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A&B

Editor's Corner

by Chris O'Donnell, CPCU, ARM, AMIM



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By now the dust has settled on the 2003 Annual Meeting and Seminars in New Orleans, LA, and we now are beginning to focus on the approaching holiday season, year-end renewals, and the new year. Personally, I found this year's seminars to be among the best that I have attended, both in terms of quality and quantity. The location was among the more interesting as well!

Our section can take a good deal of pride in the seminars that we sponsored this year. Those included Dave Dybdahl's extensive discussion of the mold topic entitled,

"Toxic Mold: Managing the Risk in a Post-Insurance Exclusion Era," as well as the second entitled, "Malecki and Tilden on the CGL: From There to Here." Don Malecki and Bryan Tilden provided their usual very entertaining and informative discussion on the CGL.

In this issue of the *Agent & Broker Solutions*, we conclude Dave's series on toxic mold. This is the final installment of our three-part serial presentation of the topic, which was discussed at great length during the seminar. Certainly, this will not be the final commentary on what is turning out to be a developing problem area, both for property owners and the insurance industry. Dave certainly opened many eyes during his presentation.

I would encourage everyone to take a look at the entire series, now that it is concluded, to fully grasp some of the areas of concern expressed by Dave in writing.

We now enter the close of yet another year of our hard insurance market and begin what appears to be another with a still firm marketplace. During the course of this past year, we have lost some significant, familiar, old line insurance company partners, not the least of which being Kemper and now Royal and SunAlliance. We are also gaining what will hopefully become new friends in terms of the new capital coming into the marketplace. Unfortunately, much of this capital remains offshore and in the realm of the excess and surplus lines marketplace.

2004 seems to be shaping up to be another year of challenge, as well as opportunity for insurance professionals. It remains my firm belief that those of us who sharpen our professional skills in an increasingly difficult, multidisciplinary field, will be up to the challenges.

It has been encouraging to experience a number of the National Leadership Institute courses now offered by the CPCU Society. In fact, I think I completed all of the ones that have been offered and have found them to be extremely valuable in providing an overview of different disciplines that are needed in this increasingly complex business world.

It is also encouraging to note the continuing search by the CPCU Society for other topics of study to develop and offer within the NLI curriculum.

Additionally, I have heard very good feedback from employees and associates of mine who have recently entered the newly revamped CPCU course of study, as well as the IIA revised curriculum. I certainly encourage our readers to take another look at the educational offerings of both the Institutes and the CPCU Society in case it's been awhile since you have sampled the "wares" so to speak. I'm sure you will be as encouraged and excited as I am.

Certainly, the challenge of a continuing hard insurance marketplace, as well as the more diversified nature of the risks facing our own businesses, as well as our customers, requires us to constantly improve our professional skills.

Additionally, two old competitors have joined forces to become The St. Paul Travelers Companies. Some may recall that Travelers had recently purchased much of the Royal & SunAlliance book. Although this will make it the largest commercial insurer second only to AIG, it may further restrict competition in the marketplace. Hopefully, this combined company will add financial stability and underwriting responsibility to our industry. Only time will tell.

I look forward to seeing all of you in the new year. ■

New Mold Exclusions = Unanticipated Coverage Gaps + E&O Exposures!

by David J. Dybdahl, CPCU, ARM

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Editor's note: This is the last of three installments of a very timely article that discusses mold issues facing our industry.

The views and observations contained in this article are the author's alone.

New exclusions for mold cause unanticipated coverage gaps and professional liability loss exposure for insurance agents and brokers on an unprecedented scale.

No residual mold coverage in claims-made insurance. . . . Professionals can have retroactively uninsured errors and omissions loss exposures.

The mold exclusion's effect on claims-made liability insurance is dramatically different from that under occurrence-based liability insurance. On a claims-made policy, a mold exclusion on the renewal of the policy is, in effect, a full prior acts and prospective work exclusion for all mold-related damage claims.

For example, an architect with a mold exclusion on the renewal of his or her professional liability insurance would not have insurance for mold damage claims that were caused by the defective design of a vapor barrier that causes water to accumulate in walls. The insurance coverage gap created by the new mold exclusion would apply to the loss regardless of when the loss occurred, when it was discovered, when the design was completed, or when the building was built.

