



CFO Conference

RECAP • June 5 - 7, 2018

Executive Summary

The CFO & Finance Managers Conference met June 5-7, 2018, in Charleston, South Carolina. The meeting began with a presentation from Steve Harvill, founder and president of Creative Ventures, who discussed the power of story and how to deliver compelling messages. Joel Wood, SVP of Government Affairs at The Council, also gave a presentation regarding the current state of political affairs pertaining to the insurance brokerage industry. The second day, The Council's CFO Working Group met and held a roundtable discussion amongst attendees. There were several presentations made and topics covered during the roundtable discussion that included revenue recognition, outsourcing, staffing, direct bill versus accrual reporting, and agency management systems. The meeting concluded on the third day with three concurrent presentations, that each ran twice to give attendees the opportunity to attend each session. These sessions included presentations by Tony O'Shea, Director of McLagan, who talked about compensation trends in the insurance brokerage space; Austin Madison, SVP of The Crichton Group, who gave an overview of health insurance captives; and Steve Anderson, President of The Anderson Network, who discussed digital innovation for agencies.

Day 1 – Leadership Training

Creative Ventures Presentation - The Power of Story

Steve Harvill, Founder & President of Creative Ventures

Highlights:

- Stories are one of the most important things to humans and to human history. Harvill described how those that tell the best stories “win.”
- The purpose of a company is to delight the end user. The tool to do that is story.
- Stories are best as a collaboration and the length of a story does not matter. If a story is important enough to be shared, then it is compelling.
- The Idea Journey – I get the idea (understand it), I value the idea, I can apply it in context
- Picture superiority effect – pictures and visual representations impact people more than sounds and voice communication. Most information comes to us visually and the best stories appear visually by using items or artifacts to connect the story visually.
- The pieces to a story – Crafting and Telling
 - Crafting – all great stories have a beginning, middle, and end. A well-crafted story should be simple and the storyteller should focus on the important ideas of the story and aim to include three main ideas vs having many. Simple = 3.
 - Telling a good story includes three pieces - comfort, connection, and influence.

- Your Story – What do I do (not your profession but what you actually do)? What value do I bring? How am I different?
- If you need to communicate information to someone, always ask the primary question, “What is the story?”
 - The group practiced diagramming different stories and then highlighting and demonstrating a particular idea or story of their own and delivering it to attendees.
 - Attendees discussed how elements of presentations had particular impact within their own positions, and then practiced polishing their presentation skills with each other and the group.

Political Update

Joel Wood, SVP of Government Affairs, The Council

- Potential for brokers to gain the same tax relief that insurers are getting from the tax bill
- Cadillac Tax delayed another two years until January 2022
- Exchange Premiums will be announced in the second week of October, but flood insurance programs will expire on July 31, in the midst of hurricane season.
- A major goal of The Council that would benefit the industry would be to get rid of the employer reporting requirements, or dramatically change them in order to benefit brokers.
- Cyber standards and GDPR have had a dramatic impact on the industry, especially overseas.

Day 2 – Roundtable Discussions

Topics Discussed included: revenue recognition, blockchain, employee ownership through stock options, other options for offering agency ownership to producers, producer compensation, financial performance, dashboarding and reporting, financial planning and analysis software, budgeting, staffing and outsourcing, perpetuation planning, agency management systems and other automation, direct bill, and changes to travel and entertainment expense policies to comply with tax reform legislation.

Revenue Recognition - IFRS 15 and ASC 606

- The group discussed how to interpret different revenue streams and the impact that the new revenue recognition pronouncement IFRS 15 and ASC 606 has had on their businesses.
- Slightly over 50 percent of the group reported GAAP accounting for their firms.
- Several members of the group are active in an industry working group hosted by the large public accounting firms and reported to the group some of the results of their meetings as follows:
 - Each firm seems to be handling their recognition slightly differently.
 - When looking at contingencies, many participants recommended posting an adjustment to retained earnings. The group discussed accruing all contingencies and setting up a reserve for cancellations, and reviewing quarterly as a good practice.

- The group discussed requirements to set up a cancellation reserve and how they were estimating their loss ratios. The group expressed the desire to create an industry standard that satisfies their firm's auditors and then companies can implement the industry standard.
- There were many questions on accounting for agency versus direct bill. The accountants focused on placements; when performance obligation was satisfied, as being the most important criteria for recognition and the most difficult part of the revenue recognition ruling to carry out in each firm.
- Some firms may want to consider setting up a separate accounting entity for recognition purposes of GAAP, and another for presentation purposes, to ensure all revenues are recorded, and reconcile to top line reporting.
- The largest barrier to implementation seemed to be getting all divisions within an agency to understand the reporting requirement and make the changes in their processes to be compliant with the ruling.
- Most attendees with employee benefits business (EB) noted that they are not changing the way they recognize revenue for benefits because benefits fall under the category of an extended service throughout the term of the policy, and they will continue to recognize income monthly.
- One member noted that after researching all of their lines of business and reviewing the performance obligations for each, they are recognizing 60 percent of benefits revenue up front, and the rest they will recognize monthly. For Property/Casualty lines (P/C) they have determined 90 percent of their contract revenue will be recognized up front with the remaining amount recognized monthly until the end of the term of the contract.
 - The EB portion of their business is broken down further by different accruals for workers' compensation plans based on the number of lives in the plan, i.e., 0 – 50 lives, 50-100 lives, and 100+ lives, that each have different rates of accrual based on the amounts of ongoing service obligation they determined the contracts require.
- Many attendees with P/C revenues noted they would likely recognize 100 percent of their contract revenues upfront because it is difficult to determine term of performance obligation. Overall, this raises concerns about the caps that will be highlighted in tax returns when these changes were implemented in their agencies.
- Some firms are posting their revenue recognition compliance statement (ASC 606 compliance) on their firm's website.
- The group decided to create a revenue recognition subcommittee that working group members signed up for to continue discussion and exchange of ideas on implementation in their firms. The first meeting will be in October after the working group meets again on September 20.

