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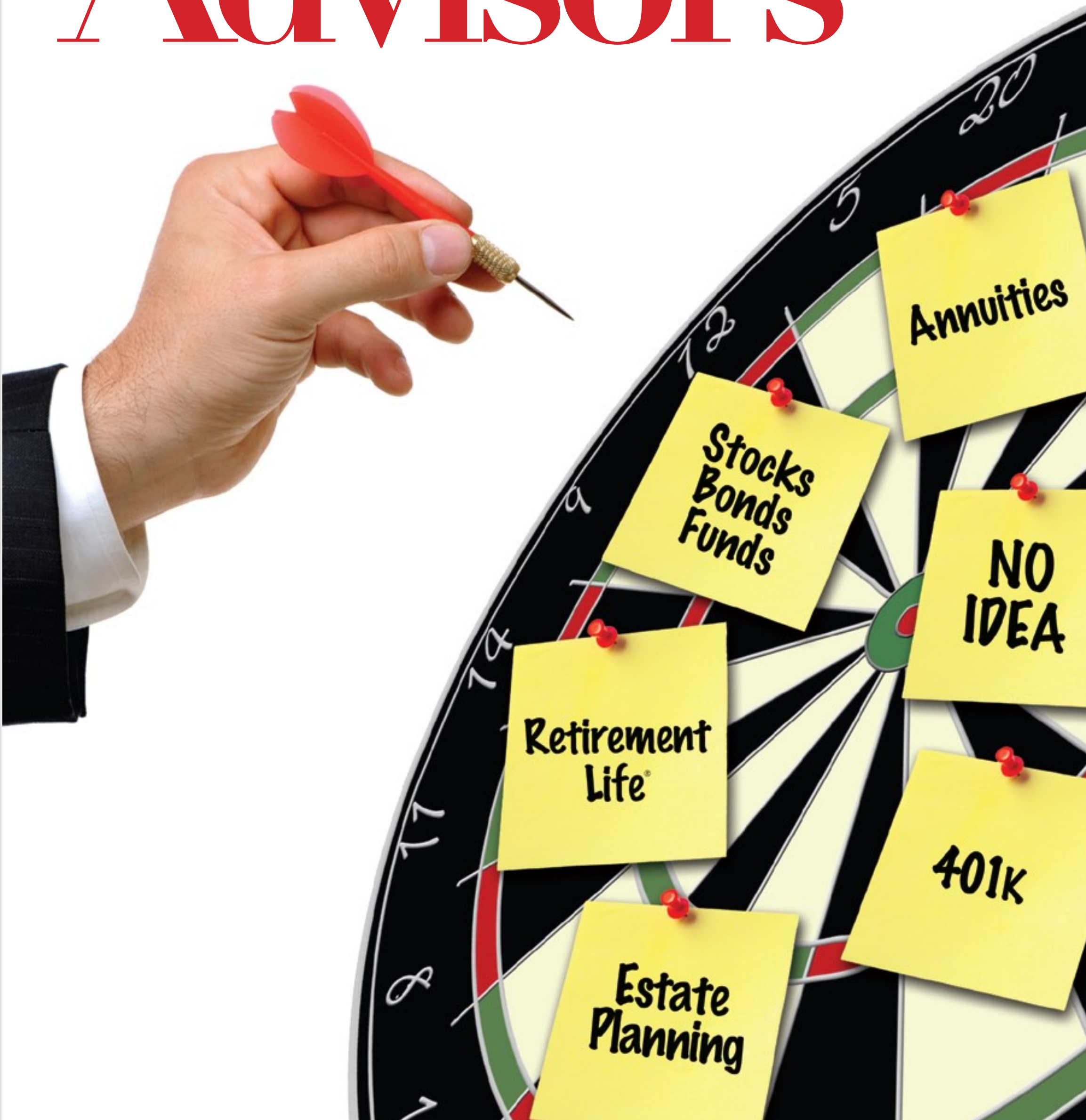
Bad Advisors

HOW TO IDENTIFY THEM & HOW TO AVOID THEM



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ROCCY DEFRANCESCO
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Chapter 2

Insurance Marketing Organizations

Why am I starting this book with an early chapter on insurance marketing organizations (IMOs)?