Professional liability insurance policies covering insurance agents/brokers, real estate brokers, lawyers, architects, and engineers are written on a claims-made basis. All of these professionals face the same retroactive insurance coverage gap if a mold exclusion is added to their professional liability insurance policy today or at any point in the future.

Many risk advisors, including insurance agents, brokers, and lawyers, will likely face a full prior and prospective acts "mold-related damages exclusion" on their professional liability insurance coverage in 2003. More than 10 million mold exclusions have been delivered in the past on commercial accounts, and only a few hundred environmental insurance policies covering mold have been sold to date. Therefore, risk advisors

on commercial accounts already have incurred 12 months worth of incurred but not reported professional liability claims exposure for leaving their customers unintentionally uninsured for mold-related damages.

These potential professional liability claims will be retroactively excluded under the insurance agent's professional liability insurance policy if it is renewed with a mold-related damages exclusion.

Mold has created unprecedented professional liability loss exposure for insurance agents and brokers. In addition to the introduction of mold-related claims exclusion on insurance agents professional liability insurance, there will be hundreds of thousands of water damage/mold claims that will be uninsured for the first time in 2003.

Our research in ARMR.net indicates that mold-related damages mirror insured fire losses in the United States for claims frequency and severity. At these rates, there could be one uninsured water damage/mold claim for every two licensed property and casualty insurance agents in the United States this year.

Most of these claims will be relatively small, but will likely strain the agent's relationship with the client. The average mold claim in Texas is \$22,000. No agent wants to tell a client that he or she is not covered for a loss, especially one for 20 or so thousand dollars.

Some of these mold losses will be more significant and potentially expose insurance agents to professional liability for failure to advise the client of the loss exposure and failure to procure the appropriate environmental insurance covering mold.

In the age of the Internet, it will be more and more difficult for agents to create a successful defense by saying they did not

know mold insurance was available or how to obtain it. A recent search for the key words "mold insurance" produced 172,000 hits utilizing the Google search engine. The entire commercial mold insurance market was summarized within the first page of search results.

■ The mold exclusion's effect on claims-made liability insurance is dramatically different from that under occurrence-based liability insurance.

To avoid having their own mold-related professional liability losses, all risk advisors should implement a mold claim loss control procedure by advising their clients on the hazards of mold and offering the appropriate environmental insurance covering mold if it is available. The mold insurance market is in constant state of flux as underwriters introduce more coverage into the marketplace in various policy forms as other underwriters move to exclude all claims for mold damages.

A summary of the current mold insurance market for commercial accounts is available on the Environmental Risk Resources Association web site at www.erraonline.org.

Conclusion

Mold exclusions will transform property insurance claims into liability insurance claims in 2003. Mold exclusions on liability insurance policies will eliminate insurance coverage for new occurrences, but most business will have some residual liability insurance protection in place.

In the absence of separate mold exclusions, mold claims may also be denied under the terms of pollution exclusions in liability insurance contracts. Nevertheless, there are a number of arguments that can be made as to why mold is not a pollutant within the context of the standard pollution exclusion.

Organizations with loss exposure to mold-related damages should actively seek to fill the insurance coverage gap created by mold exclusions with appropriate insurance coverage. Commercial insurance covering mold-related damages is available today for building owners, contractors, and environmental consultants through environmental insurance underwriters. Some homeowners insurance companies are currently offering buybacks for mold coverage.

Risk advisors who fail to advise their clients on the hazards of mold-related damages and fail to offer appropriate insurance covering mold risks face the most severe insurance coverage gaps. This risk can be managed by advising clients on their exposure to mold-related damages and offering the appropriate insurance to cover this loss exposure. ■

Are You Ready to Deal with Mold? ●

Learn all about mold with the CPCU Society's interactive CD-ROM, **MoldMania**.

Developed specifically for insurance professionals by insurance professionals, this 6-module, 2½-hour, self-study CD presents comprehensive information on:

- The basics of mold—what it is, how it grows, and how it affects human health
- How mold can be prevented and tested for
- Remediation—basics, goals, and upfront considerations
- How to address mold-related claim adjustment and investigation, as well as coverage and legal issues
- Other useful resources

The self-study program features video and audio clips from mold experts, photos identifying mold, design considerations for prevention, a policyholder's checklist, as well as a quiz at the end of each module to test your knowledge.

