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Business-driven Policy Administration Transformation

Cost per policy analysis can help drive decisions for transforming policy administration systems

Contents

1 Introduction

In the current economic climate, European insurers are taking a harder look at existing IT environments, searching for places where they can reduce costs. Insurers know they are spending a large amount of money to maintain existing legacy systems, especially when it comes to policy administration. Carriers often have multiple policy administration systems which have been put in place over many years or even decades to address changing business needs. Yet insurers struggle to find the best way to reduce the number of systems or consolidate onto a single platform.

More and more, European insurers are turning to the concept of "cost per policy" as a way to measure the cost of maintaining their existing policy administration environments. Insurers may have an accurate idea of current costs, but they find it much more difficult to measure what their costs ***could*** be if they migrate away from legacy systems, or consolidate onto a new policy administration platform. There are so many variables involved that cost per policy becomes difficult to measure.

Many software vendors and system integrators claim that their approach will help an insurer reduce costs. However very few of them are able to calculate these savings. In this paper, we will discuss a methodology that Capgemini has developed for calculating existing cost per policy, and comparing that with the potential savings an insurer could realise by migrating to Oracle Insurance Policy Administration.

2 Challenges

Let's assume we are working with carriers with five or more policy administration systems. The company wants to transform the back office for a number of reasons: to reduce costs, respond more quickly to market changes, be more transparent for regulatory purposes, and so on. Often, the first thing an insurer will do is try to consolidate all of its existing business onto one of its current policy administration systems. The IT department may assess the functionality and technical robustness of each system, and what began as a business goal quickly becomes an IT discussion.

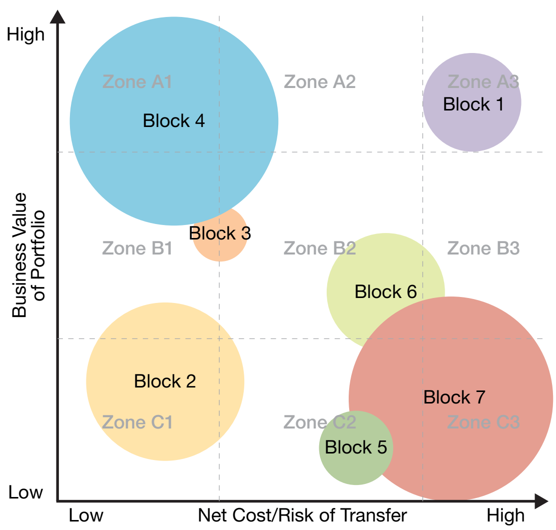
From there, the IT team may decide that none of its existing policy administration systems possesses the necessary functionality, and so they decide to build a new system in house or customise an existing system. Many IT shops are sceptical of policy administration software vendors, because they've been burned before by systems that were supposed to enable consolidation, but in the end were not flexible enough or robust enough to handle all of the existing business. A purchase that was intended to serve as a "single system" ended up being just one more platform, added on top of all the others.

We believe IT departments should look at this differently. The value of an insurer rests not in its systems, but in its policies and customers. Before an insurance company even starts to look at an IT solution, it should examine its current portfolios and decide what to do with each block of business. After careful analysis, the carrier may find that some blocks of business can be retired or outsourced, enabling the insurer to reduce its IT and administration costs.

3 Putting Business Needs First

Capgemini has developed a methodology to look at an insurer's existing costs and uncover cost savings in managing the policies for each block of business. This methodology includes examining the value of each block, and analyzing the net cost and risk of transferring it. A number of factors go into these calculations, and these factors are unique to each carrier. For more detailed information on our methodology, please refer to the Capgemini brief, "Sunsetting Systems for Closed Blocks: A portfolio management approach to deciding the fate of application systems administering closed blocks of business," at *www.capgemini.com/insurance*. Figure 1 shows the results of a sample analysis of a carrier's book of business, and the recommendations associated with each block.

Figure 1: The decision to outsource, retain or sell a block of business depends on the value of that block and the net cost and risk of transferring it. Capgemini provides an existing methodology for making these calculations



Zone	Recommendation
C1	Outsource
A1	Third Party Administration
A3	Retain
C3	Sell
Other	Decision needs to made considering detail characteristics of the Block

NB: The size of the circle indicates the size the Block

Deciding to Use Third Party Administration (TPA): In Zone A1, exemplified by Block 4, the net cost/risk of transfer is low but the business value is high. This means that there is a pay-off to transferring the business out of its current system for administration, but that transfer must not impair the enterprise's ability to control the current administration and future exploitation of the block. TPA may be way to accomplish these objectives. The enterprise still gets to sunset the policy admin system, but it retains integration with the TPA system and a high level of control to ensure user satisfaction with the administration of the block.

Deciding to Retain: In Zone A3, exemplified by Block 1, the net cost/risk of transfer is high, and so is the business value. This means that there is a little or no pay-off to transferring the business out of its current system for administration; and the business imperatives for retaining control over administration of the block is rather compelling. This situation argues strongly for retaining the block on the system on which it is currently administered.