Mainly because I need to give readers background information on what really drives a good portion of the life insurance and annuity sales made in the industry. Learning a about IMOs will help you understand why there is so much bad advice being given when it comes to sales of fixed life insurance and annuities.

This chapter is a look into the insurance industry that no insurance agent will tell you about. I consider this chapter a **dirty little secrets chapter** where I will give you valuable insight you will not receive by anyone else in our industry.

I also need to qualify the term "**fixed**" as it is used in conjunction with life insurance and annuities. Fixed life insurance and annuities by definition are not "**variable**." To sell a fixed life insurance policy or a fixed annuity, you only need a life insurance license. To sell a variable annuity or variable life insurance policy you need a securities license.

Variable products will be dealt with in the chapters on Broker Dealers and Securities Licensed Advisors.

What is a General Agent (GA)?

If this chapter is about IMOs, why am I discussing GAs? GAs were the predecessor to what we in the industry call IMOs. IMOs are also known in the industry as FMOs (field marketing organizations).

A GA is a person or more typically an entity that "in the old days" used to recruit insurance advisors to sell products.

What do I mean when I say recruit? Through various marketing efforts, GAs would try to find potential advisors (not licensed yet) and currently licensed advisors to sell life insurance and annuities through the GA.

How did they recruit? If they wanted to recruit new agents and bring them into the business, some GAs would go to college campuses. Some would advertise in various journals and papers, and some would recruit through word of mouth.

What was the sales pitch to have a not-yet licensed advisor? The GA would tout that it offered education/training on the products that will be sold, and that, once trained, the agents could make significant money selling life insurance and annuity products.

Some GAs would offer a **minimal salary** for a period of time (which was more like an advance or draw), **health insurance**, and **office space** (or an office allowance). If the recruited agent did well, the money put out up front by the GA would be recouped from future commissions generated by the agent.

How do GAs make money? They make an override on all business placed by recruited agents.

For example, if a newly licensed insurance agent sold a product that paid a $1,000 commission, the GA would make an override of between $400-$500 or more. If a more seasoned agent sells the same product, the override would be between $200-$400.

The business model of a GA is fairly simple—recruit as many good insurance sales people as possible so the maximum amount of overrides can be generated. Once built, it's a terrific reoccurring revenue model for the GA.

Independent and captive GAs

GAs can be either captive or independent. A captive GA is one who recruits only for one particular life insurance company (like Guardian). An independent GA is one who can represent multiple insurance companies. I'll give you my very negative opinion on captive GAs/IMOs later in this chapter.

Why were GAs needed?

Why don't insurance agents simply go directly to insurance companies and sign up to sell their products? There are several reasons, but the two main ones are: 1) the ability to maximize compensation of the agent is less; 2) many insurance companies did not want to put effort and money into recruiting and training.

Way back in the day (and still true for a few companies today), insurance companies actually did their own recruiting and training. Over time, recruiting and training was outsourced to GAs who, again, recruited for one company in particular or for a handful of companies.

GAs are a dying breed

Today, GAs are going the way of the dinosaur. They are slowly becoming extinct.

Why? Because the GA model is a greedy override model. Back in the day, the mentality of a new insurance agent was that they would essentially be employees of the GA. That is not technically accurate in most cases because the insurance agent was an independent contractor.

However, the sales pitch again was that the agent coming on board would be given money so the agent could afford to live until his/her sales started coming in and that the agent would be provided health insurance and be given office space or an office allowance.

When a better model came out (the IMO model) that could pay agents more or significantly more money, over time the industry has shifted away from the low agent compensation model of GAs and has shifted to the more flexible and higher paying IMO model.

What is an Independent Marketing Organization (IMO)?

As you'll find out, the term "independent" in IMO is, for the most part, a misnomer (most IMOs are not "independent").

An IMO is a company that recruits insurance agents to sell fixed life insurance and annuity products.

It sounds like a GA right? It's similar, but IMOs do not provide health insurance; and they do not provide office space or office allowances.

