Commissions & Other Omissions:

The Case For Greater Disclosure and Transparency

An opinion piece by **Matt Schoen**
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I believe, with few exceptions, that greater transparency and disclosure are in everyone's best interest. Exceptions include trade secrets, patents pending, and other intrinsically confidential intellectual property. Insurance commissions and related compensation do not fall into those categories and these amounts should be fully disclosed, particularly with institutional transactions such as BOLI and COLI.

I recognize that this view places me squarely as an outlier, if not a heretic, in most insurance brokering circles. Efforts by state insurance departments, the SEC, and others to require greater disclosure of commissions have been assailed by various groups, most notably, in the case of the states, insurance agent advocacy groups.[1]

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As explored more deeply throughout this paper, there are legitimate concerns regarding fully disclosing compensation; still, I believe the benefits of full and uniform disclosure far outweigh the disadvantages.

Our company has been providing COLI- and BOLI-related brokerage services to clients for over 20 years and has operated with a 100% disclosure model from the outset. We negotiate our pre-purchase due diligence and placement-related compensation (aka brokerage) in advance with our clients; it doesn't differ from one insurance company to another. We believe it would be inappropriate to be paid more by one insurer than another; to do so would be disharmonious with our job, which is assisting our clients in finding the best possible product and carrier given their particular facts and objectives. At minimum, getting paid differing amounts could appear as though we have a conflict of interests.

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1 Witness the legal threats and subsequent Article 78 proceeding initiated by the Independent Insurance Agents & Brokers of New York (IIABNY) and the Council of Insurance Brokers of Greater New York (CIBGNY) in response to the New York Insurance Superintendent's proposed Insurance Regulation 194, "The Producer Compensation Transparency Rule." Regulation 194 requires producers to provide written disclosure regarding their role, and the manner in which they will be compensated, prior to the sale of an insurance contract. The IIABNY and CIBGNY argued that the New York Insurance Department overstepped its powers in establishing the regulation, and asserted that the regulation was arbitrary and would impose large, needless compliance costs on producers.

Late in 2010, New York Supreme Court Justice Richard Platkin denied all petitioners' claims. Not surprisingly, the IIABNY vowed to continue to fight, but ultimately acquiesced after losing its initial appeal. One can only hope that other states—or better yet, the NAIC—will feel emboldened by New York, and we will soon see similar regulations or laws across the land. (California was utterly thwarted by agent advocates in its attempt to enact commission disclosure legislation in the aftermath of the contingent commission scandal.)

If we believed not disclosing our compensation in advance outweighed the advantages of transparency, we'd likely have backed efforts to subvert disclosure laws. But we fully support the disclosure laws for the reasons enumerated throughout this paper. Moreover, we also bifurcate our pre-purchase due diligence and placement-related services from compensation for ongoing administration.

Ultimately, we embrace full disclosure because: 1) positioning our clients to gain better ongoing control of their operational costs is clearly in their best interest; 2) contrary to popular belief, full disclosure is in our best interests as well, as, among other things, it fosters a relationship rooted in mutual respect and trust; and 3) we offer an array of demonstrably valuable services and we are confident in our ability to deliver them to the satisfaction of our clients, ergo, we are confident that we can obtain attractive compensation and retain ongoing administrative engagements based on our ability to consistently perform to high standards. Despite the downsides of disclosure, expanded upon below, our model has served us and our clients well for over two decades.

Setting aside our anomalous business model, there is ample evidence that those resisting commission disclosure are ultimately doomed in their efforts. In fact, I believe those unwilling to fully disclose compensation may be subjecting themselves to increased liability while fighting for a lost cause. Consider the fallout from scandals, abuses, or conflicts stemming from opacity,[2] and the devastating impact that the lack of disclosure of counterparty exposures had during the early stages of the financial meltdown.[3]

The Department of Labor began investigating excessive, yet often hidden, fees in 401(k) plans over a decade ago. The GAO subsequently concluded a study in November 2006 recommending better disclosure of fees associated with 401(k) plans. Since that study was released there have been no fewer than 75 lawsuits[4] filed against plan sponsors and plan fiduciaries alleging excessive fees, conflicts in interest, etc., with regard to qualified (defined contribution) retirement plans.