For more information, go to www.cpcusociety.org/?p=21788.

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The logo for MoldMania, featuring the word "moldmania" in a lowercase, sans-serif font. The letter "o" in "mold" has a small white circle above it, and the letter "o" in "mania" has a small white circle below it. The entire logo is set against a black rectangular background.

The Disappearing Duty to Read—More Courts are Placing Duty on Agent, Not Insureds, to Make Sure Policy Is Correct

by Greg Brunton and Kevin Foley

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Editor's note: This article originally appeared in the July 2003 issue of the *PLUS Journal*, the monthly publication of the Professional Liability Underwriting Society. It is reprinted here with the permission of *PLUS*.

What happens when an insured suffers a loss, makes a claim to an insurance carrier, only to find out that the loss is not covered? Increasingly, lawsuits are being brought against insurance agents by insureds who claim that their agent obtained the wrong type of policy or coverage.

Traditionally, the agents have successfully argued that the insureds have a duty to read their insurance policies as well as understand the terms of those policies. Therefore, it is the insured's own "contributory negligence" that causes any loss, and no liability can be attributed to the agent. This is currently the prevailing view in Ohio pursuant to a recent Court of Appeals decision. See *Frye v Walters and Peck Agency, Inc.* (Williams Cty. 2001), 141 Ohio App.3d 303 (customer has a corresponding duty to examine the coverage provided and is charged with knowledge of the contents of his or her own insurance policies); *Craggett v Adell Insurance Agency* (Cuyahoga Cty. 1993), 92 Ohio App.3d 443 (while the insurance sales agency has "a duty to exercise good faith" in obtaining insurance policy that

customer requests, a person has duty to examine the coverage and is charged with knowledge of the contents of his or her own insurance policies).

Several other states, including South Carolina, Virginia, California, and the District of Columbia, also place upon the insureds a duty to read and understand their own insurance policies, and therefore generally bar claims against the insurance agent on the grounds of contributory negligence. See *Carolina Production Maintenance, Inc. v United States Fidelity & Guaranty Co.* (1992), 310 S.C. 32 (insured was contributory negligent and that its president and secretary did not read the policy and therefore summary judgment was proper in claim against agent); *Insurance of Roanoke v Page* (1995), 250 Va. 409; *Redmond v State Farm Ins. Co.* (1999), 728 A.2d 1202; *Hadland v NN Investors Life Ins. Co., Inc.* (1994), 4th App. Dist., 1994), 24 Cal. App. 4th 1578.

However, a number of courts have held that an insured has no duty to read (or understand) the terms of an insurance policy, and that the defense of contributory negligence is not available to an agent who has negligently procured the wrong insurance coverage. While the most recent court to take this view is the New Jersey Supreme Court in *Aden v Fortsh* (2001), 169 N.J. 64, it is by no means the only court to bar the use of contributory negligence under these circumstances. The Supreme Courts of Kentucky, New Mexico, Rhode Island, South Dakota, and Arkansas, have all similarly held that an insured's failure to read a policy is not a defense against an agent who negligently obtains incorrect insurance coverage. See *Grigsby v Mountain Valley Insurance Agency* (1990), 795 S.W. 2d 372; *White v Calley* (1960), 67 N.M. 343; *Moore v Kluthe & Lane Ins. Agency, Inc.*, (1975), 89 S.D. 419; *Batesville Insurance and Finance Co. v Butler* (1970), 248 Ark. 776; and *Braswell*



v The People's Credit Union (1992), 602 A.2d 510.

The reasoning for these decisions is two-fold. First, some courts cite the alleged difficulty for ordinary persons to understand insurance policies. For example, the Kentucky Supreme Court in *Grigsby*, *supra*, found that due to "the highly technical nature of fire insurance policies, an insured may not be held contributorily negligent for the failure to read and understand his or her own coverage." *Grigsby*, *supra* at 373. These courts have described insurance policies as "technical" and "complicated."