IMOs tout that they provide training; but for 95% of the IMOs in the industry, that is not the case.

IMOs are **<u>supposed to be independent</u>**. They are supposed to help insurance agents sell products through multiple insurance companies (vs. one company or only a handful of companies like old-school GAs).

Because IMOs do not provide health insurance, office space, or an office allowance and because most spend little or no money on training, the IMO can afford to pay insurance agents higher commissions.

Why IMOs were formed, and why are they still in existence?

IMOs were formed to help insurance agents maximize commissions (this was not the case with GAs who paid low commission rates because of their higher expenses per agent).

I asked the following question earlier: Why don't insurance agents get contracted directly through insurance companies instead of through a GA or IMO?

The answer is **<u>MONEY</u>**. Think about it. If an insurance agent goes to insurance company XZY and says he/she can place $1,000,000 in annuity business a year, does that allow the agent an ability to negotiate a high commission arrangement? The answer is an emphatic NO!

However, what if an IMO contracts 100 agents who all can place $1,000,000 in annuity business? That's $100 million of annuity premiums. Could an IMO then go to the insurance company and negotiate a higher payout? Absolutely. Then can the IMO, in turn, give a higher commission payout to the agent and still make good money for the IMO? Absolutely.

Agents working through sizable IMOs can earn an additional 10-40% in commissions per product sold.

Therefore, when a sizable IMO recruits an insurance agent, does the IMO have an advantage over insurance companies who try to recruit direct? Absolutely.

Let me get back to the word "**<u>independent</u>**." IMOs were supposed to allow agents to be more independent. Why? Because an IMO might have contracts with 20-30 and even up to 200 different companies. The average agent on the street might be able to obtain contracts at 2-5 companies.

It will be impossible for an agent to get contracted with 20-30+ companies. The companies limit who is contracted because there is an expense per agent. Also, if you are not producing, the insurance companies will eventually terminate you.

In my opinion, in order to give clients the best advice, you have to have access to "all" the reputable companies. IMOs do give agents the best opportunity to have access to all the best products even though most IMOs do not help agents give the best advice (as you'll learn).

Insurance company recruiting is dead

IMOs have such a foothold in the industry that many insurance companies no longer try to actively recruit insurance agents directly to the company.

Over time, the percentage of business placed through IMOs in the industry is at such a high percentage that IMOs are the entities in our industry that drive what products are sold.

This has created sort of a love-hate relationship between IMOs and the insurance companies they represent. As IMOs have gotten bigger, they have become more demanding on insurance companies. As you can imagine, IMOs have been flexing their muscle and have tried to strong arm insurance companies into paying more and more override commissions to the IMO.

Insurance companies for a long period of time went along with this model which did nothing but fuel the creation of more and bigger IMOs.

Interestingly, IMOs have recently become too greedy and too demanding. As profits have been shrinking at many insurance companies due to poor stock market performance, they have pushed back a bit.

Some insurance companies have even terminated contracts with a few very large IMOs. Why? Because insurance companies have been pushing for more loyalty from IMOs; and ones that were terminated were doing some production but not enough production to keep the very high commission override contracts that had been negotiated.

Why most IMOs are NOT good for our industry or the consumer

I'm not sure if you noticed but when I explained why IMOs were formed I said very little about the reason they were formed being for the benefit of the consumer who ends up purchasing a life or annuity product.

IMOs were formed so IMO owners could make money and so agents could make more money. The theory was that agents could offer more products to clients by working through an IMO that has access to 20-30-100-200 companies, but the reality is that most IMOs do not help agents provide the best advice to their clients.

Why?

I'll give you one guess. **MONEY**.

Think about it. If an IMO does its job in helping licensed agents find the best product for each individual client, that would create a situation where premium dollars that flow through the IMO really will get spread out among many different insurance companies.

If the IMO spreads premium dollars among many different companies, what happens to the negotiating power of the IMO to demand higher commissions from the insurance companies it represents? It drops like a stone.

Therefore, guess what happens in the real world when "most" IMOs recommend products? They end up recommending the same products over and over and over. By doing so, they assure that the IMO will meet certain production marks with certain insurance companies.

