MAYER | BROWN

# GLOBAL INSURANCE INDUSTRY
## YEAR IN REVIEW 2020

EXCERPT

Technology

# Insurtech

## Introduction

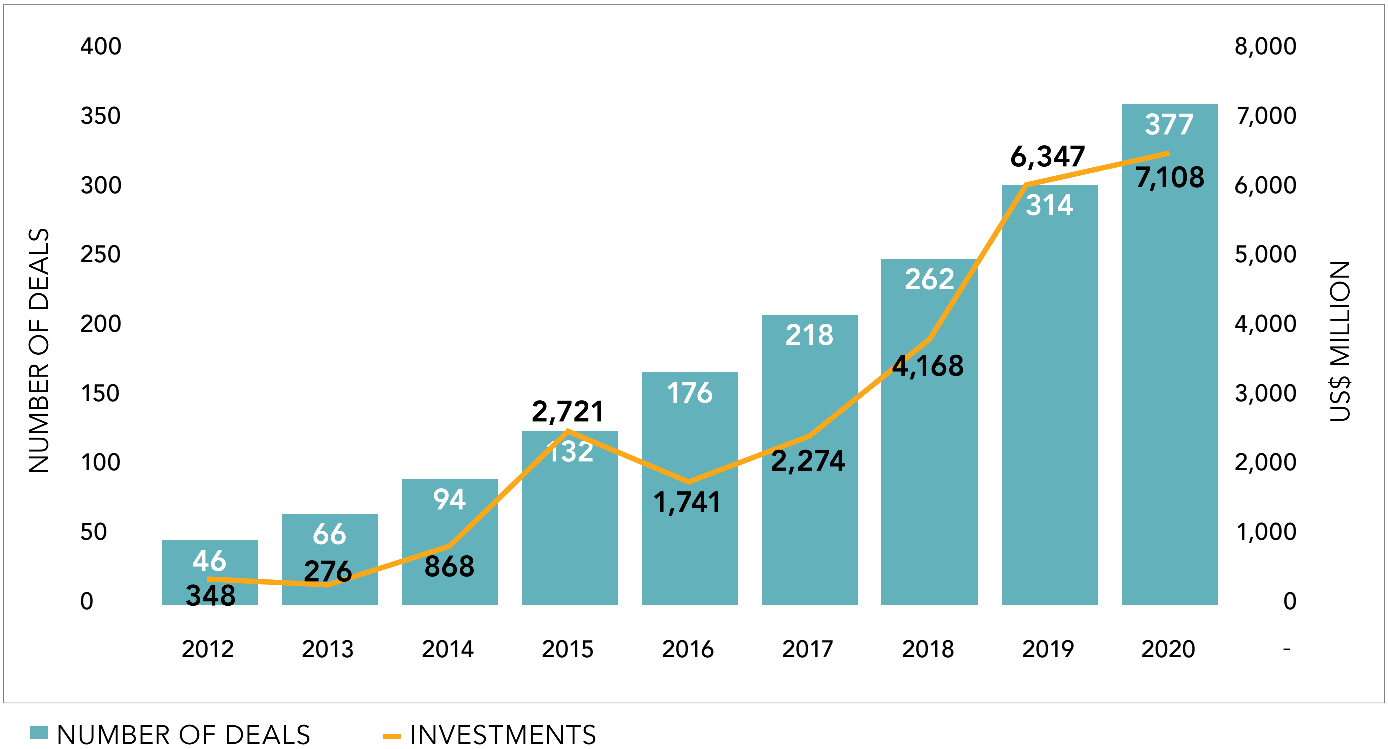
In commenting on insurance technology and innovation developments in our 2019 Year in Review, we questioned how fast and at what scale insurance carriers, brokers, service providers and technology companies would accelerate their insurtech capabilities in 2020. At the time of publication in 2019, we had not anticipated the magnitude of a global pandemic and the extent the impact would have on the insurance industry. From the perspective of insurance technology and innovation, COVID-19 forced the insurance industry – insurance businesses and regulators alike – to re-examine the application of technology and innovation to provide better services and products to policyholders. Policyholders also began to realize and appreciate differences in the delivery of insurance products, customer service and pricing to fit their changing needs and preferences during uncertain times in which there were many unknowns in terms of public health, business sustainability and just normal everyday lifestyle choices that we may have taken for granted prior to the pandemic.

