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What Did the Maestro of the Reasonably Intelligent Orchestra Weigh?

Good evening.

As with my two previous papers, I struggled with selecting the subject. I considered many possibilities from the third phase of Andrew Carnegie's life, that of self delegated international peacemaker, to the Rockefellers for another view of philanthropy, to the changing role of the corporation in our society. I always felt that my paper for the SPHEX club should be one which took original research to expand my knowledge as well of that of the audience.

Well, put all that aside. After giving it much thought, I decided the most appropriate subject for tonight is "What Did the Maestro of the Reasonably Intelligent Orchestra Weigh" or the story of First Colony. With this room as the location of the SPHEX Club meetings for over 25 years, the role of George Stewart in the SPHEX Club and the role of First Colony in the Lynchburg Community, the subject does seem appropriate. I hope you will agree.

As I am sure you now realize, the maestro refers to George Stewart. George, with his love of music and his love affair with his "fiddle" from his days at Brooklyn Tech, often referred to himself as the maestro of the First Colony Orchestra---a most fitting metaphor.

The reasonably intelligent is something about which we often teased George. He was giving an interview to the Richmond Times Dispatch when asked the question as to the secret of First Colony's success. He replied that he surrounded himself with "reasonably intelligent" people and "let them do their thing". As you might expect, we never let him forget that label.

The reference to "weight" is quite humorous. Shortly after First Colony was purchased by Ethyl, the Wall Street Journal requested an interview to learn more about First Colony. George, Pete and I dutifully traveled to Richmond to meet with the young female reporter. After exchanging pleasantries, she said we are now "on record". With a big smile on her face, her first question was "Mr. Stewart, how much do you weigh?" Seldom in 25 years did I see George at a loss for words but now he was. After stammering a bit, he gave her some number. After she left, we began to laugh and he said he had his revenge---he said with that glimmer in his eye "I lied".

Everyone in this room knows what First Colony has meant to Lynchburg. I don't need to take time to tell you about that. What I hope to do tonight is to give you more than a dry factual history of First Colony; I hope to give you a flavor of First Colony and the leading role it played in the changing the Life Insurance industry, something of which most people in Lynchburg are not aware.

I make no apology for my bias. I do not bring a balanced and uninvolved attitude to this task. I will immodestly describe the successes and the prominent role of the company in the industry. Much will center on

George Stewart, his vision, wisdom, integrity and focused leadership but it will also focus on other members of the First Colony family who with George's direction made it all possible.

I will cover the period from its founding in 1955 to 1996 when GE purchased First Colony. First Colony today continues to be a fine company. It is a good place to work, employs more people in Lynchburg than ever, is a good community citizen, provides good value and security to the policyholders but it is a different company. In fact, as I understand it, the name First Colony will ultimately disappear and all products will be marketed under the GE name. Tonight, I will limit myself to the old First Colony.

Because of both the extensive subject matter and my tendency to talk, my challenge is to selectively choose what to include within the time restraints. I was afraid you would panic if I had pizza delivered at 10:00.

On November 22, 1955 a group of Lynchburg businessmen headed by Ed Horner incorporated a new Life Insurance Company named First Colony. I have always heard that a substantial portion of the money invested in First Colony came from the sale of Natural Bridge by Mr. Horner and other investors. Maybe as an omen of big things to come, Lewis Powell who was to become a Supreme Court justice did the original legal work for First Colony and sat on the board for many years. For those of you who know him, you can appreciate Larry Blanchard huffily saying he really did the work under Justice Powell's name. Another name familiar to many of you. Paul Sackett was a founding director and served until 1991. Paul was the longest serving board member.

The initial public offering was oversubscribed and \$2,000,000 in capital was raised, a large amount in 1955.

Many small life insurance companies were being formed at this time. Throughout its history, with the exception of a small amount of accident, health and disability insurance, First Colony sold only life insurance and annuities---betting only on the life expectancy of people, not their disabilities or health nor their driving ability.

The next ten years were rather uneventful with First Colony trying to do what everyone else was doing but "going nowhere fast". The company did become involved with Equity Funding, a name some of you may remember. This was a marketing company which was one of the first to sell a combination of life insurance and mutual funds. They did not have a life insurance company and used First Colony products in this package sale. They eventually formed their own life insurance company and stopped using First Colony. The bad news, and what they are most remembered for, is that they ended as a fraud with the principals going to jail.

In 1963, the Broadway Hale Stores in California decided to buy controlling interest in First Colony to market insurance to their customers. At that time, George Stewart was an insurance analyst with Blythe & Co, a Wall Street investment banker. He represented Broadway Hale in this purchase and became a board member of First Colony.

By 1965, Broadway Hale owned 51% of First Colony with the balance held in the open market primarily by the original Lynchburg investors. Early in 1965, between Broadway Hale, Ed Horner, Larry Blanchard, and a personal desire to leave New York, George and Bonnie Stewart arrived in Lynchburg. Within six months, Broadway Hale decided to sell their interest in First Colony. As George often said, "I moved my family here from a good job in New York to a company that by any measure was 'tiny'. Now, my client is bailing out... what do I do now?"

But he was never stymied for long.

The Broadway Hale block of stock was purchased by the Los Angeles Investment Co., an investment company with extensive property holdings in Los Angeles. Fortunately, much of this land had oil under it. LAI and its shareholders continued to hold a major portion of First Colony until 1982 when the company was sold to Ethyl.

That settled the ownership but it did not provide direction as to how First Colony was going to grow. George then made what could arguably be said to be the most important strategic move in First Colony's history. He purchased Great Eastern Life Insurance Company, a small 10-year-old life insurance company in Providence Rhode Island.

It was small and it was struggling. We often teased George that had he been surrounded by Pete Karras and Ron Dolan and all us "reasonably intelligent" people, we would have talked him out of this purchase in 15 minutes. The truth was that under any reasonable valuation, they were probably insolvent.

But in addition to bringing Ed Hunt to Lynchburg, it gave First Colony the marketing direction which would result in the successful growth of a company at the forefront of changing an industry. I will talk much more about that later but let me continue with the chronological corporate history.

In 1967, renovation of the Guggenheimer's Department store was completed and the current location, including the room we are meeting in tonight, was first occupied.

In 1971, LAI and First Colony merged with First Colony being the surviving corporation. While this transaction was interesting, in the interest of time, I will leave the details for another time.

In 1973, First Colony purchased American Mayflower, a New York domiciled company. Because of regulatory considerations, most smaller companies were not licensed in New York but operated in New York using a separate subsidiary.

In 1974, First Colony was licensed in Kansas, the last remaining state where we were not licensed. The company was now authorized to write insurance in all 50 states.