Guess what happens when an IMO meets certain production marks with an insurance company. If you're following the theme of this chapter, you'll know the answer is that the IMO makes **MORE MONEY**. IMOs make millions of dollars each year by reaching various production levels and are provided cash bonuses when they reach them.

Independent?

Unfortunately, most insurance agents have no idea of the games that are played internally at IMOs. Most insurance agents are sold a bill of goods by an IMO that the IMO has "top contracts" at all the major insurance companies. Therefore, if the agent works with the IMO, the internal staff at the IMO will make sure the agents receive recommendations that are best for their clients.

Unfortunately, that is not the reality of the industry.

Let me digress for a bit to tell you how IMOs work with insurance agents. Once insurance agents decide to get contracted through an IMO with 1-5-10+ different insurance companies, they are assigned a life insurance marketer and an annuity marketer.

Marketers sit in a cubical all day answering e-mails and phone call from insurance agents who are looking to sell products to their clients.

Let me go through an example of what is supposed to happen when an insurance agent calls an IMO for help with a specific client.

The agent calls his/her marketer at the IMO and says that his/her client is 65 years old, is about to retire, and would like a product that would guarantee a rate of return coupled with a guaranteed income for life.

The marketer says, "Great. Let me get a little more information." Then the marketer will recommend 1-2 products for the agent to choose from.

The marketer is supposed to have the knowledge of "all" the useable products and be able to make an "unbiased" recommendation to the agent.

The agent picks product one and sells it to his/her client and thinks he/she received great service from the IMO.

Let me tell you the problems with IMO marketers:

1) Many of them don't fully understand the products they are recommending. This obviously makes it impossible for the best product to be recommended to the agent.

2) Many of them do not know all the available products. This is because many marketers get used to the same 1-2-3 products and are not professional enough to make sure they spend a significant amount of their time researching the frequent changes to products in the market and the new ones that come out. Again, this makes it impossible for a marketer to recommend the best product to the agent.

3) Most marketers are paid a percentage of the commission override on cases sold. Why is this a problem? **GREED!** I can't tell you the number of conversations I've had with marketers over the years where they've told me they push one product over another because the commission override for them is better (no, the commission for the insurance agent selling the product isn't any better).

Yes, this is outrageous and is one of the reasons I decided to write this book.

4) Most IMOs do not really have access to "all" the available products. Most IMOs are small or medium sized, and they simply don't have contracts with all the companies they need to be in order for marketers and agents to have access to the "best" product.

There are a handful of very large IMOs who have access to just about any independently sold product, but they are a minority in the industry (and it wouldn't matter most of the time because the marketers are still going to recommend their 1-2-3 core products to agents because the agent won't know any better and because the compensation for the marketer is higher).

Is this starting to crystallize for you?

The vast majority of "independent" insurance advisors selling products do so through IMOs. The agents are relying on IMOs (which is a separate issue I'll discuss later) to help them pick the best products for their clients.

Unfortunately, most agents are selling products through IMOs that don't have access to all the best products.

Unfortunately, most agents are dealing with marketers who couldn't pick the best product for their client if it were sitting in front of them with a blinking red light (because most marketers are incompetent).

Unfortunately, even if the marketer helping the agent giving advice is competent, the chances are significant that your agent is still not going to be given the best product to offer you because the one with the highest commission override instead is going to be recommended.

If you are sitting there thinking that **your** insurance agent just happens to be the one who is working with an IMO that has all the needed contracts, that has a competent staff of marketers, who will recommend the best product, and ignore how much money can be made by recommending an inferior product, **you're living in a fantasy world**.

Some IMOs are owned by insurance companies!

If what I've told you already doesn't put doubt in your mind about an insurance agent's ability to provide you with the best products, I wanted to let you know that many IMOs in the insurance industry are **partially owned by insurance companies**.

If you read books like I do, when you read something that is unbelievable or outrageous, you probably just dropped the book on the floor, did a double or triple take at what you just read, or you just readjusted your classes or rubbed your contacts to make sure what you read said just what you thought it said.

I'm not kidding. There are many IMOs in the insurance business that are partially or are wholly owned by insurance companies.

