INSURANCE OUTSOURCING…HOW & WHY?

It was during 1980s that the concept of outsourcing became the part of business. Outsourcing is basically subcontracting a process to a third-party company. The decision to outsource is often made in the interest of lowering firm's operating cost and making better use of technology and resources. Today, almost 75% of companies use outsourcing in some way.

India is a leading country in outsourcing delivery. Many offshore companies try to reduce their overhead cost by outsourcing to India by making use of its huge talent pool and lower cost.

Some of the main reasons for outsourcing are as follows:

- ✓ Accelerate project
- ✓ Conserve Capital
- ✓ Create a variable cost structure
- ✓ Focus on core business
- ✓ Foster innovation
- ✓ Free up internal resources
- ✓ Gain access to IT resources unavailable internally
- ✓ Grow revenue
- ✓ Improve quality
- ✓ Increase speed to market
- ✓ None core
- ✓ Reduce operating cost
- ✓ Scalability

There are different types of outsourcing depending upon the need of the firm. One important method of outsourcing which the companies have adopted is call centers. These help the outsourcing company in utilizing skilled labor at cheap cost which is not readily available in home country. Outsourcing process or projects can be done with the help of the following:

Captive Direct

- These are basically creating organisations within organisation. It has least risk involved since operation is oversean by the parent comapny.

Direct Third Party

- Firms outsource operations to a third party service provider. This model is potentially more risky because the working arrangement is limited to the contract terms.

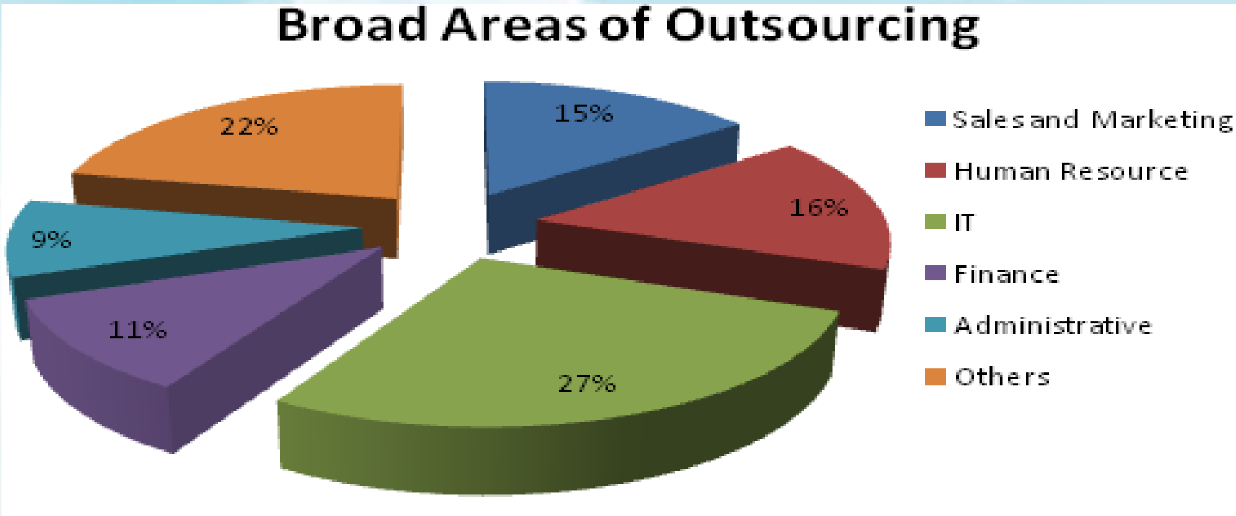
Joint Venture

- A domestic firm partners with the parent firm for shared control of the operations. It has higher risk involved compared to captive BPO.

Indirect Third Party

- A company enters into a contract with a domestic outsource service provider, who then subcontracts out all, or a part of the work, to an offshore company. This is the most risky outsourcing model.

Today, almost anything and everything are being outsourced by companies. In broader aspects, outsourcing is categorized into Technology Outsourcing (TO), Infrastructure Outsourcing (IO) and Process Outsourcing (PO). Technology Service is used when companies requires advanced IT, Application and communication technologies for their regular operations whereas Business Processes is used when companies want to focus on their main line of business and outsource certain non-core activities. From healthcare providers to software developers, everyone seems eager to leverage the benefits of outsourcing. The main sector which are actively outsourcing varied services in top outsourcing and consulting companies are given below:



Now, after analyzing the major components of outsourcing, we try to look at some of the common pros and cons of outsourcing. The table below elaborates the issue in brief way:*

Pros and Cons of Outsourcing

Pros

COST
- Outsourcing can help you save on time, effort, manpower, operating costs and training costs amongst others
- Your organization can save on investing in the latest technology, software and infrastructure as your outsourcing partner would be investing in these
- Contractual Obligation- The liability of a service provider is higher than that of an in-house employee. This makes working with them a safer bet for businesses
- Outsourcing will free up physical space that can be put to alternative uses

VALUE ADD
- Outsourcing your non-core activities will give you more time to concentrate on your core business processes
- This strategy can also give you access to professional, expert and high-quality services
- Staffing issues- By outsourcing a non-core function, you can avoid all work associated with recruiting and hiring staff for such non-core function.
- You will witness increased speed and quality of delivery for outsourced activities

Cons

COST
- There can be several disadvantages in outsourcing, such as, renewing contracts, misunderstanding of the contract, lack of communication, poor quality and delayed services amongst others

TALENT AND IP
- Outsourcing may lead to low morale of existing employees
- You may lose in-house expertise
- Your outsourcing provider will be able to see your company's confidential information and hence there is a threat to security and confidentiality in outsourcing