In addition to the home office here in Lynchburg, there was a regional sales and underwriting office in Los Angeles and the American Mayflower office in New York City. Interesting fact. In 1989 Barry Grosman became President of American Mayflower and moved to mid-town Manhattan. Barry was the most senior officer of First Colony who was a Lynchburg native. He grew up here on Rivermont Avenue. His father was Sam Grosman, a long-time roofing contractor here in Lynchburg.

In 1973, another very interesting event occurred. General Electric approached First Colony to purchase the company. Negotiations became serious reaching an agreement as to price. They were going to purchase it with stock. The week the transaction was to occur, the stock market, including the price of GE stock, went down significantly. No agreement could be reached on a new price and the deal never took place. As you might guess, had GE consummated the deal in 1973, they would have owned First Colony at a far different price than they were to pay 23 years later. But then it would have been a far different company and even Lynchburg may be a different place today.

In 1976, the Aachen and Munich Insurance Company, a large West German insurer, approached First Colony. They, like many European companies at the time, were interested in expanding throughout the world by purchasing minority participations in companies. After extensive negotiations, Aachen made a tender offer for 30% of the outstanding First Colony Stock at \$21 per share. The offer was successful. This resulted in a stock ownership distribution of approximately 30% owned by the LAI group in California, 30% owned by Aachen in Germany and 40% publicly held---a very good distribution.

Then came 1982. Sales and profits were booming. Prospects for continuing looked great. One problem. Because of reserve requirements, the business providing the profitable growth also created a need for large amounts of capital to sustain the growth. The shareholders, primarily LAI and Aachen, were faced with a dilemma. To continue this growth, new capital was needed.

There were three choices. They could contribute more capital and retain their current ownership percentage. They could obtain capital from new sources and have their percentage ownership decrease. Or they could sell the company. Both LAI and Aachen chose to offer the company for sale. With the help of the investment banking firms of Morgan Stanley and First Boston, the company was sold to the Ethyl Corporation of Richmond for \$270 million.

There are many interesting ironies associated with this purchase but I would like to expand on one---the reason for the sale.

We were selling a new product which was to play a major role in shaping First Colony. You will hear much more about that later. For now, it was a product where a premium, often quite large, was paid to First Colony. The company agreed to pay monthly payments for the life of the annuitant.

This was very profitable business that served a good social purpose and we were emerging as the industry leader. The problem was that for every dollar of premium we received, because of very conservative and outdated reserve requirements, we were required to establish a statutory reserve of \$1.60. Since we were writing millions of dollars of premium, you see the strain this was putting on our capital needs.

While other competing companies were limiting the business they were writing because of this surplus challenge, First Colony was scrambling to find ways to fund this need. One way was to reinsure the business with other companies in a manner such that they provided the necessary reserves. While we were selling these annuities at an unprecedented rate, George and I were running all over the country and Europe making reinsurance treaties to enable us to continue writing this business. It became increasingly obvious that the only long-term solution to this wonderful problem was to get more capital into the company. That is when the decision was made to sell and Ethyl purchased First Colony.

The irony is that within six months of the sale to Ethyl, the reserve law was changed and the reserve requirement of \$1.60 for every dollar of premium was lowered to approximately \$1.10. Obviously, this change drastically reduced the surplus need. The irony is that if this law had been changed six months earlier, the sale to Ethyl may never have occurred. Fate takes funny turns.

For the next ten years, First Colony was a wholly owned subsidiary of Ethyl Corporation and the company continued to grow and prosper. In 1991, the current home office building was completed at a cost of more than \$35 million.

In 1992, two significant events in the history of First Colony occurred.

On February 1, 1992 George Stewart retired after 27 years as CEO of First Colony. Everything said here tonight and much of what has been said in this room for 30 years attests to what he meant to First Colony; I won't dwell more on that now.

Second, Ethyl decided to make a public offering of 20% of First Colony and spin the remaining 80% off to Ethyl Shareholders. The public offering was made on Dec 8, 1992, exactly 20 years and one day after First Colony was merged with LAI. The initial offering was at \$28 per share. It was the most actively traded stock of the day reaching as high as \$31.25. As a result of this transaction, First Colony Corporation became a 100% publicly held company listed on the New York Stock Exchange. I believe First Colony was the only corporation listed on the NYSE at this time with headquarters in central Virginia.

Over the next four years, First Colony continued profitable growth. Being a public company listed on the NYSE and dealing with stock analysts and large shareholders brought a new and exciting aspect to the company. Things went well.

In early 1996, consistent with the rage of the time, the board of First Colony decided to explore possible strategies to maximize the value to shareholders. Again, investment bankers were retained to assist in this study. As a result of this study, a decision was made that the best alternative for the shareholders was to seek a buyer for the company.

Given First Colony's record and its stature in the industry, this was clearly the "hottest property" in the life insurance industry. A very lively sales process began. After many people "kicked the tires", the field was narrowed to four potential purchasers. These four began serious due-diligence investigations. One company sent a team of 65 people here to evaluate the company. Everyone involved was trying to keep the identity of potential purchasers a secret but as we told the investment bankers, we don't think a company can bring 65 people to Lynchburg and retain anonymity.

After a very active and intense bidding process, General Electric emerged the successful bidder and purchased the company for \$36.16 per share.

As you might imagine, there were many interesting anecdotes surrounding this process. I will mention one which I think is an interesting commentary on technology. At the end of the process, there was one Board meeting to make the final decision as to the successful purchaser. This meeting was held on a Sunday in August. Present, in a fashion, were the Board of Directors and the Investment Bankers. The Board consisted of ten people. The meeting lasted nearly eight hours and it was quite an experience.

The interesting sidelight was that no two of those directors, other than we here in Lynchburg, were physically in the same room. It was all done through an eight hour conference call. The wonders of modern technology.

There you have the corporate history of First Colony. Interesting but it doesn't begin to tell the story. We could spend more time on the history but we would miss the essence of the company.

Next, and I know it will come as no surprise to you, I want share with you some numbers. These numbers show the growth of the company both in absolute terms and relative to the life insurance industry.

The first table shows the Assets of the company. This is one of the best measures of a company's size. In 1971 when First Colony merged with LAI, total assets were \$60 million. As you see, the company grew from less than \$350 million in 1980 to over \$11 Billion in 1996. This represents an annual growth of about 25%. If the truth were to be known, for George Stewart life insurance was incidental to his goals. What he was really interested in was accumulating assets so he could have more money to invest---as you can see, his dream was realized.

Another significant measure of size for a life insurance company is the face amount of the life insurance in force. It is somewhat unusual for an industry to measure size by its liabilities but life insurance companies do. What this number means is that if every insured died, the company would owe death benefits in this amount. Obviously, if that occurred, the company would be out of business---a risk certainly but as insurance risks go, life insurance is probably the least risky.

