NINTH ANNUAL
JAMES A. AND LINDA R. MITCHELL
FORUM ON ETHICAL LEADERSHIP IN
FINANCIAL SERVICES

2009 PERSPECTIVES ON ETHICAL LEADERSHIP

THE AMERICAN COLLEGE

FORUM ON ETHICAL LEADERSHIP

The ninth annual James A. and Linda R. Mitchell/The American College Forum on Ethical Leadership took place January 17, 2009 in Palm Beach, Florida. This year's event featured deliberation on the sensitive and much debated topic of compensation and other related issues in the financial services industry by executives from this field and business ethicists from academe.

THE EXECUTIVES

Jeff Bosco, Chief Operating Officer, American Family Life Insurance Company, Madison, Wisconsin

Peter Golato, Senior Vice President, Individual Protection Business Head, Nationwide Financial Services, Columbus, Ohio

Richard Hemmings, President and Chief Executive Officer, Fidelity Life Association, Oak Brook, Illinois

James Mitchell, Chairman and Chief Executive Officer (Retired), IDS Life Insurance Company, Longboat Key, Florida (Host)

Scott Perry, President and Chief Executive Officer, Bankers Life and Casualty Company, Chicago, Illinois

Lisa Weber, President, Individual Business, MetLife, New York, New York

THE ETHICISTS

Brad Agle, Associate Professor, Joseph Katz Graduate School of Business Administration, University of Pittsburgh, Pittsburgh, Pennsylvania

Ronald Duska, Charles Lamont Post Chair of Ethics and the Professions and Director of The Center for Ethics in Financial Services, The American College, Bryn Mawr, Pennsylvania (Host)

Marianne Jennings, Professor of Legal and Ethical Studies in Business, Department of Management, W.P. Carey School of Business, Arizona State University, Tempe, Arizona

William Laufer, Julian Aresty Professor of Legal Studies and Business Ethics, Sociology, and Criminology, The Wharton School, University of Pennsylvania, Philadelphia, Pennsylvania

Richard Nielsen, Professor, Organizational Studies Department, Carroll School of Management, Boston College, Chestnut Hill, Massachusetts

Jeffrey Seglin, Associate Professor, Emerson College, *The New York Times* syndicated columnist of "The Right Thing", Boston, Massachusetts

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EXECUTIVE SUMMARY

On January 17, 2009 a group of six executives ("practitioners") and six academic ethicists ("philosophers") gathered in Palm Beach, Florida to participate in the ninth annual James A. and Linda R. Mitchell/The American College Forum on Ethical Leadership in Financial Services.

The purpose of this annual event, established in 2001 by Jim and Linda Mitchell, is two-fold:

- To provide executives with an opportunity to reflect on ethical issues they confront on a regular basis with questions posed to them by academics engaged in business ethics education.
- To afford academics the opportunity to engage in discussion about these issues with top-level executives so they can bring that experience back to the classrooms.

ETHICAL ISSUES IN COMPENSATION

Following the introduction of the participants and discussion of their goals for the day, the conversation turned to ethical issues involving compensation in the financial services industry. The participants discussed a case study that raised ethical questions about compensation models at the agent, managerial, and executive level.

Ron and Brenda Duska with Linda and Jim Mitchell welcome participants Friday night.

The participants began by noting that certain characteristics of the financial services industry, and particularly of the insurance industry, influence the ways in which financial services professionals are compensated. The high cost of training and developing new recruits encourages managers to pay young agents a portion of each sale, rather than placing them entirely on a salary. Additionally, since life insurance is generally a product that needs to be sold, companies need to motivate their sales force with commissions paid immediately upon the sale of the policy.

Some participants wondered whether another compensation model would better align the interests of the consumer, the agent, and the company. They asked why agents and managers were unwilling to disclose specific information concerning agent compensation. There was discussion about how much disclosure was necessary and the form this disclosure should take in order for it to be meaningful to the client. Participants questioned whether detailed information about compensation affected a client's decision regarding which agent to work with and what product to purchase.

The participants considered whether the current compensation model was an obstacle to serving the middle market of financial product consumers. Some of the executives expressed concern that a large segment of the population did not have sufficient life insurance. The participants considered the reasons why people fail to purchase needed life insurance. It was suggested by some participants that the public's increasing distrust of the financial services industry could contribute to a reluctance to invest in either life insurance or comprehensive financial planning.

Gigi Golato discusses the venue with Dick and Jane Hemmings.

The participants also looked at issues raised by models of executive compensation. The question arose whether executive compensation was driven by the need to recruit and maintain necessary talent in a competitive marketplace. Other participants thought that was unlikely since there were few opportunities for executives to be compensated more than as the leader of a publicly held corporation. Some participants pointed out that hedge funds and private equity are the competitors for the top CEO talent.

The possibility of tying executive compensation more tightly to performance and the best ways to incent long-term corporate performance rather than short-term stock appreciation were discussed. The participants expected that public outrage at the decline in the stock market and the current economic situation would have a significant impact on executive compensation models in the near future.

EXECUTIVES' ETHICAL ISSUES

In this segment of the Forum, the executives each presented an ethical situation or problem that they had encountered in their careers.

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The first issue concerned an "up and comer" who was forced to decide whether he should fully disclose to the management team the true extent of the problems plaguing a product line he had recently been assigned to take over. This case raised important questions about how ethical leaders can create a culture in which their employees are encouraged and rewarded for being honest and disclosing even "brutal facts" to management.

The second issue raised the question of what an ethical leader should do when confronted with a system or process that is unfair or unethical. Specifically, this question dealt with methods for responding to solicitations for political donations on behalf of elected insurance commissioners. This practice raises ethical concerns since companies are required to gain approval of state insurance departments in order to do business in those states.

Bill and Dagna Laufer join Dick Hemmings and Linda Mitchell at the opening dinner.

The third issue concerned how far one should go in pursuing a course of action that one, as an ethical leader, firmly believes is right even though one is not getting much support for it. The particular concern was over a bill, up for approval by a state legislature, which would unfairly stigmatize life insurance agents as engaging in predatory practices against certain vulnerable groups.

The fourth issue investigated ethical issues raised by defined benefit pension funds, which are of increasing importance to many working Americans given their doubts and insecurities over retirement. Ethical issues emerge regarding how these plans should be funded, especially in times of economic downturn.

The final issue focused on the ethical worth of stranger-owned life insurance. While it seems important to support the insured's right to dispose of their property, stranger-owned life insurance seems to violate the crucial component of "insurable interest", which differentiates life insurance from other investment products and justifies its tax benefits.

ETHICISTS' QUESTIONS

In this portion of the program, each of the academics posed a question or raised an issue to be discussed.

The first question dealt with what obligations, if any, an ethical leader has to oppose an unethical or unjust procedure or practice. This specific discussion examined the practice of many corporations settling frivolous or unjust lawsuits to avoid the uncertainty and negative publicity of a trial.

The second issue concerned the lack of systemic approaches in dealing with ethical crises and scandals. Would it make sense to have something like a "National Business Ethics Safety Board"? This institution would be similar to the National Transportation Safety Board and could allow evidence to be collected about the nature and causes of ethical breakdowns. This approach would perhaps allow for the development of rigorous strategies of prevention.

Jane Hemmings, Ron Duska, and Brad Agle smile for the camera.

The third issue questioned whether it was appropriate to attribute the current economic crisis and unethical behaviors to failure of compliance, governance, and culture. Is it possible that there is just a baseline of deviance in every society, and that some people seek to exploit commercial exchanges to their advantage?

A fourth ethicist asked each of the executives to talk about one practice which, while not illegal, represents something they would not want their customers or the public to know. A follow-up question was why they would not be willing to disclose this practice.

The fifth issue concerned what role, if any, trade or industry associations could play in developing and implementing more rigorous ethical standards. Given that the insurance industry is particularly well suited to analyze and assess risk, wouldn't insurance executives be uniquely positioned to take the lead?

The final issue focused on the importance of promoting the message that "ethical behavior matters" throughout the organization. While frequently we hear that the "tone at the top" is the most important, how do we make sure that this imperative is translated into specific directives to front-line employees?

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"Everyone is so busy these days that it's tough to step back and take time for reflection."

Jim Mitchell

INTRODUCTION AND GOALS FOR THE DAY

The ninth annual James A. and Linda R. Mitchell Forum on Ethical Leadership in Financial Services began with host Jim Mitchell welcoming the participants and asking them to address two questions:

- What does ethics mean to you in your organization?
- How do you hope to benefit from today's discussion?

THE PRACTITIONERS

Jim Mitchell began by noting that it is only through building an ethical corporate culture that it is possible to achieve lasting success in business. He hoped that the day's discussion would provide an opportunity for academics and practitioners to reflect on the "big picture" issues. "Everyone is so busy these days that it's tough to step back and take time for reflection. I think it's hard to do the right thing if you don't have a lot of clarity regarding your mission and values." He hoped the academics would leave the gathering "with the impression that most people in business are basically good people trying to do the right thing." He also hoped that the academics would be able to "walk away with some anecdotes to share that reveal the commitment of most business people to act in accordance with high ethical principles."

Peter Golato noted that until he had the opportunity to run a business on a day-to-day basis, he had no idea how many times he would be called upon to make decisions that sacrificed near-term results in order to act ethically and protect the company in the long term. "Trust me; you do not win popularity contests with decisions like this, especially with a sales organization. But I know that the people I worked with knew, intuitively, that it was the right thing to do. I think it takes courage to make those kinds of decisions and to be able to walk away from things that you know could be potentially hazardous going down the road." He was looking forward to this ethics discussion and believed that today would be "more of a learning and sharing experience."

Scott Perry said that he knew ethics was of the utmost importance to any successful organization. He was reminded of this lesson when the parent company of his subsidiary went through bankruptcy. "It was quite a challenge, and I viewed ethics as critical. We came through it because the business was a good business. It was good for the consumers and good for the people who worked there." Perry has also seen the need for ethics to grow and become

an industry-wide imperative. "If we aren't vigilant we won't be in business, pretty plain and simple. I know that in my case for the last six years we have really focused on not so much driving ethics through the organization, but changing the culture to make ethics the cornerstone of behavior in every aspect of the business." Perry looked forward not only to learning from the experience of other executives, but also to having time for critical reflection. "You always wonder how ethical you really are. Maybe I will gain some self-awareness. Maybe I will evaluate my own decisions and behavior differently based on this discussion."

