

# THE STANDARD

NEW ENGLAND'S INSURANCE WEEKLY

Published Since 1865  
Boston, Mass.

November 11, 2005  
Vol. 257 No. 15

## Generalist or Specialist? Meeting Challenges and Opportunities By Determining Your Agency's Structure and Goals

By J. Bruce Cochrane

Over the past generation, a mismatch has developed between the product needs of local independent insurance agencies and the insurers that supply those products. Twenty years ago, both insurers and their agents were generalists. National insurers that were committed to writing a wide spectrum of risks dominated the ranks of insurers. Agents generally marked out a local territory in which they would try to sell to as many clients as possible. Therefore, an agent's need for a broad spectrum of risk transfer products was matched by an insurer's ability and desire to provide a wide spectrum of risk transfer products.

In the past 20 years, the insurance marketplace has changed considerably. Market dominance has shifted from large national insurers to more local carriers. All insurers — even the few remaining national insurers — have narrowed their risk-bearing appetites considerably. At the same time, local agents have remained territorial, seeking to satisfy the broad spectrum

of risk-transfer needs of their varied customer and prospect base. The result is a mismatch between product need and product offering.

### Insurers Adjust

Insurers have been forced to become more specialized as a matter of economic survival. Expenses and competition for the best risks have driven them to focus their resources on risk classifications that can assure reasonable returns on equity. The old generalist paradigm forced an insurer to be all things to all people. This caused insurers to spread resources too thinly to be expert at everything and drove up expenses; it also put generalist insurers at a distinct disadvantage when competing with insurers that specialized. Specialization, whether at the insurer or agency level, creates differentiation and leverage in the sales process. As more and more insurers implemented specialization strategies, generalist insurers became squeezed.

Some generalist insurers that retooled

to become more specialized were able to survive, but many who did not adjust their strategies did not survive. Just pause for a moment to think of the insurers who have either closed up shop, merged, or been liquidated

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over the past 10 years. Most of these are the companies that could not or would not make the transition to more specialized strategies.

### **Agencies Today**

Most agencies today continue to be generalists. Locality and the ability to develop customer relationships are fundamental strengths of the independent agency system. Twenty years ago, agents could satisfy the risk-transfer appetites of their varied client base by affiliating with three or four generalist insurers. Because of the trend to insurer specialization, generalist agencies today need more carriers to satisfy the needs of their clients and to fill voids in their product availability. In addition, agencies now depend to a greater degree on excess and surplus lines facilities. By spreading their business among more insurers, an agency's volume with each insurer becomes watered down. This occurs at a time when all insurers are seeking more business from fewer agents, so agencies forced to spread their business to secure the products they need become less attractive to insurers. When agencies can't satisfy their client needs with standard carriers, they utilize E&S options, but pay a price for doing so. The commission rate with E&S insurers is about half the commission rate of standard insurers and without profit sharing provisions, driving down overall agency revenue.

There is an interesting irony to this mismatch of insurer specialization versus agency generalist strategy. Insurers want the benefits of specialization and they want ever-increasing volume commitments from their agents, yet it is the insurers' very specialist business plans that drive agencies to seek additional insurers, watering down their volumes with existing insurers. In addition, insurers constantly look to agents to be front-line underwriters and want agents to sell based on relationships rather than price. If insurer specialization undermines agents' ability to be local generalists, are insurers unwittingly undermining the relationship base they seek from their agents?

### **A Real Dilemma**

Given the mismatch between insurers and agencies, what is an agent to do? Agents and insurers cannot continue

on a path that forces them farther and farther apart. This is quite a dilemma that needs to be addressed. The following are some of the paths open to agents:

**Agency as Specialist:** Some agents have decided to specialize in a particular line or class of business that their major carriers write. This option shrinks an agent's base, making the firm more susceptible to shifts in insurer underwriting appetites and in the industries of the specialty clients they insure. What happens if the insurer decides to shrink its presence in that classification, merges with another insurer, or goes out of business? What happens if the industry in which the agency is specializing experiences an economic depression or becomes victimized by technological advances? The agency that specializes by banking its resources and its future on a specific business classification is in a precarious position.