Deciding to Outsource (BPO): In Zone C1, exemplified by Block 2, the net cost/risk of transfer is low and so is the business value. This means that there is a pay-off to transferring the business out of its current system for administration, and the business imperatives for retaining control over the administration of the block are not very compelling. These factors are arguments to utilise the BPO option.

Deciding to Sell: In Zone C3, exemplified by Block 7, the net cost/risk of transfer is high and but the business value is low. This means that there is no compelling reason to hang on to the block, and it would not pay to transfer the block to another system to consolidate its administration. In this case, it would be best to sell the block outright and let the new owner figure out how to cost efficiently administer the business.

Though some form of migration is a possible outcome of this portfolio management analysis, it is by no means the only outcome. Technology decisions made in isolation rarely deliver as much value (and sometimes cause harm) as those that are made in the full context of business drivers. Capgemini's portfolio management analysis model assesses key business issues including:

- Alignment of applications with the business and strategy
- Application contribution to business agility and competitive advantage
- Application performance with respect to customer experience and satisfaction

The above example looks at the existing business only, and does not take into consideration the technology available to the insurer. If we factor in migration to Oracle Insurance Policy Administration, the picture changes. Capgemini and Oracle customers have found that the risk of migrating to the Oracle system is low, while the business value to be gained in terms of agility, flexibility and improved speed to market is high for a few reasons:

- When migrating to Oracle Insurance Policy Administration, data integrity in inherently enforced through user-defined rules
- Capgemini has a proven track record of using proprietary tools to speed policy migration by automatically analyzing, scrubbing, mapping, translating and testing data that is being converted between systems. In addition
- Capgemini's conversion verification tool can be used to perform hundreds of edits to check data consistencies within database fields after the policy conversion is complete

If we take the Oracle system into account, the circles move to the left side of the graph. All blocks of business that an insurer chooses to retain can and should be migrated to Oracle Insurance Policy Administration without significant risk.

4 When Migration is the Option: Calculating Cost-per-Policy

When migration is the option, insurers want to know that the decision will reduce their overall costs, rather than adding to them. Capgemini has developed a methodology to measure cost per policy when a carrier chooses to migrate to Oracle Insurance Policy Administration. The variables involved will be unique to each carrier, but the cost per policy model includes two general categories: one-time and recurring costs.

One-time costs for the new system include:

- Implementation cost for the new system
- License fee
- Policy migration costs
- One-time infrastructure management costs such as new hardware

Recurring costs for the new system are estimated over a five year period and include:

- Application management costs covering upgrades, enhancements and support
- Infrastructure management fees
- Yearly cost for projects, calculated at approx. 10% of the implementation cost per year. We estimate one new product will be introduced each year during the five year period and consider this separately from application management which covers variations of existing products

Capgemini's cost per policy calculation does not include requirements analysis or integration costs in the analysis because these two factors are very dependent on the insurer.

Now let's take a look at the model at work. The following real-world example[1] shows how Capgemini helped a European insurer lower the cost per policy by 50% by migrating to Oracle Insurance Policy Administration. The insurer was using a legacy policy administration application which required over 20 FTEs a year to manage and maintain the system. The yearly cost for the system was €8 million to manage 600,000 policies, a cost per policy of €13.33 euros.

Table 1: Example of cost per policy calculation for a leading life insurance application versus Oracle Insurance Policy Administration

Current state		**Future state migrating to Oracle Insurance Policy Administration**	
Total run cost per year	€ 8,000,000	5 year cost including one-time costs for license	€ 20,000,000
5 year run cost	€ 40,000,000		
Total number of policies in the system	600,000	Total number of policies migrated	600,000
Cost per policy per year	€ 13.33	Cost per policy per year	€ 6.67

Cost savings 50.0%

Before migrating the system to Oracle Insurance Policy Administration, Capgemini prepared a cost per policy model using a five year analysis of costs. Calculations included:

- One time costs for the Oracle implementation and license, plus policy migration costs using Capgemini proprietary accelerators and tools.
- Recurring costs for application and infrastructure management plus project costs for introducing one new product a year for the five year period.

When all costs were factored in, it was estimated that the five year cost of implementing and maintaining Oracle Insurance Policy Administration for the 600,000 policies would be €20 million. This results in an average cost per policy of €6.67 per year for total a reduction of 50%.

[1]Note: This example from a Capgemini project represents real-world results which have been simplified for illustrative purposes. Due to various factors which are unique to each insurer, results for future similar projects may vary.

5 Vendor Considerations

The variables that go into cost-per-policy calculations will differ from carrier to carrier. Therefore, it's important to engage an experienced consultant with a well thought out methodology to help build the business case. Capgemini has invested in proprietary methodologies, models and tools to help insurers make the right business calculations to drive IT investments for the future. Our commitment to helping insurers with policy administration transformation includes:

- Over 75 team members dedicated to Oracle Insurance Policy Administration across the globe utilizing Capgemini's Rightshore® model.
- Two large projects underway: one in the U.S. for a leading carrier and a second in Asia-Pacific for a multi-country roll out.
- More than 15 years of experience with life insurance policy migrations using our proprietary methodology and toolset. Using our proven methods, we've achieved a consistent conversion rate of over 99% with portfolios from 50 to thousands.