There were several insurance regulatory developments in 2020 that helped to progress the further implementation of technology and innovation in the insurance industry. The state-based regulatory system is a key dynamic impacting the rate at which the insurance industry embraces technology. Insurance regulation traditionally focuses on protection of the consumer and regulator views on the use of emerging technologies are naturally colored by that lens. In 2020, we saw regulators, at the state and National Association of Insurance Commissioners ("**NAIC**") level, continuing to embrace collaboration with the industry enabling greater digital communications and more transparent online-driven insurance services between insurance companies and consumers.

## Insurtech Investment and Transactions

We noted in our 2019 Year in Review that insurtech investment, collaboration and M&A activity would continue to grow as incumbent carriers increasingly implemented new technology and innovation to find ways to analyze data at a more efficient way while being cognizant of compliance with insurance and consumer protection regulations. Although insurtech investments slowed down in the first quarter of 2020, investment activity quickly recovered for the rest of 2020 powered by several large initial public offerings ("**IPOs**"). According to data compiled by *CB Insights*, over $7 billion was invested globally in insurtech in 2020 across 377 deals, setting another insurtech investment record. This compared to over $6 billion invested across 314 deals in 2019, over $4 billion invested across 202 deals in 2018 and over $2 billion invested across 218 deals in 2017.

## Annualized Insurtech funding trends including transaction volume and dollar amount, 2012-2020




Source: *CB Insights*

A bigger proportion of the insurtech investment funds in 2020 ended up going to later stage insurtech companies. Investors rushing to proven insurtech players and management teams is not surprising given that COVID-19 accentuated the need to implement consumer-friendly digital platforms as soon as possible to keep and expand customers who expect on-demand insurance products and services in the comfort (and safety) of their homes in the same manner as the delivery of other consumer products. Businesses that are able to offer efficient and consumer-friendly digitized versions to facilitate the marketing and sale of insurance policies, underwriting, claims processing and other insurance functions have become much more valuable due to the competitive advantage that they potentially have over insurance players who are still developing their digital and technology infrastructure.

The heightened investor expectations for these later stage insurtechs has driven the rapid rise of consumer-facing digital insurance companies that have been able to attract large amounts of capital at relatively high valuations to implement their business models. Several insurtech companies raised substantial amounts of capital by becoming public companies through IPOs and others stayed private but were able to raise large amount of additional capital through venture mega rounds. Several notable examples are listed on the next page:

| COMPANY (IN MILLIONS) | CAPITAL RAISED IN 2020 METHOD OF CAPITAL RAISING | METHOD OF CAPITAL RAISING |
|---|---|---|
| Root | $724 | IPO |
| Duck Creek | $405 | IPO |
| Lemonade | $300 | IPO |
| Midwest Holdings | $70 | IPO |
| Bright Health | $500 | Series E |
| Hippo | $500 | $350 million Series E + $150 million convertible bond strategic investment by Mitsui Sumitomo |
| Ki Insurance | $500 | Private equity/Strategic Investment: sBlackstone and Fairfax Financial Holdings |
| Oscar Health | $365 | Series D or later |
| Unquork | $258 | $51 million Series B + $207 million Series C |
| Next Insurance | $250 | Series D |
| Pie Insurance | $127 | Series B/Strategic Investment by Gallatin Point |
| States Title | $123 | Series C |
| Policygenius | $100 | Series D |
| Rhino | $95 | Series B/Pre-IPO |

