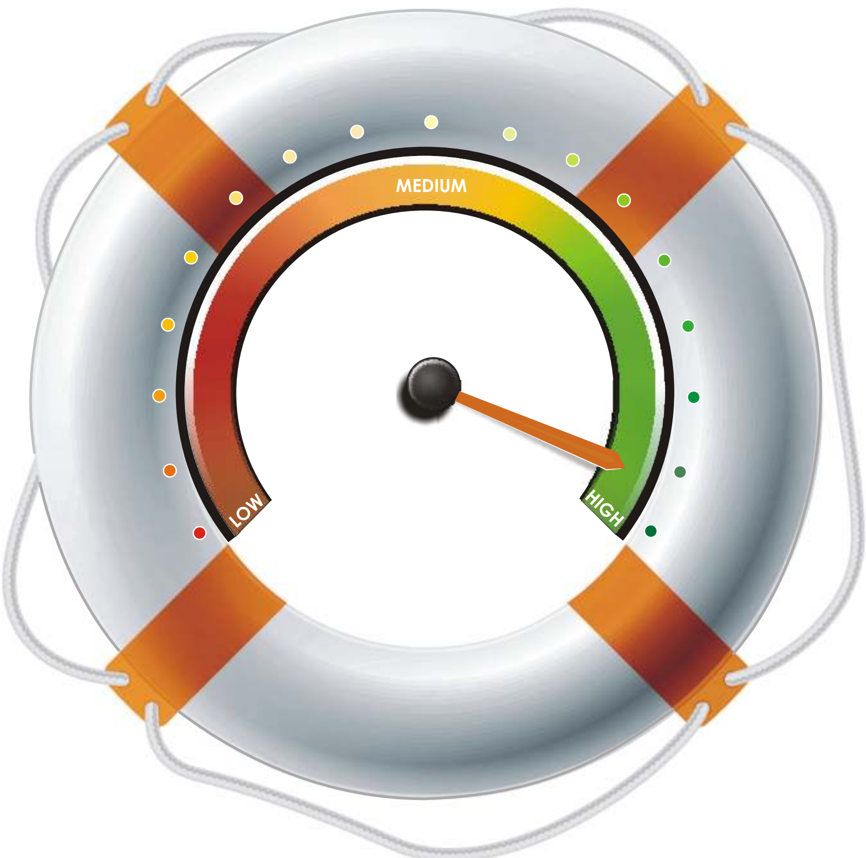
Extending Your Enterprise



BPO-led Transformation

Insures results in changing times

Extending Your Enterprise

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The changing face of the U.S. and U.K. life insurance and annuity industries

Continuous change has been the status quo for the life insurance and annuity industry over the past several years. And the monumental impact of these changes underscores a stark reality…**insurers that do not rapidly transform their operations across the board will not be able to effectively compete in the near-term.**

Why is the situation so dire for insurance companies? Several causes stand out.

First, aggressive merger and acquisition activity over the last few years has, in many cases, resulted in an **illogical geographical footprint or branch structure**. As a result, enterprise systems, post integration, often operate on disparate platforms. Second, it is the day and age of the Internet. Insurance customers are looking to more self-fulfill capabilities. However, back-office operations may not be configured or sized to support a change in channel. Overarching pressures to compete by differentiating operations through enhanced service delivery, whether via a live customer service representative or IVRs, means that customer care, policy set-up, claims management, processes and technology must be fully integrated.

On the legal front, increasing **compliance requirements are becoming even more complex** and system-intensive. For example, the U.S. is seeing potential regulations such as Rule 151a – which would require annuities products to be governed by regulations similar to those for brokerage investments coming into play. The U.K. on the other hand is preparing for the advent of Solvency II, which will expect insurers to maintain capital adequacy for different kinds of risk.

From an economic perspective, **legacy products and customers are becoming increasingly expensive** to service. At the same time, intense pricing pressure is driving the need to reduce the cost base driven by the fact that the industry may have lost, according to informal estimates, as much as USD 1 trillion during the recent economic downturn due to lost investment and policy holder income.

Finally, the **competitive marketplace has expanded** from players focused solely on the sales and servicing of traditional insurance products to those now offering a broad range of financial services products. As a result, traditional insurance companies must now fight for wallet share by offering new or hybrid products such as guaranteed living benefits, health riders, investment and growth offerings, and expand their offerings through Web-based, menu-driven coverage options to gain stronghold in a cautious and slowly recovering market.