Second, most courts have adopted this holding on the grounds that insurance agents hold themselves out to have an expertise in procuring the correct insurance and, therefore, insureds are justified as a matter of law in relying on the expertise of the insurance agents. See *Aden*, *supra*; *Braswell*, *supra* ("the risk of falsity should fall upon the party making the representation" because of the agent's "superior position"); *Batesville*, *supra* (contributory negligence is not a defense because agents "hold themselves out as having more knowledge than the ordinary citizen"). See also, *Village Furniture v Associated Insurance Managers* (3d Dist., Ind., 1989), 541 N.E.2d (insured was not contributorily negligent for failing to read the insurance policy because reliance upon agent's representation was reasonable and insurance policies are "unreadable").

The Supreme Court of Pennsylvania has accepted the argument that an insured does not have a duty to read a policy because "by the time the written policy is received, it has lost its importance to the insured," and, therefore, it is not unreasonable "for a purchaser of insurance to 'pass' when the time comes to read the policy." *Rempel v Nationwide Life Insurance Company, Inc.* (1977), 471 Pa. 404.

A Growing Middle Ground?

Several State Supreme Courts take the position that an insured's contributory negligence for failing to read an insurance policy is an issue for a jury depending upon the facts and circumstances of the case. For example, the Supreme Court of Montana in *Fillinger v Northwestern*



Agency (1997), 283 Mont. 71, held that while an insured's failure to read the policy may amount to contributory negligence, it will not operate as a bar to relief as a matter of law. In its holding, it adopted the reasoning of the Supreme Court of Oregon finding that "insureds and insurance policies are not all alike" and that a higher duty may be on business persons and large corporations to understand their insurance policies. See *Martine v Beaverton Insurance Agency, Inc.* (1992), 314 Ore. 200.

Similarly, the Supreme Court of Nebraska has held that "if an insured could have read and understood the policy, then the insured should be charged with knowledge of the policy's contents." Under such circumstances, "the insured's failure to read the policy provision will insulate the agent from liability for failure to explain that provision." See *Dahlke v John F. Zimmer Insurance Agency* (1994), 245 Neb. 800. See also *Darner Motor Sales, Inc. v Universal Underwriter's Ins. Co.* (1984), 140 Ariz. 383 (insured's failure to read policy and reliance on statements made by agent creates a question of fact).

Many Courts of Appeals are following suit, finding that the doctrine of contributory negligence, while not a

complete bar to recovery, can be considered if the insured fails to read the policy. See *Kron Medical Corp. v Collier Cobb & Assocs., Inc.* (1992), 107 N.C. App. 331; *Perelman v Fisher* (1st Dist. 1998), 298 Ill. App.3d 1007; *EER Systems Corp. v Tri-City Insurance Brokers* (Fairfax Cty. 1999), 51 Va. Cir. 84 (question of fact regarding insureds' failure to read policy).

What Agents Can Do

Clearly, there is a growing trend to limit an insured's duty to read his or her insurance policy. The agent's "expertise" in the insurance industry, the fact that the agent gets paid for such expertise, and the highly technical nature of insurance contracts are persuading courts that any mistake in coverage should be borne solely by the agent. For many courts, a failure to read a policy on the part of the insured merely creates a question of fact for the jury on the issue of contributory negligence.

Under these circumstances, agents should become more aware of the customer and the complexity of the insurance sought. Clearly, the more sophisticated the consumer, the more likely a judge and a jury will find that the consumer should have understood and read the insurance policy. On the other hand, individuals and small business owners will be more sympathetic for either failing to read the policy, or failing to understand it, particularly if the issue is technical or complex. Therefore, the agent should take extra precaution when procuring coverage under these circumstances, and make sure the client has read and understood the policy terms. ■

New Jersey Holds Comparative Negligence Defense Unavailable in Broker Malpractice Actions

by John L. Slimm, Esq.

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The New Jersey Supreme Court has now held that the insured's failure to read the insurance policy cannot be asserted as comparative negligence in an action against the broker for negligent failure to procure insurance. In *Aden v Fortish*, 169 N.J. 64 (July 18, 2001), the court held that the comparative negligence defense is unavailable to a professional insurance broker who asserts that the client failed to read the policy and failed to detect the broker's own negligence. The court emphasized that it is the broker, not the insured, who is the expert, and the client is entitled to rely on that professional's expertise in faithfully performing the very job he or she was hired to do. In New Jersey, professionals may not diminish their liability under the Comparative Negligence Act when the alleged negligence of the client relates to the task for which the professional was hired. That rule is premised on the heightened responsibilities of professionals in New Jersey.