Assuming the original risk selection is consistent with the pricing, once the policy is in force everyone's interests are aligned. Few people want to die. This is different from many kinds of insurance where the interests of the insured and insurer often are not aligned. Disability insurance may be the best example of this. The number in any group who will die is very predictable based on past experience. Again, unlike many other types of insurance, it is perfectly clear when a claim is payable and the amount of the claim. And the larger the block of business, the less chance of significant adverse random fluctuations in claims---the life insurance risk can sound quite large but in reality is very manageable.

Realize that this risk amount grew from \$8 billion in 1980 to \$175 billion in 1995 and almost \$200 billion when GE purchased the company in September of 1996. The bottom table shows the amount of insurance in force for the 10 largest insurers by this measure. As you can see, First Colony ranked 9th in the industry and was in some rather elite company.

A quick word about the number of life insurance companies. There are about 2200 life insurance companies in the United States. In reality, there are about 600 companies which actively sell life insurance to the public. The other 1600 are subsidiary companies of other life insurance companies, captive companies established by banks and other companies for specific needs, often tax related, and various other companies which are not actively engaged in selling life insurance to the public.

The next table shows the new sales of life insurance also measured by face amount. You see the growth of annual sales from less than \$2 billion in 1980 to more than \$41 billion in 1995. Again, the bottom table shows the sales for the 10 largest insurers. In 1995, First Colony was the fifth largest seller of "death benefit" in the industry, more than Metropolitan Life.

I might mention here that over the years First Colony has insured many well-known people in all walks of life including two presidents, Reagan and Carter. Were it not for confidentiality considerations, Ed Hunt would regale you with stories about the celebrities we insured.

Keep in mind that these last two measures reflect only life insurance and do not include annuities which also represented a large part of the company.

I will talk about the fourth sheet, Immediate Annuity Sales, a little later.

You can see that First Colony compared favorably in size with those companies you know as household names.

Just a few more statistics.

In 1995, there were over 40,000 new policies being issued every quarter.

By 1995, there were approximately 800,000 life insurance and annuity policies in force. Including policyholders, shareholders, agents and employees, First Colony touched the lives of over a million people.

In terms of employees, First Colony grew from 200 in the early 70's to over 400 in the mid 80's to 700 in the late 80's to approximately 1200 in 1996. Today, over 1500 are employed by GEFA in Central Virginia.

You have now heard many facts but I promised you more than just facts. To understand the company and its accomplishments, you first must understand the revolution which occurred in the life insurance industry from 1965 to 1995.

In 1965, nearly all life insurance in the United States was sold by an agent in a "one on one" sales situation with a client. The agent sold a policy offered by the company which he or she represented. It was most unusual for an agent to sell a policy for a company other than his primary company; in fact many companies did not allow its agents to sell another company's product.

Over 85% of the life insurance was sold by mutual companies which, as you know, have only policyholders and not shareholders. Many of these were started in the mid to late 1800's. They were formed, not as profit making ventures, but to provide insurance protection to the policyholders---there are no shareholders. Thus, nearly all insurance sold was mutual insurance where a premium based on very conservative assumptions is collected and a dividend is paid at the end of the year if actual experience is better than the assumed experience.

There was little or no competition among companies. The only competition was among the agents. Most individuals purchased insurance because of a relationship with the agent, not the price, the company or even the policy terms. The buying public knew little about life insurance, was uncomfortable talking about it, perceived that all companies were alike and that it made little difference from which company you purchased insurance.

Life insurance was not purchased for potential investment return. Even by those few people who considered the financial implications of a life insurance policy, it was correctly assumed that the actual investment return on a life insurance policy was not good but it provided insurance and it was a very safe investment ranking with government bonds---little reward but virtually no risk.

Nearly all insurance sold was what we call “cash value” or “whole life” insurance as opposed to term insurance. A quick actuarial lesson. The difference between these two types of insurance is the premium structure. In cash value insurance, the premium is designed to be level for life. To accomplish this, extra premium must be paid in early years when the risk of death is relatively smaller in order to build up a fund to pay the higher cost of insurance in later years when the risk and therefore the necessary premium is much higher.

In term insurance, the premium charged is consistent with the current mortality risk. This results in an increasing premium as the age and probability of death increases. At any age, there is a premium sufficient to provide life insurance. The problem is that this premium becomes very high with increasing age. Because of this premium increase and the risk of antiselection to the company, these policies were not written for “whole life” but rather for a specified “term”--- thus the name term insurance.

Since its beginning, the entire life insurance industry operated on the basic assumption that “Life insurance is sold, not bought” or that left to their own initiative, few people would proactively buy life insurance.

By 1996, each one of these market realities had dramatically changed---the life insurance industry had gone through a revolution, not just a normal evolution.

Much life insurance was still sold by individual agents working directly with the client but more and more was sold through other financial planners, in employer-employee relationship situations, through the mail, over the phone, over the net and in many other creative ways.

Where an agent rarely sold a policy for other than his or her primary company, today the typical agent who still has what they would consider a primary company probably sells less than 50% of his business with that company. Many agents consider themselves totally independent and do not have what they would consider a primary company.

As the differences among life insurance companies and the products they offered grew, it became clear the company was important and that no one company could be all things to everyone. The professional agent committed to doing the best job for the client and for his own economic success needed to sell products offered by many companies, not just one.

Today, the majority of the life insurance sold is sold by stock companies rather than mutual companies. This is a result of the growth of new stock companies but also because many, possibly even most, of the old large mutual companies are demutualizing to become stock companies. The motivations behind this “rush to stock” are most complex and controversial and beyond the scope of tonight.

The majority of insurance sold today is term insurance rather than cash value. It is often sold in conjunction with other investment vehicles offered by the insurance company or other products offered by the agent. Also, most policies are designed to pass the investment return risk to the policyholder rather than providing the long-term investment guarantees of the traditional cash value life insurance contract.

The market for life insurance, especially term insurance, is now fiercely competitive. One thing which encourages this competition is that it is far easier to compare the cost of term insurance from many companies. While sales over the net are still in the infancy, there are many sites easily available where an individual can purchase insurance or at least compare what he or she is being offered by an agent.

It was these realities that changed the industry and it was this revolution which First Colony led. First Colony was clearly a major catalyst in bringing about every one of these changes. That is the message I want to leave you with tonight.

To elaborate, let me return to the purchase of Great Eastern Life Insurance in 1966.

At that time, it was clear to certain visionaries that an opportunity existed within the life insurance industry for some innovative product and marketing ideas. One group promoting change was a few European reinsurers who realized there was an underwriting opportunity in the US. The big mutual companies were very conservative in underwriting individuals for life insurance. A hangnail might result in a higher premium and something a little more serious may prevent obtaining any insurance.

Since, for many reasons, it was impossible to get companies to change this underwriting approach, the only way to take advantage of this opportunity was to encourage and enable an agent to offer a product for a company other than his primary company---another heresy. But this is exactly the marketing approach which Great Eastern was using.