If it weren't so pathetic, it would be laughable. Have you ever heard of the saying, "having the wolves guard the hen house"? I think that analogy is right on the mark when it comes to having an IMO that is owned by an insurance company give "independent" advice to insurance agents (it's not going to happen).

You don't have to be a genius to follow the bouncing ball on this one. What products do you think get preferential treatment at an IMO that is owned in part or in whole by an insurance company? You're right—the products of the insurance company with an ownership interest.

Are the products from that one company always or even most often the "best" product for all of an insurance agent's clients? The question actually makes me laugh out loud. Of course not.

Do you think the IMO that is partially or wholly owned by an insurance company discloses this to the insurance advisors it recruits? The answer is no.

This illustrates a significant issue in the insurance community. Insurance agents do not make a habit of being in the know and doing their own independent research on products or the IMOs they deal with.

A hopeless picture?

What are the odds that the agent who sold you your last life insurance policy (term, whole, universal, or indexed) or annuity (fixed, deferred, fixed indexed, etc.) works with an IMO that **<u>can't possibly</u>** provide the agent with the best product?

If you were working with an "independent" insurance advisor, I'd say the odds are in excess of 80%. That means, in my opinion, you have less than a 20% chance of working with an agent who is working with an IMO that gives that agent a chance to provide you the best product (I said a chance because the actual percentage is less due to other issues I'll discuss in other chapters).

Are you sick to your stomach yet?

What I've disclosed to you in this chapter, 50% or more of the insurance agents selling products don't even know.

Most IMOs are set up by design to NOT provide insurance advisors with the best life insurance and annuity products. Because of this, you should be sick to your stomach.

If you are receiving advice from what I call a "captive" agent (see Chapter ____), the chances are virtually zero that you will be offered the best product for your particular situation. Then you'll really be sick to your stomach.

Full disclosure

Why do I know so much about IMOs? Several reasons. First and foremost, I dedicate myself every day to learning as much as I can about the insurance industry in general and specifically the products offered to make sure when I educate advisors I am providing them with the best information.

Why do I really know the GA/IMO structures?

As I indicated in my bio section, I am life and annuity licensed. I used to have real clients before I decided to take my research and knowledge and put it to use to help advisors through The Wealth Preservation Institute.

Over 10 years ago when I obtained my insurance licenses, I **<u>unfortunately</u>** got licensed through an old school GA out of Indiana by the name of Tom Dyer. He was recommended to me by a good friend, and so I made the incorrect assumption that Tom would treat me fairly when it came to commissions. He was your classic GA, and I was your classic newbie to the industry who didn't know anything about contracting and compensation.

I used to market myself exclusively to physicians. This made sense since I wrote a book called <u>The Doctor's Wealth Preservation Guide</u>.

I didn't look to my GA to educate me on products. I did my own detailed research. I didn't look to my GA to help me understand the use of cash value life as a wealth-building tool.

I had no problem finding a handful of clients each year who wanted to buy insurance and/or annuities from me. Since I didn't know anything about contracting and the GA was recommended to me by a friend of mine, I just signed the contracts that were put in front of me so I could sell products I recommended to various clients. I didn't know anything about commissions and I assumed incorrectly that I would be treated fairly.

Again, I wasn't concerned about selling the best products to my clients because I did my own research to make sure that was the case.

After placing a few life cases through the GA, I found out why life insurance agents like the industry. The money wasn't bad (and keep in mind that, when I sold my first policies, I was actually fully employed at the time and running a five-doctor orthopedic clinic (meaning that I didn't rely on the life commissions to earn a living)).

After continuing to do my research on life and annuity products, I ended up interacting with many different insurance agents. Like employees in a small employer setting who sit around and discuss what each other earns, insurance agents like to sit around and discuss/brag about what they make.

What I found out was that I was in a "career system" under the GA with whom I was working. The career system is one where agents are provided health insurance, office space or an office allowance, and where the ultimate commission to the agent is far less than an independent channel.

I had health insurance and an office through my orthopedic-clinic employer. I didn't look to my GA for support on anything. But what I found out was that I was paid significantly less than I should have been on the life policies I sold. Why? Because the GA I worked with put me on a beginner's compensation schedule even though I was doing all the work on advanced life insurance sales.