Dick Hemmings said he looked forward to learning from all of the participants and agreed that the Forum served as an excellent opportunity for self-reflection. "I'm nearing the end of my career, and it's time for me to look and reflect on where I have been and what lies ahead. We would all like to come into life and leave the world a better place than we have found it. Unfortunately, I don't think we can say that today." Hemmings raised concerns about the increasing focus on the compliance mentality. "I don't think that you can legislate morality. You are who you are, and I happen to believe that people are born with a moral compass. You can't leave that moral compass at the door when you go into the office. We know what the right thing to do is. We just ignore it."

Gigi and Peter Golato enjoy the evening.

Jeff Bosco said that he had recently completed the requirements for a Master of Science in Management (MSM) from The American College. During the ethics course, he had a chance to think about what is and what is not an ethical dilemma. In an ethical dilemma, there are two competing ethical values at stake. However, those conflicts that masquerade as dilemmas result from temptations. You know what you should do, what is ethically required of you in this case, but you do not do it on account of self-interest. "You would like to think you are the most ethical guy in the entire world. You're dealing with all the compliance officers and have 40 attorneys on staff. But then you realize that maybe that's not what we are talking about here."

Lisa Weber looked forward to the discussion since it would provide her with the opportunity "to think out loud and share ideas with people." She agreed with Dick Hemmings that we all possess a moral compass, but added that it is also necessary

to continue learning. "You can learn empathy. It is an important skill in life and when you practice it, you'll be surprised how it really becomes part of who you are." She has been struck by the increasingly intense corporate focus on profit maximization and the bottom line with little consideration for sustainability. The current environment increases the imperative for ethical leadership.

THE PHILOSOPHERS

Jeff Seglin related a story from his days at *Inc.*, a magazine where he served as an executive editor. "We would get letters saying things like, 'How dare you champion these business people? They're dishonest.' Then we would get a whole series of other letters that said, 'What are you talking about? This is how business is done. They are not doing anything wrong.' Therefore, it just became fascinating to me how people drew that line for themselves. Because there is not always a clear right answer; it is a choice between multiple right answers." For the day, he hoped "to get a sense both from the practitioners and from the academics about where and how they draw that line themselves."

Bill Laufer thought that while he and his colleagues spent a good deal of time trying to figure out how to bring ethics into the curriculum in meaningful ways, he is concerned that both business schools and corporations become satisfied with the mere appearance of ethics. "In complex business organizations, you are able to appear ethical if you use the right sort of moral imagery and invest in compliance and all the trappings. But I'm not too sure we have figured out how to actually *be* ethical in the workplace, or even if there is a genuine commitment to it." He hoped today's proceedings would move the discussion between the academics and practitioners "beyond the moral rhetoric of the importance of honesty and integrity in the workplace and figure out how we can actually have an impact in the organization."

Brad Agle said he was interested in business since, more than any other human institution, it has contributed a great deal in terms of human progress. "I think business has an amazing capacity to create a better world, and I think that there is plenty of evidence for that." But he expressed frustration that despite the decades of effort by business ethicists and concerned practitioners, there seemed to be no end to the scandals and wreckage caused by unethical business people. "I look at it and say, 'Have we done any good?' You just keep seeing these scandals getting bigger."

Marianne Jennings, like Brad Agle, was fascinated by the working of business and the market. "When you consider what business does for society, and the risk that business people take, you realize that capitalism is a wonderful thing. But a part of capitalism is trust, and a part of trust is ethics. We are at a turning point here where we really have to start thinking about it more deeply than we have." Jennings believed that it was necessary to turn our attention to the psychological components that affect decision making more than we have done in the past. "Psychology needs to be brought in since you can't counteract what is going on without knowing the factors that cause it in the first place." She is looking forward to what she will be able to bring back to her classroom. "My excitement over being here is for the stories. Stories are how students learn. We can't really evaluate our ethics until we see it in application. When I go back to my students, I can say that I was talking to a business person and here is an example he or she gave me. Then they know it is real. Then they can put themselves in that situation."

Richard Nielsen discussed how his experience with European companies revealed a different approach to corporate ethics than what is found in the United States. "In America when you talk about business ethics, people primarily regard it as an individual phenomenon. They don't like to talk about systems or criticize systems. Europeans also believe in capitalism—that you have to create wealth and capitalism is the best way to do it. But European companies are more willing to look at the systematic causes." He believes that systemic change is needed to repair and improve our economic system. "The only way we are going to make things better is from the ground up. It is the people who are going to restructure and improve the system."

Ron Duska remarked that he thinks ideas and words have consequences, even though sometimes these consequences are not immediately evident, and therefore talk is important. "I remember one of my colleagues writing the first book about 'stakeholder theory'. The editors kept trying to replace the word 'stakeholder' with the word 'shareholder'. Now 'stakeholder theory' has become common parlance. "You can't go anywhere without hearing the word 'stakeholder'. If you start talking that way and thinking that way then possibly the actions will start following the thinking." He thanked everyone for attending the Forum. "I'm delighted you are here to share your thoughts with us today. This has always been a rewarding experience, and I enjoy throwing ideas around with good people."

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CASE STUDY: COMPENSATION ISSUES IN THE FINANCIAL SERVICES INDUSTRY

A CASE STUDY

Jim and **Tom** are having a conversation about compensation arrangements in the financial services industry.

Jim is a financial advisor in his second year in the business who works for commission (although he can take a draw from his future commissions if he wishes). His commissions are "front-loaded", which means that the commission is paid to him primarily out of the very first premium/payment made by his clients toward their new financial product. Unsure of his future success in the financial services industry, Jim works a second job most evenings and weekends as a contract interior painter. It is good money, and the older financial advisors generously hire him every chance they can, but he is becoming increasingly frustrated with this arrangement and is seriously considering leaving the financial services business.

Tom is a Regional Vice President at the same company, where he has progressed through the ranks from beginning as a life insurance agent 30 years ago. He receives a base salary, but most of his compensation depends on the sales performance of his region and the results of an "employee survey". Tom is increasingly frustrated over the form of his compensation. He feels as though he has "no control" over his salary, which only increases 3 or 4% per year regardless of how successful his region is. His bonus is mostly dependent on his ability to motivate his advisors, but he has no real control over them. Further, his bonus is in part dependent on the "mood" of his employees when they respond to the annual employee survey. He finds himself wishing he had stayed in sales. At least then he could be "his own boss" and be compensated on the basis of his own efforts. Although he is committed to the company, he regrets signing on to the "manager trainee" program 25 years ago. He had a young family and his wife stayed home with the kids, so it seemed like the safest step at the time. Now, as he watches the people in his training class who were successful in the field begin to retire on the sale of their book of business, he is convinced he did not choose well.

Normally, Tom would not be meeting "one-on-one" with a less-than-successful second year advisor, but Jim's supervisor, knowing Jim is thinking

of leaving the business, asked Tom to talk with him. Tom is not feeling very inspired about his own situation at this point, but it is his job to try to help motivate the young advisors, and he has agreed to meet with Jim. After some small talk, the discussion turns to a sore point for both, forms of compensation.

THE DISCUSSION

Jim: This whole financial services industry "bailout" thing is getting out of control. People are getting really worked up about how much money the CEOs of those companies made. Did you see that Congress is going to look at executive compensation again?

Tom: People think these guys shouldn't be rewarded for running a company into the ground. I can't say that I blame them.

Jim: I don't know many other jobs where "pay for performance" means "no matter how badly you perform, you still get paid!"

Tom: Well, a good number of those CEOs did lose their jobs. And most of the ones who still do have jobs will be getting no bonuses this year.

Jim: But it's so different from my situation. I'm out there six days a week, and I only get paid when I make a sale, which is no small feat these days.

Tom: Believe me, I remember all that. It's rough in the beginning. No one can deny that the first couple of years in this business can be tough going.

Jim: You have no idea. It's always been hard to get people to commit their hard-earned money for an intangible product like ours, but it's gotten worse with this economy and the financial services crisis. If I can get people to meet with me at all, I need to convince them that the company is not going to file for bankruptcy next week. And if I can clear that hurdle, I need to convince them that I am not like one of those guys selling indexed annuities that they saw on "Dateline" a couple of months ago. It's like they tar us all with the same brush. So I need to sell them on the industry, the company, and on myself and my character before I can even begin to talk about the product.

Tom: Well, you know, I actually do understand. I got into this business in the 1970s. This country was in a major recession with over 7% unemployment and inflation was raging at about 14% per year. I just put my head down and tried to be oblivious to all of that. I kept making my calls and sharpening my sales skills, and eventually I

started to be successful. I was a young kid, just out of college, and I married Liz a week before I started here, so I didn't feel like I had any choice but to succeed. I hope that's what you will decide to do. I agree with you, though, that the compensation model isn't the best.

Jim: It's not only what people think, although that's trouble enough these days. But, you know, I am beginning to think it causes real ethical problems for some of the people here in the office. I mean, it's hard to resist selling whatever product you know is going to pay you more. How do you walk away from that kind of money? I think it just makes it harder to do right by your clients.

Tom: I get it, and once you've sold them all you're going to sell, what do you do? There is no incentive to stick around and try to do right by these clients and maintain a real relationship with them. If you quit the business, we've got a bunch of clients who can't get their advisor on the phone. And if you're wildly successful, you're too busy to deal with the "little people" who bought from you when you were starting out, so we reassign them to a junior advisor they don't know.

Jim: And that's why I want to get out, Tom. This business is not for me. I mean, you're fine. You work hard every day, I know, but at least you know you'll get a paycheck for your efforts.

Tom: Think about why you got into this business, Jim, really think about it. In addition to helping people achieve their financial objectives, you get to be your own boss. You're in charge, and you can do as well financially as you want. Some days that feels like incredible freedom and others like an unbearable burden. Your success is not dependent on anyone else. If you want to go fishing all weekend, go for it! If you want to stay in the office all weekend and make those prospecting calls, go for it! It's all up to you; it's all in your hands.

I know it's not a perfect system but if you think about it, the company is in the same situation. You invest all of your time in a client and if you don't make the sale, you're out of luck. We invest our time and money into training a new advisor, and if in a year, he decides he's not up for this business, we're out of luck. You take a risk on your prospects, and we take a risk on you. If it works, we both win, and if it doesn't, we both lose.