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2 Among the study findings were that without information on all fees, Labor's oversight is limited because it is unable to identify fees that may be questionable. In addition, Labor and plan sponsors may not have information on arrangements among service providers that could maneuver plan sponsors toward offering investment options that benefit service providers but may not be in the best interest of participants. For example, service providers that assist plan sponsors in selecting investment options for the plan may also be receiving compensation from mutual fund companies for recommending their funds, fees that may differ from manager to manager. The service provider may not disclose this business arrangement, and consequently, participants may pay higher fees than they otherwise would. Finally, effective December 20, 2010, Labor's Employee Benefits Security Administration published 29 CFR Part 2525, titled "Fiduciary Requirements for Disclosure in Participant-Directed Individual Account Plans," setting forth final regulations requiring far more granular disclosure of plan fees. There have also been several legislative proposals put forth since this issue came to light (see the New DOL Fiduciary Rule below).

3 Over-the-counter derivatives transactions with notional values in the trillions of dollars contributed to the sudden dearth of liquidity because banks did not know, with any degree of precision, what others' net counterparty exposures consisted of. The financial industry and legislators got busy devising ways to assure no such vacuum of vital information happens again. Some of those efforts are manifested in the new rules requiring most derivatives to be transacted through central clearinghouses or exchanges (or to pay for exceptions with punitively high risk capital). Other notable examples include the punitive banking sector risk-weighting treatment (1250%) attributable to non-agency securitized investments lacking the granular risk-related data of the underlying individual loans and the NAIC's replacement of rating agency–based risk weighting of RMBS and CMBS by selected service providers.

4 These suits largely fall into three categories: 1) general excessive cases, 2) proprietary fund cases, and 3) university cases.

In April 2006, the New York Times ran an article[5] regarding possible conflicts of interest between compensation consultants and the major corporations they serve. The article prompted Representative Henry Waxman, then Chairman of the House Committee on Oversight and Government Reform, to commission a study titled "Executive Pay: Conflicts of Interest Among Compensation Consultants," released in December 2007. Among other things, the report found that conflicts of interest are pervasive and widespread: Over 100 large publicly traded companies hired compensation consultants with substantial conflicts of interest in 2006. The consultants providing both executive compensation advice and other services to Fortune 250 companies in 2006 were paid almost 11 times more for providing other services than they were paid for providing executive compensation advice. Perhaps most disturbingly, there was a correlation between the extent of a consultant's conflict of interest and the level of CEO pay.[6] Not surprisingly, as of February 2010, SEC rules require shareholder proxies to disclose whether these paid consultants perform other work for companies and what compensation they receive. Legislation requiring the SEC to fashion independence standards for compensation consultants also began circulating in 2010.[7]

Most germane to the discussion of BOLI/COLI compensation disclosure is the backlash to opacity, conflicts of interest, and excessive fees signaled by the Department of Labor's adoption of the new Fiduciary Rule,[8] which greatly expands the definition of fiduciary to cover a far broader universe of advisors and firms working with retirement plans and accounts, effectively sweeping in many advisors that historically needed only to meet the suitability standard. In addition to expanding the classes of advisors considered fiduciaries, the new DOL rules expand and change a number of Prohibited Transaction Exemptions, modify rules governing advisor compensation, and establish meticulous new disclosure requirements that apply to new and existing clients.

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Curiously, despite all the recent scrutiny and consequent litigation related to hidden and excessive fees, especially as they relate to qualified retirement plans and accounts, little attention has been focused on lack of disclosure and potential conflicts of interests, which appear to be omnipresent, between many non-qualified deferred compensation (NQDC) plan service providers and the insurance companies and mutual fund companies they often represent. Consider that many NQDC plan administrators still use a business model very similar to those targeted by the DOL's 401(k) disclosure regulations.[9] Specifically, qualified plan service providers offered to provide "free" or bundled administrative services, deriving the bulk of their revenues from soft dollar fees/commissions within the product (many of which are at the heart of pending litigation). In the case of NQDC service providers, the soft dollars are derived from COLI or mutual funds, the dominant asset classes used to informally fund the plans.

