MAYER | BROWN

GLOBAL INSURANCE INDUSTRY
YEAR IN REVIEW **2020**

EXCERPT

Technology Transactions

Introduction

2020 was a year of rapid digital transformation in the insurance industry. The pandemic dramatically altered the way people worked and lived, giving increased importance and urgency to long-running trends in data, digital, outsourcing and software transactions. As insurers and producers sought to gain competitive advantages in a challenging marketplace, prominent trends included an increased interest in managed services agreements, rapid adoption of cloud and "as a Service" technologies, the use of big data and data monetization concepts, a rise in collaboration deals between incumbent insurers and digitally-native insurtech companies, and continued growth in the use of AI.

Managed Services

With significant disruptions to existing employment arrangements and business models, insurers and producers took renewed interest in managed services, including as IT outsourcing, business process outsourcing and offshoring. Managed services can replace the fixed overhead costs of employees with variable cost services and streamline back office operations. The need to control costs and improve financial performance was an obvious driver of increased interest; however, the pandemic also demonstrated that insurers and producers have the ability to perform many critical functions remotely that they formerly believe must be "under one roof." With employees working at home, insurers and producers were forced to adapt to the new normal. Through the reexamination and adjustment of critical business processes to make them work in a remote environment, companies removed a massive barrier to the outsourcing of those key processes.

The pandemic also highlighted the value of a resilient supply chain. Beyond having well-defined business continuity and disaster recovery plans, insurers and producers saw value in having contractual rights to exercise. With some suppliers forced to choose among their customers, companies saw business value where they had secured a firm commitment to deliver to acceptable standards at a reasonable price despite the pandemic. There is likely to be an increased focus on contract terms moving forward, including contract terms protecting against unlikely events.

Cloud & "As A Service" Technologies

The trend in the insurance industry towards digital transformation continued in 2020. In transformational deals, suppliers took responsibility for performing critical functions and agreed to transform service delivery using technology such as robotic process automation, cloud services and "as a Service" solutions. In particular, there was a rapid acceleration of the move to the cloud. Insurers moved from on-premises software options to Software as a Service solutions and replaced conventional dedicated and shared data center hosting deals with hosting on large cloud platforms such as Microsoft Azure, Google Cloud and Amazon Web Services.

While these moves are not new, the pace and scale of the migration to the cloud increased significantly over the past year. Much of this was driven by the economic effect of the pandemic. Cloud services allow a company to cut costs, replace fixed costs with variable costs and replace assets with operating expenses, all of which can dramatically improve a company's balance sheet, earnings and return-on-assets. This change also reflects growing customer expectations, with the cloud enabling more agile platforms that can win business and help sustain customer relationships in a competitive industry.

Data Monetization

One effect of the move to the cloud has been to significantly lower the cost of gathering and storing data. Lower costs have driven an exponential increase in the amount of data stored and have accelerated a move beyond data mining and analytics and into data monetization. The insurance industry has historically collected large amounts of data but used that data primarily for underwriting, marketing and servicing. We see insurers and producers increasingly viewing data as a core asset that has the potential to create new revenue streams and improve profitability in new ways.

With data monetization initiatives a strategic priority, insurers and producers will increasingly need to work with large technology companies on infrastructure solutions such as data lakes. Often housed on cloud platforms, data lakes enable a company to store vast amounts of its own internal data and enrich it with data from third-party sources to help extract insights and inform key organizational decisions. While data monetization has the potential to improve business performance and generate new forms of revenue, companies in heavily regulated industries, including insurance, need to be particularly careful. Companies must manage a web of rights and restrictions on their various data sets in order to protect the company's own data (and IP rights in that data) as well as ensure compliance under third-party contracts and data privacy and other laws. This can be a complex undertaking and often requires coordination between a company's lawyers, compliance specialists, data scientists, procurement department and IT professionals.

Insurtech Collaborations

As company's look to change the way value is delivered to customers, incumbent insurers and producers are increasingly opting to collaborate with new, digitally native insurtech companies. Digital transformation requires significant change for many incumbents, with upgrades to important technology infrastructure on the back end and improvements to customer-facing products and services on the front end. While incumbents are working to digitize their data and move more of their systems to the cloud, this can be a time consuming process and the pandemic has only increased the urgency to complete these digital transformation projects. To quickly address perceived gaps or shortfalls, some incumbent players in the insurance industry have opted to collaborate with Insurtech platform companies. [*See* "Insurtech Investment and Transactions" for further information on insurtech collaborations].

Despite being competitors in some cases, these collaboration deals have the potential to bring significant benefits to both parties. The incumbent gains access to an entirely new, digital channel without the time or monetary investment required to build that digital channel itself. This new channel can expand the reach of the incumbent, introducing it to a broader range of customers than it would be able to do on its own. The insurtech company shares in this upside and may need to partner with the incumbent to offer new types of products or insurance policies to its own customers. Since these deals involve an insurtech company who is not only a service provider, but also a collaborator with its own customer relationships to protect, particular care and thought needs to be exercised when incorporating a deal of this type into your company's overall digital transformation strategy.

Continued Adoption of AI

With cloud-based storage resulting in exponential reductions in the cost of storing data and exponential growth in the ability to process data, insurers and producers continue to adopt AI as a way to make business processes more efficient and to solve problems faster. AI is currently being used in the insurance industry to, among other things, more accurately price policies, recommend useful products to customers, recognize and reduce fraudulent claims and improve claim processing time. The FBI estimates the total cost of insurance fraud (non-health insurance) in the US at over $40 billion per year alone, the cost of which is passed on to consumers through higher premiums. Companies who successfully integrate AI to avoid these claims can create significant competitive advantages over other industry players.

AI is also changing the way insurers interact with customers through the use of new AI-driven tools like chatbots. Progressive Insurance, for example, has developed its Flo Chatbot to help customers file claims, get auto insurance quotes and answer general questions all through Facebook Messenger. Competitors Allstate and GEICO have also both developed chatbots to provide similar services. These tools have the advantage of being available 24/7 and can free up significant time and resources for insurers to devote towards more profitable activities.

While AI can deliver insights and significant operational improvements to a company, its implementation continues to face challenges. Some challenges include uncertainty in intellectual property rights surrounding AI developments, determination of the necessary contractual allocation of rights and obligations between licensors, licensees and the end users of the AI, and legal compliance in the use of AI, such as being able to explain the logical and algorithmic decisions and outputs produced by the AI to ensure its decisions comply with legal and regulatory obligations. Insurers and producers who recognize and address these challenges early in their AI adoption stand to maximize the value of their investment and reduce their risks. [*See* "Insurtech Regulatory Developments" for further information on the NAIC adopting guiding principles on AI].

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