Jim: I never really thought about it like that before. Do you think it'll ever change?

Tom: The time is coming where advisors are going to have to fess up about how they get paid. Every night on the financial shows and even the nightly news, people are hearing that they need to ask their advisor about their compensation. With all of the emphasis on transparency, disclosure of compensation is bound to come. Then, if people really don't want to work with commission-based advisors, the compensation system will change.

Jim: I hope that change comes soon, for my sake. But I would like to talk to you about the managerial training program. I think I would be really good at it! I have a knack for motivating people, that's what my coach said when I was playing ball in high school. Did you know I was the captain? Anyway, I think that I've got real leadership skills. And I can tell you that I would love to stay in the business if I could know that I would get a check every week.

Tom: We can certainly talk about the program, Jim, but I'm not sure you understand the way that the compensation system works. You do get a base salary, but most of your compensation is designed to come from your bonus, and your bonus depends mostly on how your sales team performs. And their performance varies for all sorts of reasons. As a manager, all you can do is coach people; you can't make them sell anything. Look at what's going on in the industry now; some of the most successful advisors are jumping ship to go to another company where the compensation package is richer for them. The point is this, Jim, they can walk out the door; they've got their clients and their reputation. In that sense, they are protected from this economy. But the managers, we're tied to the company; we rise and fall with its fortunes.

Jim: I didn't think of that. So your job is risky as well, isn't it?

Tom: This business can be risky all the way around. You just need to decide where to bet. As a sales agent, you bet on yourself and your ability to produce. As a manager, you bet on your ability to motivate people and to coach them to be successful. You sell to clients, I sell to you, and the big guy upstairs sells to the Board of Directors and to the Street. We're all selling something!

Jim: You know, it's funny you should say that. I was watching TV last night, and one of the pundits was saying that it's hard being on the compensation committee of a major public company right now.

Tom: I'm not sure I agree with that. As far as I can see, all those directors do is hang out in Boca or Palm Beach and decide how much to pay all of their friends. I say, "Sign me up for that!"

Jim: The guy on TV, I think it was on Bloomberg, he was saying that they're watching these guys like hawks now, particularly in financial services. Everybody is on top of them, the shareholders, the regulators, and now Congress. But the guy was saying that, even with all the scrutiny, if the compensation committee isn't willing to pay the CEO the big bucks, they can't compete for the top candidates. It's really important that financial services companies have good CEOs.

Tom: I do know that to recruit a CEO from another company, you're competing for a relatively small group of experienced senior executives. Now they need to worry about competing with the hedge funds, too. These days the hedge funds are paying the big bucks for people to run the companies they own, and they're not regulated at all.

Jim: When you think about what these CEOs are paid, it's ridiculous! There is no way you could spend all that money in your lifetime. At some point, it is just a means of keeping score. But what I want to know is how I can get into that pool of candidates?

Tom: The lottery, I think. If a Board is not going to promote from within, it doesn't seem like they've got many options except to pay the big bucks.

Jim: That's what the guy on Bloomberg was saying. If you go outside of the company to get someone, you've got to deal with the fact that they've got options that have not been vested and an expensive retirement package. It seems to me that the smartest thing to do is to let the shareholders decide. They're the owners of the company anyway.

Tom: I'm not sure that's realistic. These compensation committee guys are pretty savvy about this sort of thing. They have to be, since they have a fiduciary responsibility to the shareholders. When I think about our company, I don't think I want a bunch of investors who don't know anything about the business or the industry making strategic decisions we all need to live with. That being said, I do think it would be smart to move away from so much emphasis on stock options. All the focus on the stock price plays into the "short termism" mentality.

We've gotten pretty far afield from our original conversation, Jim. I think it is safe to say that none of the compensation systems are perfect. Each of them has its own problems.

Jim: I get what you're saying. I guess no one has it all. You just need to figure out where to place your bet. I guess I want to bet on myself and see where I end up.

Tom: I think that is a wise choice.

FACTS

1. In the 2007 Report on Agent Production and Retention, LIMRA reported a small increase in the four-year retention rate from 15% in 2006 to 16% in 2007. In other words, in the average agency-building company, for every 100 agents recruited today, only 16 will remain after four years. 70% of the agents who were terminated in 2007 were separated from the company within their first two years on the job. The 16% four-year retention rate in 2007 actually represents a 5% improvement from 2003. Of the agents who decided to leave their original company, 51% left during or after their 4th year with the company.[1]

2. CEO compensation has soared since 1996. The median total compensation for a large company CEO increased from $3.2 million in 1996 to $6.8 million in 2005, fueled largely by increased use of stock options during the dot-com era. After the dot-com bubble burst, long-term incentives became more performance-based, but their level did not decline much initially.[2]

3. However, there has been a "sea change" in executive pay in the last couple of years. A recent study shows that among Fortune 1000 companies there has been a significant drop in pay in 2007, as corporate performance declined. The CEOs of 50 large U.S. companies (with median revenue of $66.2 billion) took a 15.8% cut in total compensation.[3]

4. In a poll designed by *The Los Angeles Times/Bloomberg*, almost 80% of Americans believe that CEOs are overpaid. This response was constant among different political parties and income.

5. It is generally agreed that previous attempts on the part of Congress to legislate compensation standards have been less than successful. "In 1984, Congress passed a law eliminating the tax deductibility of golden parachutes that exceeded three times base salary . . . golden parachutes worth 2.99 times base salary proliferated,

where before there were none at all." In addition, according to some people, the ire expressed by the public regarding the prevalence of stock options can be laid at the doors of the Congress as well. "In 1993, Congress said that only $1 million of an executive's salary would be tax deductible. So companies began paying their CEOs massive amounts in other forms, like stock options and deferred compensation."[4]

6. In 2008, investors at more than 100 companies (including Coca-Cola, IBM, General Motors, Exxon Mobil, Citigroup, Anheuser-Busch, General Electric, and Wal-Mart) have asked for a "say on pay".[5]

DISCUSSION QUESTIONS

1. "Commissions paid to agents for the sale of life insurance products to consumers comprise a large percentage of the first year premium that consumers pay for these products. As the marketplace for financial assets becomes ever-more information perfect, a marketplace pressure to allow agents and their clients to negotiate commissions has developed. This pressure has emerged despite the regulatory environment . . . discouraging the "rebating" of commissions to consumers and the concerns . . . (that) two similarly situated clients who get different values from their policies based solely on negotiated commissions?"[6] Do you believe negotiated commissions pose an ethical problem? Why or why not? Do you believe that, given the increasing transparency of compensation methods, negotiated commissions are inevitable?

2. Given the asymmetry in information between the financial advisor and his or her client regarding both the workings of financial markets and the specifics of financial products, what information do you believe the advisor has a moral obligation to disclose to his or her client? Is the advisor obliged to disclose the exact amount or percentage of any commission that they receive upon the sale of a particular product? Does the advisor have an obligation to disclose in what manner this commission is paid? What does "meaningful disclosure" regarding compensation require for a commission-based practitioner?

3. Some scholars have referred to a shift in the power dynamic between financial advisors and their clients on account of the "disintermediation" occasioned by the emergence and popularity of online financial product providers. Others believe that this shift is overstated since "the majority of financial services consumers do not have the access or inclination to

master the information necessary to match that of a sales representative."[7] How do you think the emergence of online financial product providers will affect the financial services industry? Do you have any concerns regarding their increasing popularity?

4. Some empirical studies suggest, "Neither commission level nor fee-for-service level influences the likelihood of product recommendations (made by insurance agents)."[8] Contrary to that study, it is ordinarily assumed that a culture with an incentive system, which rewards results, will cause self-interested and unsuitable recommendations. Are you surprised by the results of these studies? Do you agree or disagree with the conclusions of the authors? Why or why not?

5. Charles Elson, a compensation expert at the University of Delaware, offers the following critique of the current system of executive pay, "We're paying executives like successful entrepreneurs, without asking them to take entrepreneurial risks."[9] Do you agree?

6. Robert Reich argues in a *Wall Street Journal* editorial that changes in the economic environment have necessitated increasing executive compensation, "The CEO of a big corporation 40 years ago was mostly a bureaucrat in charge of a large, high volume production system whose rules were standardized and whose competitors were docile...The CEO of a modern company is in a different situation". Do you agree or disagree with this statement? Do you think that the changing environment explains and/or justifies the increase in executive compensation?

7. Do you believe that boards of directors and their compensation committees are independent regarding the determination of CEO compensation, or are they unduly influenced by the CEO?

8. What role do you believe the shareholders should have with respect to executive compensation? What role do you believe Congress should play regarding various "say on pay" initiatives?

9. In 2002, the United Kingdom passed a law that gave shareholders an "up or down" vote on executive pay packages. The vote is only advisory, but it could prove a powerful incentive for the board to avoid what is effectively a vote of no confidence. Do you think that something like this strategy would be appropriate and/or desirable for American companies?

10. How do you see CEO compensation evolving in the next couple of years? Do you think that we will continue to see the type of increases we've seen in the last decade? Why or why not? How do you think the various components of compensation—salary, bonus, stock options, restricted stock, etc.—will change?

THE DISCUSSION

STRUCTURAL LIMITATIONS OF THE SYSTEM

Ron Duska opened the discussion by asking, "Is there a better way to set up the compensation structure in the life insurance industry than the current commission system?" He added that some people have raised concerns regarding the failure of most agents to disclose the amount of the commission they receive or how that payment is distributed.

The group gathers for the evening.

Peter Golato suggested that the compensation structure of the life insurance industry is determined by the nature of people's emotional response to the idea of life insurance. "No one wakes up and says, 'It's a beautiful day outside, and I'm feeling great, so I think I'll go and buy a million dollars worth of life insurance.' Life insurance is a product that has to be sold even though it is a product that everyone needs."

Dick Hemmings noted that the compensation structure was driven, in part, by the changing complexion of the life insurance industry. "Is there a better way to do it? Of course, but you have to consider the total number of agents in the life insurance business is declining. As the older agents are retiring, there aren't any new agents to replace them. Because of the declining numbers, companies aren't just competing for customers or products, they are also competing for distributors. So what do they do? They pay them more."

Jim Mitchell added that the high cost involved with training and developing new recruits is one reason for the current system. "The alternative can be an

expensive system from the company's standpoint. This is why we pay agents a lot of money upfront to sell insurance. You would have to finance new agents much longer if they didn't get paid as well upfront for the business they do sell."