5 See "Outside Advice on Boss's Pay May Not Be So Independent" by Gretchen Morgenson.

6 The median CEO salary of the Fortune 250 companies that hired compensation consultants with the largest conflicts of interest was 67% higher than the median CEO salary of the companies that did not use conflicted consultants.

7 In response to overt concerns expressed by the SEC, the Institutional Limited Partners Association (ILPA), developed and a reporting "template" intended to improve the capture and disclosure of details regarding fees, expenses, and carried interest paid to General Partners and their affiliates by investors in private equity investments. The initial "template" was released in January 2016. The ILPA launched a second phase of the reporting initiative in March 2017 to support and expand adoption of the "template."

8 Note that the final effective date for full implementation of the rule has been postponed numerous times, including most recently by order of the Trump administration. While portions of the rule are in effect, other aspects have been delayed while also being open for further review and modification.

9 DOL's participant disclosure regulation (404a-5) and service provider disclosure regulation (408b-2), which both went into effect in 2012.

There is no doubt that plan administration services can be highly complex and demanding. Because employer sponsors do not fully grasp the extent of compensation embedded in these products, they often have no idea whether the amount they are paying is reasonable in relation to the services rendered. Further, they often unwittingly put themselves in a compromised position with little long-term operational control. Should the service provider fail to deliver services in an acceptable manner, the plan sponsor will likely be unable to discontinue or redirect product-based commissions or fees, even if it means having to pay a new service provider additional hard dollar fees. This arrangement is quite telling: Are the insurance company's interests and loyalties aligned with those of policyholders, or policy distributors?

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A good portion of the evidence suggests it is the latter. When interest rates were higher, insurers routinely payed as much as 20% of first-year premiums as commissions, in addition to paying 0.25% of cash value trailing commissions (often, fully vested). Bear in mind that due to state insurable interest concerns, IRC §264(f) cost considerations, and premium/DAC tax costs, replacing COLI via IRC §1035 exchanges is far more problematic and costly than changing mutual funds. When insurance companies "front" commissions to brokers from surplus capital, they must ultimately recoup these costs, and they do so at a price: Policyholders are effectively borrowing from the insurer to pay the broker's first-year commission. Insurers don't lend for free. When they amortize the commission and other expenses (e.g., DAC tax and premium tax), most often in the form of a higher M&E charge, they include a cost of capital factor, usually ranging from 12% to 15%. There is nothing inherently wrong with this practice, but full disclosure is essential for plan sponsors to understand the potential impact on long-term policy performance and its effectiveness as a hedge or financing tool.

Given that soft dollar fees embedded within COLI can be a multiple of the loads within mutual funds, one wonders why these arrangements haven't been subject to the same degree of scrutiny as 401(k)-related fees. Perhaps it is because, unlike with 401(k) plans where excessive, hidden fees are ultimately passed along to plan participants, NQDC-related excess costs are often absorbed by the employer-sponsor. ERISA fiduciary standards generally do not apply. Here is the rub. If this is so, and if needless costs are material, it seems only a matter of time before some resourceful lawyer takes up the banner on behalf of shareholders. If that happens, and if they are successful in exacting a settlement or favorable judgment, waves of successive suits will likely follow. Isn't it better to unbundle all services and pay for them separately? Among other benefits, one can obtain professional services agreements clearly spelling out deliverables and services to be performed with rights to terminate the service provider for non-conformance—not to mention enabling plan sponsors to answer elemental questions: How much do you pay for those services? How do you know that product has competitive pricing? And, perhaps most importantly (in light of the long-term nature of the instrument), just how favorable are its terms? If your current provider is unwilling to address such questions, rest assured there are service providers who are. There are even a few NQDC administrative service providers that don't sell products (COLI or mutual funds) at all.

