service to the public."[91]

Independent Agents Own Almost Half the Bank-Based Insurance Agencies Nationwide

The Wyatt Co., a leading actuarial and consulting firm, recently surveyed insurance activities of approximately 2,000 banks nationwide and found that one-quarter had insurance agency operations beyond strictly credit-related insurance activities. Of those "expanded" operations, 40 percent of the bank agencies are owned by a bank. But an astounding 46 percent of bank insurance operations are actually owned by independent agents who are also directors or CEOs of the banks. Owners of independent insurance agencies appear to see nothing unfair about their "wearing two hats" as an agent and a bank CEO or director.[92]

In fact, many traditional insurance agents are playing an important part in bank sales of insurance products; and third-party marketers, a form of independent or brokerage general agency, are responsible for billions of dollars of insurance sold on behalf of banks. Bank-based agencies provide jobs by hiring full-time agents or using independent agents. At least "35 percent use both separate agents and existing annuity or mutual fund salesmen." Banks that do well frequently recruit salespeople and managers from the insurance industry. This means more opportunities for insurance agents.[93] Despite the legislative and regulatory roadblocks thrown in its path, the business of banks in insurance has created an estimated 45,000 new job opportunities.[94]

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89 Michael D. White, "Some Key Findings from FIIA's Survey of State Banking and Insurance Regulators," *The FIIA Survey of State Bank Insurance Laws*, 1995, p. 3.

90 *Ibid.*, p. 2.

91 James Gilleran, California Superintendent of Banks, quoted in Matthew Schwartz, "Banks in Insurance: Action Is At State Level," *National Underwriter*, October 29, 1990, pp. 3, 50.

92 The Independent Bankers Association & The Wyatt Company, *1991 Bank Insurance Activities Survey*, 1990, pp. 3, 8.

93 Evan Guillemin, "Faced with Exodus of Deposits, Banks Fight Back," *Financial Planning*, May 1992, pp. 37-39.

94 Association of Banks-In-Insurance, *Banks In Insurance Fact Book*, 1994, p. 5.

An astounding 46 percent of bank insurance operations are actually owned by independent agents who are also directors or CEOs of the banks. Owners of independent insurance agencies appear to see nothing unfair about their "wearing two hats" as an agent and a bank CEO or director.

Nationally, thousands of bank holding companies and banks--principally, state-chartered banks--are already legally empowered to sell noncredit-related insurance products. In doing so, they provide tens of thousands of jobs for those who sell insurance products to millions of bank customers. Banks in many states and small towns historically have engaged in insurance sales activities with no risk to the safety and soundness of the banking system. Instead, these banks have positively impacted their customers, agents, communities and the banks themselves.

Consumer Attitudes and Purchases in the Annuity Marketplace

Thus far, banks have made their greatest effort and had their greatest success selling annuities, a product traditional insurance agents do not sell very much--some think because annuity commissions are so much smaller than typical life insurance commissions. Annuity sales account for only 6 percent of traditional agents' first-year commissions.[95] Only about 1 in 4 annuities are purchased from traditional life insurance agents.[96]

When measuring the interest of consumers in talking to traditional agents about annuities, the ACLI found only 4 percent were "very interested" and 14 percent "somewhat interested." Twenty-two percent were "not too interested" and 53 percent were "not interested at all."[97] Yet 34 percent of respondents to a banking customer survey said they are willing to buy annuities from a bank, and 5 percent already had. Thirty percent said they would buy life insurance from a bank, and 10 percent already had.[98]

The desire for annuities among bank customers and growth in the annuity market are strong, especially since traditional life agents have largely neglected the annuity marketplace.[99]

Bank Customers Buy One-Third of New Individual Annuities

Agent neglect, banker efforts, and consumer interest explain the origin and subsequently rapid growth of bank annuity sales over the last decade. In 1987, consumers bought from financial institutions $4 billion of the $33.8 billion of individual annuities purchased, or 11.8 percent of the market. These were

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95 LIMRA, *The U.S. Survey of Producer Opinion*, 1991, p.16; J. Scott Dunn, "Annuities: Will They Continue To Shine?" *Marketfacts*, May/June 1992, pp. 35, 37.

96 D. Layne Rich, "Annuity Ownership: Highlights from the *1992 U.S. Annuity Ownership Study*," *Marketfacts*, 1993, pp. 22-23. According to this survey, banks sell 15 percent of all annuities (group and individual); financial planners account for 11 percent; and stockbrokers 8 percent. Five percent are bought direct from the company, and 30 percent are bought from employers.

97 ACLI, *1992 Monitoring Attitudes of the Public (MAP) Survey*, p. 68.

98 Ellen Memmelaar, "Public Willing To Shop Banks for A Range of Products," *American Banker Consumer Survey*, 1990, pp. 20-21; and E. Memmelaar, "Banking Public Favors One-Stop Concept," *American Banker*, October 2, 1990, pp. 1, 6.

99 Only 3 percent of U.S. households own individual nonqualified annuities, and only 1 percent of the population (or 2.5 million people) own more than one annuity. *Ibid.*, pp. 22-23.

virtually all fixed annuities.[100] By 1992, bank sales had tripled to $12 billion,[101] accounting for 26.5 percent[102] of the total $45.2 billion sold.[103] In 1993, annuity sales by banks were a whopping 32.2 percent of the market.[104] (See Table 7.)

Table 7. Bank Market Share of U.S. Individual Annuity Premiums

Year	Total Individual Annuity Receipts in the 50 States and District of Columbia (a) ($ Billions)	Annuity Premiums by Banks (b) ($ Billions)	Bank Share (c) (Percent)
1990	45.02	8.0	17.8
1991	43.43	9.0	20.7
1992	45.21	12.2	27.0
1993	41.97	13.5	32.2

Sources: (A) AMERICAN COUNCIL OF LIFE INSURANCE (ACLI)
(B) KENNETH KEHRER ASSOCIATES
(C) INSTITUTE OF BANK INSURANCE STUDIES (IBIS)

Final 1994 annuity sales figures for banks and the entire insurance industry are not yet available. However, bank annuity sales were up 29 percent for the first half of 1994,[105] projecting a year-end sales total of $17.4 billion. If this growth trend continues, bank annuity sales will exceed $29 billion in 1996.

Of additional interest is the growth of bank variable annuity sales. In 1990, sales were a relatively meager $100 million. In 1991, they grew to $500 million in 1991.[106] By 1992 bank variable annuity sales had more than doubled to $1.35 billion.[107] In 1993 they doubled again to approximately $2.8 billion. 1994 bank variable annuity sales are projected to double again to $5.6 billion. That projected number is almost equal to total bank annuity sales in 1988 and half of all variable annuity sales in 1992.[108]

These facts and figures demonstrate that, in an open insurance marketplace in which they are at liberty, consumers exercise their freedom of choice to buy products where they please; and consumers often choose to buy their insurance products through banks. All that is needed now is an economic and legal system that liberates all banks to serve as a greater source for meeting consumers' alternative insurance preferences.