"What standards need to be met for disclosures to be meaningful and relevant to the consumer?"

Jim Mitchell

Scott Perry agreed, noting that to spread commissions over a longer time period could be financially risky for the company. "If you spread compensation out, it would increase the amount of the subsidy the company has to provide to new agents. When you do that, you increase the cost to the firm of new agents failing. Training a new agent is already expensive, and spreading out the compensation would make it even more expensive."

IS AGENTS' COMPENSATION AN ETHICAL ISSUE?

Perry was not convinced, however, that the current compensation system offered a unique ethical problem. "The reality is that we could change the system, but you still have to pay someone to sell the product. That cost is going to be a part of the product and is going to be passed on to the consumer. You can draw an analogy to selling real estate. There is a fixed percentage of your home's value that you agree to pay to the agent when you decide to sell your house. What's going on here is no different; the distribution cost is embedded in the product, that's all."

"We have to start thinking about how we can develop better products to meet consumer needs."

Scott Perry

Jeff Seglin wondered what reasons agents would offer for not being transparent about their commissions. "I'm thinking if you want your clients to trust you, why aren't you fessing up? If you've done a good job in earning the trust of the client and selling the product, would you lose clients as a result of disclosing this?"

Lisa Weber commented that there are different levels of transparency and not all may be appropriate. "I personally don't think an agent should have to disclose exact commission amounts on a product-by-product basis. I think it changes the conversation. You can't put a price on the brand, you can't put a price on the company's reputation, and you can't put a price on the service structure. But, on the other hand, I am all for disclosure in terms of the fact that it is a commission-based product. It is also important to disclose that agents may make more money if they work for a company and sell a proprietary product versus selling another company's product."

Richard Nielsen, Jim Mitchell, and Jeff Seglin confer.

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Perry agreed with Weber. "The industry has made things more complicated than they need to be. Essentially, I work on commission and what that means is that part of the money the client pays for their product is used to pay me. When you get into the specifics of that percentage is when the client says, 'Now I am going to shop around and see if somebody will sell it to me for less.'"

Bill Laufer wondered if the question of whether the client could get a better deal isn't a good question for them to ask. "Is that such a bad thing? What would happen to your margins if you had full transparency?"

Weber responded, "I suppose an alternative would be to offer a side by side comparison of various products, including commission, and then let the consumer decide which product they want. If you did that, I think you would see a decrease in the margins. Not because of the competition from other firms, but because people wouldn't buy the product. The reason that people don't buy is because of the incredible complexity of the product. I think it's the responsibility of the industry to 'demystify', but the issue is not demystifying compensation, but demystifying the product."

"The conundrum is a classic one in business ethics and it is 'either I behave in this way or I am out of business.' Sometimes in our zeal to defend a current practice we dismiss the ethical side of it, and we may not realize what an opportunity there is in it."

Marianne Jennings

Laufer replied, "I don't know much about this industry, but I suspect that part of the reason you wouldn't want to disclose is because you would like to protect the margins. It appears that, in all likelihood, if you were to disclose the amount or percentage of the commissions, the margin would decrease."

THE ROLE OF MEANINGFUL DISCLOSURE

Mitchell raised the issue of meaningful disclosure and inquired what standards need to be met for disclosures to be meaningful and relevant to the consumer. "As a society over the last decade, we have concluded that more disclosure is better, to the point where we seem to be disclosing a lot of information that no one wants or needs. I think the overarching question is 'what would be meaningful information to disclose in this case?'"

Marianne Jennings suggested that the industry was heading down a well-trodden path in its debate about commissions and disclosure. "You are grappling with a very basic ethical issue and the reason you're struggling with it is because, doggone it, if you were on the other side you would want to know how much commission your agent received on your policy. The conundrum is a classic one in business ethics, and it is 'either I behave in this way or I am

out of business.' Sometimes in our zeal to defend a current practice we dismiss the ethical side of it, and we may not realize what an opportunity there is in it."

Jeff Bosco wasn't confident that disclosure made a difference in consumer's decision to purchase life insurance. "Consumers buy whether you disclose that our commissions are 50% or that they are 150%. I've never had anybody be mad at me because they bought too much life insurance. I have had it the other way where they have been really upset they did not buy enough."

Golato agreed with Jeff Bosco that commissions were not a concern for most clients. "If people were concerned about paying commissions, they could work with fee-only advisers who don't get paid on commissions. I think that the issue comes down to the fact that we have to pay a sales force that will go out and motivate people to take action and buy this product."

MIDDLE MARKET CONCERNS?

Hemmings suggested that perhaps the current model of compensation was tied to the problem of failure of the life insurance industry to reach the middle market. "There is another element of this which is that the industry does not serve all of the public. There is a huge part of the population that doesn't have what we are selling. The reason that they don't is because of producer compensation. There is not enough money in it for the agency or the company to sell that policy. How can we let this stand as an industry?"

Scott Perry, Dick Hemmings, and Jeff Bosco review the day's events.

Brad Agle commented that he was struck by the fact that the industry appeared to recognize an obligation to people who did not own their product. "A lot of business people would say, 'Hey, I'm out there making money from whomever I can make money from, and the others I don't really care about.' There is an interesting undertone here that 'because I am in this industry, I have some moral duty to try to take this product, which I believe is helpful to people, and somehow get it into their hands'. I think that's an interesting thing to even say 'I have a moral duty here'."

Jennings remarked that perhaps the failure of the middle market to purchase life insurance could be attributed to other causes. "I think that we need to look at why are the middle market people not buying? You are assuming that it is because you

have not reached them, but what about the reputation of the industry among that part of the public?"

Duska was not sure that it comes down to a lack of trust. "I think Peter is right when he said earlier that these agents have to go out and sell life insurance since no one is thinking about it."

"Most agents look at the relationships with their clients as long-lasting. I don't think that there are many agents out there who look at it as once and done. What they are all looking to do is build a relationship with the client."

Lisa Weber

Perry offered another possibility as to why the industry has failed to penetrate this market. "Frankly, I think that one of the reasons is because companies have not been looking out for the best interests of the consumer and are too worried about satisfying their own organizational needs. We have to start thinking about how we can develop better products to meet consumer needs."

Mitchell agreed. "I think that this begins to respond to the challenge that Marianne gave us earlier. Products are complex since complex products benefit producers. Producers love to have something to sell that only they can understand. What if we had products that consumers were able to understand? It may be as simple as that."

Weber suggested that perhaps all of these issues affect the consumer's decision to purchase life insurance. "There are a couple of different issues going on here; the first is that people aren't buying life insurance since they haven't been approached by an agent. This is unacceptable. The second reason is that the process is so confusing. People wonder, 'How do I get out of this alphabet soup of product names and what does it all mean?' It is a big decision, and if it is complicated then people are willing to put it off and put it off. Finally, there is an issue of trust and in this era in particular. Trust has probably never eroded more than it has in the last six months."

Marianne Jennings, Richard Nielsen, and Jim Mitchell compare notes.

TOO COSTLY?

Laufer brought the discussion back to the consequences of fuller disclosure. "Let me ask you this: If you were the first firm in your industry to engage in this courageous disclosure, what effect would that have on other competitors? Would you see a cascading effect with other firms adopting the same policy?"

Bosco doubted there would be a cascading effect, "because, again, I think that the disclosure of the commission is just a small piece. The thing about a life insurance policy, which differentiates it from an auto or home policy, is that it is only priced one time. So the up-front commission might seem high, but it is for the lifetime of that product."

Seglin responded, "Why not explain that then? That makes sense. Consumers would understand that. Or is it that if he's selling me a product I want, I don't care how much he makes?"

Perry noted that it was important to remember that regulations require that some disclosures be made to every client. "There are disclosure requirements for all proposals and illustrations and these are standardized across the industry. All companies are required to disclose the expenses embedded in the net return. So without getting into the specifics, it would be possible for a client to make a decision from these comparisons if they wanted."

Gigi Golato, Linda Mitchell, Scott Perry, and Bill Laufer.

Duska remarked that the complexity of the agency system makes detailed disclosure difficult. "I can see that a client, after they learned about the front-loaded commission structure, may think, 'You got really lucky when I walked in here today. All you had to do was write up the policy and you get to take home $5,000.00.' But you can't explain that this is the only money you'll get from this sale, that the manager needs to get paid, and all of that other stuff. You can't explain that if you didn't get paid this way, there wouldn't be enough agents to sell the product. If you had to do all of that, you would need half an hour."

Weber added that most agents look at the relationships with their clients as long-lasting. "I don't think that there are many agents out there who look at it as once and done. What they are all looking to do is build a relationship with the client. Even in that conversation that Ron mentioned, it is not as simple as just buying life insurance. You are also talking the life needs of the client and offering advice about that."

Hemmings said that he believed that developments in technology would enable the industry to approach customers in a different way, which would lead to significant changes in the business model. "Once you have electronic medical records and medical scoring, then the whole underwriting business will change. It will be much easier to sell life insurance over the web than it is today. We are all aware of impediments in the business model and why things are the way they are. We don't like it. But it's the system that we have, and we deal with it. The biggest obstacle to the disclosure of commissions is that the agents, the ones who are benefiting from the current system, have a much stronger lobby than the insurance manufacturers do."

Richard Nielsen observed that the structure of the current system comes down to political power. "It seems that in the financial services industry in general, there has been a push to get away from short-term compensation. If the deal does not go through then the person who made the deal has to give back part of their compensation. Is this idea of longer-term compensation or "call-back" relevant to your industry?"

Perry responded that there have been some companies that have tried to spread out agent's compensation over the longer term, but this has not been successful. "There is a 'call-back' if the policy lapses in the first 30 days and a couple of firms have tried to incent their agents by spreading compensation out over a longer period of time. But the problem, as someone brought up before, is that companies are competing for distributors. If the agent wants to get paid all up-front and some other company is willing to do that for them, you've got a problem. A company needs to compete for successful, experienced agents and also to minimize the subsidy for new agents entering the business. The high up-front compensation is how we do that."

THE PRACTITIONERS' ETHICAL ISSUES

At this point, each of the practitioners was asked to present an ethical dilemma that he/she has faced in business.

