Former Allianz exec Bob MacDonald spills life insurance industry's 'dirty little secret'

Kevin Allen

Bob MacDonald has more than a few pointed opinions about life insurance. More than 40 years in the industry — including a turn as chairman and CEO of Allianz Life of North America — will do that to you.

MacDonald, who has earned a reputation as a business maverick, retired from Allianz in 2002. Now, he runs CTW Consulting LLC and closely monitors the life insurance industry. MacDonald blogs about life insurance at BobMacOnBusiness.com.

InsuranceQuotes.com spoke with MacDonald from his home in Key West, Fla., about why his faith in the industry has, to say the least, dwindled.

InsuranceQuotes.com: Let's start out with a broad question: What is the life insurance industry's "dirty little secret"?

Bob MacDonald: The dirty little secret they have is the way they keep track of their sales and the way they report their sales. It's been kind of an unsaid thing in the industry that the industry has not attracted any new money in a generation. Once you see all these reports of increases in annuity sales, a big piece of those numbers are just moving annuity assets from one company to another. And at the same time a company is moving assets from another company, they report it as new sales. There are other companies that are moving assets from that company and moving over there and they're reporting that as new sales, when, in fact, all it is is moved sales. It's not new sales.

So a company might report that they did $2.3 billion in new sales, but if you look into it, you would find that of that $2.3 billion, more than a billion of it and maybe even the majority of it was sales that came from annuities that had been on the books of other companies. Then if you look even deeper, you might see that that company lost about a billion dollars in sales that got moved to another company. And yet, when the numbers get reported and they're tracked in the industry, it might indicate that the industry is up and this company is up 20 percent. In reality, it's not new business. And that's the dirty little secret the industry keeps. They don't want to admit that a lot of those sales are not sales. They're just what we used to call "turning the business."

Bob MacDonald says the biggest mistake that consumers make concerning life insurance is failing to shop around for the best deal.

InsuranceQuotes.com: How does this affect the life insurance consumer?

MacDonald: It can affect the consumer in two ways.

One, most of the products have surrender charges, which usually will wear off over a period of time. But if that business gets moved to another company, it will often trigger these surrender charges, or fees, which reduce the value that the consumer receives in their product, and they start over again with all new fees. … If you've been with one company for four or five years and that business gets moved to another company, you incur the fees for moving it and you start over with new fees again. So that can substantially reduce the value the consumer receives.

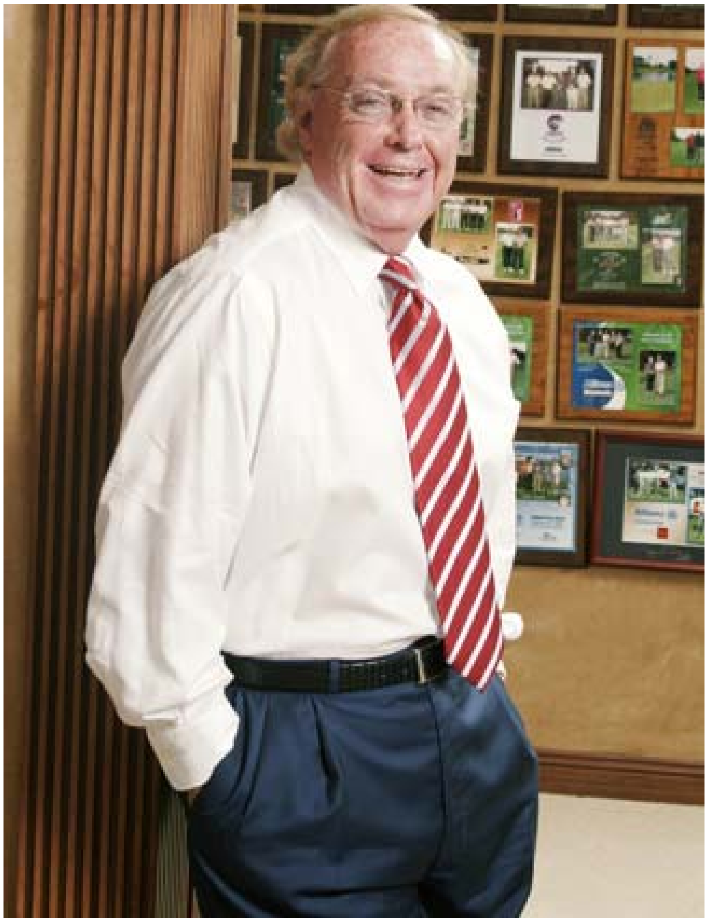
There's another factor where consumers can be hurt in the sense that most of the companies today are trying to move the business or sell the business based on commission levels. It's a constant battle to pay these higher commissions. Rather than selling the product based on value and benefit, they try to entice the agent with higher commissions. Well, when you pay those higher commissions, it means that you have less available to provide benefits for the consumer, so they can end up paying more for the product and getting less value … .