Many COLI products that are used to hedge NQDC plans contain insurance-dedicated mutual funds (IDMF) with what amount to retail (read – exceedingly high) investment management fees (IMF), despite the fact that more cost-efficient alternatives are readily available for many policyholders. I don't buy the conventional argument that the manager's performance justifies the higher fee; this claim is rendered vacuous when the same manager offers a substantially similar fund on other COLI platforms at less than half the investment management fee of its IDMF. The higher IMF likely contains generous 12(b)(1) fees,[10] payable to the insurance company. In turn, insurers use those fees to recoup high front-end distribution costs sooner or share the fees with the broker. If the broker doesn't realize the extent of these egregiously high IMFs in relation to those available within suitable alternative products, something is wrong. But that scenario may be the lesser of two evils, because if brokers do realize how much fat is loaded in these funds and still steer clients to these products, one must question their motives and integrity. We believe brokers' incremental income hardly justifies shifting superfluous, disproportionately high costs to their clients. The broker makes more, but the insurance company ultimately makes much, much more. Clients receive a double dose of disservice.

Shame on producers for not making buyers aware of all suitable products; shame on buyers for not exercising more rigor in selecting more objective advisors

Shame on producers for not making buyers aware of all suitable products; shame on buyers for not exercising more rigor in selecting more objective advisors. Given the complexity of these products, it doesn't seem plausible to suggest that buyers become experts themselves, but blithely accepting a bundled offering, without demanding full disclosure in advance, seems naïve at best. It's essential for prospective policyholders to insist upon full written disclosure of all compensation prior to consummating a purchase because whatever leverage the buyer has to secure it surely drops precipitously the moment the deal closes.

When it comes to embedded commissions intended to support ongoing administrative services, we think employer-sponsors should strongly consider excluding soft dollar commissions altogether (COLI can be structured with 0% service fees). However, if one opts for the soft-dollar route, one has an obligation—perhaps a fiduciary duty—to secure full rights to redirect commissions under clearly defined circumstances (as explained further below).

10 A 12b-1 fee is an annual marketing or distribution fee on a mutual fund. The 12b-1 fee is considered an operational expense and, as such, is included in a fund's expense ratio. It is generally between 0.25% and 1% (the maximum allowed) of a fund's net assets, although it is often expressed as a percentage of the manager's IMF.

An Alternative to Opacity

Is our business model perfect? Of course not, but we think it serves our clients' best interests better than any other approach we have considered. By describing it here in detail we hope to prompt inquiry and discourse regarding how it may be further optimized, with the ultimate objective of establishing an industry standard that achieves a fair and sustainable balance of all parties' interests.

As touched upon earlier, we draw a clear distinction between brokerage services (pre-purchase due diligence and placement) and ongoing administrative services. Each set of services is appended by a separate statement of work that enumerates, in painstaking detail, the services we are to perform and the deliverables we are to provide, along with concise corresponding timelines for the fulfillment of each.

Why do we separate placement/brokerage from ongoing administration? When we fulfill our contractual obligations for the former, we are entitled to be paid (that is, as long as the client consummates the transaction). In the case of administration, however, the fulfillment of our duties is continual and therefore our success or failure to deliver as agreed should be measurable, and our conformance thereto verifiable. If we fail to deliver as promised, clients should have the right to fire us. Hence, our administrative-related compensation is not irrevocably vested.

When recommending products and insurers, we undertake an exhaustive request for information/request for proposal process. This process is conducted in stages, narrowing the number of prospective candidates to no fewer than two by the final stage. While we include a meticulously granular cost comparison, and evaluate each carrier's financial condition and administrative aptitude, we focus even more on the representations, warranties, and indemnifications we can secure on behalf of clients. As required by governing bank regulations, policyholders are proactively involved in evaluating and negotiating with candidates throughout the entire process; consequently, they learn critical product characteristics and distinctions.

We don't seek or accept compensation from money managers who receive allocations from our clients

Often our pre-purchase due diligence includes helping clients find the most suitable line-up of available investment choices within the policy and, in the case of BOLI, to secure the best available terms and pricing for stable value protection (SVP).