Capgemini is one of the leading service providers in IT outsourcing, with clients in the life insurance domain. Over 36 percent of Capgemini's 2009 revenue came from outsourcing, primarily application and infrastructure management. We have over 400 insurance clients across the globe and our financial services business in 2009 was €1.4 billion.

In addition to selecting the right consultant, choosing the right system is key to managing your costs per policy. It's important to select a vendor with staying power who will be able to adapt to the ever-changing technology landscape to provide support and an upgrade path for your system today and tomorrow. Oracle Insurance Policy Administration has been implemented in more than 25 insurance companies and provides unmatched flexibility and adaptability.

Oracle provides the world's most complete, open, and integrated business software with more than 370,000 customers in over 145 countries—including 20 of the top 20 insurance companies—and has over 30 years experience helping customers to adopt modern technology. Oracle's flexible, rules-based insurance applications are built upon a core of extensible business content that can be readily adapted to enable carriers to migrate existing products without losing functionality and rapidly develop new products to meet their changing needs.

6 The Benefits of a True Business Transformation

When considering policy administration replacement, many insurers feel overwhelmed by the sheer breadth of functionality that must be taken into account. Many older systems not only administer policies—they include general ledger functionality, commission, claims and even more. This approach may have worked well in the past, but in today's rapidly changing market these integrated systems place constraints on a carrier's ability to adapt and make changes quickly. In older, monolithic systems, if a carrier wants to change its general ledger process, it must rewrite the underlying code in part of the policy administration system. This can impact every other process in the system, and usually requires a significant IT engagement for programming and testing. Similarly, new products require changes in underlying code, meaning they cannot be introduced quickly nor easily.

Oracle's approach is different. Oracle Insurance Policy Administration is rules-driven. Nearly all functionality can be configured using business rules, without any changes to underlying code. This makes the system incredibly flexible and significantly shortens the time required to introduce a new process. In addition, Oracle Insurance offers separate systems to handle parts of the business that are better left outside of policy administration—such as rating and underwriting. All Oracle Insurance systems are flexible, rules-driven and designed to work together seamlessly. If an insurer decides to make a rate change, it makes the change using business rules in the rating and underwriting system, not the policy administration system.

Capgemini is working with these flexible, rules-driven systems to help carriers achieve true business transformation. For example, we are working with a major insurer in the Asia-Pacific region to migrate its existing business onto Oracle Insurance Policy Administration. This transformation is already providing the carrier with increased agility and improved speed to market. A transformation of this scale touches nearly every department, so we are working with the carrier to provide change management oversight. A strong change management process is key to helping such a transformation succeed. Insurers who wish to undertake this transformation must consider four key areas: people, processes, product, and technology. If you begin with the insurance products in mind—in other words, with the products that will help you win more customers and grow market share—you can see what kinds of changes will be required in terms of people, process and technology.

In summary, the benefits of a true business transformation include:

- Increased business agility
- Improved transparency
- Ability to shorten time to market
- Reduced total cost of ownership, including significantly lower cost per policy

7 Conclusion

Few European carriers would argue that there is value in knowing their existing cost per policy. Some have even begun to measure their current state, but most still struggle with ways to calculate what their cost per policy *could* be if they improved operations. Moreover, they lack the methodology to determine the best course of action, such as deciding whether to keep, sell, migrate or outsource a particular block of business. An experienced consulting firm such as Capgemini, with a proven methodology for making these calculations, can help insurers achieve the cost savings they are seeking.

U.S. life insurer reduces time to market for new products by 66%

A large, Tier One life insurer based in the U.S. migrated away from its legacy systems and onto Oracle Insurance Policy Administration. Originally, the carrier's key business driver was to replace aging technology. However, mid-way through the project, the insurer decided to implement a new product and shifted the project goals and focus.

Using the configurable business rules in Oracle Insurance Policy Administration, the carrier was able to introduce a complex new annuity product to keep pace with changing market demands and competitive pressures. This product was tremendously successful, accounting for approximately 25% of the carrier's new business sales during its first year of availability.

In addition, the carrier successfully completed the migration of existing policies from its legacy systems onto Oracle Insurance Policy Administration. The carrier's legacy systems are now in read-only mode and the average time to market for new products has been reduced from 12 months to four.

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Capgemini, one of the world's foremost providers of Consulting, Technology and Outsourcing services, has a unique way of working with its clients, called the Collaborative Business Experience.

Backed by over three decades of industry and service experience, the Collaborative Business Experience™ is designed to help our clients achieve better, faster, more sustainable results through seamless access to our network of world-leading technology partners and collaboration-focused methods and tools. Capgemini utilizes a global delivery model called Rightshore® which aims to offer the right resources in the right location at competitive cost, helping businesses thrive through the power of collaboration.

Capgemini reported 2009 global revenues of EUR 8.4 billion and employs over 90,000 people worldwide.

More information about our services, offices and research is available at **www.capgemini.com.**