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100 Kenneth Kehrer, "Bank Annuity Sales Surge During 1992," *Bank Investment Representative*, January/February 1993, pp. 12, 14, 16.

101 *Ibid.*, pp. 12, 14, 16.

102 Michael D. White, "Banks Have Won a Third of Individual Annuity Market," *American Banker*, January 9, 1995, p. 19; Michael D. White, "Banks Now Command One-Third of Annuity Market," *Bank Insurance Marketing*, Winter 1995, pp. 10-11.

103 ACLI, *1993 Life Insurance Fact Book Update*, p. 39.

104 Michael D. White, "Banks Have Won a Third of Individual Annuity Market," *American Banker*, January 9, 1995, p. 19; Michael D. White, "Banks Now Command One-Third of Annuity Market," *Bank Insurance Marketing*, Winter 1995, pp. 10-11.

105 "Bank Annuity Sales Up 29 Percent," *Newsletter of the Bank-Insurance Industry*, Number 3, 1994, pp. 1, 3, 6.

106 Mary G. Moore, "Sales Savvy is Sorely Needed," *Financial Services Week*, April 6, 1992, pp. 1, 33.

107 Jeffrey Marshall, "Variable Annuities: Hope or Hype?" *United States Banker*, June 1993, pp. 25-26.

108 "Bank Annuity sales Up 29 Percent," *Newsletter of the Bank-Insurance Industry*, #3, 1994; Kenneth Kehrer, "Bank Annuity Sales Surge During 1992," *Bank Investment Representative*, January/February 1993, pp. 12, 14, 16.

> ***"In selling insurance, banks do not assume the risk of insurance underwriters, and banks' capital remains unimpaired.... On balance, we believe that selling insurance entails minimal risk for banks. In addition, we believe that consumers may benefit through increased services, greater convenience, and potentially lower insurance prices."***
>
> - TREASURY UNDERSECRETARY FRANK NEWMAN BEFORE THE SENATE BANKING COMMITTEE, NOVEMBER 2, 1993

BANK SAFETY AND SOUNDNESS, AND COERCION OF CONSUMERS: THE AGENT ASSOCIATIONS' OLDEST STRAW-MEN

National insurance agent trade associations have long opposed bank entry into insurance sales activities. Key to their efforts to keep banks out of the insurance marketplace have been flimsy straw-men arguments about bank safety and soundness and customer coercion. They argue that selling annuities and insurance jeopardizes the safety and soundness of banks, threatening to make them insolvent. Additionally, they claim that banks coerce--or might coerce--customers into buying insurance by refusing to extend credit until customers first purchase insurance products from them.

These claims are without merit and range from being scurrilous denials of fact to being just plain silly. Yet, the safety, soundness and coercion "arguments" are their bread and butter of disinformation.[109]

Bank Insurance Is Safe and Sound

The sale of insurance is an agency activity, and it is universally recognized that agency activities present no safety and soundness risks to banks. Offering life insurance products through banks, however, does benefit consumers. Previous and current Administrations, Treasury officials, federal bank regulators, government research offices, and past congressional legislative actions have consistently and universally acknowledged this.

> ***"The [Federal Reserve] Board sees no argument on either competitive or risk-management grounds to retain or impose limitations on insurance agency activities.... Broader insurance authority would provide wider household and business choices at better prices."***
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> - JOHN P. LAWARE, GOVERNOR, FEDERAL RESERVE SYSTEM, BEFORE THE SENATE BANKING COMMITTEE, OCTOBER 5, 1993

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109 Most recently, David Winston, associate general counsel for the National Association of Life Underwriters (NALU), sarcastically claimed: "Banks have never met Adam Smith. Banks want annuity powers so they can coerce consumers into buying products and increase fee income." Steven Brostoff, "Industry Ponders Next Move After VALIC Setback," *National Underwriter*, January 23, 1995, pp. 1, 42.

Deputy Treasury Secretary Frank Newman noted, "We believe that national banks' insurance activities under current law pose no safety and soundness problems. In selling insurance, banks do not assume the risk of insurance underwriters, and banks' capital remains unimpaired . . . . On balance, we believe that selling insurance entails minimal risk for banks. In addition, we believe that consumers may benefit through increased services, greater convenience, and potentially lower insurance prices."[110]

The Federal Reserve Board governors agree that bank insurance agency activities should be permitted because they represent no threat to banks' safety and soundness. "The Board sees no argument on either competitive or risk-management grounds to retain or impose limitations on insurance agency activities . . . . Broader insurance authority would provide wider household and business choices at better prices."[111]

> ***"The argument that selling insurance creates safety and soundness problems for banks simply lacks credibility, while the argument that selling insurance would benefit consumers seems virtually self-evident."***
>
> - EUGENE LUDWIG, COMPTROLLER OF THE CURRENCY

Former Comptroller of the Currency Robert L. Clarke concluded, "expanded insurance activities would not impair the safety and soundness of banks."[112] And his successor, Eugene Ludwig, recently reaffirmed the same view that "the argument that selling insurance creates safety and soundness problems for banks simply lacks credibility, while the argument that selling insurance would benefit consumers seems virtually self-evident."[113]

> ***"In 8,000 banks we regulate, we have not seen one instance where banks were put at risk because of insurance activities."***
>
> - WILLIAM SEIDMAN, THEN-CHAIRMAN, FEDERAL DEPOSIT INSURANCE CORPORATION

Before a Senate Banking Committee hearing, Comptroller Ludwig testified that "permitting national banks to sell a broader array of insurance products and services would not pose any material risk to the safety and soundness of individual banks, or any systemic risk to the banking system as a

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110 Frank Newman, "Statement before the Committee on Banking, Housing and Urban Affairs, United States Senate," November 2, 1993, pp. 16, 18.

111 John P. LaWare, Member, Board of Governors of the Federal Reserve System, "Statements to Congress before the Committee on Banking, Housing, and Urban Affairs, U.S. Senate, October 5, 1993, *Federal Reserve Bulletin*, December 1993, pp. 1093-1097.

112 Comptroller Robert L. Clarke, testimony before a House Engery and Commerce subcommittee, quoted in Steven Brostoff, "Bank Regulators Urge Insurance Sales," *National Underwriter*, September 19, 1988, pp. 3, 20.

113 Brendan Intindola, "Comptroller Plumps For Bank Insurance Sales," *National Underwriter*, September 20, 1993, pp. 1, 39. See also Kenneth H. Bacon, "U.S. Comptroller Favors Letting Banks Sell Insurance, Other Financial Services," *The Wall Street Journal*, September 14, 1993, p. A20.

whole."[114] Limiting banks' powers to offer insurance to their customers "impoverishes our marketplace and economy."[115]

Speaking at the 1988 annual convention of the ACLI, William Seidman, then-chairman of the Federal Deposit Insurance Corporation (FDIC), noted: "In 8,000 banks we regulate, we have not seen one instance where banks were put at risk because of insurance activities."[116] That's an outstanding record for all banks that have any kind of insurance selling powers; it's also a tribute to those insurance agents who are directors or officers of state banks and also own the agencies that sell insurance on their behalf.