Travel and Entertainment Policies

- The group discussed the changes in tax legislation regarding the deductibility of travel and entertainment (T/E) expenses for agencies.

- In general, if a firm incurs expenses for entertainment, the firm can no longer claim a 50 percent tax deduction. These activities include things like golf outings, sporting events, concerts, hunting and fishing trips, and country club dues.
- There has been no change to legislation regarding “travel,” i.e., transportation expenses.
- Many firms are still interpreting whether eliminating the deduction for entertainment expenses applies to business meals. Without further guidance from Congress or the Treasury Department, many participants noted that it might be best to stay on the safe side and consider meals with business associates, clients, customers, prospects, or anyone other than employees as nondeductible.
- Meals provided for team members at the convenience of the employer, as opposed to with current or prospective clients, used to be 100% deductible. Starting in 2018, employers will only be able to deduct 50 percent of what they spend on employee meals such as catered lunches, company cafeterias, meals for company meetings, or food provided to enable an employee to work overtime. This may change to 0 percent deductibility in 2025. (Based on actual facts of expense) Many firms no longer reimburse employees for meals they have together.
- Several firms do not pay any travel and entertainment expenses. They are paid by the producer. Others pay 80 percent of the expenses and the producer will pay 20 percent.
- Some firms are reporting expenses, such as club dues, that are paid for by the firm, as taxable income to the employee.
- Most attendees had changed, or were changing the items that they will reimburse or otherwise cover for T/E.
- There are readily available resources online to help with interpretation of the tax reforms related to T/E.

Blockchain

- The group discussed industry use of blockchain in the claims process and in contracts via smart contract.
- Most participants’ firms were looking at uses for blockchain/cyber currency for the future.
- Several industry consortiums have formed to explore potential use cases, including the RiskBlock Alliance, made up of brokers, carriers and reinsurers.
- The Council just completed a series of blockchain webinars, and will continue to present information on the topic through its newsletters and online webinar series.

Day 3 – Concurrent Sessions

Health Insurance Captive Overview

Austin Madison, SVP, The Crichton Group

- Employer Sponsored Health Insurance - Top 3 drivers of health care spending:
 1. Claims – Make up majority of spending

2. Prescription drug cost - 5 years ago made up 10 percent. Now 20-25 percent with future projections up to 40-50 percent.
 3. Administrative Spending
- Health Insurance Cost vs. Healthcare Cost
 1. Working on reducing health insurance trend (inflation or health insurance cost.) If nothing changes, costs are forecast to increase 9.5 percent each year.
 - Madison described how a captive, if set up correctly, may help reduce the trend of health insurance costs. He said when a firm is self-insured, anything to improve loss ratios will reduce claims, which will ultimately improve profits.
 - Madison reported that there has been a huge migration in middle market firms towards self-insured. He said the reason for the change is that firm performance is much more positive when self-insured.
 - Fully insured – The average expense increase over 10-year period, year over year, was 10 percent
 - Self-insured – The average expense increase over 10-year period, year over year was 3.5 percent

Digital Innovation for Agencies

Steve Anderson, President, The Anderson Group, and creator of The Digital Broker Podcast

Anderson noted to the group that because of the constant changing nature of risk, he believes technology is a time accelerant. He said firms should be thinking of risk as an investment, there is a return on innovating but it is risky.

- Anderson discussed his recommendation that technology divisions should be in the revenue part of the P/L, not on the expense side because they are on the solutions side of business and assist in finding opportunities to grow, streamline and protect revenue.
- Other notes from the discussion included:
 - Digital acceleration is exponentially increasing. Because of this, broadband access and speed is increasingly important for agency clients. What information might they want and how can broadband provide greater value?
 - 10,000 Experiment Rule: Through greater amounts of experimenting, you increase the chance of success. One way to do this is by creating an innovation culture to nurture unorthodox technology thinking and its application. It can be cultivated in many ways – competitions, gamification, DIY communities, microwork, and crowd ideation.
- Next steps to take for agencies: understand precisely how automation is affecting, both positively and negatively, an agency's business culture. He notes that leaders should cultivate curiosity within an agency for new technology and quantify the return on technology risk.

Compensations Trends

Tony O'Shea Director of McLagan

- O'Shea described his background in compensation and other types of services such as performance benchmarking and strategic consulting.
- He noted that The Council has worked with McLagan since 2007 to provide high-quality industry compensation information that is a broad representation from all sizes of agencies.
- Survey results show what is a reasonable compensation for agency employees and producers, validated vs. non-validated, and what are normal benchmarks by company size, by ownership structure, location and P/C and, or EB.
- By considering many variables to recommend a reasonable compensation for a person in the business, the survey allows companies to see where they stand and whether or not they are paying below the norm or above.
- O'Shea reported that the median compensation changes from 2016 to 2017 was an increase of 3 percent but there is a range of changes over the last year. He noted typical EB compensation had surpassed P/C compensation over the last few years.
- He said most agencies are looking to increase their staff, with technology position recruiting growing the fastest.
- For more information on the survey and how Council members can participate and receive the results, please visit The Council website.