And this surely is not the end of the change in this industry. Much more is to come, and if there is one certainty, it is that the industry will never be the same again. Leading insurers will be those that can adapt to the changing scenario with agility, flexibility and scalability.

The need for transformation

Industry Scenario

Illogical geographical footprint or branch structure owing to aggressive merger and acquisition activity.

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The go-to-market and operating models for the traditionally conservative insurance industry have gone through immense change. With the result, insurers must transform their operations by implementing actions that will reduce unit cost, enhance delivery quality, and improve the producer and policy holder experience without significant capital investment. The usual step-change approach is too slow-footed in the current economic environment, which demands agility from insurers to quickly transform their businesses, taking a significant leap forward with new products supported by cost-effective processes and platforms.

Leading insurance companies are now stepping up to the plate to transform their operations. For example, an August 2009 blog by Celent, an international strategy consultancy for leading financial institutions, noted in one of its recent research initiatives that streamlining of processes is the top area of focus for insurers. And, that changing the operating model by embracing outsourcing is on the agenda of insurance companies. Responses to the study indicated a higher level of plans and interest in Business Process Outsourcing (BPO), as compared to Information Technology Outsourcing (ITO). Celent believes this is most likely attributable to the already high level of ITO implementation in the insurance industry.

ITO-led transformation may not deliver

Most insurance companies have historically had an initial predilection to approach transformation as an information technology initiative, starting with ITO. In this approach, operational transformation is primarily viewed as a technology challenge program, which demands investment in one global instance of a system or global standardization of platforms, complete with continuous refreshes and upgrades. This is then followed by wrapping a BPO solution around the capital – and people-intensive systems implementation. In effect, the approach pursues a 100 percent solution to fix all operational elements at once, rather than focusing on addressing the most pressing needs for change – reducing cost and driving increased revenues through improvement in customer experience.

ITO-led transformation may be the right option for a financially solid insurer that does not foresee major business challenges within the next two to three years – typically the time-frame for a major systems implementation – and has the capital to rationalize multiple policy administration and new business systems into one. But this approach is extremely costly. For example, one insurer spent GBP 10 million on installing a new system and an additional GBP 10 million on consultancy fees associated with the system implementation. This GBP 20 million equated to the company's entire operational spend for an entire year. And time-to-benefit was delayed until the implementation was complete and the system was fully functional.

Given the current cautious business environment, ITO-led transformation may not be the most viable option for many insurance companies.

First, this **approach is linear by nature**. The majority of insurers adopt comprehensive outsourcing in a sequential manner, believing that extensive changes and modernization efforts to existing systems are a prerequisite to achieving successful business process transformation, as opposed to changing business processes directly to yield higher productivity and fewer errors. As a result, obtaining a steady state stream of benefits can take at least two to three years if the system changes are implemented smoothly, and often more, if the scope involves a systematic deployment across functions and business lines, no matter the number of policies administered or claims settled.

Second, the **pursuit of the latest or standardized technology may take on a life of its own** as it can require a wholesale replacement of all platforms and tools in order to move to a single platform. And rather than leveraging the existing substantial investment in engines and tools with a focus on filling in the processing gaps, most insurers approach the change from scratch, replicating 80 percent of the functionality available in one or more of the existing platforms.

Third, **IT-driven transformation brings into play the need to re-engineer business processes**, which requires participation and buy-in by a host of stakeholders from the range of insurance lines with an associated substantial investment in resources. The time required to promote change through the adoption of new business rules and workflow further delays delivery of results.

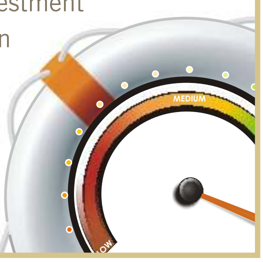
Insurance companies tend to implement a pilot in advance of full-scale deployment in their quest to avoid organizational dissonance by starting with a proof-of-concept. Generally trialed in one product line with lower volumes and less complex processes, the test often does not resolve the challenges associated with scale, regulation, volume, process complexity and comprehensive change management. And as the pilot may not be representative of a full roll-out, results often cannot be replicated, requiring modifications which lead to a delayed stream of benefits.