The United States General Accounting Office (GAO) concluded that "expanded bank sales of insurance...would not endanger bank safety and soundness, . . . [but rather] could strengthen safety and soundness and protect against bank failure."[117] Little wonder, then, that, in passing the Financial Institution Reform, Recovery, and Enforcement Act of 1989 (FIRREA) and the FDIC Improvement Act of 1991 (FDICIA), Congress rejected the notion that insurance agency activities pose a risk to insured depository institutions. Those Acts imposed limitations on the activities of savings and loans and state banks in order to reduce their potential to engage in unsafe or unsound activities. Those Acts did not restrict insurance agency activities by thrifts or state banks.

> ***"Expanded bank sales of insurance...would not endanger bank safety and soundness, . . . [but rather] could strengthen safety and soundness and protect against bank failure."***
>
> - UNITED STATES GENERAL ACCOUNTING OFFICE

Debunking the Coercion Myth

Federal and state laws make it illegal for banks to coercively tie the sale of insurance to any extension of credit. Thus, it is not surprising that study after study shows that banks do not coerce their customers into buying insurance products from them. Research over the last three decades includes a study by the National Association of Insurance Commissioners (1970), The Ohio University Study (1973), The Huber Study (1976), University of Michigan/ Federal Reserve Board consumer credit survey (1977), Federal Reserve Board study of tie-ins (1978), University of Michigan/Federal Reserve Board consumer attitude and credit insurance survey (1985), Federal Reserve Board report on consumer experiences with credit insurance (1986), a study published in the *Journal of Insurance Regulation* (1988), Gallup/*Best's Review* consumer poll (1990), and the GAO study of bank insurance powers (1990). These and other research studies disprove claims of coercive tie-ins between insurance purchases and loans.

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114 Eugene Ludwig quoted in Steven Brostoff, "Bank Regulators Push for Bank Insurance Powers," *National Underwriter*, October 18, 1993, p. 10.

115 Eugene Ludwig quoted in John M. Covalski, "Clinton's Man Sides with Banks," *Best's Review*, February 1994, pp. 20-22, 24-25, 28-29.

116 Stephen Piontek, "Seidman: 'You Can't Protect Industry Through Politics,' *National Underwriter*, November 21, 1988, pp. 3, 5.

117 United States General Accounting Office, *Bank Powers: Issues Relating to Banks Selling Insurance*, GAO/GGD-90-113, September 1990, pp. 5-6.

A 1985 Federal Reserve Board study showed that approximately 95 percent of all borrowers believed that taking credit insurance made no difference in whether the lender could or would grant the loan. Indeed, consumers thought credit insurance was a good product, which they would buy again, and recommend to others.

The Office of the Comptroller of the Currency and Board of Governors of the Federal Reserve System determined there is no evidence of coercive tie-ins in states that allow banks to sell insurance and "there is no competitive or risk related rationale to justify further restrictions on the conduct of insurance agency activities by banking organizations."[118] Coercion "is not a widespread or significant problem in lending by banks or bank holding companies."[119] The 1990 GAO study echoed these findings.[120]

Surveys of state banking and insurance departments indicate that coercive tie-ins in the sale of insurance by banks are very rare. Regulators expressed no concern to the GAO about abuses in small town banks.[121] Nor is there evidence of systemic coercion in bank sales in states where banks sell insurance. A 1994-95 survey of state regulators about possible abusive bank insurance practices drew responses from 27 states. Each of their responses summed up the experience of all: coercive tie-ins by banks are negligible to nonexistent.[122]

The American Insurance Association conceded that "deposit-taking institutions generally do not dominate their markets to such an extent that substantial market powers could be used to force their way into the insurance market by compelling the purchase of an insurance product by their depositors."[123] "Coercion by banks is more myth than fact. Studies such as those reported by the *Journal of Insurance Regulation* reveal that 'while the possibility for coercion does exist, the threat is not great enough to justify prohibiting banks from engaging in insurance distribution.'"[124]

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118 H. Robert Heller, Governor, Federal Reserve System, quoted in Steven Brostoff, "Bank Regulators Urge Insurance Sales," *National Underwriter*, September 19, 1988, pp. 3, 20.

119 Letter to Senator William Proxmire, Chairman of the Senate Committee on Banking, Housing and Urban Affairs, from G. William Miller, Chairman of the Board of Governors of the Federal Reserve System, October 6, 1978.

120 United States General Accounting Office, *Bank Powers: Issues Relating to Banks Selling Insurance*, GAO/GGD-90-113, September 1990, pp. 3-4.

121 United States General Accounting Office, *Bank Powers: Issues Relating to Banks Selling Insurance*, GAO/GGD-90-113, September 1990, pp. 21-23.

122 Michael D. White, "Some Key Findings from FIIA's Survey of State Banking and Insurance Regulators," *The FIIA Guide to State Bank Insurance Laws*, 1995, p. 3.

123 Edgar W. Armstrong, Jr., "Overview: Bank Insurance Regulation," *The Banker's Guide To Income-Producing Insurance*, 1989, pp. 213-217.

124 Scott J. Cipinko, letter to *National Underwriter* (P/C), January 1, 1990, pp 13-14. See Jerry D. Todd and Michael L. Murray, "Banks in Insurance: Increase or Reduce Competition?" *Journal of Insurance Regulation*, June 1988, pp. 518-537.

Commercial banks provide a shrinking minority of consumer and mortgage loans. Yet all other credit providers, including diversified insurance groups that own banks and engage in consumer lending--are permitted to sell insurance. "Coercive tie-ins" is not raised as an issue with these lenders that also sell insurance products.

Consumer studies indicate coercion is not a concern for most consumers. The 1990 Gallup/*Best's Review* poll revealed that the vast majority of consumers do not fear coercion when purchasing insurance from banks.[125] A 1985 Federal Reserve Board study showed that approximately 95 percent of all borrowers believed that taking credit insurance made no difference in whether the lender could or would grant the loan. Indeed, consumers thought credit insurance was a good product, which they would buy again, and recommend to others.[126] Moreover, 30 percent of consumers prefer to buy noncredit insurance from banks, and 30 percent have bought insurance through nontraditional sources. Almost half prefer to buy or would consider buying insurance without the use of a traditional agent.[127]

Finally, it is important to note that banks are not the dominant source for consumer credit. In fact, commercial banks provide a shrinking minority of consumer and mortgage loans.[128] Yet all other credit providers--savings and loans, credit unions, mortgage companies, finance companies, and other lenders, including diversified insurance groups that own banks and engage in consumer lending--are permitted to sell insurance.[129] "Coercive tie-ins" is not raised as an issue with these lenders that also sell insurance products.

Aetna, Gulf & Western, J.C. Penny, Control Data, ITT, American Express, AVCO, John Hancock, The New England, Merrill Lynch, Montgomery Ward, Ford Motor Co., General Electric, USAA, Prudential, Sears/Allstate, Metropolitan

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[125] The GALLUP/*Best's Review* Survey, "Bank Coercion Not a Concern for Most Consumers," *Best's Review* (P/C edition), September 1990, p. 12.