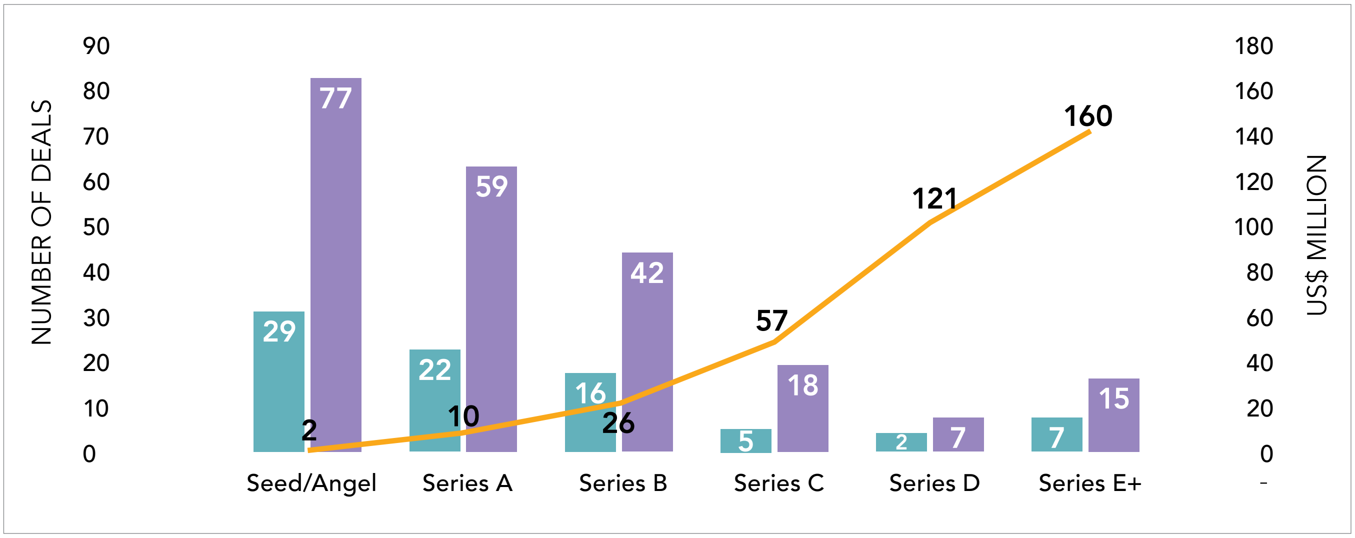
Source: *CB Insights*

In addition to raising capital through IPOs and venture capital financings, some insurtechs are considering merging with a publicly traded special purposes acquisition company ("**SPAC**") to raise capital, potentially lowering its cost of capital and develop a liquid market for its securities through being a publicly listed company. At the date of publication, Metromile, Inc. ("**Metromile**") agreed to merge with SPAC, INSU Acquisition Corp. II. If this transaction is successful, Metromile will have access to an additional $294 million in cash and become a publicly listed company on Nasdaq. [*See* "Mergers & Acquisitions – SPACs" for further information on SPACs in the insurance industry].

While some later stage insurtechs enjoyed high valuations and readily available access to capital, many earlier stage insurtechs struggled to get access to funds in 2020. In general, corporate venturing by incumbent insurance players decreased in 2020. COVID-19 created significant insurance losses to insurers and created operational challenges in meeting customer needs during a pandemic, especially if the insurer employed outdated technology and digital customer interfaces. In short, many incumbent insurance players did not have the luxury of time or extra cash to invest in companies that did not have technology or innovation that could be implemented quickly. This development, together with a few leading insurtechs raising large amounts of capital, resulted in a lower proportion of early stage insurtechs being funded in 2020 relative to total insurtech funding compared to previous years. According to the data, as illustrated by the graphs from *CB Insights*, below, the size of Series D and above deals in 2020 were greater than the average size Series D and above deals from 2012 to 2020. In addition, the number of Series D and above deals (31 deals) comprised almost one-third of all Series D and above deals from 2012 to 2020 (101 deals).