There were individuals throughout the country who were becoming independent General Agents. What this meant was that they represented more than one company, they were a "wholesaler" of life insurance. Their customer was not the individual buying life insurance. Their customer was the agent selling life insurance. For example, the local agent for Prudential had a client who needed \$100,000 of life insurance. The problem was that he had a history of high blood pressure and therefore the Prudential would offer coverage only at an increased rate or possibly not offer any coverage.

This new general agent would go to this Prudential agent and say, "I represent a number of companies, some of which specialize in insuring individuals with a less than perfect health history. Let's see if we can get a better deal for your client. If we can, everybody wins. You will have done the best job possible for your client providing insurance at an affordable price. And you will be able to place more business with more clients thus helping your income."

And thus the birth of what became known as the Brokerage Distribution System.

Sounds simple, doesn't it? But then, in retrospect, innovation often appears simple and obvious.

With the purchase of Great Eastern, First Colony started down the path which enabled it to become the premier company in this new distribution system. Our primary customer was the general agent. We competed in his or her office with other companies. I must acknowledge that we have one of these general agents present with us tonight---she also happens to be my life partner. We needed to create a combination of product, underwriting, service, compensation and relationship which made it easy and desirable to put the business with First Colony and not our competitors.

And so at the heart of the First Colony story was a marketing approach new to the industry.

Over these 30 years, First Colony became a household name in the insurance industry. It never achieved that recognition among the consuming public but it did in the industry. To sell life insurance for a company, an agent must be specifically licensed with that company. The largest companies such as Prudential or Metropolitan, at their peak, would have had maybe 15,000 agents licensed with them.

In the industry, there were approximately 400,000 licensed agents. In 1995, more than 100,000 of these agents were licensed with First Colony, the largest number of agents licensed with any one company. 25% of all agents in United States were licensed to sell with First Colony. They might only sell one policy every two years but they were able to sell a First Colony policy when appropriate to fit their client's needs.

At the core of the new marketing approach was also a product revolution. This started with the more aggressive underwriting or risk selection of the companies. This gave the agent a legitimate reason to sell business for other than one company. He or she was doing it in response to needs of his client. First Colony became known as the company for the impaired risk or the client with some past or current health problem.

While encouraging that aspect of the business, First Colony moved quickly to find other ways to differentiate itself from the traditional companies again to give agents a reason to place their business outside their primary company. This was accomplished by offering products and services different from what the traditional mutual companies offered.

The clearest example of this was term insurance. This was a product which most people could easily understand and recognize the need for it. But the traditional companies had always avoided term insurance because they believed it was not as good for the client nor as profitable for the company or the agent as "cash value" insurance.

Brokerage companies, led by First Colony, brought about this change in the industry. The good news is that the real winner, in addition to companies like First Colony and the agents who sold term insurance, was the consumer of life insurance. Today, many individuals can purchase one year of death benefit coverage for 25% of what they could purchase the same coverage for 25 years ago. Again, the sales figures we looked at earlier show that First Colony was a leader in this revolution.

But term insurance was not the only product innovation for First Colony or other companies. There were other products, often centered around tax considerations, which companies could offer to differentiate themselves from others. In this regard, the First Colony strategy was to be quick in reacting to product opportunities. First Colony positioned itself as a manufacturer of life insurance and annuity products for sale through independent distribution channels.

Keep in mind, there is no such thing as a patent in the insurance business. We constantly monitored the market to identify new products and ideas offered by other companies. When a new idea appeared which was attractive for First Colony, we would quickly move to produce it. First Colony developed the product development, legal, data processing and marketing structure which enabled it to react quickly to these product opportunities. For First Colony product efforts, reaction was not a bad word, it was the operative strategy.

An ideal market situation for First Colony was to have a product offered by 5 or 10 visible companies including First Colony but not by the other 600 companies. The 10 companies which had the product would create a demand. First Colony was then the company through which the agents of the other 590 companies could provide that product to his or her client.

Another revolutionary change in the life insurance industry which occurred in the 80's was in the area of investments and the role of financial strength as a competitive consideration. As discussed earlier, because of both regulation and company policy, life insurance companies were traditionally quite conservative investors. They were correctly perceived as the investment equivalent of government bonds---low return but ultimate safety. Also, the company assumed most investment risk and long-term returns, while low, were guaranteed; the insured was at little risk.

In the 80's this all changed. Companies became more aggressive investors, especially in the area of junk bonds and real estate, and at the same time passed more of the investment risk on to the policyholder. While this approach may be appropriate, companies sometimes did not communicate this change to policyholders who continued to retain their image of life insurance companies as conservative but risk free investors.

Again, First Colony was in the middle of this change and positioned to take advantage of the opportunities which this change presented.

Knowing George Stewart, I don't need to tell you of his investment expertise and his solid, conservative approach to investing. George believed that if you managed the assets carefully, you would avoid disaster. He often reminded anyone who would listen that the only reason a life insurance company ever failed was because of asset mismanagement or fraud, not underwriting or expenses or anything else.

From the beginning, First Colony's investment portfolio looked different from the average company. George believed the only appropriate investments for a life insurance company were high quality, fixed income instruments and usually, the longer the better. Traditionally, the asset side of the First Colony balance sheet consisted of more than 95% of high quality bonds and preferred stocks. For the industry, this number was 75% with the balance in mortgages, real estate and equities.

This attention to assets and the general risk management enabled First Colony to be recognized as an industry leader in another area---financial strength.

There are many indications of this reputation but the clearest is the A. M. Best rating. The A.M. Best Company has been providing financial evaluation of insurance companies for more than 50 years. In 1992, they introduced a new rating scale under which the highest rating was A++. This rating was given to only 45 life insurance companies: 38 large mutual companies and seven stock companies. As you might have anticipated, First Colony was one of those seven stock companies and its impeccable financial strength was recognized throughout the industry.

One example. I had a close friend who was the CEO of a large life insurance company. When his mother needed an immediate annuity to guarantee income for life, he purchased it from First Colony because of its reputation for financial strength.

At one time, financial strength was not an especially important point of company differentiation. All companies had a relatively conservative balance sheet and there was little difference among companies. This environment changed drastically in the 80's. It became clear that some very large, well-known and respected companies did not have the balance sheet strength usually associated with large life insurance companies. There were household name companies which were at significant financial risk.

As agents and customers became aware that financial strength might be an important point of differentiation among companies, they would search for a company with impeccable financial credentials. There were many, remember 45 companies rated A++ by A.M. Best, but most of these companies did not make their products easily available to agents of other companies.

What company had the highest financial strength ratings and actively solicited the business of all agents? Again First Colony was positioned in the right place at the right time. This emphasis on financial strength was a significant impetus for the growth in the 80's and continues to be an important factor in company differentiation.

I have spent much time talking about life insurance, the revolution in the industry and First Colony's role in that revolution. But that is only part of the story. There is more.