We don't seek or accept compensation from money managers who receive allocations from our clients. Not only does accepting such compensation create potential conflicts at the outset, it can cause greater conundrums for us over time. For example, when is it appropriate to recommend that a client allocate funds away from a poorly performing manager? Might that recommendation tend to be deferred if the manager in question is paying us more than other available alternatives? I don't even want to be in that position, because no matter how diligent and objective we might be, it could appear that we dragged our feet. The only way it makes sense for us, or any similarly positioned advisor, to receive a portion of our compensation from managers is if all managers paid a uniform percentage of assets to brokers (e.g., 5 basis points). This may be achievable, but it is unlikely worthwhile. When all is said and done, what is the purpose of this particular layer of cost? Does it achieve anything truly beneficial or does it merely make it more difficult to distinguish between manager's IMFs, insurers' charges, distribution-related costs, and ongoing service fees? It seems more straightforward to remove all 12b-1 fees from IMFs that are intended for brokers, instead structuring administrative fees according to bank preference (e.g., as a policy asset-based charge or a fee paid external to the policy).

Prior to the financial crises, our pre-purchase engagements included a distinct and significant sub-assignment. This consisted of comparing the relative strengths of SVP providers and their offerings. It was a labor-intensive process involving an exhaustive comparison of each and every provision of the respective stable value agreements, as well as the pricing and financial condition of each provider. However, pre-crises, few insurance carriers offered SVP and there was a viable competitive market between several non-insurer counterparties, including JPMorgan Chase, Bank of America, Royal Bank of Canada, and AIGFP. Since mid-2008, none of these counterparties have been actively writing new BOLI SVPs. (Their withdrawal is beyond the scope of this paper.) Presently, the BOLI SVP market is almost entirely accommodated by the underwriting BOLI carrier. Thus, until there are SVP solutions available from non-underwriting insurers, the process of selecting an SVP provider will be intrinsically linked to choosing the best overall insurance carrier and product.

I am part of a team that has developed intellectual property intended to help BOLI insurers sufficiently mitigate the risks attendant to offering BOLI SVP so that they can offer an economically worthwhile product. We license our intellectual property to BOLI insurers and, consequently, we fully disclose this role and compensation prior to consummating any pre-purchase engagements. Although we believe we are still fully capable of being objective when advising clients regarding the selection of the best insurer(s) and product(s), we also respect a prospective client's decision to have us recuse ourselves from an engagement.

We organize and maintain comprehensive documentation of the product/insurer selection process for future access. Our fee for performing these pre-purchase due diligence and placement-related services and negotiations can be paid as a onetime fee or spread out over time. Clients elect whether to pay us directly or whether to structure the fee in the policy. Either way, the fee is agreed upon in advance; it does not vary from one product to another or one provider to another. We warrant in writing that we will not receive any other compensation. This fee is vested if paid over time because we have fulfilled all services and deliverables at the time the transaction closes. If it does not close, we are not paid. In exchange for lowering our overall placement fee, some clients have offered to provide us a minimum breakage fee (i.e., in the event they elect not to consummate the purchase, we are paid a smaller fee).

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Our ongoing administrative service fees are usually paid directly by clients. (We leave it up to clients, but thus far few have opted to embed our administrative fees within policies.) The services we provide are so extensive and so thoroughly documented that clients believe they can deduct our administrative services fees for income tax purposes. Again, these fees are not vested; they hinge upon our ability to successfully perform services according to precisely defined timelines.

BOLI Vendors and Applicable Bank Regulations

Since bank regulations have long[11] mandated many characteristics inherent within our model, it is curious that ours differs so much from the norm.

OCC Bulletin 2013-29, which covers Third-Party Relationships, fundamentally requires banks to practice effective risk management, including works performed by third parties. Responsibility ultimately rests with the bank's board of directors and senior management. Among other things, OCC Bulletin 2001-47 expresses concern regarding inadequate risk management over third-party relationships and it points out that effective risk management of third parties entails a continuous lifecycle, beginning with the planning phase.