Additionally, as IT-led transformation initiatives are generally led by an IT team, as opposed to insurance operations teams, **the system implementation becomes the deliverable**, not the critical change in processes or customer care. In extreme cases, this can lead to even more inefficient processes where the operations team comes in after creating manual workarounds to ensure the system works, rather than ensuring the system supports the re-engineering of the processes in the first place.

The ITO Versus BPO Debate

ITO-led transformation involves extensive upfront capital expenditure, a lengthy deployment program, and a substantial investment in program management.

BPO-led transformation revamps the operating model with a focus on specific, quickly attainable business outcomes, enables better resource utilization with limited or no investment in technology, and can encompass enabling functions such as finance and accounting, IT helpdesk and HR.



Fundamentally, **an ITO-led approach to transformation does not break down operational silos**, which work against knowledge-sharing and cross-selling, creating a major obstacle for effective and efficient insurance operations. Typically, a common base platform is radically customized by each business line to such an extent that the benefits of a common platform are lost and the ability to cross- and up-sell products is reduced due to the lack of a single view of the customer.

Finally, experience indicates that most insurance companies spend between two to five percent of their premium revenue on IT, and ITO-led transformation requires an additional and steep capital investment, which typically starts to **deliver cost savings only in the second or third year** due to the cost of transition and training. Teams of change managers, system testers and 'model office simulation' representatives are frequently recruited from the existing workforce, requiring their positions to be back-filled or jobs doubled-up by existing staff. As a result, the IT-led transformation may impact the customer experience during the change process.

The bottom line is that ITO-led transformation involves extensive **upfront capital expenditure**, a **lengthy deployment program**, and a **substantial investment** in program management, all of which are disruptive to the core business and do not get to the heart of the transformation initiative – delivering **standardized processes at lower cost** while simultaneously providing a **high-quality service experience** to new and existing policy holders.

Pursuing a BPO-led transformation strategy for faster results

There is a simpler, less expensive and quicker-to-benefits realization path for insurance companies seeking immediate cost savings, sales growth, improved customer experience and an empowered sales force – BPO-led transformation. Here, the focus is on transforming business operations, which represent an average of 40 to 60 percent of an insurer's operating budget cost, rather than changing the IT systems and tools as a first step.

The underlying strategy is in effect predicated on an **80/80/80 rule:** First, focus on 80 percent of the high-volume processes such as quotes / illustrations, new applications, changes in policy / contracts, (including financial transactions, surrenders, withdrawals, 1035 exchanges in the U.S.) interaction and communication with agents, incentive and commission calculation, campaign management and claims / payouts. Second, plug 80 percent of the technology gaps, which affect straight-through processing of customer service functions (For example, not merely indexing but incorporating it into a workflow, or not just imaging but linking the process to case management solutions). Third, obtain 80 percent of the potential cost savings available from the labor arbitrage and process efficiencies delivered by outsourcing. Because this strategy focuses on reducing operational costs via streamlined and more efficient processes, enhancing productivity and leveraging enabling tools – as opposed to IT system replacement – the 80 percent savings can be achieved in an accelerated time-frame.

What specific benefits can an insurer gain from a BPO-led transformation initiative?

- **Delivers first tranche savings within six months of contract commencement**, which includes the transition phase, due to a number of drivers:
  - Process changes are implemented ahead of any IT reconfiguration, alleviating the need for significant upfront technology investment
  - Operational delivery is focused directly on business performance-related SLAs, rather than system performance, ensuring the customer experience is enhanced early in the program
  - Contract structures promote gain-sharing incentives in which the BPO provider may make an investment in the change, resulting in 'skin-in-the-game'
  - Insurance operations become more efficient, increasing support of agents and advisors in areas such as closed-book aggregation, open book and new product processing, policy and contract management, accelerated claims and payout processing. There is the opportunity to create immediate cost savings as a result in the reduction in error ratios through implementation of methodologies such as Six Sigma
  - Functional operations are consolidated across multiple divisions including life, annuities, group and health insurance by as much as 50 percent by cross-training staff, even if the underlying systems supporting them are disparate, leading to significant savings as operations typically constitute 50-60 percent of insurance companies' costs
- **Shifts management focus** to product development and the end-customer experience, rather than the prolonged period of operational change required by IT-led transformation
- **Results in speed-to-launch of new products and services** as the BPO provider's trained business process delivery personnel are able to rapidly process the influx of new incoming applications
- **Focuses on the integration of process efficiency with intelligent human intervention**, leading to incremental revenue generation and greater customer satisfaction and retention
- **Creates a self-funding structure** which allows costs savings achieved through continuous process improvement to fund future investments in process innovation and technology
- Specifically **focuses process improvements on business results** such as revenue generation, cross-sell / up-sell and faster claims processing
- **Lends itself to alternate pricing / financial models** according to defined SLA-based quality norms and turnaround times which are directly related to business results.