One day in 1978, a general agent in California who represented First Colony was approached with a new idea. They chose First Colony because of its reputation as an underwriter of insurance on individuals with some history of health problems. The General Agent called and wanted to know who to talk to about this revolutionary new idea. The General Agent was referred to Mike Bodtker, an actuary who worked in the area of new product development.

Mike himself was an interesting story. He was very intelligent and very articulate but was undoubtedly the most eccentric human being I have ever met. I could tell Mike Bodtker stories all night but let me share only one to give you some idea of Mike. Mike often wore monogrammed shirts to work---not unusual except that they were not his monogram. He bought all his clothing at flea markets and the monogram on any shirt was purely random.

Mike invited them to Lynchburg to tell us more about the idea. They arrived and Mike, George, Pete and I, met with them. It was an interesting idea which I will explain in a minute but after listening and thinking about it, the three "reasonably intelligent guys", George, Pete and Ron decided we were not interested in this product. We told Mike to communicate this decision to them. Case closed.

About a month later, Mike walked in and said, "Well, we sold our first settlement annuity". We said, "Mike, you don't understand, we decided to not pursue this business." He shrugged his shoulders and walked out of the office.

Another month passes; Mike comes in and says, "Well, we sold our second one". It became clear that we either had to fire Mike or get in the business. We thought about it and decided to fold our hand and get into the business.

The policy was what is known as a settlement annuity. These are immediate annuities where a single premium is made to the company and the company is responsible to make monthly payments beginning immediately and continuing as long as the annuitant is alive. Obviously, this is the exact opposite risk from life insurance. Life insurance companies had always sold immediate annuities but never sold very many and certainly never expended any marketing effort on them.

But what was different was that a settlement annuity is sold to a casualty insurance company to fund the settlement of a claim against the company. The other unique twist is that often the annuitant receiving the lifetime payment has a significant health condition which lowers their life expectancy. While for life insurance, this would result in an increased premium, for an annuity this health impairment might well justify a lower premium. That is why First Colony's underwriting expertise was attractive.

For example, an individual is involved in an accident and everyone agrees that a payment of \$100,000 to the injured party is appropriate. Historically the casualty insurance company would write a check for \$100,000 and the transaction is complete. The idea of the settlement annuity is to replace that single payment with a series of payments over the lifetime of the injured party.

In many cases, the injured party has lessened or lost their ability to earn an income. Replacing that loss with a lump sum current payment is often not a good solution. Studies showed that in far too many cases, the money was gone in 2 or 3 years but the impairment remained. Every injured party had a brother-in-law with a great investment idea or they just had to have that new BMW.

In addition to the desirable income security, there are substantial tax advantages to a settlement annuity. This makes them an attractive alternative even for the most sophisticated and responsible investor. For the casualty company, it enables them to settle the claim and get it off their books.

From a mortality risk point of view, it balanced to some small degree the mortality risk inherent in a life insurance product. From an investment point of view, the risk to the company is of guaranteeing an interest rate or investment return far into the future. While this involves significant risk, one of the biggest dangers of a long-term interest guarantee is not present in a settlement annuity. That is that the annuitant does not have the option to surrender the policy at a defined "par" value. There is no call on the principal. The only cash flow requirement is a series of future payments completely defined at time of issue. The only deviation from that defined flow is when death occurs and the payment stops. Even if people live longer than expected, the adverse experience effects the company over a long period of time unlike life insurance where adverse mortality experience can have an immediate and devastating effect on current earnings.

For First Colony, settlement annuities were an outstanding opportunity. At this time, there were only three other companies writing settlement annuities. First Colony was in this market from its very beginning. This was the product which created the need for surplus and resulted in the sale of the company to Ethyl. It was a very profitable product, took advantage of our expertise and reputation, and satisfied a real social need.

Now you can see why it was so important for First Colony to do what was necessary to remain in this very attractive market in 1982. No new companies were entering this market and the existing writers were limiting the business they would accept. First Colony did what was necessary to continue to write the business and firmly established its reputation in the industry. It is the only company which has been in this business since its beginning and continues to be acknowledged as the industry leader. It has been among the top three writers of settlement annuities every year since 1978 and is the only company that can boast of that consistency.

The industry trade organization, the National Structured Settlement Trade Association was founded in 1982 at a First Colony sales conference at the Greenbrier Resort. The current president of that organization and the person acknowledged in the industry as the "home office guru" was going to be with us here tonight but needed to go to Washington. Andy Larsen has been in this business for 20 years and responsible for this business for First Colony for 10 years.

This line of business provided the strong asset growth of the company. It fulfilled George's fantasy---it gave him assets to invest and not just assets but assets to fund long term liabilities with no call on the principal---a need most consistent with his love of long term, high quality, fixed income securities.

Not only did First Colony become the leader in the settlement annuity market, this positioned First Colony to be a leader in another of the fastest growing segments of the life insurance industry today. Traditionally, life insurances companies have provided financial protection against the risk of dying too soon. In immediate annuities, the insurance company protects against the risk of living too long.

In the past, when a person retired, they would receive a defined monthly pension payment for as long as they lived. Today, many individuals receive a lump sum payment from their profit-sharing plan, a 401(k) plan, or their defined contribution pension plan. They are then responsible for investing this sum to provide an income for life.

At first, most individuals are excited about this opportunity and are confident that they can manage this money to provide themselves a secure lifetime income. But at some point, most individuals realize they may not be able to manage these investments forever and become concerned about the possibility of outliving their income. They fear not that they will die too soon but rather they will live too long.

With the demographics of an aging population, you can see the growth potential. This market is just now beginning to be widely recognized as the outstanding asset growth opportunity in the industry---and First Colony or now GEFA because of the First Colony roots is positioned to take maximum advantage of this opportunity.

If you will, look at the last sheet in the package I passed out earlier. You will see that in 1995 First Colony was the second largest writer of settlement annuities and the third largest writer of retirement annuities in the industry. When you combine the two immediate annuity products, First Colony was clearly the largest provider of individual immediate annuities in the industry. While I don't have current figures, I am confident they are at or near that same position today.

You have heard about product and distribution and financial strength but there is even more to the story.

Another key ingredient in the success formula was its stature in the industry. When I first came to First Colony, I would go to an actuarial meeting, certainly an exciting place, and someone would look at my name tag and say "First Colony in Lynchburg Virginia---who, where?". Not many years later, at the same meeting, when you said you were with First Colony, people would gather around and pepper you with questions as to how you do this or why do you do that. First Colony people were in demand to speak at industry meetings, serve on industry committees and to be active in professional organizations.

Not only was it industry organizations but it was the rating agencies. I've talked about A.M. Best but Moody's, Standard & Poor's and Duff & Phelps were all active in rating life insurance companies. Each had a relationship with and respect for Pete Karras personally and First Colony second to none in the industry. They knew Pete and the company to be of the highest integrity and could be confident that they knew the truth, be it good or bad. They respected the technical competence of the entire company and often called upon Pete and others for opinions on everything from industry trends to the rating of individual companies.