ISSUE #1: WHETHER TO DISCLOSE THE "BRUTAL FACTS"

The story I want to tell concerns an "up and coming" executive who was assigned to take charge of a product line whose performance had deteriorated significantly over the last quarter. Upper management was concerned, since this particular product line represented about 25% of the company's earnings. They were also surprised, since this line had produced solid earnings for the last six quarters. The young executive was told to turn things around by next quarter.

How responsible are (senior executives) for making certain that people feel comfortable coming and talking to you?

Jeff Seglin

He soon discovered some brutal facts about this particular line. The first was that the previous results were positively impacted by a number of one-time developments that wouldn't necessarily be repeated. These one-time developments tended to mask the underlying troubles that had been emerging in this business. These negative trends were likely to increase and continue to negatively impact profitability. While the young executive was able to identify some actions he could take to mitigate the deterioration of performance, it was going to be some time before these results would be visible. He realized that if he applied some pressure to the valuation actuaries as well as the claims reporting team to get more aggressive on their assumptions, he could speed up that apparent improvement. He was concerned that if he was honest about the problems in the product line, there would be a personal cost. He was worried he would be marked as "overly negative" or "not resourceful enough".

Jane and Dick Hemmings arive at the opening dinner.

His ethical dilemma was whether he should present the "brutal facts" to the executive management team as well as realistic actuarial assessments and a fair and honest projection of a timetable in which this product line could be turned around? Or, should he present a more optimistic picture of the business, ignoring some of the disturbing trends, pressure the actuaries and administrative staff to get more aggressive with their projections, and hope for potentially more one-time events to continue to mask the ongoing problems?

In the end, he decided to go to the executive committee and give his honest assessment of the problems with the product line and the reason these problems had not come to light before now. What is interesting is that, after this person told the truth with openness and candor, it ended up being a very positive thing for the company. Since he did such a great job of uncovering all of the variables that were driving the performance of this product, the company was able to come up with a better solution for managing the business going forward.

Jim Mitchell flanked by Scott Perry, Linda Mitchell, and Brenda and Ron Duska.

Brad Agle, in commenting on the case, made a distinction between an "ethical dilemma" and an "ethical issue." "Ethical dilemmas are the kind of thing where you put ten ethicists in the room and five would say you should do one thing and five would say you should do another. In this case, you are dealing with an ethical issue. An ethical issue is a situation where there is agreement as to what the solution should be. In this case, it is to tell the truth. The real ethical issue here is 'how do I do that and not have it destroy my life or my career?' Academics have very little to say on this question, and I think it is a challenge to us as a profession to have more to contribute on this issue."

"An ethical issue is a situation where there is agreement as to what the solution should be. In this case it is to tell the truth. So the real ethical issue here is 'how do I do that and not have to destroy my life or my career?'"

Brad Agle

Jeff Seglin thought it disturbing that the young executive assumed a negative report would be poorly received by the executive committee. Something was lacking in the culture of the company. "This makes me wonder how you guys, as senior executives, view your responsibility to the people who report to you? How responsible are you for making certain that people feel comfortable coming and talking to you?"

Scott Perry thought executives are responsible for making people comfortable with doing the ethical thing and believed that creating this comfort level is important to creating an ethical culture. "People want to know whether the culture of transparency is nothing more than a bullet point on a poster board or whether people have actually been rewarded when they bring things to light."

Agle commented that in some companies employees get the message that openness and transparency are neither encouraged nor welcomed. "Just this week I was talking to a manager at a Fortune 10 company. He told me he was let go because he brought matters to light that management wanted to remain hidden. One of his employees informed him that inventory was being inflated and, after he did some checking, he discovered that not only was the employee telling the truth, but also that this had been going on for 12 years. This just shows that there is a reason for employees of some companies to be wary."

Richard Nielsen indicated that different sectors might have more flexibility than others regarding quarterly earnings and performance expectations. "If you're working in an industry where it is possible to survive and even be considered good if you make 10%-12% returns, that's one thing. But if you're working in another industry where you have to make an 18%-20% return to be competitive, it might be a lot harder for an executive to be the bearer of bad news and keep his job."

Jim Mitchell thought that one of the hardest things for a CEO to do is to find out what is really going on inside of the company. So many people will tell a CEO what they believe he wants to hear. He asked, "How do you create a culture where people will feel free to bring things like this up?"

Marianne Jennings suggested that stories reinforce which company values are most important. "Stories have great power and more importantly, what you signal with a story like this is, 'We would rather know about bad news early. It is not like fine wine; it doesn't improve with age.'" She encouraged the use of stories in maintaining a culture.

Brad Agle and Scott Perry share opinions.

Agle asked the executives to give him three factors that determined why the young executive chose the path he did.

Perry proposed these three motivations. "I think that there must have been some sense of trust. He must have been able to trust that the members of the executive committee wouldn't hang him out to dry. I think that there

was probably some self-interest as well. It's likely he could have thought 'I own this product line now and this is eventually going to bubble up and get to a point where I can't hide it anymore so it is best to get it out on the table now. Finally, I think that he must have had a desire to do what he thought was right."

Brenda and Ron Duska enjoy the evening.

Peter Golato was convinced that you have to reward the behavior you want to see in your employees. "I want to make sure people know that I know that this is exactly the type of behavior we want from people. However, it is also important that there is public praise as well. One of the best things you can do for someone is to publicly praise them and use them as an example."

Lisa Weber agreed with Jennings about the importance of story telling to create an ethical culture. She said that it is necessary to create an organizational environment that encourages disclosure. "Beyond the individual personalities, we need to consider the structure of the organization. When something happens, I don't just want to hear from the compliance person. I also want to hear from the human resources department and the business manager because then I hear it through three different lenses. If any one of those three isn't telling me something, there is a lack of ownership. It also helps me since I know I'll take away something different from each of these conversations, even if they are describing the same situation."

...you have to reward the behavior you want to see in your employees.

Peter Golato

ISSUE #2: CONFRONTING AN UNETHICAL SYSTEM

A colleague shared this story with me last week. It deals with what to do if you encounter a system that is unfair or unethical. In the insurance business, in order to sell products in a certain state, you need to have your company and products approved by the State Insurance Commissioner. The Commissioner of Insurance is an elected position in some states. This colleague of mine was looking to expand the business into a state in which the commissioner is elected. Soon after his company made contact with the office, he started getting invitations to political fundraisers for this commissioner's election fund. The dilemma is that if the implicit understanding is that you need to "pay-to-play", should my friend contribute and, if so, how much?

Bill Laufer stated that the "pay-to-play" strategy was recently investigated in a legal case. "There is a case that I am very familiar with, that involves a company that had an adverse judgment and was ordered to pay something like $15 million. The company then underwrote the campaign for a judge who won. The judge declined to recuse himself, heard the case on the appeal, and reversed the judgment. The case is now before the Supreme Court, dealing with issues raised under due process and recusal."

Brad Agle raised the point that even though each contribution to a "pay-to-play" scheme may be small, the cumulative effect is a system that few people feel comfortable with. "It's just a whole bunch of little decisions. You think, 'I'll just give $500 or $5000' but, to the extent that everyone says and does the same thing, we end up getting a system that we don't like. So now, you have questions about your duty to shareholders and employees and your duties as a citizen. How do we stop this sort of thing? There has to be a better way than 'pay-to-play'."

Richard Nielsen offered a possible solution. "One of the methods that sometimes works in this type of situation is to secretly threaten to blow the whistle. The problem is that with public whistle blowing, the whistle blower is often retaliated against, and it can damage the reputation of the whole organization for the unethical behavior of a few individuals."

ISSUE #3: STICKING YOUR NECK OUT

This case raises the issue of how far you should go in pursuing a course of action you truly believe is right, even when you aren't getting much support for it. There was a bill moving through a state legislature that would make the "twisting and churning" of life insurance and annuities a felony.

"Twisting and churning" refers to unsuitable sales. An agent sells someone a life insurance policy and collects a commission and then six months later comes back and tries to sell the client another policy simply in order to collect an additional commission. Lately, there has been a lot of bad press concerning this practice, especially since in many cases these agents are targeting seniors.

Angela Nielsen jokes with Nancy and Jeff Seglin.

The problem was that this legislation seemed to be calling attention to and putting a spotlight on a practice that is not systemic in our industry. It makes it seem that all agents are trying to rip off elderly clients and sell them this bad stuff. No one disputes that what is going on in these cases is fraud and a crime. But the focus in the legislation is on these products, life insurance and annuities, and the message is that we need to put lots of laws in place to protect the public from insurance agents, and that's not right.

For me, it comes down to choosing the battles I am going to fight. This was one of them.

I discovered that none of our competitor firms were willing to take a position on this issue. I can appreciate their stance, since it could appear that they were condoning these tactics if they fought the legislation, which is clearly not the case. So, when I really started to get active on this issue, I was going at it alone. There are obviously some problems that come with this, since you do not want to look like the company that doesn't care about seniors. But if I had stayed quiet on it and everyone else had also, this legislation would have passed. In the end, we were able to work with the legislature and reduce the charge to a misdemeanor. I could have lived with this being a felony level charge as long as you expand it to apply to the "twisting and churning" of all financial products for people over 65, not just life insurance and annuities.

I've told this story to all of our agents, whenever I had the opportunity to do so. I figured that even if I lost the battle, I could still win the war by reinforcing the fact that we're committed to protecting seniors and developing a comprehensive framework to protect them. Currently, our company is looking to develop a "Senior Citizen Bill of Rights" which will build certain protections and contingencies into the products, such as allowing a senior to withdraw funds with zero penalties in the event of a terminal illness. I believe that something like this gets at the heart of the needs and concerns of seniors in this marketplace.

Richard Nielsen suggested that the regulators might be looking for a place to start, rather than focusing exclusively on insurance and annuity sales. "From the point of view of the politicians, their rationale could be that you can't do everything all at once, so you start from what seems to be the most egregious offense and expand from there."

Scott Perry commented that this case raises the ethical issues involved in marketing products to seniors in general. "Most of the regulations and compliance requirements make good sense on the surface. Sometimes when you start digging into what they actually require, the standards are pretty subjective. This is a challenge since there is a real need to serve this market. It's a fine line we have to draw since there is subjectivity as to what is a suitable sale to someone who is 70 years old. Should you be selling annuities at all to people who are over 80? Are there maximum surrender charges that should be allowed? It's tough. The state approves the product design and approves the desirable age limits set for that product. But when the company sells it, the state may come back and say that these are unsuitable sales."