[126] Anthony W. Cyrnak and Glenn B. Canner, "Consumer Experiences With Credit Insurance: Some New Evidence," *Federal Reserve Bank of San Francisco Economic Review*, 3, Summer 1986, pp. 5-20.

[127] A research survey by Claritas Corp. reported in Howard L. Lax, "Life Insurance Survey Has Some Good News for Banks," *American Banker*, July 26, 1990, p. 9.

[128] James L. Pierce, *The Future of Banking*, The Twentieth Century Fund, Inc., 1991, pp. 80-81. See also "Home Loans Up, Other Consumer Loans Down," *ABA Banking Journal*, December 1992, pp. 83-84; and United States General Accounting Office, *Bank Powers: Issues Relating to Banks Selling Insurance*, GAO/GGD-90-113, September 1990, p. 29.

[129] See, for instance, Robert E. Litan, *What Should Banks Do?*, The Brookings Institution, 1987, pp. 112-117; James L. Pierce, *The Future of Banking*, The Twentieth Century Fund, Inc., 1991, pp. 73-74; Dennis W. Toivonen, "What's Good for the Goose..." *Best's Review* (P/C), April 1990, pp. 28-30, 32, 84; E. James Morton, president and chief operating officer, John Hancock Mutual Life Insurance Co., "The Futility of Supporting Barriers in the Financial Services Arena," *American Banker*, May 28, 1986, pp. 8-10, 14; Lynn Brenner, "Crosscurrents: Bank/Insurance Update," *American Banker*, June 23, 1986, pp. 1, 19, 21; Thomas W. Thompson, "They Know How To Sell," *United States Banker*, May 1987, pp. 70, 72; Philip S. Corwin, "ABA Director Responds To IIAA President On Banks," *National Underwriter*, January 22, 1990, pp. 13, 20; "Looks Like 'Full Service' Financial Services Providers Will Dominate The Next Decade," *Inside Financial Services Marketing*, July 30, 1990, p. 1; Mitchell Pacelle, "Financial Firms Push Residential Services," *The Wall Street Journal*, September 16, 1992, p. B1; and Peter Pae, "Loophole Lenders," *The Wall Street Journal*, November 17, 1992, p. A1. A13.

> ***"Why is it wrong for banks to sell insurance, but OK for insurance companies to sell all sorts of non-insurance financial products? Unless the industry can answer that question to the satisfaction of the public, it's going to be extraordinarily difficult to forestall further banking incursions."***
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> \- EDITOR, "SOME HARD QUESTIONS," *NATIONAL UNDERWRITER*

Life, and Xerox are some of the major corporations that both make loans and sell insurance. These companies cross-sell credit, insurance and other financial products and services. They offer credit cards, CDs, residential mortgages, commercial and consumer loans, and checking accounts. When Prudential bought a thrift in Georgia in 1989, the insurer observed that this purchase would "allow it to expand its banking business, which operates nationwide through its network of agents." The country's largest insurance company markets credit cards, certificates of deposit and other banking products through Prudential Bank & Trust Co.[130] In fact, Prudential Home Mortgage is "one of the most active players in home mortgages," ranking as "the nation's No. 2 residential lender."[131]

In response to this double standard, even the editor of the *National Underwriter* asked, "Just answer me one thing: Why is it wrong for banks to sell insurance, but OK for insurance companies to sell all sorts of non-insurance financial products? Unless the industry can answer that question to the satisfaction of the public, it's going to be extraordinarily difficult to forestall further banking incursions."[132]

Not All State Agent Trade Associations Oppose Bank Insurance Sales

Bankers and traditional insurance agents are not born enemies. In states where both traditional and bank insurance agencies developed at the same time, competition between traditional agents and bank-based agents is viewed as healthy and wholly American. Of the agents doing business in midwestern states, 50 percent of them are estimated to work for or with bank-owned insurance agencies. John Randers, who oversees agencies in South Dakota, Minnesota, Nebraska and Iowa for Norwest Bank, says, "The whole insurance population, particularly in the rural Midwest, is populated by former bank agents. The two groups [i.e., bank agents and traditional agents] get along pretty well."[133]

Agent representatives in states that already permit banks to sell insurance say coercion is "not a major factor." Agents peacefully coexist with lenders. As a matter of fact, in those states, the banks and their agents are "professional members of the insurance community."[134] Says one owner of three Minnesota agencies, one of which rents space in a bank, "Coercion has been the age-old argument . . . , but . . . it's not a problem." Forty percent of the state's agencies are bank-owned, and 85 percent of all

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[130] Michael Weinstein, "Prudential's Thrift Purchase Strengthens Foothold in Banking," *American Banker*, August 9, 1989, p. 3; and Paulette Thomas, "Prudential Gets Approval to Buy An Ailing Thrift," *The Wall Street Journal*, August 8, 1989.

[131] Phil Roosevelt, "Prudential Emerges as Mortgage Giant," *American Banker*, April 10, 1992, p. 1; and Jonathan S. Hornblass, "Amex Hires Prudential to Sell Loans to Cardholders," *American Banker*, February 7, 1995, p. 9.

[132] Joe S. Diamond, "Some Hard Questions," *National Underwriter*, November 7, 1988, p. 24.

[133] Nick Janulis, "Agents and Bankers Pursuing Paths to Harmony," *Bank Insurance Marketing*, Spring 1993, pp. 15-18.

[134] Colleen Mulcahy, "Banks and Agents: Is The Battle Worth The Cost," *National Underwriter*, July 10, 1989, pp. 31, 38.

Minnesota banks have an insurance agent on-site. Half the members of the Minnesota Insurance Agents Association work in banks.[135]

> ***Bankers and traditional insurance agents are not born enemies. In states where both traditional and bank insurance agencies developed at the same time, competition between traditional agents and bank-based agents is viewed as healthy and wholly American. Of the agents doing business in midwestern states, 50 percent of them are estimated to work for or with bank-owned insurance agencies.***

"People have to realize that in a lot of small towns, they wouldn't have an agent if not for the bank," adds the executive vice president of the Independent Insurance Agents of South Dakota, another state where 40 percent of member agencies are bank-based.[136] The executive director of the Professional Insurance Agents of Wisconsin asserted, "In Wisconsin--where banks have been selling insurance 'practically since day one'--agents have had few problems with lenders."[137] The executive vice president of the Independent Insurance Agents of Indiana affirmed, "There are valid reasons for an independent agency to work with a bank."[138]

Indeed, the Insurance Opportunities Network (ION) is an excellent example of the professional, collegial spirit that exists in states with a history of both traditional and bank-based agency distribution systems. This five-year-old organization is composed of a group of more than 250 rural agencies in Minnesota and North Dakota. This personal-lines network serves as a market-finder for participating agents who need access to insurance carriers that offer much-needed product. "In fact, the network was created in part by bankers--the Independent Community Bankers Associations in Minnesota and North Dakota--in an effort to solve the market problems of their insurance operations."[139] Yet ION is open to all agents who pay the modest up-front membership fee. Significantly, 40 percent of the participants are traditional insurance agencies and agents. ION is another example of how bank insurance agencies do not coerce clients or stifle competition, but instead serve the needs of customers and other agents in a competent and professional manner.