In *Aden*, the court found a fiduciary relationship between the professional and the client. The import of the fiduciary relationship between the professional and the client is no more evident than in the area of insurance coverage. Insurance intermediaries in New Jersey must act in a fiduciary capacity to the client because of the increasing complexity of the insurance industry and the specialized knowledge required to understand all of its intricacies. Also, N.J.A.C. 11:17A-4.1 provides that an insurance producer acts in a fiduciary capacity in the conduct of his or her



insurance business. That fiduciary relationship gives rise to a duty owed by the broker to the client to exercise good faith and reasonable skill in advising insureds. See, *Weinisch v Sawyer*, 123 N.J. 333 (1991).

Accordingly, an insurance broker who agrees to procure a specific insurance policy for another but fails to do so may be liable for damages resulting from such negligence. *Ryder v Lynch*, 42 N.J. 465 (1964). Liability resulting from the negligent procurement of insurance is premised on the theory that a broker ordinarily invites clients to rely upon his or her expertise in procuring insurance that best suits their requirements. *Id.* at 477. Furthermore, if a broker neglects to procure the insurance, or if the policy is void or materially deficient or does not provide the coverage he or she undertook to supply, because of his or her failure to exercise the requisite skill of diligence, the broker becomes liable to his or her principal for the loss sustained thereby. *Ibid.*

The court in *Aden* held that the client is entitled to assume that a broker has performed his or her fiduciary duty. That duty is not diminished when a policyholder fails to detect the broker's breach of that

duty. Commentators on insurance law are in accord with that view. 12 Holmes, Appleman on Insurance 2d, §87.3. McCawn 3, Couch on Insurance, §46:69 (3d Ed. McCawn annotation, Liability of Insurance Agent or Broker on Ground of Inadequacy of Liability Insurance Coverage Procured, 60 A.L.R. 5th 165, 189-90, 1998 W.L. 329 515 (1998) (discussing the view that the insured's failure to read a policy is generally not a defense). Therefore, in *Aden*, the court concluded that the plaintiff's failure to read the policy could not be asserted as comparative negligence in an action against the broker for negligent failure to procure insurance. The court reasoned that brokers hold themselves out as having more knowledge than members of the public with regard to the insurance policies and coverage they procure. A broker is not an "order taker" who is responsible only for completing forms and accepting commissions. When an insured employs the assistance of a professional insurance intermediary, the insured then has the right to rely on the skilled broker's presumed competence in executing the instructions given. *Aden*, 169 N.J. at 86.

As noted in *Aden*, an insured who hires and pays a professional broker does so to reduce, if not eliminate, the risk that an inadequate policy will be procured. In New Jersey, a plaintiff's conduct cannot be charged as negligence in actions in which the plaintiff failed to detect error in the discharge of the very responsibility he or she hired a professional to perform. ■

Business Planning: Making It Happen in Your Agency

by Daniel J. Devlin

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How often have you thought about making changes in your agency? Perhaps you had some great ideas in sales and marketing to generate new sources of revenue. Or, maybe your operations manager is thinking about making changes to the job design of your customer service area to improve service to producers and customers. But, somehow time goes by without the ideas being implemented. Why? Our experience indicates that it is usually the absence of a formalized planning process that allows you to share ideas with your key employees, develop action steps, assign responsibility, and set target dates for completion.

Our experience further indicates that agencies that conduct their business from a written plan outperform the competition and are leaders in facing the challenges of the changing insurance marketplace. Business planning is essential for any agency having recently experienced a major change, like a merger, acquisition, shareholder transition, or sale to a bank.

Getting Started

A planning session should take place off-site. Key management and sales and service personnel are included. The session is enhanced by the use of an outside facilitator, particularly one with no close ties to the agency. The facilitator brings outside perspective to the session, and is comfortable challenging stale and

unproductive agency strategies. Next, the participants identify the “key result areas” that warrant discussion and solutions. These topics need to be limited and prioritized. Too many topics will make the session lengthy and create boredom. A master facilitator keeps the session on track, and is capable of bringing real solutions to the table when participants cannot.

Detailed below are frequent topics on the agendas of business plans that this consultant facilitates. Keep in mind that this outline is of a basic business planning session. Organizations planning for the first time, and those that have lost their strategic direction, may need to devote time to an agency mission statement and an assessment of outside forces adversely impacting their business model.

