

Learn from the Pros—Common Attributes of Successful Agencies

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You're a 15 handicap on the links. Your swing isn't perfect, but you have managed to rationalize, or compensate for, your deficiencies. If you worked with a golf pro, you could probably correct several different elements of your swing to improve your score, but you don't have the time and you're pretty happy with where things stand. Sound familiar?

Now, if that same golf pro offered to simply tell you the four most common swing characteristics of successful golfers would you be willing to listen? Would you evaluate what he told you and compare that against your individual swing?

Like your golf swing, your agency could probably improve in a multitude of areas. However, you have learned to accept and compensate for certain deficiencies within your organization. You may be satisfied with where your agency stands, but you understand it could be better.

Now, if someone offered to tell you the four most common attributes exhibited by successful agencies would you be willing to listen? The remainder of this article describes the four most common attributes of successful agencies and identifies ways to incorporate these into your business practices.

Four primary indicators of high performance

As consultants to the insurance industry, we have seen the operational and financial fundamentals of hundreds of agencies. We have conducted numerous agency valuations, facilitated perpetuation plans and participated extensively in the merger and acquisition arena. Based on this experience within the independent insurance marketplace, we have identified the four most common attributes of successful agencies, as measured by growth, earnings and value.

These four primary indicators of success serve as a quick, easy and sound benchmark in assessing an agency's performance. As an agency manager, your knowledge and understanding of these indicators, and your ability to implement them, will often be critical in defining the success of your firm. These indicators are absolutely critical to your financial performance. While the top performing agencies may not be the best at all four, they are always very good at two and at least average at the other two.

Average account size. Larger accounts almost guarantee greater productivity and profitability. Successful agencies do not rationalize small accounts but take concrete measures to maximize account size. While we realize that not every agency can write the jumbo accounts, every agency can seek ways to increase their average account size given their location, markets and staff.

Agency owners and managers can implement processes and procedures to ensure producers are writing larger accounts thereby driving your agency towards improved financial performance.

First, agencies should track their average account size departmentally and review it with their producers and department managers regularly. The entire organization should be repeatedly educated as to the advantages of larger accounts.

Second, agencies should create a floor on the size of accounts on which the agency will pay commissions. In conjunction with this floor, any accounts below the agency threshold should be transferred from commercial producers to a small accounts department or to the service staff. This not only forces each producer to target larger accounts but saves the agency the renewal commissions associated with these small accounts.

Third, agencies can trim the bottom 10 percent to 20 percent of each producer's accounts every year and reallocate these to house accounts or a small accounts department. This will allow the producers more time to generate larger accounts vs. servicing smaller accounts.

Size of producers' books of business. One common rationalization in underperforming agencies is the belief that producers with small books of business do not hurt the agency because the producers are paid on commissions. While such small books reduce profits, they also hinder opportunities for growth in profitability and value. More often than not, agencies that employ a smaller number of large book producers will realize higher earnings and values than those agencies of like size and commission splits with more small book producers.

The worse thing an agency can do is to allow producers with small books that are not growing to remain with the agency. The agency is much better served to have five producers generating its revenue than it is to have 10 producers generating the same revenue.

Small book producers create multiple layers of reduced efficiency. They create the need for greater numbers of support personnel as well as the resulting increased selling and operating expenses. They negate the agency's efforts to reduce headcount and usually tend to write smaller accounts.

There are many ways to help producers grow their books of business.

1. Agencies should define the roles and responsibilities of a producer. Producers that do not sell new accounts may not in reality be producers. They may be account executives. It is important that all employees be appropriately titled and compensated based on what they actually do, not based upon what they are supposed to do.

2. Agency owners can increase the spread between new and renewal commissions. Agencies that pay splits of 40 percent new and 25 percent renewal will typically achieve higher growth levels than agencies paying 35 percent new and 35 percent renewal. The increased spread between new and renewal commissions helps force the writing of new business versus riding renewed accounts. While the retention of current accounts is critical to the survivability of

any operation, the most successful agencies create an infrastructure that promotes and ensures growth.

3. Agency executives should implement and enforce new business production goals on an annual basis. Producers with small books or those that can not achieve new business production goals should be carefully pruned from the firm or reallocated into other positions. These books of business should be transferred to the remaining better producers or to the service staff. This difficult but doable process will result in drastic gains in agency performance.

4. Agencies need to assess producer's books of business relative to their tenure at the agency. Successful agencies require that all producers validate within a certain time frame. Historically unvalidated producers not only drain profitability, but they also hinder the growth potential of the agency.

5. Agency owners can institute some type of outside sales coaching process. Finding, qualifying and hiring producers requires a considerable investment. Once producers are hired, however, many agencies do not have an established process to help the producers succeed. Having a defined sales coaching process, which often involves a culture shift, will maximize both producer potential and the return on your investment.

The many benefits of these processes include potential increased compensation for the remaining producers and principals, headcount reductions, reduced operating expense over the long-term and significant gains in profitability.