Most Big Life Insurance Companies Sell Insurance Through Banks and Other Financial Institutions

Despite the opposition of agent trade associations to bank insurance, not all agents share this anti-competitive perspective. Neither do the opponents of banks-based insurance distribution garner much support these days from the insurance companies.

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135 Colleen Mulcahy, "Agents Support Banks' Right To Sell Insurance," *National Underwriter*, July 10, 1989, pp. 31, 36-37; United States General Accounting Office, *Bank Powers: Issues Relating to Banks Selling Insurance*, GAO/GGD-90-113, September 1990, p. 29.

136 Colleen Mulcahy, "Agents Support Banks' Right To Sell Insurance," *National Underwriter*, July 10, 1989, p. 31.

137 *Ibid.*, p. 37.

138 *Ibid.*, p. 37.

139 Colleen Mulcahy, "Small, Rural Agencies Gain Markets, Clout Via Network," *National Underwriter* (P/C), January 10, 1994, pp. 9-10.

In his farewell address as 1989 chairman of LIMRA, Robert Bates, president and CEO of Guarantee Mutual Life of Omaha, declared that granting expanded insurance powers to all banking organizations "could . . . provide growth opportunities for both banks and life insurers." Mr. Bates told LIMRA's annual conference that vociferous opposition to bank entry into insurance sales "may serve the interests of some, but it is not the opinion of all segments of the business." Mr. Bates observed, "The number of people selling life insurance needs to increase, not decrease." He added that permitting banks additional insurance agency powers could "turn this issue into an opportunity for growth and expansion for our industry."[140]

Over 75 percent of the nation's 50 largest life insurers market products through banks and other financial institutions.

A 1988 Lou Harris poll showed "considerable interest in...selling insurance products through banks." It also showed that 34 percent of life and health insurers use banks and other retailers to distribute products. More than 4 out of 5 insurers reported they planned to increase their distribution through banks.[141] In 1990 A.M. Best reported that 67 percent of banks and 45 percent of insurance companies polled "are active in bank/insurance marketing, and that such activities are highly profitable."[142]

A 1990 headline in the *National Underwriter* called attention to insurer activity in the bank marketplace: "Biggest Life Companies Selling Through Financial Institutions." The article was based on a Tillinghast/Towers Perrin survey of the top 112 life companies based on assets. Results showed that over 75 percent of the nation's 50 largest life insurers market products through banks and other financial institutions. Eighty percent of those insurers active in this market distribute annuities; 32 percent, universal life; 24 percent, term life insurance; 18 percent (none of which are bank-owned) market credit life insurance; and 15 percent, permanent or whole life insurance.[143]

Not surprisingly, Ernst & Young's subsequent survey of insurance executives found that more than 80 percent expect a rise in bank/life insurance company alliances in the 1990s. "Banks will become a significant distribution channel for insurance, and they will have a fairly good share of the insurance market," the firm concluded. However, "there will still be lots of room for other distribution methods other than through banks," the report affirmed.[144]

While some life insurers may be publicly quiet in the debate over bank annuity and life insurance distribution in order not to provoke their traditional agency forces, most big-name companies are already actively distributing their insurance products through banks and other depository and lending institutions.

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140 David C. Jones, "Threat From Banks May Be Overstated: Bates," *National Underwriter*, December 4, 1989, pp. 4, 30.

141 Walter Bussewitz, "Insurers Backing Out of Bank Lobbies," *Life Association News*, July 1988, pp. 41, 42, 44, 46. See also United States General Accounting Office, *Bank Powers: Issues Relating to Banks Selling Insurance*, GAO/GGD-90-113, September 1990, p. 28.

142 *Best's Insurance Management Reports* (P/C), Release No. 45, November 5, 1990, p. 6. See also Colleen Mulcahy, "Agents Profit from Bank Link-Ups," *National Underwriter*, November 19, 1990, pp. 15-17.

143 David C. Jones, "Biggest Life Companies Selling Through Financial Institutions," *National Underwriter*, July 16, 1990, pp. 1, 4. For more detail, see Tillinghast/Towers Perrin, *Survey on Marketing Insurance Products Through Financial Institutions*, 1990.

144 Matthew Schwartz, "Insurers Eye Alliances With Banks," *National Underwriter*, July 22, 1991, p. 19.

These insurers are doing ever larger and more substantial volumes of bank-based business, through their parent companies or lesser-known subsidiaries. In recent years, the list has included many well-known names, among them:

Aegon, Aetna, AIG, Alexander Hamilton, Allstate, American General, American Life of New York, American Life and Casualty, Ameritas, Beneficial Standard, Blue Cross, Capitol Holding, Chubb Life, Colonial Penn, Conseco, Continental, Equitable Life, F & G, Fidelity Bankers, Fireman's Fund, Ford Life, Fortis Financial, GEICO, General Electric's GNA, Great West Life (Denver), The Hartford, IDS, Integon, ITT Life, Jackson National, JC Penny Life, John Alden, John Hancock, Kemper, Keyport, Liberty Mutual, Life of Virginia, Lincoln National, Manulife, Metropolitan, Minnesota Mutual, Mutual of New York (MONY), National Home, Nationwide, The New England, Pacific Mutual, Penn Mutual Life, Protective, The Prudential, Royal Life, SAFECO, Security First, State Farm, Sun Life, Time Life, Transamerica (Occidental), Travellers, GE Capital's United Pacific, UNUM Life, USF&G, and Xerox Life.

Life insurers are the banks' allies and partners in the bank-insurance business.[145] Together, life insurers and banks are doing business in increasingly voluminous amounts. That's why four dozen life insurance companies and their marketing subsidiaries signed a letter to the Senate Banking Committee early in 1994 opposing the Dodd Amendment, which would have further restricted the ability of banks to sell insurance to their customers.[146]

Some life insurers may be publicly quiet in the debate over bank annuity and life insurance distribution, but most big-name companies are actively distributing their insurance products through banks and other depository and lending institutions.

As former LIMRA chairman Robert Bates indicated, the views of the majority of insurers and agent trade associations diverge. Agent associations have publicly disseminated the myth of "unity"-- that all segments of the insurance industry oppose bank agency powers and insurance distribution to banking customers.[147] However, the truth is that the vast majority of major insurers--and many small insurers, too--sell their products through banks and, consequently, are not united with agent trade associations in the latter's attempts to roll-back bank insurance powers. As a spokeswoman for the American Council of Life Insurance (ACLI), whose members number over 600, or 30 percent of, life insurance companies and account for approximately 94 percent of the life insurance in force in the United States,[148] recently said: "We aren't really opposed to banks selling insurance products . . . ."[149]

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145 "...[M]any [life insurers] have found lenders to be an attractive addition to their annuity distribution strategy." Editorial Comment, "Time For A Reality Check on Banks," *National Underwriter*, December 12, 1994, p. 16.