ISSUE #4: ETHICAL PROBLEMS WITH PENSIONS

My story relates to defined benefit pension plans, which are declining rapidly in our country. Except for government employees and college professors, there aren't many left. The defined benefit pension plan is one of the great things that came out of the private sector for the benefit of all employees.

At one point in my career, I was a partner in a law firm with a defined benefit plan. Each year the partners would be faced with a question of the amount of funding to do for the plan. We were one of the last law firms in our city that had one, and we used it as a recruiting tool. Also, it benefited all the employees of the firm, not just the partners, even though there were probably five times as many employees as there were partners.

American law firms frequently compete with one another for partners on the basis of net income per partner, or NIPP. The ethical dilemma for the partners in determining how much money to put into the plan was that, if we funded the plan less well, our NIPP would be higher. I stood up at the partner meetings and tried to remind the other partners of the promises we had made to all the employees of the firm, and how the defined benefit plan had served us so well as a recruiting tool. But they were more interested in maximizing their NIPP currently.

While putting less funding into our pension plan would increase our NIPP, over a period of time with interest rates dropping, our plan became underfunded. When it became underfunded, we really had no choice but to freeze the plan, with no new entrants and no new accruals. I voted in favor of freezing it, not because I wanted it to go away, but because at the point there was no other choice. I really do think that, over a period of years, the partners dropped the ball.

With these defined benefit pension plans disappearing all over the country, the only two sources of guaranteed lifetime income are Social Security, which is dramatically underfunded itself, and annuities sold by insurance companies.

In an annuity, there is a deferral period, during which money accumulates inside the annuity on a tax-deferred basis. Then comes the payout phase, when people can take their money out in guaranteed annual increments or withdraw the entire amount as a lump sum. So guess how many people at retirement actually choose to receive a guaranteed payout over time.

Brad Agle proposed "20 to 30%?"

Marianne Jennings suggested "10%?"

Dick Hemmings responded, "The actual number is closer to one to two percent."

Jim Mitchell said, "I would like to think that would improve over time, as people get better educated about annuities."

Jane and Dick Hemmings along with Gigi and Peter Golato and Richard Nielsen listen to opening remarks.

Peter Golato added, "There aren't any vehicles out there other than annuities that can guarantee a lifetime of income. The mutual funds are trying to introduce a similar feature, but it is not as good."

Hemmings remembered that when he was at an annuity conference two or three years ago, someone asked the audience, "'How many of you would buy the annuities that your own company sells?' But only a few hands went up."

Richard Nielsen wondered how this was allowed to happen. "Is it that regulations are not enforced?"

Hemmings responded that the problem was not lack of regulation. "People just decide to cash out."

Scott Perry offered that, "Individuals have the right to choose. Most of them either choose to take the money in a lump sum or they don't need the money so they leave it in their estate for their heirs."

Jeff Seglin suggested another option. "They could roll the money over into another tax-qualified plan, so they would be keeping the money but putting it someplace else."

Hemmings is convinced that this is an ethical issue for the industry. "Why should Federal Tax policy favor products where the mortality risk assumption in the product is almost non-existent? Wouldn't it be better to tax the accumulation during the deferral period and allow the customer to not pay tax on the payout?"

Bill Laufer listens as Brad Agle presents his case.

Golato added that, "As a life insurance agent, I was trained that an annuity is just another form of a life insurance contract. It has a guaranteed income component—income that you cannot outlive. I never thought of it as a tax-deferred mutual fund."

Perry responded, "Some people sell it that way, though. The lifetime payout may never even come up in the sales presentation".

Golato concluded, "We need to get back to selling annuities for their lifetime income benefits, rather than just as tax-deferral vehicles."

ISSUE #5: STRANGER-OWNED LIFE INSURANCE

This issue is about Stranger-Owned Life Insurance Policies. These policies are known in the industry as STOLIs or IOLIs, which means Investor-Owned Life Insurance. A STOLI begins with a group of investors that have capital to invest. They approach an individual, usually a senior citizen, and propose to use his insurability to obtain life insurance on his behalf. Simply put, they will pay the premiums on a life policy in his name and collect the death benefit upon his death. The insured receives a payment for lending the investors his insurability. Since investors look at this as an investment, they will not permit the policy to lapse. Over the years this has become increasingly popular since their profit, the death benefit, is tax-free. This has to be one of the most unethical and unscrupulous things that I have ever seen.

Now, there is nothing wrong with a true-life settlement. If you want to sell your life insurance contract, you should have the right to do that. If someone is willing to pay you more than the cash reserve of the policy, the amount you could get from the

company that issued the policy, so be it. It's your property. I should mention, however, that not everyone in the industry would agree with me on that. Additionally, there is no particular reason that if a person wanted to finance life insurance that they should not be allowed to do so. There are people out there who would like to buy, and who need to buy, life insurance, but do not want to unwind their assets in order to fund the premium payment. The problem occurs when these two things come together in a way that is not initiated by the individual, but rather perpetrated on people, usually seniors, by unscrupulous agents.

Our company started to notice a significant spike in life insurance applications. These applications were for people in their 70s and for contracts upwards of $5 million. We were generally allowing the premium financing and had our advance sales folks trying to make sense out of these premium financing arrangements to make sure that they were on the up and up, and not part of a STOLI transaction. I can tell you that it was not only taxing the underwriters, but also the advance sales team. I felt like I was putting my advance sales people in a position to evaluate these premium finance contracts when they really did not have the adequate tools to do that. It was not their job, but we were relying on them to do it.

Scott Perry noted that life settlements emerged originally to meet an entirely different purpose. "This whole market originated to help people who were diagnosed with terminal illnesses pay their bills. They didn't need the life insurance policies they were paying on; they needed money now. An investor would buy the life insurance contract as an investment, and the insured received the cash he needed, more than he would've received by simply cashing out the policy. It made sense."

Peter Golato warned that the use of life insurance policies in STOLI transactions could threaten the tax benefits that many people depend on when both purchasing and selling life insurance. "If practices like this, which are a complete misuse of life insurance, continue unchecked, the consequences could be very negative for all concerned."

Jim Mitchell agreed. "The public policy is that life insurance is a desirable thing since it removes the burden of care for survivors from the state and places it on the individual. The government wants people to own life insurance. The tax benefits are to encourage people to purchase sufficient life

insurance. But if it's just another security, an investment like anything else, why should it keep its tax advantages?" He added that a zero lapse rate would force companies to increase their prices, which threatens to price many people out of the life insurance market since it'll simply cost too much for most people.

Bill Laufer wondered why anyone would want to invest in a life settlement. "Why would investors take this bet? It doesn't make sense to essentially bet on someone's mortality unless they have either information that the insurance company doesn't have about the health of the insured, or they were somehow going to help that person pass on earlier so they could collect the death benefit."

> **"It's the question of when a leader has to say, enough is enough. The system is corrupt and someone needs to stand up and say that this is wrong."**
>
> **Ron Duska**

Jeff Bosco responded that once Wall Street firms became involved in the life settlement industry, no fewer than a hundred policies were bundled together and then sold as investments with a consistent return. He also raised the issue of how investors are changing the calculation of lapse rates. "This changes the game for the companies since, when you have Stranger-Owned policies like this, you have investors that are not going to lapse the policies."

Perry added, "Twelve years ago, life settlements were really kind of a 'mom and pop' business, but when the Wall Street firms got involved, they began to build a sort of exchange to trade bundled life insurance contracts. It was getting completely out of control, but I think that, fundamentally, there is some value in the basic concept. The question is, 'How can you have a product that is good for the consumer and that meets consumer needs without it being abused?'"

Lisa Weber noted that, at least in terms of Investor-Owned Life Insurance policies, legislative intervention is making this a lesser issue. "Every insurance company in America has taken a pretty strong position against IOLIs. There is not a firm in the industry that would go out and say that the IOLI business is a good business. One of the reasons is that, as Peter said earlier, this is not life insurance. Life insurance is intended to have "insurable interest", which means that the beneficiary of the policy has an interest in the insured's continued life. Obviously, the investors who are funding the IOLI have no such interest. Someone wanting you dead is not an insurable interest."

Dick Hemmings commented that the insurable interest standard is applied inconsistently. "We need to recognize that the industry is not lily white here. Think of the insurance policies taken out by some big companies on all of their employees.

What's the difference between an IOLI and what a big company is doing in terms of Employer-Owned Life Insurance? You can't take the attitude that we can't have IOLIs since there is no insurable interest and ignore the lack of insurable interest when writing contracts on employees where the employer is the beneficiary."

THE PHILOSOPHERS' QUESTIONS

QUESTION #1: DUSKA

There is an issue that has been running through a couple of the cases the executives have raised today. It's the question of when a leader has to say, "Enough is enough. The system is corrupt and someone needs to stand up and say that this is wrong." An example of the sort of thing I am talking about is whether any of the executives here would settle a lawsuit, even if you weren't guilty, to save the money, uncertainty, and reputational losses that could come from a long and drawn out trial? I have asked several executives this question and the arguments that I get back usually are, "Well, we have to be concerned with the finances" or "It's the easiest way" or "It's what everybody does." Another issue that we've mentioned today is lobbying. Lobbying has a legitimate function in providing people with information that they might not know otherwise. It seems that lobbying has become a subtle form of extortion and contributes to the "pay-to-play" system we were talking about before. When lobbying is not about providing needed and relevant information, but instead is a means to facilitate campaign contributions, it's a bribe.

Peter Golato and Bill Laufer are intent participants in the day's events.

Bill Laufer shared that he has done some research on the lobbying question as well. He focused particularly on Corporate Political Action Committees (PACs), which raise monies from their employees to fund their lobbying efforts and outreach programs. "There is a theory of public goods which says that people will not contribute to a public good on account of the "free-rider" problem. The "free-rider" problem is when people say, 'Why should I contribute, when I can benefit from the contributions of everyone else?' So in order to get people to contribute, you need to compel them or persuade

them through selective inducements. This raises the question of how a PAC gets its money. The theory says that there should be no money in a corporate PAC, but there is a lot of money there. Therefore, I went and interviewed 30 directors of corporate political action groups all around the country and found that they forced their employees to donate by offering selective inducements for them to do so. Now, this is all illegal, but I have all of these tapes where people are telling me they are doing these clearly illegal things that they think are perfectly normal!"

