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Bringing The Carrier-Intermediary Relationship Into The Twenty First Century

By Russell Devitt

Recent years have seen technology have a major impact on the ways in which carriers and intermediaries work together. However the underlying relationship has remained the same and in fact is essentially unaltered since the days when Edward Lloyd first opened his coffee house in the eighteenth century. It is based on an agent-principal model founded on adversarial principles – that one side can win only if the other loses.

If the industry is to move away from head to head competition on price only, and the resulting cyclicality, then this model has to change. Instead of a zero sum game, it has to become a search for a true value proposition for all the parties involved – the carrier, the distributor and the client.

This search means that the parties have to abandon the confrontational approach in favour of a cooperative game, where short-term unilateral gains are foregone in favour of mutual long-term advantage. The new relationship is built on trust, evidenced by transparency and two-way sharing of information. New developments arising from the search for continuous improvement are undertaken as a joint process. Each side has an 'open book' approach to financial data. The relationship is seen as being of indefinite duration and both sides aim to enjoy joint learning from it.

Much of the economic benefit from the new model relationship comes from process improvement. The parties seek to eliminate waste in current processes and share the value created equitably. The fundamental driver is what represents value for the end customer – that is what the customer says he wants, not what the carrier and/or intermediary think he wants. Waste in current business processes is eliminated by eradicating duplication and using minimum effort. The focus is not on an individual organisation but on the entire value chain – carrier, distributor and client.

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How can carriers and distributors set about realising these benefits? They need to embark on the joint development of a financial model which captures how economic value is created by their collaboration. This model will reflect the usual cash flows of the insurance business – premiums, claims, expenses, investment income, reinsurance payments and recoveries. It will show the surpluses created and how these are shared. It will be a multi-period model, which takes account of the economies in marketing costs which arise from customer loyalty.

A key part of the methodology is process redesign. This involves a joint exercise in process mapping, activity definition and quantification. Once the current processes are documented, then they can be redesigned for collaborative working. This is the way in which the inherent waste and frictional costs endemic to the present way of working are eradicated.

Understanding the value creation processes is dependent upon an ability to jointly model expenses to reflect the forces that drive their behaviour. This involves using the outputs of the process mapping work, identifying the cost drivers and putting these together to create a model that explains cost behaviour in terms of causal relationships. Information of this sort is not shared in the traditional carrier/intermediary relationship

The way in which reinsurance is used to preserve and enhance value is not shared with intermediaries in the traditional carrier-distributor relationship. Similarly, the level of capital committed to the business on both sides, and the cost of so doing is not disclosed. In the new relationship, this information is made available, as it is critical to understanding the value creation process.

The process mapping, expense modelling, reinsurance analysis and cost of capital projections together lead to a financial model that provides the basis for collaborative working. It enables both parties to approach the relationship from the perspective of maximizing mutual long-term advantage and to plan future cooperation in this way. It invariably leads to radical redesign of processes throughout value chain, with the elimination of duplication and waste, and the equitable sharing of the benefits. It gives the basis for future process improvement. In short, it provides the foundation for a true partnership relationship.

A brief paper like this can deal only with generalities. It is to be hoped that it has at least indicated the nature of the new carrier-intermediary model, highlighted some of the practical implications in its implementation and given a flavour of the benefits that it can achieve, for carrier, intermediary and client.

If you are interested in the practical application of these ideas, then please contact Russell Devitt on russell@tgpadvisers.com.

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