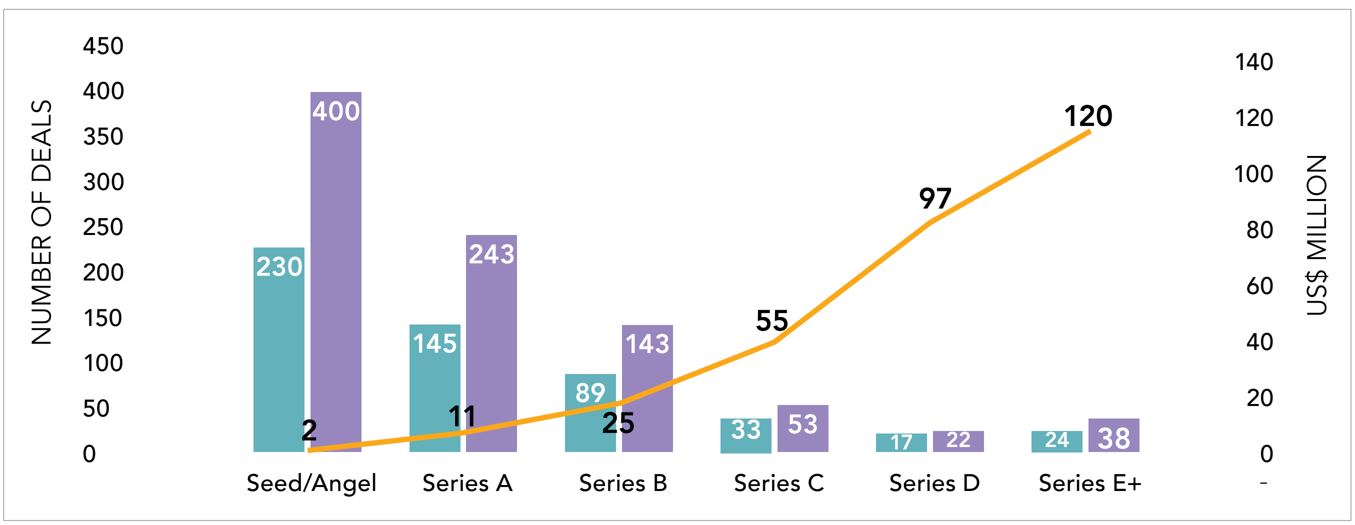
Although early stage insurtech corporate venturing declined in 2020, we continued to see a dynamic level of collaborations between insurtechs and incumbent insurance players. Collaborations allow incumbent insurance players to quickly access digital platforms and other technology required to enhance their insurance offerings. During the challenges posed by the pandemic, collaborations also help

## Number of deals at each stage vs. the average deal size in 2020*




This graph above omits "other" as a round type.

## Number of L&H and P&C Insurtech deals vs. the average deal size, 2012-2020*




This graph does not include the round characterized as "other" in its calculations.

L&H NUMBER OF DEALS P&C NUMBER OF DEALS AVERAGE DEAL SIZE

Source: *CB Insights*

incumbent insurance players to buy time to build out their technology infrastructure either through internal growth or M&A while giving insurtechs a lifeline to continue to develop and customize their insurance industry solutions. While there were only a few strategic insurtech M&A transactions in 2020, there were numerous examples of collaborations and strategic partnerships that we saw in 2020, some of which are listed on the next page:

| INSURTECH | STRATEGIC INSURANCE PARTNER | DESCRIPTION |
|---|---|---|
| Athenium Analytics | Aon | Athenium Analytics and Aon are collaborating to develop a next-generation claims platform that enables insurers to identify and address high-risk claims before they close |
| Bold Penguin | Berkshire Hathaway | Berkshire Hathaway is using BoldPenguin's technology to address growing demand for workers compensation coverage – under the partnership agreement, agents and brokers will be able to triage, quote and bind commercial insurance coverage through an API integration |
| Flyreel | QBE | QBE is working with Flyreel, an AI platform for property insurance, to help customers manage risk and prevent loss through an AI-assisted tool |
| Ladder | Hannover Re | Hannover Re continues to support Ladder with risk management solutions, underwriting consultation and outsourced underwriting services |
| Notion | Nationwide | Nationwide is working with Notion to offer customers with smarthome technology a monitoring service that allows them to detect when a leak or a smoke alert occurs |
| Oscar | Cigna | Cigna and Oscar announced the launch of Cigna + Oscar, a new affordable and consumer-first health insurance for small businesses |
| Policygenius | Lincoln Financial Group | Policygenius, an online insurance marketplace, is offering an innovative life insurance product underwritten by Lincoln Financial Group to give consumers the flexibility of multiple policy options |
| Policygenius | Brighthouse | Brighthouse and Policygenius launched Brighthouse SimplySelect, a new term life insurance product available online through Policygenius |
| Risk Genius | Guy Carpenter | Guy Carpenter entered into a strategic partnership with Risk Genius on the detection and qualitative analysis of silent cyber exposure. |
| Roost | American National | Roost, a telematics insurtech, and American National are partnering to develop strategies to mitigate claims costs and increase customer engagement with American National offering free sensors to select policyholders |
| Slice Labs | AXIS Capital Holdings | AXIS is distributing small business insurance through Slice Labs on-demand digital insurance platform |
| Thimble | Hiscox | Hiscox is using Thimble's on-demand insurance app to allow small business policyholders to modify their coverage based on a project's needs, add additional insureds or pause coverage as necessary |
| Tractable | MS&AD | MS&AD is using Tractable's AI technology to accelerate how it processes auto claims |
| Verily | Swiss Re | Verily, Alphabet Inc.'s life sciences division, is partnering with Swiss Re to launch a unit to provide stop-loss insurance for employers to cover unexpected and large employee health care costs |