A comprehensive discussion of the bulletin's guidance is far beyond the scope of this paper. In part, and perhaps most apropos to BOLI vendor relationships, it stipulates that 1) in order to ensure contract enforceability, limit the bank's liability, and mitigate performance-related disputes, a contract must clearly define the third party's responsibilities and expectations of performance; 2) management should negotiate contracts that clearly specify the rights and responsibilities of each party, and specifically identify the frequency, content, and format of the services and tasks to be provided; and 3) managers must determine if the vendor's fee structure and incentives would result in inappropriate risk taking.

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While conducting BOLI governance assessments over the past 20 years, we have encountered numerous instances where a BOLI vendor's compensation has not been fully disclosed, where there is no documentation in evidence that the bank performed due diligence regarding the vendor's risk-management practices or capabilities, where the BOLI vendor had incentives that ran contrary to the bank's best interests (e.g., a portion of the vendor's compensation was covered indirectly by specific money managers), and where the contract failed to adequately define rights and responsibilities, services and deliverables, and the timing thereof (including many instances where there was no written agreement at all).

11 OCC Bulletin 2001-47, "Third-Party Relationships: Risk Management Principles," and OCC Advisory Letter 2000-9, "Third-Party Risk," both rescinded by OCC Bulletin 2013-29, shared many similar requirements.

The Downside of Transparency

One obvious downside of our approach is that once all compensation is out in the open, clients negotiate it down as much as possible. Far more vexing, however, is the strong tendency (usually emanating from procurement departments) to press for full rights to terminate a service provider (without cause) at the end of a specified, typically a very short term. Although this is, on the surface, an understandable, instinctive response, I think it is largely responsible for our approach remaining an exception to the pervasiveness of non-disclosed, irrevocably vested compensation. It hardly tempts others to join us in our full-disclosure approach. It is little wonder the two models are so diametrically at odds.

We believe there are solutions that can fairly and equitably balance the interests of BOLI/COLI service providers and end-buyers such that vendors can begin representing the policyholder's best interest without placing themselves in insupportable peril. To reach such solutions, one must tackle two fundamental questions:

1. *What is the proper split of compensation between placement-related compensation and ongoing administration?*
2. *How does one assure that providers of ongoing administrative services retain appropriate protection from being terminated without cause?*

Publicly available documents pertaining to bonds collateralized by BOLI commissions suggest that, historically, an average of about 80% of trailing commissions are fully vested with the broker. (This is consistent with our findings as well.) This 80/20 ratio has no doubt shifted further toward the non-vested side in recent years, as carriers realized the pickle irrevocably vested compensation often places them in (e.g., when policyholders receive unsatisfactory service from the vested broker and learn they are powerless to redirect or discontinue commissions, acrimonious feelings tend to extend beyond the broker to the carrier—and rightly so).

That 80/20 ratio seems unmerited; it is highly suggestive that a disproportionate amount of compensation relates to product placement. When this is so, it also suggests that carriers design products to win the attention and allegiance of producers instead of focusing on the policyholders' best interests. There are a few exceptions to this rule. Those select few trailblazers establishing beachheads in non-existent markets certainly deserve a higher share of compensation, particularly when they lead carriers into these new markets. But such compensation, which is essentially a form of intellectual property, could and should be separated from traditional distribution fees and administrative fees.

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Clearly the amount of ongoing administrative service work differs depending upon whether the policy is a general account or variable separate account product, and that should fittingly impact the amount and ratio of vested compensation. General account products are far less complex and require less investment in infrastructure by the BOLI vendor. It is therefore rather ironic that general account products tend to have 1) higher overall compensation than variable products, and 2) higher amounts of vested commissions (or, at minimum, commissions that cannot be redirected at the discretion of the policyholder).

A dialogue seems long overdue with insurers, service providers, and policyholders all at the table to align fair ranges of compensation, appropriate splits between irrevocably vested placement commissions, and partially vested ongoing administrative related compensation. My view of an ideal outcome includes a coalition of leading BOLI carriers agreeing upon standards for overall compensation, the ratio of vested to partially vested, and the terms for redirecting ongoing administrative-related compensation. By establishing industry standards, they would effectively remove economic incentives favoring one carrier over another. In so doing, brokers would be able to focus entirely on the task of determining which carrier has the best combination of product, financial standing, and service support capabilities to fulfill a client's particular objectives.