BPO-led transformation revamps the operating model with a focus on specific, quickly attainable business outcomes, enables better resource utilization by reengineering processes for greater efficiency and delivery quality with limited or no investment in technology, and can encompass not only core insurance functions but also enabling functions such as Finance and Accounting, IT helpdesk and HR, further reducing the overall cost of operations.

Key components of BPO-led transformation

As illustrated in the following chart, BPO-led transformation targets three key elements of insurance companies' operations to obtain the greatest benefit in a compressed time-frame:

Three key elements of insurance companies' operations to obtain the greatest benefit in a compressed time-frame

Operational Model

- Review the cost structures against industry benchmarks (cost per policy, new business application cost, cost of processing claim)
- Identify drivers of higher cost structures
  - Automation vs. human intervention
  - Operating structure (customer servicing teams deployed products-wise / division-wise vs. functionally across all divisions / products)
- Classify processes into back-office and front-office (producer / policy holder)
- Implement back-office transition
- Identify critical / non-critical front-office processes
- Retain only critical front-office processes in-house
- Pilot non-critical processes onshore / transition offshore

20-30% operating cost savings (primary contributor - labor arbitrage)

Process Improvement

- Document processes to be outsourced
- Review detailed process flows (application processing, surrenders, withdrawals, compensation)
  - Identify best practices to be replicated
  - Re-structure processes to promote straight-through processing of document processes to be outsourced
- Define the 'to-be' process
  - Ability to be automated
  - Requirement for apply analytics
  - Define SLAs, TAT, CSAT and other metrics
- Transition to-be processes to offshore
  - Set-up centers of excellence for each function
  - Six Sigma / Lean Sigma projects

Productivity: +20% (primary contributors – error reduction, increased quality, proactive analytics, increased TAT,

Technology Optimization

- Identify technology challenges and gaps
- Triage them as supporting open books and closed books of business
- Focus only on open books
- Assess existing technologies (especially in indexing, imaging, workflow, case management, rules engine and business intelligence)
- Identify opportunities to leverage existing investments and fill gaps
- Re-design and implement to support process improvement
- Outsource maintenance and improvements to technologies

15% reduction in IT budget (primary contributor – leveraging existing investments)

BPO-led transformation model

BPO-led transformation for insurers starts by mapping and performance benchmarking the processes in their current state. It then evaluates the gaps between current and desired future state in terms of efficiency, effectiveness and end-customer service delivery, and subsequently 'lifting-and-shifting' the processes to an outsourcer's offshore centers in order to deliver immediate savings through labor arbitrage. Concurrently, it forces a re-alignment of the client's organizational structure to improve resource utilization, increase controls and scale easily. The shifted processes are then improved by the BPO provider to deliver higher productivity and quality, and consolidated and moved into functional Centers of Excellence(CoE) where processes such as policy set-up, closed book aggregation, open book and new product processing, policy and contract management, accelerated claims / payout processing, and tasks supporting agents and advisors, provide rapid cost savings simply through aggregation.

This change in operating model can yield as much as 30 percent savings in operational costs. It also eliminates technology investments, which could range from as little as USD 2 million for the implementation of simple workflow systems to a multiple of that amount for a more comprehensive integration.