146 Letter to members of the U.S. Senate Banking Committee from the Coalition for Competition in Insurance Sales, February 22, 1994.

147 In the wake of the U.S. Supreme Court's unanimous decision in the *VALIC* case that banks may sell annuities, insurance agent trade associations announced that they will "be actively pursuing legislation" to roll-back bank insurance powers. David Winston, associate general counsel for the National Association of Life Underwriters (NALU), tried again to promote the myth of "unity" when he said, "I have every expectation that the insurance industry will be united on this." Steven Brostoff, "Industry Ponders Next Move After VALIC Setback," *National Underwriter*, January 23, 1995, pp. 1, 42.

148 Stephen J. Friedman, executive vice president and general counsel of The Equitable Life Assurance Society of the United States in a draft of testimony to be presented to Congress on behalf of the ACLI, July 1990, p. 1.

149 Kimberly Lankford and Joe Wilcox, "Supreme Court Speaks: Banks Win Annuity Rights," *Life Association News*, February 1995, p. 23.

SECTION THREE:
SOLVING THE LIFE INSURANCE CRISIS WITH FREE-MARKET COMPETITION

Another argument agent trade associations make against bank entry into the insurance business uses "competition" as its centerpiece. On the one hand, the associations contend that, if banks that lack insurance powers were to get them, they would be unable to compete with traditional agency distribution because banks "have no idea how to do the one-on-one counseling agents excel at. It's practically a certainty that banks will sell the wrong product to the wrong person at the wrong time for the wrong price."[150]

> ***"Very few agents indicate that they encounter competition on a sale-by-sale basis."***
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> - ERNIE CRAGG, THEN-CEO LIMRA, 1992

On the other hand, the agent trade associations claim, "We welcome competition from any realm. We're not afraid to compete. Why, our very business is competition." But, when banks try to enter the insurance marketplace, the agent associations cry, "We didn't mean banks. Banks engage in 'unfair competition.'" [151]

Opposition to competition and resistance to change is nothing new to insurance agent trade associations. Their history is one of using any and all possible objections to resist new products and new distribution methods. Bank insurance is just one current target of agent trade association contention.

Agent Associations Are Historically Against Competition

In 1971, Thomas P. Bowles, Jr., president and CEO of Georgia International Corp., warned a gathering of life insurance executives that "many companies blindly and almost arrogantly defend the so-called agency system." He observed that "the insurance industry has the unenviable reputation as being 'against'--against social security,...against equities and variable annuities." Mr. Bowles declared, "Particularly did agency leadership at all levels fight like a cornered coon any threat to its comfort and security."[152]

In order to protect their oligopoly, agent trade associations (and certain insurance companies) have historically opposed progressive advances and developments that have broadened distribution of life insurance and its protective coverage. According to insurance historian J. Owen Stalson, these advances in life insurance coverage "have given the industry many an uneasy hour, although it has perhaps been more helped than hampered by these developments."[153]

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[150] Steven Sullivan, "Don't Bank on Insurance," *Life Association News*, July 1993, pp. 60-67.

[151] For recent examples, see Michael D. White, "Bank Insurance Engine Stalled in Michigan," *Bank Insurance Marketing*, Summer 1994, pp. 30-32; Michael D. White, "Remember the Maine...Amendment," *Bank Insurance Marketing*, Autumn 1994, pp. 37-39; and Michael D. White, "How Well Are Citizens of Maine Served by the Traditional Agency System," *Bank Insurance Marketing*, Autumn 1994, p. 39.

[152] Janet Corrado, "Agency System Is Millstone of Life Marketing Strategy," *National Underwriter*, October 9, 1971, pp. 1, 7, 8. See also Editorial Comment, "Those Agentless Sales," *National Underwriter*, December 18, 1971, p. 16.

[153] J. Owen Stalson, *Marketing Life Insurance: Its History in America*, 1942 and 1969.

Initially, agents and some companies opposed group life insurance and, euphemistically speaking, "made a concerted effort to ease the momentum of . . . a trend toward the mass distribution of life insurance."[154] Savings Bank Life Insurance (SBLI) was "an especially sore point with regular life [insurance sales] men."[155] When trust officers and SBLI agents wanted to earn the CLU, the professional life insurance designation, their applications caused "heated discussion" among the agents who comprised the Board of Trustees of The American College. Eventually, the SBLI agents were permitted to enroll in the college's CLU program, but The American College continues to resist marketing the CLU program to SBLI and other bank insurance agents.[156]

Opposition to change has been the hallmark of the traditional agency system. In the 1930s, agents "fought the passage of Social Security legislation."[157] In the 1940s and 1950s, agents opposed the sale of mutual funds by "renegade" agents, and ostracized life agents who sold them. The early years of the variable annuity saw tremendous "infighting." "The fledgling variable annuity company was opposed by the entire industry."[158] Today, most life insurance agents are securities-licensed members of the National Association of Securities Dealers and sell billions of dollars of mutual funds and variable annuities.[159] Moreover, many supported their old nemesis, the Variable Annuity Life Insurance Company, in its lawsuit to prevent national banks from selling annuities.[160]

When the New York Stock Exchange approved the licensing of its member firms to sell life insurance,[161] established agents cried "foul." When universal life insurance was first introduced, vocal agents opposed its development, its sale, and its lower commission schedule. When universal life commissions were subsequently increased, agents learned to love universal life, and it ultimately became the fastest selling product in the mid-1980s.

More recently, agents and their trade associations have vociferously opposed the direct marketing of life insurance products "to people who have already indicated they want to buy directly by phone or mail." These agents caused Prudential Insurance to scuttle its attempts to reach an under-served market. In an effort to offer their "customers choices," the company launched the PruDirect program in

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[154] Davis W. Gregg, *An Analysis of Group Life Insurance*, 1950, p. 19. See also Davis W. Gregg, *Group Life Insurance*, 1962; C. Manton Eddy, "Development and Significance of Group Life Insurance," Robert D. Eilers and Robert M. Crowe, eds., *Group Insurance Handbook*, 1965, pp. 45-56; and Louise Wolters Ilse, *Group Insurance and Employee Retirement Plans*, 1953, pp. 48-54.

[155] J. Owen Stalson, *Marketing Life Insurance: Its History in America*, 1942 and 1969, p. 568. See also Steven F. Sullivan, "N.Y. State's SBLI Group Hole," *Life Association News*, July 1993, p. 62.

[156] Mildred F. Stone, *A Calling and Its College*, 1963, p. 138; interview with Davis W. Gregg, former president of The American College, November 1992.

[157] Alan Press, "What Are We For?" *Life Association News*, March 1989, p. 17.

[158] Robert P. Gatewood, "Let Life Begin in the '90s," *National Underwriter*, December 4, 1989, pp. 10, 18-19.

[159] In 1993, 82 percent of career ordinary life insurance agents were NASD registered, with 7 percent planning to obtain registration. Of those registered, 39 percent "placed noninsurance products for 10 percent of their commissions." LIMRA, *1993 Survey of Producer Opinion: Producer Background Characteristics*, 1994, pp. 3-4.