This respect was possibly most evident in the relationship with the state regulators. Life insurance companies are regulated by each individual state. As you might guess, the quality of that regulation varies greatly among different states. But among the regulators, First Colony was widely recognized and respected as a leading company in product innovation providing good value and financial security to consumers. Again, its people were known to be knowledgeable and of the highest integrity.

Two good examples of this reputation. The New York Insurance Department is probably the strongest and most competent insurance department in the country. Over the years, they came to know our Steve Smith. Steve's personality is beyond tonight's talk but suffice it to say, he is the "poster boy" actuary. Very competent, very honest, and very persuasive---some would say very stubborn. They forged a relationship with Steve where they would routinely call him to talk about new ideas, changes they were contemplating and trends they were seeing in the industry. They knew they would get an intelligent, well considered opinion from Steve regardless of the implications of that opinion on First Colony or American Mayflower. That is the kind of relationship Steve and First Colony had with the regulators.

For many reasons, the stature of First Colony with the Virginia Insurance Department again was second to none. The best indication of this relationship is an incident which occurred in the late 80's. The department was faced with the unpleasant and difficult task of taking over a large company which they determined to be in serious financial trouble---resulting from poor asset management I hasten to add. It was a company with which we were quite familiar and the Virginia commissioner had talked with us extensively prior to this decision. One Friday, we received a call saying that they were going to take over the company unannounced on Monday morning and would like George, Pete and me to be there with them. I think that says it all.

I have talked a lot about the tangible aspects of First Colony---such things as distribution, product innovation, financial strength and investment philosophy, industry reputation and technical competence. But there was yet another important ingredient in the success formula.

Although articulated in many ways, our strategy was always two-pronged. First, to provide a balanced package of product, underwriting, service, compensation, and financial strength so that there was no reason to not do

business with First Colony. And second, to create a personal relationship with the customer, especially the General Agent, such that First Colony was the company of choice.

This is more difficult to explain but First Colony was clearly successful in doing exactly that.

Two objective measures of that success. In 1989, NAILBA, an industry organization of Brokerage General Agents commissioned an independent study which determined, among other findings, that First Colony was considered the most visible company by a 2 to 1 margin among agents who broker business. Second, a group of 23 General Agents who belonged to their own "study group" organization asked the question of its members "If you could represent only one company, who would it be" The vote was unanimous---First Colony. Ironically some of those saying First Colony did not even represent us---we were often quite selective in picking who represented us.

As the currently popular phase goes, this relationship building was a 7/24 (or is it 24/7) task. It was a part of everything we did.

I could site many examples of this relationship building many of them seemingly quite small but still important, but let me specifically discuss one.

One of the ways in which we built this relationship with the General Agent was our incentive travel journeys. The life insurance industry is famous for taking agents on trips as a reward for sales performance. These are usually annual trips to the beaches of Hawaii or the golf courses of the Greenbrier. The General Agents who represented First Colony were routinely offered trips like this and had to pick and chose which to accept. Most of them also had the personal resources to visit these places on their own.

Rather than adopting a "me too" posture, this was recognized as another opportunity to differentiate First Colony from the other 599 companies. Instead of offering annual trips to similar destinations, we decided to make the trips a memorable event. Instead of every year, there would be a trip every 5 years but the trip would be one to remember. The trips were designed to take people to places they would not go on their own and to provide an experience far beyond a round of golf, a morning of shopping or an afternoon at the beach.

The first trip occurred in 1974 when about 200 general agents and guests went to Israel for 10 days. Unheard of in the industry. In 1980, we took 400 people to Kenya, in 1985 to China, Hong Kong and Tokyo, in 1990 to Bali and Bangkok with an extension trip for the largest qualifiers to India and Nepal and in 1995 to Morocco and Istanbul with an extension trip to Moscow and St. Petersburg. GEFA continued this tradition in 2000 with a trip to South Africa.

This approach worked wonders in relationship building. The trips became legend in the business. About six months before the announcement of the trip, anxious speculation would begin as to where First Colony was going this year. The question for most general agents was not if they would qualify but only a question as to how many trips he would qualify so he could take his staff or selected agents. We had smaller GA's who could not reach the qualification level but would offer to buy trips from the company to be able to attend.

They returned laden with gifts and souvenirs. At their next neighborhood cocktail party, when asked what they had been doing lately, they proudly said, "Oh, I just returned from Kenya. First Colony, this wonderful company with which I work took 400 of us on a photo safari." Remember, this was in 1980 when no one went to Kenya. What a way to create and cement a relationship.

But this relationship building was at the core of First Colony. The most important customer was that group of 50 to 100 general agents who provided over 90% of our new business. In many situations, this general agent decided whether a specific application went to First Colony or company X.

To repeat the strategy, by the combination of product and service and personal relationships, we strived to create an environment where the general agent's mindset was to place the business with First Colony when possible. I know the general agents would agree that this strategy was successfully realized. With that group, over the years we built a close personal relationship. As "hokie" as it sounds, they became family and not just a life insurance salesman.

The last aspect I would like to address discuss is possibly the most important one. And I may get a little "preachy" or "emotionally involved".

The people and the company they created.

First Colony was a place that cared about and nurtured people. It was a place which allowed individuals freedom of expression---remember Mike Bodtker---it gave them latitude to be creative. It enabled them to grow professionally and personally. And above all, it gave them an opportunity to make a difference. When people went home after a normal busy day, when another group of General Agent's went home from a First Colony University, when we returned from the annual NAILBA meeting where First Colony was king, when we finished another successful year, people felt good about themselves. What a wonderful feeling.

Give me one more minute to site some of the people successes.

Shirley Smith joined First Colony in 1960 after graduating from Appomattox High School in the commercial curriculum. She began as an entry-level clerk. 25 years later, with no formal education or training, Shirley was vice-president of claims for First Colony and was elected the president of the International Claims Association, the industry group of life insurance claim professionals from throughout the world. What an accomplishment to receive this recognition from her peers.

Linda Mayhew joined First Colony in 1966 again as an entry-level clerk with a high school education from Johnson City Tennessee. Linda retired last year as a Vice President. She was selected by her peers to serve on the board of the American College of Life Underwriters, the most prestigious group of marketing professionals in the industry. They bestow the CLU designation which is the highest professional achievement for a life insurance agent.

Ed Hunt, here with us tonight. Most of you know Ed as a wonderful community citizen and a calm crusader on the Boonsboro links. But did you know that Ed Hunt is one of the premier underwriters of life insurance in the country? Here is an individual who has been responsible for underwriting policy and the implementation of that policy at First Colony for over thirty years. In those years, mortality experience has been profitable in all but two years. I can tell you that is a record which may be unmatched in the industry. It is even more impressive when you realize that during those years First Colony was clearly on the cutting edge of underwriting. Most underwriters move from company to company staying a year or two ahead of their decisions.