Revenue per employee and headcount. Due to minimal hard assets, insurance agencies like all professional service firms are headcount driven businesses. Most agency owners can tell you their revenue per employee, but how many can tell you how this performs relative to their peers and more importantly how this performs relative to the most successful agencies? Please refer to the attached exhibit for revenue per employee and headcount statistics.

An agency's single biggest expense item, payroll, is affected far more by the number of employees than by its wage rates. Likewise, operating expenses such as rent, telephone, office supplies, insurance expense, utilities, employee education, computer costs and employee benefits are defined to a large extent

by the number of people employed. The more people an agency employs, the more space they need, the more computer terminals they need, etc. Agency managers can realize substantially greater profitability by first controlling headcount (as this affects multiple operating expenses) and then focusing on the individual line expenses.

In general, agencies are better served to hire more qualified, higher paid personnel who are more productive and less likely to create expensive turnover. The key to higher profitability is greater production from fewer bodies; not reduced costs achieved by low salaries and low cost work environments.

Greater productivity and therefore, reduced headcount, is also encouraged by fewer large book producers writing larger accounts. Individual productivity is often enhanced through the proper use of the best operating tools (i.e., a highly automated agency management system) or the standardized processes that some specialty and niche programs generate.

Competitive differentiation. Establishing and selling a unique and powerful competitive differentiation is the fourth component of successful agencies. This differentiation may be realized through a variety of vehicles including local or regional geographic dominance (in small markets), niches or specialties, a distinctive distribution process or even an innovative partnering arrangement. The most successful agencies seek compelling ways to add value. They do not compete on price alone but also through their unique qualities or value-added services.

Small market agencies with strong local dominance are a common example of this attribute. These agencies focus on the domination of their local markets but do not necessarily try to expand into nearby metropolitan markets or other small markets where their strong regional reputation may have little value. While they might write every type of account in their region, they write very few outside that area.

Other examples of competitive differentiation include agencies selling through association-endorsed programs, those specializing in a particular industry or line of business, and agencies concentrating on certain high hazard industries. Partnering with a powerful referral source such as a bank, attorney or CPA is often

a useful way to gain an advantage over the competition.

Please note that bigger does not unequivocally mean better.

The most successful agencies maximize their earnings stream and the amount of cash that they can distribute or reinvest in the company. The characteristics of successful agencies listed above are the best gauge of this success as they most readily transfer into higher profit margins on the increased business being written.

It is important for owners to realize that writing unprofitable or low margin business, solely in an attempt to increase producer's books of business or revenue per employee, can have an adverse effect. The investment in time, money and resources spent on selling and servicing these small margin accounts can be unproductive, as the agency will be better served reallocating that investment into targeting fewer but higher margin accounts.

There are an infinite number of other agency characteristics that influence growth, profitability and value. While such traits are extremely important and contribute to the success of your agency, they do not necessarily have the strongest correlation to overall performance. In other words, they do not readily and easily predict agency success across multiple organizations.

Profile of success

Let's now look at two sample agencies. Agency No. 1 has numerous small book producers and a large staff compensated commensurate with the market. It is housed in a low cost work environment and focuses extensively on cost control. They attempt to write every account that comes in the door.

Agency No. 1 is a generalist agency that typically competes on price. Agency No. 1 has an excellent reputation and great customer service and their agency management system is state of the art.

Agency No. 2 has a few large book producers who target large accounts. They also have minimal service and support staff who are paid well above market rates. Moderate effort is directed at controlling agency expenses but customers are carefully qualified before sales

and service investments are directed at them. They refuse to expend effort on low margin accounts or accounts where they do not have some competitive advantage.

Agency No. 2 consistently seeks to create value-added services and ways to differentiate itself from its competitors as they refuse to compete on price alone. Based on our experience as consultants and appraisers of insurance agencies, Agency No. 2 will offer significantly better financial performance by nearly every measure over Agency No. 1.

Conclusion

We have touched upon the four most common characteristics of successful agencies.

Please review the "Revenue per Agency Employee and Headcount" chart (see below) and determine where your agency stands versus your competition. Then ask yourself whether you are rationalizing or compensating for the deficiencies within your organization. Finally, ask yourself how successful you want to be. Then, do something about it.

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Revenue per Agency Employee and Headcount Statistics						
	\$2M Agency		\$5M Agency		\$10M Agency	
	Average	Best 25%	Average	Best 25%	Average	Best 25%
Average Account Size Commercial Lines	\$1,644	\$3,113	\$2,319	\$4,713	\$3,643	\$7,621
Average Account Size Personal Lines	\$197	\$361	\$218	\$385	\$223	\$405
Commissions & Fees per Producer	\$406,721	\$644,413	\$432,682	\$674,404	\$522,143	\$833,032
Revenue Per Employee	\$106,224	\$141,145	\$120,688	\$155,925	\$134,669	163,009
Headcount	18.83	14.17	41.43	32.07	74.26	61.35

Source: Marsh Berry & Co. Inc.

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