[160] By unanimous decision, the U.S, Supreme upheld the right of national banks to sell fixed and variable annuities. See *NationsBank of North Carolina v. VALIC* (S. Ct. Nos. 93-1612; 93-1613), January 18, 1995.

[161] "Big Board OKs Life Insurance Sales by Member Firms," *National Underwriter*, November 27, 1971, pp. 1, 17.

September 1994. The following month Prudential bowed to "very heated" agent pressure and temporarily withdrew the program.[162]

> ***"Antitrust laws are concerned with injury to* competition *and not to* competitors*. . . . [Bank] entry [into insurance agency activity] could only have a procompetitive effect."***
>
> - BANKING AND ANTITRUST EXPERT ROBERT E. LITAN, NOW DEPUTY ASSISTANT ATTORNEY GENERAL, ANTITRUST DIVISION, U.S. DEPARTMENT OF JUSTICE

Alan Press, past president of the National Association of Life Underwriters (NALU) objected that Prudential had gone into "direct competition" with its agents. He acknowledged that "the savings provided by buying PruDirect" were "significant" and compared Prudential's strategy to adultery. He condemned Prudential for "going into direct competition with [agents] with products that will look a lot better to most buyers." He accused Prudential of "knocking the agency distribution system." According to Mr. Press, agents "need this like we need bubonic plague." He wished the Prudential "total failure" and reminded agents they could "vote with their pens."[163]

And vote with their pens they did, as exemplified by one agent's letter to Prudential's CEO. The agent announced that he had just written a $4 million Prudential policy "because the customer insisted on it." However, he asserted it "would be the last Prudential business he would write unless [the CEO] nixed the direct selling of insurance." In January 1995, Prudential's CEO announced --in the words of the NALU--that "Prudential will not compete with its agency force by selling life insurance directly to the public." The NALU also noted, without protest, that Prudential will continue its "direct-to-the-consumer banking and mutual fund businesses."[164]

Effective Competition Is Not "Unfair Competition"

Despite agent association claims that banks don't need to sell insurance because there is more than enough competition among life insurance agents, the lack of coverage for low and middle-income households and the disproportionate sales to the affluent lead rational observors to conclude otherwise.

Addressing the ACLI's annual meeting in 1992, the president of the National Association of Life Underwriters, Stephen C. Shaw, stressed that 80 percent of his sales involved no competition. "The decision," Shaw stated, "is not whose product to buy, but whether to buy insurance at all."[165] Ernie Cragg, LIMRA's recently retired CEO, agreed. LIMRA studies show that "very few agents indicate that they encounter competition on a sale-by-sale basis."[166]

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162 Carole King, "Pru Reviews Direct Sales Move After Agent Protest," *National Underwriter*, December 12, 1994, p. 7; "Pru's No-Load Insurance Program Threatens Industry Upheaval," *Financial Planning*, December 1994, pp. 12, 16; News Analysis, "PruDirect Shakes Up Agents," *Life Association News*, December 1994, pp. 21, 27.

163 Alan Press, "Gettin' a Little on the Side," *Probe*, October 10, 1994, pp. 1-2.

164 Jeffrey R. Kosnett, "New Prudential Chief Yields on Direct Selling," *Life Association News*, February 1995, pp. 23-24.

165 Stephen C. Shaw quoted in Eric Weissman, "Shaw Urges Agents To Sell Americans on Saving," *Life Association News*, January 1993, pp. 30, 31.

166 Ernie Cragg, "Agents Have to See and Sell to More People," *Marketfacts*, May/June 1992, p. 1; interview with Ernie Cragg in Larry Albright, "What's Going on in the Life Insurance Business," *Life Insurance Selling*, June 1991, pp. 6, 8, 10, 12, 14, 17.

As advocates of governmental economic protection for a select group of insurance salespeople through restrictions on other competitors, agent associations seek protection of their oligopoly. Through concerted political, legal and lobbying action, they demand legal privilege to maintain their command of supply.

In contrast, where banks have their own licensed insurance agents and consumers buy insurance products from bank agents, traditional national agent associations claim this marketing success results from "unfair competition."[167] But a competitive marketing advantage or competitive performance does not translate into unfair competition. As banking and antitrust expert Robert E. Litan has said, "Antitrust laws are concerned with injury to *competition* and not to *competitors*."[168] At issue is whether the public is served well by sufficient competition, not whether particular competitors are able to compete effectively. In this regard, bank entry into insurance agency activity can "only have a procompetitive effect."[169]

Competition constitutes a rivalry between two or more parties who independently try to secure the business of another party by offering the most favorable terms, e.g., price, design, features, benefits, service, guarantees, convenience and so forth. Competition exists when many people or companies try to sell the same kinds of goods to the same buyers. Banks want to compete in marketing and selling life insurance.

As advocates of governmental economic protection for a select group of insurance salespeople through restrictions on other competitors, agent associations seek protection of their oligopoly. Through concerted political, legal and lobbying action, they demand legal privilege to maintain their command of supply. They attempt to justify this special protection by alleging a contradictory assortment of fantastic dangers that threaten if competitors are allowed into the marketplace.

The agent associations rail against bank distribution of insurance as a form of "unfair competition." But unfair competition is marked by injustice, partiality, or deception. It harms competition and engenders anti-trust concerns. Charges of unfair competition on the part of banks that sell insurance are groundless. Effective competition is not unfair competition.

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Agent associations intermingle the argument of "unfair competition" with that of "unfair trade practices." Unfair trade practices are specific acts of deception and misrepresentation in marketing,

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[167] See, for example, Steven Brostoff, "Banks Threaten Agency System," *National Underwriter*, January 22, 1990, pp. 3, 6.

[168] Robert E. Litan, *What Should Banks Do?*, The Brookings Institution, 1987, p. 139.

[169] *Ibid.*, p. 72.

selling and advertising. Evidence substantiating allegations of unfair trade practices on the part of banks marketing insurance does not exist.

Virtually all states permit banks either to directly sell insurance products or contract for their indirect sale by an independent agent via space leases, list rental arrangements, and so forth. In allowing bank-based selling arrangements of one sort or another, state governments permit competitive marketing. However, it is competitive marketing that agent associations truly oppose when they protest bank insurance powers. Competitive marketing is not unfair, nor is it an unfair trade practice. Competitive marketing is good business.

Bank Insurance is Not Unfair Competition

The GAO examined the matter of bank insurance competition and concluded that any competitive advantages banks enjoy over existing insurance agencies result from operational efficiencies attained through economies of scale and scope, not unfair competition.