Source: *CB Insights*

Despite the variety in insurtech partnerships, there are certain insurance regulatory issues that we find common place in insurtech deals. The most prevalent is an imbalance in regulatory risk tolerance between the insurtech and the interested incumbent. In our experience, regulatory risk tolerance is often higher at insurtech companies who are keenly aware of regulation but do not have the same depth and breadth of experience with compliance (and the consequences of non-compliance) as incumbents. Insurtechs are rightly focused on growing a business and often place undue legal and compliance significance on competitor behavior. By contrast, regulatory risk tolerance for incumbents is typically low, particularly given the reputational damage that incumbents face with non-compliance vis a vie customers and regulators.

We see the imbalance of regulatory risk tolerance most often where market conduct related issues are identified at the insurtech. Such issues often include engaging in licensable activity without a license, offering rebates or inducements, non-compliant compensation arrangements with partners, tie-in or force-placed sales, non-compliant white labeling/co-branding arrangements and non-compliant marketing practices. While the insurtech may have flown under the radar for years without regulatory scrutiny, when the incumbent's diligence reveals these types of issues, the incumbent rarely has the appetite to continue the deal with those practices remaining in place. This is particularly true where the incumbent is an insurance company which is legally responsible for its agents behavior and remains legally responsible for meeting statutory and regulatory obligations, regardless of whether it outsources operations.

Large insurtech M&A activity was limited in 2020. Many of the leading insurtechs had ready access to capital through both public and private markets and so had options to grow their business without relying solely on a larger strategic partner. Some insurtechs went one step further, such as Hippo and Buckle, by deciding to become a "full stack" insurers themselves by acquiring insurance companies. In light of the challenges of COVID-19 and high valuations, many incumbent insurance players may not have been ready to make a risky acquisition. However, we anticipate from the high level of collaboration among insurtechs and incumbent insurance players that we are already seeing and the need to own technology to remain relevant in the new digital insurance environment, that insurtech M&A will accelerate as the challenges of COVID-19 start to dissipate.

## Insurtech Regulatory Developments

Despite the insurance industry's continued investment in insurtech in 2020, the COVID-19 pandemic posed particular challenges for state insurance regulators. Consumer dissatisfaction, whether expressed or simply feared, caused regulators to issue varying degrees of guidance and mandates. Regulators that historically would have balked at mid-term premium rebates encouraged, and even ordered, return of premium on insurance products whose risk profile changed dramatically due to the pandemic. Regulators embraced technology and demonstrated a willingness to reconsider long standing positions when faced with pressing need, including mandating forbearances related to cancellation for nonpayment of premium, easing the rules around telemedicine and easing the burden of paper filings with the state.

At the state and NAIC level, regulators further embraced collaboration with the industry. For example, New York's Department of Financial Services launched DFS FastForward in June 2020, expanding on its existing insurtech support program (Project Whitehall) to support innovators seeking to deliver new solutions in financial services, fintech, insurtech and healthtech during COVID-19. Vermont launched a regulatory sandbox in January 2020, under which companies can seek waivers of certain statutory/regulatory requirements for a limited period while piloting a program or product in Vermont.