InsuranceQuotes.com: What are some of the common mistakes you see consumers make when it comes to buying life insurance?

MacDonald: I guess the mistake made today would be not shopping around and comparing prices. It used to be when I got into the business years and years ago, there was no value for the consumer to shop around, in reality, because all of the companies were selling the same product, and basically you were sold (coverage) at the same price.

For example, 30 or 40 years ago, as a consumer you were going to buy a $100,000 life insurance policy. If you were to go out and compare the prices, the lowest might be $1,000 a year and the highest might be $1,100 a year. So you might go out and shop, but you'd only save yourself $100. But what you didn't realize at the time was that because there was no real competition in the industry and everyone was selling the same product, it only cost the companies about $200 a year. When there is no competition and everyone is selling the same thing, there wasn't any value to shop around.

Today, it's evolved to where life insurance has become not a value proposition. Most people don't buy it for the value of the policy. It's become a commodity. Like a commodity, it's become very price-sensitive. There are significant differences in prices, but really the only thing that's being sold is the death benefit. There are no real values being sold. So today I think the mistake the consumer can make is to not aggressively shop around and compare prices.



Bob MacDonald retired as chairman and CEO of Allianz Life of North America in 2002.

InsuranceQuotes.com: During your time at Allianz Life of North America, what did you do to try to buck the system?

MacDonald: Well, it goes back much further than that. It goes back to when I was president of ITT Life in the 1980s. I felt that while the life insurance industry had been very successful and had done a very good job of meeting the needs of the consumer in the early part of the 20th century, the needs of the consumer had changed significantly. But the insurance company was still selling the products it wanted to sell, which was traditional whole life insurance.

When an industry gets comfortable and successful selling certain products, they want to keep selling them; they get an attitude that "We'll sell the products we want to sell and not the products consumers want to buy." A classic example is what happened in the automobile industry, where they were selling big, inefficient cars that didn't last very long and they kept selling them after the demand had changed.

In the insurance industry, they tried to continue to sell traditional whole life insurance, which was focused on benefits if you die. There's a fundamental shift that happened in the industry. Consumers began to become less concerned about the cost of dying young and more concerned about the cost of living too long. My argument was and what I attempted to do throughout my career was to say that you need to design products that reward people for living rather than dying. That was a fundamental change in how companies approached things.

Of course, that way of thinking was vociferously and aggressively dismissed by the industry because they wanted to sell the products they wanted to sell. In fact, I believe that the insurance industry has got significant challenges right now. I'm very bearish on the industry because they failed to recognize the change in the consumer needs — this fundamental change from being worried about what happens to my family if I die to being worried about what happens if I live.

Because they ignored that change and didn't respond to it, they've become irrelevant in the financial services industry for most consumers. They still have not recovered from that. Instead of sitting at the table, eating the main meal as they used to, they're now scrambling for crumbs with products that are still not in sync with the consumers.

InsuranceQuotes.com: Which companies out there are doing it right and addressing consumer demand?

MacDonald: I don't think anyone is doing it right. That's why I'm bearish on the industry. If the consumer is just concerned about what happens if they die, they can shop around and get a good deal. But the companies should turn this around and develop a product which enables people to accumulate value for retirement and — oh, by the way — if they die before they get retirement, then they get a lump-sum benefit of what they would have had for retirement.

Why do people go into 401(k)s and mutual funds? They're trying to build up value so that when they reach retirement they can maintain their standard of living. That's what people are concerned about. But the insurance companies are still locked in that conundrum of "We're going to help you when you die."