Note that I classify ongoing service-related compensation as partially vested. If a service provider is fulfilling its contractual obligations, it simply isn't fair or appropriate for it to be terminated without cause at the complete whim of the policyholder (notwithstanding procurement's predisposition to place all providers in such a box). Consider a situation where the provider is replaced by the golfing buddy or brother-in-law of the CEO, with no prior BOLI service experience. The carrier could act as an appropriate protector of the service provider in these and other similar instances. On the other end of the spectrum, a service provider should not receive any protection when it continually fails to perform promised services and fails to cure such breaches within the stipulated period. Likewise, protection should be forfeited if the service provider is found to have been grossly negligent or fraudulent in its dealings with the policyholder.

While these extremes seem easier to resolve to everyone's satisfaction, it is far more nuanced and challenging in between. For example, what percentage of compensation should the policyholder be able to redirect to a new service provider when the incumbent is fulfilling its original contractual services and deliverables, but bank regulatory changes now require previously unknown, additional services to be provided (and the incumbent is unwilling or unable to perform such services)? A bank may legitimately want to consolidate all services under a single service provider capable of performing all regulatory mandated services. It may not be feasible to wrap the supplemental services around existing services and reporting, without undue delays or complexity. Having multiple service providers generally entails greater vendor oversight burden, and increases overall costs and risks (e.g., exposure to data breaches). These situations require thoughtful discussion, but arriving at suitable standards seems workable and necessary.

By establishing industry standards, they would effectively remove economic incentives favoring one carrier over another

There is another area begging for an industrywide standard: the 12b-1-related compensation paid by investment managers to insurance companies. A standard seems essential within both the BOLI and COLI sectors. Assume, for the sake of argument, that none of these fees make their way downstream to the broker. Unless a standard can be reached, I favor striking 12b-1 fees from COLI/BOLI altogether. Frankly, for the same reasons identified for barring them from being passed along to brokers, I remain persuaded that the disadvantages of including them far outweigh the advantages. The presence of 12b-1 fees, which can vary materially from manager to manager, simply makes it more difficult to compare products and to understand carrier net costs, and throws enormous uncertainty into a policyholder's ability to manage future costs. Although it arguably causes uncertainty for the carrier as well, remember that the carrier retains the legal right to hire and fire all managers; so, if push comes to shove, the carrier can, over time, insist on higher 12b-1 fees or extricate managers unwilling to acquiesce.

One more cautionary tale on a related topic: Carriers can make money from unaffiliated investment managers, even when they are not paid 12b-1 fees. We found this out the hard way. While conducting an RFP on behalf of a client we asked whether the insurers "were paid any 12b-1 or other fees by the managers? If so, how much?" The initial answer we received was "No." Then we reworded the question to: "Is the IMF you charge the policyholder identical to the IMF the manager charges you? If not, explain in detail the difference." We learned they didn't pass along all of the breakpoints they received from some managers. Despite the fact the insurers still offered a highly competitive product overall, they lost credibility with the client. There is a real risk of damaging one's reputation when offering anything short of full disclosure. Once damaged, good reputations are fittingly difficult to restore.

Conclusion

In conclusion, it is a personal mission to make opacity of institutional insurance-related compensation an anachronism. My hope is that others will begin embracing a model of full disclosure now, while it's still meaningful to do so, rather than when required by seemingly inevitable regulation. There is still an opportunity to be part of a change that is clearly in the best interest of policyholders. An overarching mission is to extend our approach to individual markets, which can be summed up as:

Doing major damage to the broker/agent-centric distribution model and doing everything in our power to make a consumer-centric model ubiquitous.

About the Author

Matt Schoen

MB Schoen & Associates, Inc.,
2754 Brandt Drive South, Suite 200
Fargo, ND 58104
(701) 235-1183
mbschoen@coliaudit.com

Matt Schoen is founder and president of MB Schoen & Associates, Inc., an institutional insurance placement, restructuring and administrative services provider. Specializing in performing independent, automated reconciliations of separate account BOLI since 1992, MBSA currently administers BOLI with aggregate cash values exceeding $18 billion.