At the NAIC level, on August 14, 2020, the NAIC Executive Committee/Plenary unanimously adopted guiding principles on artificial intelligence ("**AI**"). The NAIC's Principles on Artificial Intelligence were developed by the NAIC's AI Working Group, a working group established by the NAIC's Technology and Innovation Task Force. The AI Working Group studied the use of AI in the insurance sector, its impact on consumer protection and privacy, its interplay within the state-based regulatory framework, as well as solicited comments from key industry stakeholders.

The Principles on Artificial Intelligence, which are general guidelines on regulatory expectations with respect to the use of AI in the insurance industry, are based, in part, on the Organisation for Economic Co-operation and Development's ("**OECD**") AI principles, adopted by 42 countries, including the US. The principles outline five key tenets, summarized by the acronym FACTS:

- Fair and Ethical. Respecting the rule of law and implementing trustworthy solutions. Encourages industry participants to take proactive steps to avoid proxy discrimination against protected classes when using AI platforms.
- Accountable. Responsibility for the creation, implementation and impacts of any AI system.
- Compliant. Have knowledge and resources in place to comply with all applicable insurance laws and regulations.
- Transparent. Commitment to responsible disclosures regarding AI systems to relevant stakeholders as well as ability to inquire about and review AI driven insurance decisions.
- Secure/Safe/Robust. Ensure reasonable level of traceability of datasets, processes and decisions made and implementation of a systematic risk management process to detect and correct risks associated with privacy, digital security and unfair discrimination.

In addition, on December 9, 2020, the NAIC Executive Committee/Plenary adopted amendments to anti-rebating provisions of NAIC Unfair Trade Practices Model Act ("**UTPA**"). The amendments were designed by the Innovation and Technology Task Force after careful consideration of industry claims that the anti-rebating provisions were outdated and hindering insurers and producers ability to use technology to improve outcomes for insureds.

The amendments to the UTPA allow insurers and producers to, among other things provide, without charge or at a reduced cost, on a non-discriminatory basis, nine categories of "value added" services, provided the "value added" product or service relates to the insurance coverage, and the cost to the carrier or producer of providing the value added service/product is reasonable in relation to the policy premium.

These value added services include those that are primarily designed to satisfy one or more of the following:

1. Provide loss mitigation or loss control;
2. Reduce claim costs or claim settlement costs;
3. Provide education about liability risks or risk of loss to persons or property;
4. Monitor or assess risk, identify sources of risk, or develop strategies for eliminating or reducing risk;
5. Enhance health;
6. Enhance financial wellness through items such as education or financial planning services;
7. Provide post-loss services;
8. Incent behavioral changes to improve the health or reduce the risk of death or disability of a customer (defined for purposes of this subsection as policyholder, potential policyholder, certificate holder, potential certificate holder, insured, potential insured or applicant); or
9. Assist in the administration of the employee or retiree benefit insurance coverage.

In addition, the amendments to the UTPA, allow insurers and producers to offer or give non-cash gifts, items, or services, including meals to or charitable donations on behalf of a customer, up to a stipulated cash value (for personal lines) or up to an amount that is reasonable in relation to the policy premium (for commercial lines).

## Conclusion

Despite the various challenges for the insurance industry in 2020, developments in insurtech helped to pave a path for better customer experience and operational efficiency in the insurance industry. The insurance industry proved to be resilient and flexible during the pandemic, in no small part to the contribution of technology and innovation to drive business processes forward and meet the needs of policyholders. Although it is to be seen whether the high valuations attributed to several high growth insurtechs are justified, it seems clear that the digital transformation will continue to accelerate through the insurance industry and impact the way insurance business is conducted and regulated.

## Authors


**Paul P. Chen**
Partner
pchen@mayerbrown.com
Palo Alto
+1 650 331 2050

**Stephanie Duchene**
Partner
sduchene@mayerbrown.com
Los Angeles
+1 213 229 5176


View the full Global Insurance Industry 2020 Year in Review.