Carlos Whaley started his data processing career in the Marine Corp. He led First Colony through the data processing and information revolution playing a major part in the company successes. With our strategy, reaction time and ability to support new ideas were very important. Carlos never once told me or Butch Britton that we couldn't do that product because we couldn't support it. His answer was always, "we can do it."

We once approached a large company to encourage and assist them in offering a new product we were selling. Their top management expressed a strong interest in working with us but they determined that even with our help they could not do the product for at least two years. Carlos saw to it that we were never in that position.

I've mentioned Steve Smith and Andy Larsen and Mike Bodtker and Barry Grosman. I could go on and on but suffice it to say, the people ingredient was a circular relationship---people made First Colony special and, in turn, First Colony gave people a chance to be special.

Some months ago, Bill Johnson gave a paper to this group posing the question as to whether a corporation has a soul.

I will tell you that if a corporation can have a soul, and I believe it can and must, First Colony had a soul. Its soul was created by the people.

Consistent with today's mantra, it cared about its shareholders and certainly did its best to create shareholder value. But that wasn't the only care.

While ranking responsibilities is always dangerous, we believed our first responsibility was to the policyholder. The life insurance contract is unique. It provides long-term financial guarantees to the policyholder. Based on that guarantee, it is the first responsibility of the company to be there in 10 or 20 or 50 years to deliver on that promise. The policyholder is not someone who put his or her money with First Colony as a speculative investment. They put it there to provide financial security for the future and the company must deliver on that promise.

It cared about employees. Shareholders invest capital. Employees invest themselves in the company and deserve a return on that investment: the respect and care of the company.

Finally, no individual or corporation operates in a vacuum. The company does have responsibilities to the community and I think you would all agree, First Colony believed and lived that responsibility.

It was a balanced caring among all these stakeholders (to use a thoroughly modern word) which made First Colony successful in both economic and human terms.

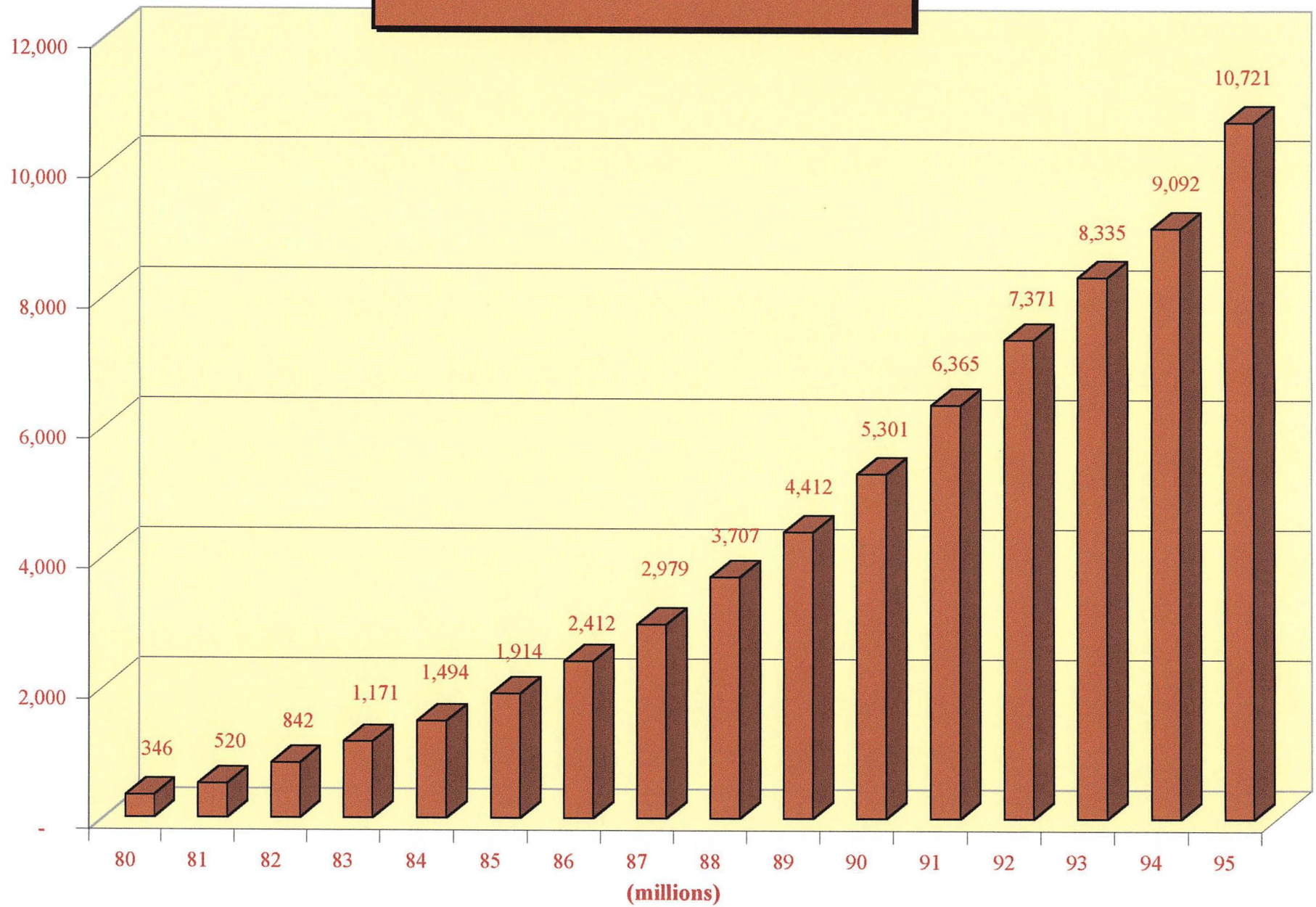
I better quit there before I get downright maudlin but I will leave you with a question. In today's reality, "Can a company so conceived and so dedicated long endure"? I'm not certain of the answer but I have a feeling we may visit that question in this room one night two years from now.

When I was talking with Pete regarding tonight's presentation, he came up with the perfect ending.