These advantages are not unique to banks. Many large, diversified financial service providers have similar competitive advantages. For example, insurance companies have purchased independent agencies or agency computer systems in order to consolidate administrative functions and reduce operating costs. Independent agencies have joined consortiums and developed information systems to reduce processing costs.[170]

> ***In allowing bank-based selling arrangements, state governments permit competitive marketing. However, it is competitive marketing that agent associations truly oppose when they protest bank insurance powers. Competitive marketing is not unfair, nor is it an unfair trade practice. Competitive marketing is good business.***

Nonetheless, agent associations and their hired experts continue to argue that banks selling insurance constitute unfair competition. They claim that, if banks were universally allowed to sell insurance, "competition in insurance would decline and customer service would decline as well."[171]

However, when these agency advocates are sworn under oath and subject to cross-examination, they concede that their assertions are purely "speculation . . . not based on any empirical evidence whatsoever." They admit "the basic reason for the opposition of insurance agents . . . to banks in the insurance business is their own profit." They acknowledge they "have no reports . . . that there has ever been any problem whatsoever with respect to financial institutions' safety and soundness as a result of their having engaged in insurance sales activities." And, they confess there is no evidence "that that

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[170] United States General Accounting Office, *Bank Powers: Issues Relating to Banks Selling Insurance*, GAO/GGD-90-113, September 1990, pp. 30, 35.

[171] Testimony of Sophie M. Korczyk before the Committee on Banking, Housing and Urban Affairs, United States Senate, October 5, 1993, p. 1. Ms. Korczyk is the chief economic consultant for the Alliance for the Separation of Banking and Insurance, a coalition of agent trade associations that opposes bank distribution of insurance.

phenomenon [of insurance agencies being acquired or going out of business] has any relationship whatsoever to the sales of insurance by financial institutions."[172]

In fact, a 1990 study comparing the insurance markets of North Carolina, where banks have been permitted to sell insurance, and Virginia, where bank insurance legislation was being considered, documented that, in the seven years from 1981-87, the number of insurance agencies in North Carolina increased 50 percent from 1,738 to 2,598; and agencies per 10,000 residents rose from 2.92 to 4.05. Whereas, in Virginia, during a nine-year period from 1981-89 when banks could not sell insurance, agencies increased by only 35, or 2.6 percent; and agencies per 10,000 residents declined from 2.47 to 2.26. The study concluded "there is no evidence that permitting banks to distribute insurance will result in fewer insurance agents, agencies and premiums written."[173]

> ***"There is no evidence that permitting banks to distribute insurance will result in fewer insurance agents, agencies and premiums written."***

BANK INSURANCE POWERS MEAN FREE-MARKET COMPETITION AND CONSUMER FREEDOM OF CHOICE

Laws and regulations that deprive consumers of ready access to insurance products and services through their banking relationships inhibit competition and deny consumers freedom of choice. Arbitrary barriers to bank insurance powers buttress traditional insurance agency oligopoly, constrain competition, increase costs and decrease service.

Freedom to contract, on the other hand, assures freedom in the marketplace. Freedom to buy and sell insurance through banks nourishes competition and benefits consumers. In a time we call "the information age" and praise consumers as being "sophisticated," it is paternalistic to restrict their freedom to decide where they will purchase their own insurance.

Freedom of Competition Affords Opportunity and Growth

Freedom of competition in the U.S. insurance market is equivalent to free trade in foreign markets. Like the NAFTA and GATT treaties, bank insurance is about free trade and economic growth, about jobs and prosperity. The logic that drove the insurance industry's argument in favor of expanding insurance markets in other countries and its support for passage of NAFTA and GATT is the same logic that drives the argument in favor of expanding bank insurance distribution in the United States and justifies support for bank insurance.[174]

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172 Testimony of Sophie M. Korczyk in *Great Northern Insured Annuity Corporation, et. al. v. State of Florida, Department of Insurance*, Case Nos. 92-4332RP, et. al., Volume IX, December 18, 1992, pp. 1230-1377.

173 Neil B. Murphy and Dennis M. O'Toole, *Insurance Activities in Virginia and North Carolina: A Comparison of States with Differing Bank Participation in the Distribution of Insurance*, 1990.

174 See Michael D. White, "After NAFTA, Pass BAFTA," *Bank Insurance Marketing*, Winter 1994, pp. 30-31. There is this additional bit of reasoning as well: "As insurers become more global, they're developing links with multi-faceted financial services operations overseas, many of them affiliated with lenders. For them, maintaining our nation's status as one of the last remaining developed countries with federally-mandated separation of banks and insurance is unlikely to be a priority." Editorial Comment, "Time For A Reality Check on Banks," *National Underwriter*, December 12, 1994, p. 16.

Banks are a natural and, in many states, a traditional sales channel for insurance. Their sales record is strong and clean. Where permitted, bank insurance activities improve competition and customer service and provide more product access, insurance alternatives, and choices for more consumers, especially middle and low-income earners who are now sorely under-served by the traditional agency distribution system.

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Banks have relationships with households of all income levels, including 9 out of 10 households with annual incomes of less than $15,000. Therefore, they can offer insurance products to those sectors of the population that are largely ignored by the traditional insurance agency system. More individuals can choose to insure their own lives, relieving taxpayers of the social welfare burden of supporting families of deceased, uninsured heads of households.

Bank insurance agency increases employment opportunities and offers an alternative workplace for agents, including those struggling to stay in the insurance business under the traditional agency system. Because the number of consumers dealing with insurance agents increases, 4-year agent retention rates and incumbent agent survival rates will increase. By improving marketing opportunities for traditional insurance agencies and agents, expanded bank insurance powers will also improve customer service and reduce policy lapse ratios.

Competition and Consumer Choice Ensure Social and Economic Security

The life insurance industry's own data document a crisis situation in life insurance coverage, distribution and agent productivity. Too few sellers result in too few people owning sufficient life insurance protection, proving the dictum that the public is never advantaged when marketplace protections are given to narrow interest groups.

Forty percent of our population are uninsured and at least 50 percent are under-insured. With uninsured Americans needing at least $5 trillion in life insurance coverage, there are plenty of sales to be made and many uninsured lives and families to be protected. One agent's sale is not another agent's loss. Therefore, competition in insurance distribution is not a zero-sum game. The broader the sale of insurance to the general public, the more capital is invested to create more wealth, expand the economy, and create more jobs and greater need for life insurance.

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Freeing the insurance marketplace by expanding bank insurance powers will help solve America's life insurance crisis. Bank insurance activities represent competition and freedom of choice for consumers. These, in turn, can only produce more insurance protection for Americans, more jobs, and greater economic activity and productivity.

The life insurance industry's own data document a crisis situation in life insurance coverage, distribution and agent productivity. Too few sellers result in too few people owning sufficient life insurance protection, proving the dictum that the public is never advantaged when marketplace protections are given to narrow interest groups.

With expanded bank insurance powers, consumers have greater access to insurance protection at competitive prices; agents have additional job opportunities and income; banks sell more products; insurance companies improve their profitability; taxpayers are protected from increasing welfare tax burdens; and individuals, communities and the nation prosper.

Bank insurance is the reality in the global financial services marketplace, where banks, insurers and agents are free to compete. When the domestic marketplace for insurance products is fully opened to banks, the opportunity for economic growth at home will increase, and the public will be assured a greater and more enduring degree of economic freedom and security.