The day I realized that is the day that I decided to become an expert in the flow of money in the insurance business (from insurance company to IMO/FMO/GA to the insurance agent).

More full disclosure

As I've stated, I send educational newsletters out to over 300,000 life insurance licensed agents. I have also educated hundreds of advisors through in-person seminars over the years. I have also created dozens of marketing tools advisors can use to educate and communicate the value of life and annuity products to their clients.

My point is that there are a lot of insurance advisors who value what I do and who call me for help on case design, products, tax, estate, asset-protection planning, etc.

One question I didn't expect to receive years ago when I started what I do is now one of my more frequent questions. That question is what IMO do I recommend?

As you can tell from reading this chapter, I have significant disdain for IMO/FMOs and GAs. I've dealt with many of them over the years; and three years ago, I actually started looking for one I could work with.

I once tried to form a deal with an IMO to refer agents who wanted me to refer them to an IMO I thought would do a good job. It was a massive failure because the IMO I worked with was woefully understaffed and could not support the agents referred in a manner I wanted them supported.

However, in the fall of 2009, by pure accident, I ended up finding an IMO I could work with. I received a call from the president of the IMO who asked me if I would come speak at his IMO's annual agent convention.

I was quite taken back by the question. I asked the president if he had read my newsletters over the years and understood my attitude about IMOs (which is that I loathe them). He said he fully understood my disdain for IMOs, and that's why he wanted me to come speak. He asked me to speak on whatever topic I wanted and encouraged me to give my opinion on any subject I wanted to discuss including my thoughts about the industry in general and IMOs specifically.

To make a long story short, after doing several months of due diligence on the IMO, I ended up cutting a referral deal with the IMO. Now when an insurance agent asks me for a referral to an IMO, I have one I can confidently recommend. And, yes, I give full disclosure to the advisor that I will get paid if the advisor places business with the IMO.

Part of my deal with the IMO I work with is that, at any time advisors I recommend to the IMO desire, they can always call me to second guess the advice/recommendation given to them by a marketer at the IMO. Instead of being offended by this, the IMO I work with welcomes my second guessing as a way to help the marketers learn to do a better job and to make sure the agent is provided the very best product possible (and, by the way, I also learn from the marketers through my interaction with them which also helps me continue to improve what I do).

So that's the not-so-short explanation as to why I know so much about IMOs/FMOs/GAs, the compensation structure, and what really happens on a day-to-day basis within an IMO.

Questions to ask your agent to determine if he/she is a "bad advisor"

The following questions are simple and will let you know if your agent is working with an IMO that gives the agent a chance to provide you the best products for your individual situation.

1) Do you work with an IMO, FMO, or GA?

If the agent doesn't know the answer to this question, just hang up the phone or walk out of the meeting. An agent who doesn't know the answer to this question is clueless and should not be used.

If the agent says they work through a GA, know that the chances go down dramatically that he/she is working with a firm that can provide the best products.

2) Is the IMO you work with owned by an insurance company?

I'm not expecting your insurance advisor to know the answer to this even though he/she should. If it were me, that would be enough to show the agent the door; but if you'd like to give the agent a shot, allow him/her to call the IMO and ask (or you can call or e-mail me; and I'll look the IMO up on my list, and I'll tell you). If the answer is that the IMO is owned in part or in full by an insurance company, you are working with a bad advisor (or with pretty bad one who is working with an IMO that can't possibly provide access to the best products).

3) How long has the marketer(s) the agent works with been in the industry?

If the answer is less than two years, the chances that the marketer is not proficient in his/her trade (meaning the chances that the marketer understands the products he/she is recommending and why one is better for a particular client than another) is significant.

4) This is not a question so much to do with IMOs, but you need to make sure to ask your advisor if he/she is "captive."

If your agent is captive, he/she isn't even attempting to work through an independent channel; and, as such, it would be an accident or miracle if the agent provided you with best products for your particular situation. Even though the independent channel is flawed, you'll be infinitely better off working with an independent agent vs. a captive agent.