Lisa Weber noted that persuasion can take other forms than the sort of material inducements that Laufer discovered in his research. "I'm sure that there are a lot of companies, like ours, that don't do anything like selective inducements. But you do get the message that it's important to get involved in issues that can impact your industry, to support your government, and get involved politically. Moreover, if you ask the people who contribute to the PAC if they weren't getting five of those sorts of messages during the contribution time, would they have actually made the contribution? I think it raises the question of whether we should have a PAC in the first place."

Jeff Bosco, Lisa Weber, and Marianne Jennings comment on a point.

Jim Mitchell thought that it was necessary to consider corporate political action committees in the context of all of the other groups that have active and well-funded lobbying efforts. "The labor unions are very active in getting out their positions on these issues and they spend a considerable amount of money on their efforts. Shouldn't management get to tell their side of the story to the legislators as well?"

Richard Nielsen suggested that Mitchell's question pointed back to the issue of fairness that Duska initially raised. "If the union is doing something unethical, does it make sense for the corporations to 'double the money'?"

Jeff Bosco asked the group if they had heard of a now-infamous life insurance claim that occurred a couple of years ago. "There was a man who had taken out approximately 5 or 6 half million dollar life insurance policies with about five or six different companies. He and his family traveled to Mexico for a vacation, and he died while traveling there. The only problem was that there was no body. After

some time passed and the companies were refusing to distribute the death benefit, the family retained a lawyer who asserted that they were acting in bad faith and that they needed to make good on the claim. All of the other companies paid the death benefit, except our company. When we finally asked a judge to exhume the body, lo and behold, we exhumed a soda can. So now, they are suing us since they claim that we stole the body! To answer your question, Ron, you have to stand your ground, but at the same time, as a company, you can get involved in all sorts of situations."

Nielsen suggested that if the insurance companies got together perhaps they could prevent the sort of behavior that Jeff was talking about, as well as work to mitigate any ethical harm posed by the political action committees. "This may be naïve, but in some countries, sometimes, the main competitors all agree to resist the unethical behavior and since they are all refusing to cooperate with the unethical behavior, no one is at a competitive disadvantage for acting ethically."

Laufer agreed that this was a possibility, but that it was unrealistic on account of the amount of consensus that would have to be in place. "You might be able to do that, but you have to remember that the insurance companies are competing with other industries. You would have to get the entire financial services industry on board. They probably would not go for that unless the other PACs that have a stake in the game, like the unions' PACs, would also get on board. Good luck."

QUESTION #2: LAUFER

My question has to do with the fact that it is difficult to determine which problems need to be solved at the systemic level, organizational level, or individual level. I have been part of many conversations like this one, and I think that we need to take a more comprehensive approach to figure out how to solve these problems. I will throw this out as my question, "Do we need an organization analogous to the National Transportation Safety Board? Perhaps something called the National Business Ethics Safety Board?"

After we see these corporations crash and burn, do we need to send an expert team to go in and figure out what went wrong? If we have enough pieces of data, we'll be able to develop a database and have this evidence inform not only future legislation, but also the corporate ethics programs we develop in response to these crises.

Right now, I think that we have some sort of hodgepodge data driven by whatever academics feel like studying. We have no systematic research that really addresses why these crises happen and how they can be prevented. The financial services industry specializes in assessing risk, so how do you go about assessing risk in terms of the ethical lapses that occur in your firms?

Scott Perry thought part of the challenge of a systematic approach was the fact that different industries face different sets of obstacles to ethical business practice. "I think that's part of the challenge; what are the fundamental systemic breakdowns that cut across every industry? Because once you get into the details of a business, you're right, it becomes a mish-mash."

Dick Hemmings suggested part of the difficulty in investigating and developing effective ethics programs, at least in the financial services industry, results from the complexity of the products. "I used to work as an insurance corporate regulatory lawyer. I didn't do securities work for a living, but I was certainly familiar with the structure of products. I was looking at the documentation we were supposed to be familiar with for purposes of regulation and I knew that if you follow the money, you could understand the financial instrument. I have to say that I looked at this stuff, and I couldn't figure it out. And if I couldn't figure it out, how could I expect a company that was buying this to understand it either? However, what I heard from them is that the products were Triple-A rated, and they weren't worried about it. I think we've lost something. We are relying on someone else, in this case, the rating agencies, to make judgments for us about whether or not this is an acceptable product. In large part, this current mess is a failure of common sense."

"We are relying on someone else, in this case the rating agencies, to make judgments for us about whether or not this is an acceptable product. In large part, this current mess is a failure of common sense."

Dick Hemmings

QUESTION #3: AGLE

If you look back in time, every 10 or 15 years we have some sort of corporate scandal. You can follow it from the 1800s. We have periods of scandals, followed by periods of reform and then periods of regulatory laxity when the cycle begins again. Maybe it's just that there is a baseline of deviance. Criminologists find that this is generally the case, and then someone like Madoff comes along and reminds us that we have problems that can't be explained through a lack of compliance. Maybe the problems have persisted since the beginnings of commercial activity; maybe there are just some people who exploit the nature of commercial exchange?

"Do good compliance and good ethics go hand in hand, or do you have good compliance just because people do what they know they have to do so they don't get in trouble?"

Lisa Weber

Lisa Weber noted that there is an important difference between ethics and compliance. "We have an extensive program in place that monitors the sales

activities of our agents. We have been doing this for quite some time, and we make about a $50 million investment in compliance every year. This is compliance, and it is different from ethics. I am not sure how you measure ethics. Do good compliance and good ethics go hand in hand, or do you have good compliance just because people do what they know they have to do so they don't get in trouble?"

Bill Laufer said that while people often offer anecdotal evidence of the success of ethics programs, the fact is that we really don't have any statistically significant information about how well these programs work, if indeed they do work. "We generally don't put real time into developing sophisticated evaluation procedures for our ethics programs. This may be because many companies really don't want to know how these programs work. The bottom line is that intuition isn't good enough and ideology isn't good enough. We need some sort of systematic assessment of these efforts so that our policies are evidence based. As it is now, we don't put programs and policies in place that are grounded in empirical evidence. We put programs in place because they are politically expedient or ideologically pleasing. But we need to do more and better than that."

Scott Perry comments as Dick Hemmings thinks through the issues.

"The bottom line is that intuition isn't good enough and ideology isn't good enough. We need some sort of systematic assessment of these efforts so that our policies are evidence based."

Bill Laufer

QUESTION #4: SEGLIN

My question is actually pretty simple. Of all the things that you do in your company, is there one thing you would rather that your customers not know you did? It could be something concerning compensation, or the way that you treat employees, or maybe the way you do reviews of claims. I am not talking about practices that are illegal or anything like that. But is there some practice within the company that you would rather the outside world not know about? My follow-up question is: Why do you choose not to disclose this?

Scott Perry provided an example from the long-term care business. "Part of what we have to do is deny some claims. This doesn't mean that the person is not legitimately suffering from an illness or in a nursing home, but they do not meet the qualifications that trigger the benefits in the contract. A year ago, I would have responded to your question by saying that 'this is a pretty messy business, and I would not want to talk to a customer who bought a policy five years ago and go through the last ten claims that have been denied.' We started a program a year ago where, when we have

inquiries, before they actually evolve into someone filing a claim, we place an outbound call to those people to make sure that they understand their policy. We wanted to make it clear up-front what the triggers were for certain benefits, and what sort of services were covered and what were not covered, under the policy they had chosen. Even in cases where people later submitted a claim that was denied, they were thankful for the explanation. Now they knew what would not be accepted and why it was not covered under the policy. It was an enlightening experience for us, and the customer feedback was positive. There was a business benefit as well, since we were avoiding some claims that would have been denied if they were filed, either for lack of proper documentation or because the benefits weren't triggered. Handling such claims is costly business.

Dick Hemmings said that he is concerned about the complexity of some products in the marketplace. "There are plenty of accident and health insurance products I can think of that are designed primarily to provide profits to the company and have very low loss ratios. If we handled those products, which we don't, I'd frankly be embarrassed to explain them to the customer, because we would have to explain that we are providing them with something that really doesn't provide them with much value."

Jeff Bosco and Lisa Weber participate in the discussion.

Jim Mitchell reminded the group of the previous conversation about disclosing agents' commission. "I think that there are certainly reasons why companies might not want the compensation they pay their field people to be disclosed. If consumers knew that more than half of their first year premium went to compensate the agent, some would walk away."

Perry suggested that perhaps the public would be equally surprised to learn how much top-performing agents receive in compensation. "More than the compensation of CEOs, I think that people would be shocked to know the level of compensation for top performing agents. It would not be the role of the company to disclose this information. That decision would be up to the individual agent. My guess is that it is not common knowledge. Probably the immediate reaction on the part of the consuming public would be that

these top producers are being paid too much, but I don't know who is to judge something like that."

QUESTION #5: NIELSEN

My question concerns what industry associations could do to be more effective in preventing, not just reacting to, ethical disasters? How could these organizations work to lead change? One concern is the fact that a lot of effectiveness depends on the cooperation of the larger organizations with one another. However, the tenure of the leaders of these organizations, the chief executives, is short. Therefore, if you are to be an effective chief executive officer, and have to work with other chief executive officers, you only have three to four years to build relationships and get to work.

As much as I love education, we know that there are enormous limitations to the education solution. In fact, there is some evidence, in the form of surveys, that students are more ethical before they begin ethics training. To use a sports analogy, at times leagues have appointed strong commissioners who were selected by the owners to clean up the industry. Would something like this work in your industry?"

Jeff Bosco commented that he had seen changes for the better in the ethical environment in the insurance industry over the last several years. "I have been in the insurance industry for the last 20 years, and it's my personal opinion that it is better today than it has been in the past from an ethical standpoint. I don't see the amount of problems that you used to see 20 years ago. I see companies supporting new rules and regulations. I know that at a recent ACLI meeting there was a suggestion that perhaps there should be a national officer that oversees both federal and state regulations that govern the industry. But I see fewer problems in the insurance business than even five years ago."

Richard Nielsen said that what he just heard from Bosco about ethical progress in the insurance industry did not reflect what he has heard from members of other financial services industries. "If you are comparing the insurance industry with the financial services industry in general, it seems as though they are quite different. When you talk to people in New York in retail banking or the brokerage houses or in investment banking, they say behavior is about as bad as it has ever been. If this is the case, then how has the insurance industry been able to get better when the rest of financial services industry has not?"