**Agency as Generalist:** To maintain a generalist strategy, an agency must generate sufficient business volume with enough insurers to meet customer needs and yet must also have the volume to be important to each. With insurers seeking ever-increasing volume commitments from their agents, continuing to be important to insurers means being able to generate enough new business to satisfy each insurer's appetite for premium growth. When an agency needs a new insurer to meet product demands, this often results in a "robbing Peter to pay Paul" strategy of shifting business from existing insurers to stock the new insurer, eroding the relationships with existing insurers. One way or the other, agencies need to have significant volume with their insurers to be a player in their marketplace. This means that agencies must grow to thrive.

Among the growth options available to generalist agencies are:

\* Grow fast enough organically to create a mass of volume capable of satisfying enough insurers to satisfy the broad risk transfer appetites of their entire client base. The difficulty with this strategy is that agencies need the benefit of mass now and cannot afford to wait several years to achieve the necessary

mass. Realistically, how fast can an agency organically generate sufficient mass to be important to the number of insurers they need?

\* Merge with another or multiple agencies to create mass. This can create the necessary mass, but each of the merging agencies must be on the same page regarding a whole host of business, vision and economic issues. If merging agencies devote the proper time and shared commitment to address and align these issues, growth can be achieved more quickly.

\* Purchase agencies. Purchasing agencies as a means of building mass is a viable option if time and capital expenditure requirements can be achieved. Significant time must be devoted to properly integrate the staffs, processes, procedures and business philosophies of the buying and purchased agencies. The challenge in this strategy is the significant potential of shifting focus from building volume to the art of making the deal. Again, timing is crucial as there are only so many deals and acquisitions one can make in a given period in the marketplace.

\* Collaborate with other like-minded agencies. There are many agency "groupings" or aggregations that have cropped up in recent years to address a variety of business issues facing agencies today. Joining a grouping can enable an agency to gain instant size with multiple insurers. The tricky part of this strategy is matching the needs of the agency with the needs of the group. There are no two agency groupings that are alike. They all have differing philosophies, agency composition and means of accomplishing their goals. Some groupings are created strictly to solve market problems by simply sharing markets among the group's agencies; others are designed to solve a variety of issues facing agencies today. To determine compatibility prior to joining a group, an agency must be introspective about their own needs and goals, and must examine several basic functional questions:

\* How does the group share markets?

\* Is adverse selection a factor with some markets?

- \* Is there a means of self-policing to be sure an individual agency does not damage the relationship of the group with insurers?
- \* How is market access attained by each agency?
- \* How do the insurers the group represents view the grouping? Are they happy with how the group operates and the results to date? Is there stability in the carrier relationships? Engage in conversations with the group's insurers. There has to be a win-win in the relationship for both the agencies and the insurers for both to be happy with the arrangement. It is definitely a good sign if both are happy.
- \* Is there a centralized and coordinated marketing strategy and functionality shared by the group?
- \* Is the group professionally man-

aged or is it managed by one or two member agency principals in a part-time basis?

- \* Are the group's centralized activities capitalized and, if so, by whom?
- \* Is profit sharing with each insurer aggregated?
- \* Does the group achieve sharing of markets by brokering among the member agencies, a practice frowned on by most insurers?
- \* Does the group have a far-reaching, shared and lasting vision, or a single-minded purpose?
- \* Are the members of the group compatible? Do the members share business philosophies and can they work together?
- \* Is your agency willing and able to proactively adapt to the changes required for significant growth within an agency grouping environment?

It is critical for agencies that choose to join a grouping to ensure that they make the right choice. Agencies must take the time to conduct due diligence to find the right solution to enhance market position and solve identified problems.

The generalist/specialist insurer/agency mismatch is a real dilemma for both agencies and insurers. If left unaddressed, this condition can only serve to exacerbate friction between agents and insurers, and friction in any relationship inevitably leads to trouble. The good news is that this condition creates a tremendous set of opportunities. Enterprising agents who can recognize the need for change and who can make change happen will have a tremendous leg up on their fellow agents in the years ahead. As Will Rogers, the early 20th century humorist, once said "Even if you're on the right track, you'll still get run over if you stand still." The American agency system is on the right track and has a bright future, but agents need to be proactive in adapting themselves to a changing business environment. Procrastination is not an option. ■