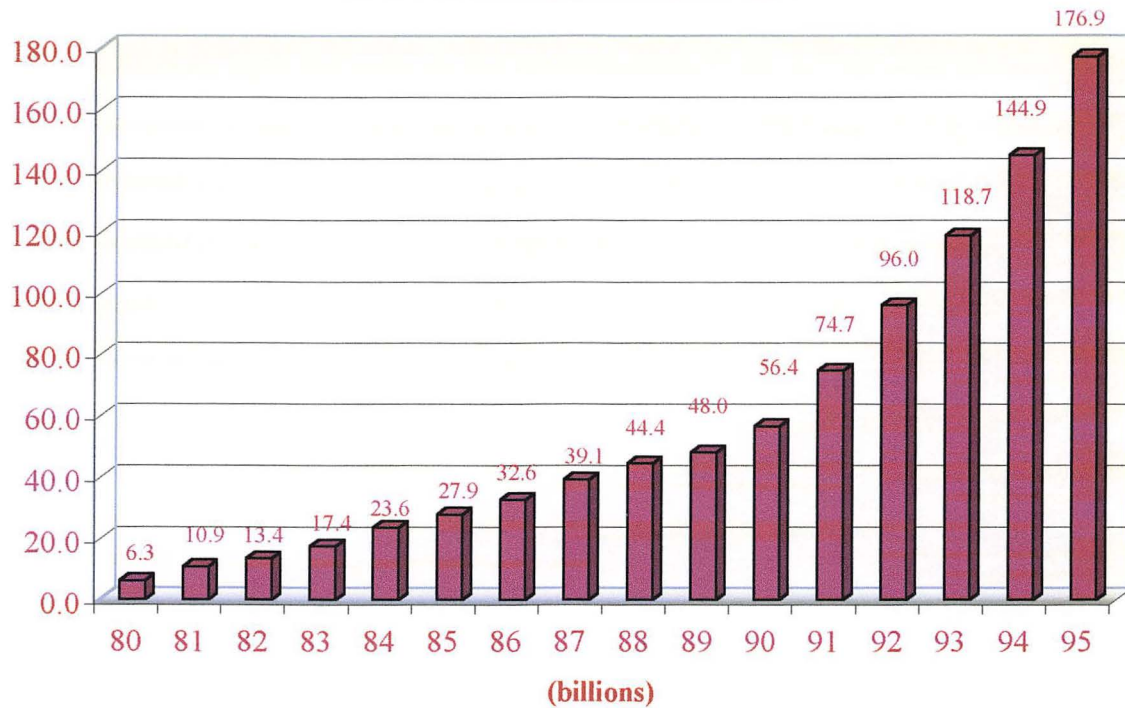
"Not bad for reasonably intelligent people."

Thank you for your attention and I would take any questions or comments you may have.

First Colony Life Assets



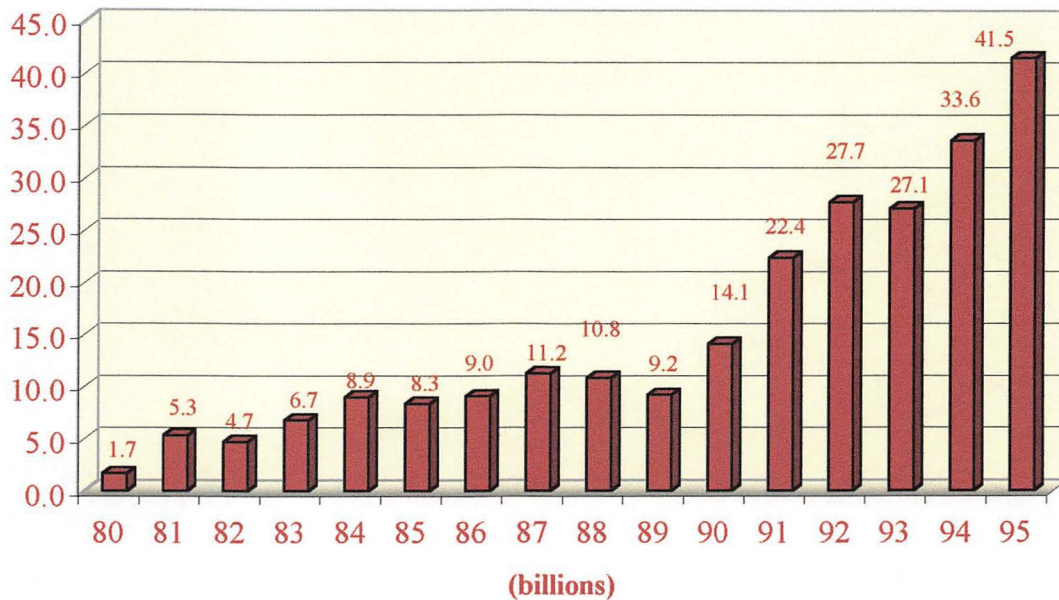
First Colony Life Life Insurance In Force



1995 Top Ten Life Insurers *Individual Ordinary Life In Force*

	(billions)
1 Prudential	\$387.8
2 Northwestern Mutual	380.1
3 Metropolitan Life	337.7
4 Transamerica	326.7
5 Primerica	319.1
6 New York Life	278.8
7 State Farm Life	272.6
8 RGA Reinsurance	180.4
9 First Colony Life	155.5
10 Allstate Life	146.7

First Colony Life Life Insurance Sales



1995 Top Ten Life Insurers *Individual Ordinary Life Issued*

	(billions)
1 Northwestern Mutual	\$52.9
2 Primerica	45.8
3 Prudential	44.1
4 New York Life	43.5
5 First Colony Life	40.2
6 Metropolitan Life	38.4
7 State Farm Life	38.3
8 Valley Forge Life (CNA)	34.5
9 Connecticut General	27.0
10 Allstate Life	23.3

First Colony Life

Immediate Annuity Sales

1995 Top Ten Life Insurers

SPIA - Settlement Annuity Premiums

	(millions)
1 SAFECO Life	\$484.0
2 First Colony Life	401.4
3 Transamerica Occidental	358.6
4 Allstate Life	349.8
5 Metropolitan Life	254.4
6 New York Life	230.2
7 Aetna Life & Annuity	212.5
8 Great Northern	175.0
9 Hartford Life	150.0
10 Allstate Life of New York	146.8

1995 Top Ten Life Insurers

SPIA - Retirement Annuity Premiums

	(millions)
1 Delta Life & Annuity	\$316.0
2 Metropolitan Life	302.4
3 First Colony Life	238.5
4 United of Omaha Life	195.6
5 New York Life	169.9
6 Prudential Insurance	132.7
7 Lincoln National Life	109.7
8 Sun Life of America	91.0
9 Northwestern Mutual Life	77.0
10 Protective Life	73.0

Sphex Club Meeting

Date: *February 1, 2001*

Time: *8:15 p.m.*

Place: *First Colony Life Insurance
Company Board Room*

Speaker: *Ronald V. Dolan*

Topic: *“What did the Maestro of the
Reasonably Intelligent Orchestra
Weigh?”*

Next Meeting: *February 15, 2001*

Speaker: *Peter T. Marcy*

2/1/01

addition to minutes - Booth would have insisted
number slightly favored at 2:30

Each audience only half

Guests: Walter Weber, Ed + Sue Hunt MJ son order
Bernard Stewart George Zipplo 15 min. occur like
Peter runs since 17 forever

Regrets: D. Harris
B. Muhlenthal
Jeff W. Iser
Carl Zeman