Focus transformation on processes yielding the highest benefits: A rapid path to benefit is to first transform processes, which are high-volume and highly transactional (manual) in nature, and thus can have the biggest early-on impact on reducing costs or improving services. These processes include quotes / illustration, new application processing, underwriting, claims / payout processing, changes in policy / contracts including financial transactions, surrenders, withdrawals, 1035 exchanges, interaction and communication with agents, incentive and commission calculation, campaign management, and claims and payouts, as these can be easily and rapidly streamlined to their to-be state. For example, by first introducing parameterized forms for data capture, there is a potential reduction in the 'Not-in-Good-Order' (NIGO) applications by at least 50 percent, which leads to improvement in customer service productivity by 30-50 percent depending on the length of the queue; and second, improving information capture to speed-up the applications process by modifying the underwriting parameters (while preserving the underwriting standards) can reduce the cost of the process by 20-30 percent due to enhanced underwriter productivity.

Five Steps along the Path to BPO-led Transformation

1. Map all front- and back-office processes end-to-end
2. Identify all processes to be outsourced
3. Design the desired processes
4. Outsource non-critical back-office processes
5. Outsource non-critical front-office processes, helpdesk and HR.

Invest in technology enablement and training: Concurrent with process improvement identification, BPO-led transformation implements gap solutions – rather than full-scale platform replacement or consolidation – that expedite the movement of work through tools such as workflow, case management and rules engines. These have visibility into operational and business risks via business intelligence tools. For example, rather than adding additional resources to handle peak volumes, implementing indexing along with workflow and imaging with case management builds a balanced work queue that can easily be delivered by cross-trained resources. This approach leverages existing technology to retain the focus on operational effectiveness and initiates an assessment of the current use and efficacy of enabling technology solutions. The results of this assessment can drive better utilization of existing IT assets and avoid significant capital outlay.

In an era of stringent corporate budgets, capital availability for large-scale, traditional platform changes – even if staged over time – is virtually non-existent. BPO-led transformation is essentially self-financing as savings from labor arbitrage; leveraging existing systems and applications; and elimination of process gaps provide immediate savings benefits.

How is BPO-led transformation implemented?

There are five steps along the path to BPO-led transformation:

1. **Map all front- and back-office processes end-to-end,** and segregate them into critical and non-critical categories.
2. **Identify all processes to be outsourced:** Generally those identified as critical processes may be best retained in-house. Group the processes as shown in the following illustration.
3. **Design the desired processes:** This would require streamlining the steps involved in delivery of the processes, training resources to deliver processes by function across product lines, and applying tools such as indexing, workflow, imaging and case management to simplify and correctly allocate tasks, verify, validate and manage compliance.
4. **Outsource non-critical back-office processes:** The first wave of outsourcing could involve moving out processes such as beneficiary changes, withdrawals, application processing, commission calculation, agent licensing and registration.
5. **Outsource non-critical front-office processes:** The second wave of outsourcing could involve moving out processes such as contacting an agent or customer on documents required to issue a policy, gathering additional information required to execute a policy change request, or follow-up with agents on campaign leads.

Agent Services	Agency Administration	▪ Licensing and contracting ▪ Correspondence	▪ Renewals ▪ Terminations	▪ Commissions ▪ Special compensation ▪ Abandoned properties
Policy Acquisition / Setup	Sales	▪ Sales ▪ Conversion ▪ Quote acceptance	▪ Cross- and up-sell ▪ Customer enquires	
	Policy Setup	▪ Prescreen and capture ▪ Underwriting ▪ Underwriting support	▪ Delivery requirements ▪ Follow-up ▪ Policy issue	
In-force Administration	Policy Changes	▪ Name, owner, beneficiary, changes ▪ Address changes ▪ Certificate reissue	▪ Assignment and collaterals ▪ Reinstatements and quote	
	Policy Benefits	▪ 1035 exchanges ▪ Policy loans ▪ Withdrawals	▪ Dividends ▪ Policy surrenders ▪ Maturities	▪ Fund switches
Payouts	Death Claims / Settlements	▪ Claim setup ▪ Examination ▪ Review	▪ Settlement ▪ Correspondence ▪ Tax compliance	
Billing	Billing	▪ Premium billing ▪ Receivables and collections ▪ Lockbox	▪ Premium mode changes ▪ Bank changes	

Summary

The five steps along the BPO-led transformation path enable insurance companies to revamp their operating model with a focus on specific, quickly attainable business outcomes, better utilize resources through processes re-engineered for enhanced efficiency and delivery quality, and eliminate or greatly reduce a financial investment in technology purchases or consolidation. Insurance companies that quickly embrace BPO-led transformation can become highly effective competitors in the face of monumental marketplace changes.

About WNS

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