Scott Perry believed that the successes of the insurance industry could be explained, in part, by the degree of the regulation. "About six or seven years ago, the winds started to blow in terms of heavier regulations on this business. So I guess that some of the regulations that we really weren't crazy about actually work."

He added that organization change needs to be led from the top of the organization. "I think that analogy of the sports commissioner is kind of interesting. The message that ethics matters has to be driven from the top of the organization on down. I think that there are a lot of things that organizations can do to improve the ethical fabric of their company. I don't think that there is a real shortage of ideas. I think that the question is how committed are the people at the top? Do they have good intentions but no follow through, because the problems of the day take precedence?"

Ron Duska thought the fact that the insurance industry was regulated on the state level, rather than at the federal level, may make a difference as well. "I don't know whether the executives here would agree with me, but I think the fact that regulation in the insurance industry is local has a lot to do with it. The insurance commission for Pennsylvania is here in Pennsylvania and can deal with local issues. They don't need to go to 'crooked' Washington."

Bosco raised the possibility that increased technology had helped the insurance industry remove possible temptations agents might have to act unethically. "We used to accept premium payments in checks or cash. The amounts were large enough so that an agent might want to play a game with it, but not large enough where it was going to be an institutional or systemic problem. With the technology we have now, we can receive these payments electronically, and the agents aren't handling the premium payments. So technology has taken some of the risk away of premiums not showing up where they should be."

QUESTION #6: JENNINGS

I have more of an observation than a question. In my experience working with companies, I have discovered that people at the top and those on the front lines have almost completely different perspectives. For example, I knew a CEO who was shocked to learn in a survey that those employees who are 28 and younger in her company believe that 100% of their performance evaluations were determined solely by the numbers. In her mind, this CEO had all of these beautiful platitudes about what counts and what doesn't count in terms of performance, and she was absolutely shocked by these results.

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I really do believe that we have faint signals warning us of ethical problems, signals that were present in other industries, but weren't acted upon quickly enough. Everyone tends to think that they are ethical or that they have been in business long enough so they don't need to be concerned about their own behavior. But those below you probably have some real concerns, concerns about issues that you may not even recognize as issues, and the message that they take from you is that you don't really care.

Ron Duska and Scott Perry comment on the issues.

I will finish with an example that I think gets at what I am talking about. A few years back I had just heard a CEO of an insurance company speak. He talked extensively about ethics and in fact, I asked for a copy of his talk when he finished speaking because I thought it was so impressive. One of our children passed away, and I submitted a claim to this insurance company. Those in HR at my university explained to me how to submit the claim and I did everything that they asked, including providing a death certificate. I then heard from the insurer that my daughter was ineligible since she was almost 20 years old and a full-time student at the time. My daughter had significant disabilities and was still in the public school system at the time of her death, so I sent the insurance company all of the information requested. Instead of receiving the death benefit, I got a letter asking for a copy of her death certificate, which I had already sent to the company when I submitted the claim. So I paid to have another death certificate issued and sent it to the company. Finally, I received a letter from the company stating that the circumstances of her death are "suspicious." The process went on for 10 months—for a $5,000 policy.

"You need to get to the people on the front line and engage them by giving them opportunities to openly discuss the ethical issues they see in the organization."

Scott Perry

Finally, I pulled out my legal letterhead and composed a letter that warned the company that their actions were approaching "bad faith" if they continued along this same path. The day after they received that letter, I got the death benefit sent to me with interest. It was sent via overnight delivery.

This is an ethical issue. The front-line employees who were dealing with me knew what was going on. They knew that this was a valid claim and that everything had been submitted. I know that somewhere along the line they had received instructions to stretch these claims out as long as they could. So we can talk a good game, but operationally, it may be very different.

Peter Golato expressed his concern with Marianne's situation. "I guess, from time to time, these things do happen. Insurance companies exist to pay claims. That is our whole reason for being. We literally need to work with our claims department, not to change attitudes, but to adjust the way that they are looking at their job. The marching orders are to find a way to pay the claim immediately, if not sooner, and don't delay since this is the moment of truth. We are sent the death certificate, and we will pay the claim within 24 hours. We do have the occasion where people take out larger policies and then pass away during the first two years, and we do have to look more closely at those situations. Even then, we need to be as expedient as possible. We are not trying to figure out how to deny the claim or lengthen the period or any of that. But I know that this sort of directive needs to come from the top."

Lisa Weber and Marianne Jennings listen intently.

Jim Mitchell noted that the larger the organization, the more difficult it is for leaders to know what is going on among the front-line employees. "On a regular basis, people would say to me 'Jim, I get that you really believe in these corporate values, so how can you let this thing go on?' At least 80% of the time I had no idea that thing was going on. 20% of the time, I could explain why I thought it was consistent with our values, but 80% of the time it gave me the opportunity to change one of our work processes for the better."

Scott Perry agreed with Marianne about the importance of giving people concrete examples and sharing stories about the kind of actions that exemplify the values management is trying to promote. "Marianne is right. You need to get to the people on the front line and engage them by giving them opportunities to openly discuss the ethical issues they see in the organization. You have either cultures by design or cultures by default. And the cultures by default are those sub-cultures that emerge which undermine the sort of ethical culture that you are trying to promote."

Jennings added that without concrete engagement shared with the front-line employees, it is impossible to build support for doing business in

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accordance with ethical principles. "It erodes the trust of those employees when they hear you saying one thing, but then also see you failing to correct their behavior or the behavior of other people when they fall short of these expectations."

Jim Mitchell and Jeff Seglin take in the commentary.

"... without concrete engagement with the front-line employees, it is impossible to build support for doing business in accordance with ethical principles."

Marianne Jennings

"In spite of all of the difficulties that they (executives) face, they are still trying to do the right thing and that gives me enormous energy and hope."

Richard Nielsen

CONCLUDING THOUGHTS

At the end of the day, the participants were asked to indicate what benefits they had received from participating in the Forum and what they would take away from the discussion to reflect on afterwards.

Brad Agle said that he would reflect on the desire of the executives in the room to do the right thing. "There are certainly some executives who are not necessarily motivated to do the right thing, but for those who are, how can I help them do that even better?"

Bill Laufer thought that he would take away "a much greater appreciation for the challenges facing the insurance industry. I knew very little about it coming into this Forum, and I still know little about it, but more than when I started, and I appreciate what I have been able to learn."

Peter Golato was grateful for the opportunity to listen to and learn from the other executives and academics. "The opportunity to just talk about this in an open forum, to hear what other people are thinking and how other people are handling these situations is extremely helpful."

Jeff Seglin was interested in seeing how both the academics and executives were challenged in similar ways. "It was interesting to see the academics trying to quantify things like ethical progress and buy-in and to learn that the executives are having the same difficulties. It is challenging on both sides, and it was helpful to see that all the way around."

Bill and Dagna Laufer on the final night.

Jim Mitchell said that he was always thankful for the chance "to rub minds with smart people who are trying to do the right thing." He also appreciated the opportunity to think more deeply on the topic of compensation. "Part of what you all did was to provide me with a better context for future thought on the subject. It's not just about compensation. It's about compensation in the context of distribution and the product."

Richard Nielsen was impressed by the executives' commitment to doing business in accordance with ethical principles. "I'm inspired by the executives. In spite of

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all of the difficulties that they face, they are still trying to do the right thing and that gives me enormous energy and hope."

Marianne Jennings was struck by the fact that no matter what industry you are in, the issues are the same. They have the same dynamics, the same layers, and people respond with the same behaviors. "I will continue to reflect on the 'dashboard', to see if it is possible to construct a mechanism that tells us where we are and where we are going."

"It is very refreshing to have people push back and challenge what I am saying or offer a different point of view."

Jeff Bosco

Lisa Weber was thankful for the opportunity to "think out loud" and for the openness of the conversation between the academics and the executives. "When we were talking about 'What we would do differently if we knew we had to disclose it to our customers', I think that raises a lot of interesting questions and presents a different way of looking at things. There is something very pure about that kind of questioning that I think is really terrific."

Jeff Bosco appreciated the opportunity to talk with the other executives and academics. "As executives, we typically have people who tell us what we want to hear or what they think we want to hear. It is very refreshing to have people push back and challenge what I am saying or offer a different point of view. I feel like I have a back-up team now that I can count on, so I thank you for that. It feels good since oftentimes you are out there by yourself wondering if you are making the right decisions."

Scott Perry welcomed the chance to spend the day talking about ethics and said that he came away with an increased appreciation of all of the stages a decision maker has to go through to make a good decision. "This discussion today reinforces for me the importance of the business ethicist having a seat at the table when we make these sorts of decisions."

Ron Duska thanked everyone for attending this year's Forum. "I started out saying that I do this because it is fun, and once again it has been fun. I really do believe that ideas have consequences, and while we might not be able to change systems, if we keep talking and thinking about issues long enough, it will help to a certain extent."

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James A. and Linda R. Mitchell.

The James A. and Linda R. Mitchell/ The American College Forum on Ethical Leadership in Financial Services

The American College Center for Ethics in Financial Services is the only ethics center focused on the financial services industry. The Center bridges the gap between sound theory and effective practice in a way that most ethics centers do not. Under the leadership of Director Ron Duska, PhD, the Center's mission is to raise the level of ethical behavior in the financial resources industry. We promote ethical behavior by offering educational programs that go beyond the "rules" of market conduct, help executives and producers be more sensitive to ethical issues, and influence decision making.

"By reflecting on these questions and recognizing ethical dilemmas when they arise, all of us are more likely to make good choices."

Jim Mitchell

The Mitchell Forum is a groundbreaking, one-of-a-kind event that underscores the Center's emphasis on collaboration and conversation among academics and practitioners. Jim Mitchell was recognized this year for his dedication to business ethics and was included in the "100 Most Influential People in Business Ethics" by *Ethisphere*, a global publication dedicated to examining the important correlation between ethics and profit. The list recognizes individuals for their inspiring contributions to business ethics during the past year.

The Forum is the cornerstone of the Center's activities highlighting how to bring industry leaders, accomplished producers, and prominent business ethicists together to reinforce the need to connect values and good business practices.

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270 South Bryn Mawr Avenue
Bryn Mawr, PA 19010-2196
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