Chapter 24 Types of Insurers and Marketing Systems

Topics

- Overview of Private Insurance in the Financial Services Industry
- Types of Private Insurers
- Agents and Brokers
- Types of Marketing Systems
- Group Insurance Marketing

Overview of Private Insurance in the Financial Services Industry

- The financial services industry consists of:
  - Commercial banks
  - Savings and loan institutions
  - Credit unions
  - Life and health insurers
  - Property and casualty insurers
  - Mutual Funds
  - Securities brokers and dealers
  - Private and state pension funds
  - Government-related financial institutions

- Changes in the financial services industry include:
  - Consolidation means that the number of firms has declined due to mergers and acquisitions
  - Convergence means that financial institutions now sell a wide variety of financial products that earlier were outside their core business area

Types of Private Insurers

- Insurers can be classified by their organizational form:
  - Stock insurers
  - Mutual insurers
  - Reciprocal exchanges
  - Lloyd’s of London
  - Blue Cross and Blue Shield Plans
  - Health maintenance organizations (HMOs)
  - Other types of private insurers

- A stock insurer is a corporation owned by stockholders
  - Objective: earn profit for stockholders by increasing the value of stock and paying dividends
  - Stockholders elect board of directors
  - Stockholders bear all losses
  - Insurer cannot issue an assessable policy

- A mutual insurer is a corporation owned by the policyowners
  - Policyowners elect board of directors, who have effective management
  - Policyholders may receive dividends or rate reductions
  - There are three main types of mutual insurers:
• An advance premium mutual is owned by the policyowners; there are no stockholders, and the insurer does not issue assessable policies
• An assessment mutual has the right to assess policyowners an additional amount if the insurer’s financial operations are unfavorable
• A fraternal insurer is a mutual insurer that provides life and health insurance to members of a social or religious organization

• The corporate structure of mutual insurers is changing due to:
  – An increase in company mergers
  – Demutualization, whereby a mutual company is converted into a stock insurer by a pure conversion, merger, or bulk reinsurance
  – The creation of mutual holding companies
  – A holding company is a company that directly or indirectly controls an authorized insurer

• Lloyd’s of London is not an insurer, but a society of members who underwrite insurance in syndicates
  – Membership includes corporations, individual members (called Names), and limited partnerships
  – New individual members now have limited legal liability
  – Corporations with limited legal liability and limited liability partnerships can also join Lloyd’s of London
  – Members must meet stringent financial requirements
  – Lloyd’s is licensed only in a small number of jurisdictions in the U.S.

• A reciprocal exchange can be defined as an unincorporated organization in which insurance is exchanged among the members (called subscribers)
  – Insurance is exchanged among the members; each member of the reciprocal insures the other members
  – It is managed by an attorney-in-fact
  – Most reciprocals are relatively small and specialize in a limited number of lines of insurance

Types of Private Insurers

• Blue Cross and Blue Shield Plans are generally organized as nonprofit, community oriented plans
  – Blue Cross plans provide coverage for hospital services
  – Blue Shield plans provide coverage for physicians’ and surgeons’ fees
  – Most plans have merged into one entity
  – Many sponsor HMOs and PPOs
  – Some plans have converted to a for-profit status to raise capital and become more competitive

• A Health Maintenance Organization (HMO) provides comprehensive health care services to its members
  – Broad health care services are provided for a fixed prepaid fee
  – Cost control is emphasized
  – Choice of health care providers may be restricted
  – Less costly forms of treatment are often provided
• A captive insurer is an insurer owned by a parent firm for the purposes of
  insuring the parent firm’s loss exposures
  – A single parent, or pure, captive is an insurer owned by one parent
  – An association captive is owned by several parents
• Savings Bank Life Insurance refers to life insurance that is sold by mutual
  savings banks, over the phone or through Web sites

Agents and Brokers
• An agent is someone who legally represents the principal and has the authority
  to act on the principal’s behalf
• Authority may be:
  – Expressed
  – Implied
  – Apparent
• The principal is legally responsible for all acts of an agent when the agent is
  acting within the scope of authority
• A property and casualty agent has the power to bind the insurer
  – A binder provides temporary insurance until the policy is actually
    written
• A life insurance agent normally does not have the authority to bind the insurer
  – The applicant for life insurance must be approved by the insurer before
    the insurance becomes effective
• A broker is someone who legally represents the insured, and:
  – solicits applications and attempts to place coverage with an appropriate
    insurer
  – is paid a commission from the insurers where the business is placed
  – does not have the authority to bind the insurer
• A surplus lines broker is licensed to place business with a nonadmitted insurer
  – Surplus lines refer to any type of insurance for which there is no
    available market within the state, and coverage must be placed with a
    nonadmitted insurer

Life Insurance Marketing
• The majority of life insurance policies and annuities sold today are through
  personal selling distribution systems
  – Commissioned agents solicit and sell life insurance products to
    prospective insureds
  – Career, or affiliated, agents are full-time agents who usually represent
    one insurer and are paid on a commission basis.
  – In a multiple line exclusive agency system, agents who sell primarily
    property and casualty insurance also sell individual life and health
    insurance products.
  – Independent property and casualty agents are independent contractors
    who represent several insurers and sell primarily property and casualty
    insurance
  – A personal-producing general agent (PPGA) is an independent agent
    who places substantial amounts of business with one insurer and has a
    special financial arrangement with that insurer
Brokers are independent agents who do not have an exclusive contract with any single insurer.

Many insurers today use commercial banks and other financial institutions as a distribution system.

A direct response system is a marketing system by which insurance products are sold directly to consumers without a face-to-face meeting with an agent.

- Acquisition costs can be held down, but complex products are difficult to sell this way.

Other forms of life insurance distribution include:
- Worksite marketing
- Stock brokers
- Financial planners

Property and Casualty Insurance Marketing

- The independent agency is a business firm that usually represents several unrelated insurers.
  - Agents are paid a commission based on the amount of business produced, which vary by the line of insurance.
  - The agency owns the expirations or renewal rights to the business; it may bill the policyholders and collect premiums, but most insurers use direct billing.
  - Agents may be authorized to adjust small claims and may provide loss control services to their insureds.

- Under the exclusive agency system, the agent represents only one insurer or group of insurers under common ownership.
  - Agents do not usually own the expirations or renewal rights to the policies.
  - Agents are generally paid a lower commission rate on renewal business than on new business.
  - Exclusive agency insurers provide strong support services to new agents.

Marketing Systems in Property and Liability Insurance

- A direct writer is an insurer in which the salesperson is an employee of the insurer, not an independent contractor.
  - Employees are usually compensated on a “salary plus” arrangement.

- A direct response insurer sells directly to the consumer by television or some other media.

- Many property and casualty insurers use multiple distribution systems.

Group Insurance Marketing

- Many insurers use group marketing methods to sell individual insurance policies to:
  - Employer groups
  - Labor unions
  - Trade associations

- Products are sold through group representatives, employees who receive a salary and incentive payments based on sales.

- Some property and liability insurers use mass merchandising plans to market their insurance.

- Employees typically pay for insurance by payroll deduction.

End.