Financial Issues

Many agencies believe that a budget is a business plan. While it is not, it is a document that needs to be completed in advance of a planning session. The budget sets financial parameters on planning participants. It is usually Act I in a business plan. Corporate needs for revenue and earnings growth will drive sales goals for the production staff. And expense constraints may limit the participant's ability to devote capital to new marketing ideas. This all needs to be presented by the financial manager, and assessed by participants.

Overdue receivables, the firm's credit and collections policy, and anticipated carrier contingency income are frequent topics raised by the financial manager in this early part of the planning session.

Sales Goals

One of the most important parts of the business plan is setting sales goals. Before establishing these, management needs to detail carrier commitments and communicate target markets by product line to producers. Once established, the financial manager can present the firm's revenue needs. Now watch the stress meter

rise. Growth goals by product line are divided up among the sales staff, *including principals*. Politics and posturing often develop at this point, particularly if the sales goals are aggressive. Many producers will plead that their book of business is too large for new production goals. The sales manager, in conjunction with the facilitator, can guide the group through this difficult process. Tentative goals may have to be adjusted upward in light of normal attrition and potential rate decreases in some product lines. Be warned that aggressive sales goals set for the first time may drive a salesperson out of the agency. Usually this is not a loss, as frequently they are poor performers.

Marketing

This is the fun part of the program. The sales staff is always in need of improved sales and marketing techniques. These include telemarketing, direct mail, advertising, and custom newsletters that rotate features on members of the sales staff. Proven techniques to obtain leads from existing customers are also effective. Marketing and promotional techniques that identify and build agency name recognition and value are also a key part of the discussion. The facilitator should bring to the session samples of proven marketing and sales material, so that planning participants instantly can see the quality and creativity necessary to wage an effective marketing campaign. It has been the consultant's experience that most agencies are weak in the development and use of quality marketing material. Accordingly, upgrading marketing material can be expensive. However, experience shows that it often pays for itself with increased sales.

Many of the action steps developed in this category are divided among the sales staff. By putting “sweat equity” into initiatives that can bring improved sales results, participants are usually motivated to contribute their time and expertise. In larger agencies with the resources to hire a

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Business Planning: Making It Happen in Your Agency

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marketing manager, many of these action steps are completed by this one person. However, regardless of the size of an agency, many marketing tasks can be outsourced to local professionals.

Operations

In most agencies, operations do not support sales. Unfortunately, this often comes to light when sales staff are asked to take sizable increases in their goals. Their first objection is that they are servicing many of their accounts (instead of selling) because CSRs are either too busy or incompetent. This may not always be true, with the real reason sometimes being that the producer cannot delegate. All of this needs to be sorted out in advance of the planning session. Complaints about CSR support from the majority of the sales staff during a planning session can derail the setting of mutually agreeable sales goals.

Forward-thinking operations managers are wise to address these issues well in advance of the meeting. This can be done by surveying the sales staff on the quality of CSR support 90 days prior to the annual meeting. Many of my clients have *operational reviews* performed every few years by Devlin Consulting, LLC to ensure that operations are supporting sales.

During a planning session, support staff costs and overall agency efficiency are usually discussed. Keeping support staff payroll at between 20 to 22 percent of total revenue is a sure way to free up funds for marketing ideas and select acquisitions.

Additional Topics

Customize and focus your business planning session with topics that are important to *your* team. They may include automation, perpetuation planning, expansion, acquisitions, bank joint ventures, etc. Survey your staff in advance of the session for ideas. They may surprise you with subject matter not on senior management's radar screen.

Set It to Writing

One of the benefits of a formal planning process is that a written document is produced at its conclusion. This serves as a common "game plan" for all to follow. Action steps by topic include a person responsible and an agreed-upon date of completion. This makes monitoring easy. Accountability increases, as employees conduct their business in the new year using a plan they helped to develop in full view of peers. Another natural by-product of group planning is a sense of teamwork and commitment to agency goals. Successful implementation of the plan requires that management and staff meet regularly to assess progress on each action step and production goals. Those behind schedule, or struggling to get started, have the opportunity to bring this to management's attention early.

After enjoying the benefits of doing planning right, working from a written business plan becomes a luxury that your team won't be able to do without. ■

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