THIRD PARTY RISKS
- Supplier Bankruptcy—In case your offshore service provider becomes bankrupt or goes out of business, your organization will have to immediately move your business processes in-house or find another outsourcing provider
- Scattered Attention—Your outsourcing provider might not be only providing services for your organization. Since your provider might be catering to the needs of several companies, there might be not be complete devotion to you and your company
- Loss of Control—In outsourcing, you may lose your control over the process that is outsourced

*Source: CEB Views

An outsourcing process is a simple process but can be made complex due to lack of understanding. Basically, it is a process where different functions as well as works of the company are sent or given to a service provider to complete or execute the task. This service provider is often a Third Party Administrator (TPA) or Joint venture firm. Companies who understand all of the factors impacting outsourcing are the most successful. The typical process of outsourcing is highlighted below:*

*Source: Tytus Infotech

Insurance Outsourcing:

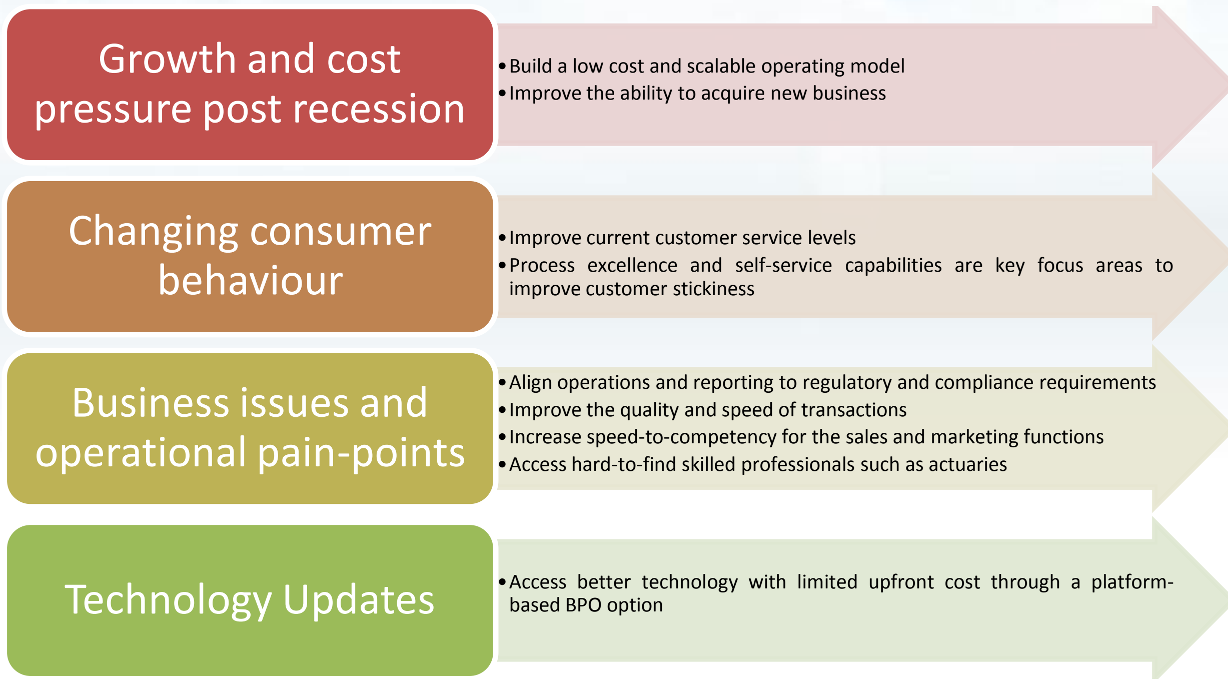
In this paper, we are trying to analyze insurance outsourcing from close angles. Insurance is defined as a commercial mechanism for transferring risk and spreading loss. Theoretically, the insurance industry bridges private interests and public good. Insurance outsourcing has gain great speed in the current market scenario. The majority of work that is being outsourced in Healthcare Insurance sector comes from US especially after Healthcare reforms implemented by the current government.

What can outsourcing do to an Insurance company?

- ✓ Outsourcing helps insurance companies launch new products
- ✓ Outsourcing can help check insurance claims fraud
- ✓ Reduce costs associated with legacy systems
- ✓ Support agents and customers
- ✓ Enables Cheaper, Better & Faster outcomes

The Insurance vertical represents significant third-party spends across IT and business processes within Banking, Financial Services & Insurance (BFSI), and the largest buyer segment in the outsourcing and offshoring industry. According to the data available, the number of contracts signed in Insurance BPO and Insurance AO dipped in 2008-2009 but is starting to witness a

revival. Growth and cost pressures, business pain-points, changing consumer behavior, and technology issues are the four major drivers for outsourcing within Insurance vertical. Again, the growing operational pressures are forcing insurance majors to invest in IT-BPO legacy modernization, innovation and administrative improvement initiatives. We try to discuss the insurance outsourcing drivers and Insurance BPO
value proposition in greater detail:*



*Source: Everest Group

<u>Latest Trends in Insurance Outsourcing:</u>

The general perception about Insurance Company's operation is quite tradition-bound in how they conduct business, using the same conservative attitude that governs how they invest policyholders' premiums. They consider outsourcing to be a bit too risky affair and due to this outsourcing have been comparatively low in this sector compared to other sectors. But the trend is on the move specially post-recession 2008 era. One of the main drivers towards outsourcing is the growth of eInsurance and mHealth applications. The existence of virtual insurance company is made possible by the internet. Some of the latest trends observed in the market are as follows:

- ✓ Insurance outsourcing deals increased drastically by more than 50% from 2010 to 2011.
- ✓ Application outsourcing is on the move as companies are outsourcing major work.
- ✓ Apart from India, other small nations are also making a mark by grabbing major deals.
- ✓ Global majors dominate insurance market in terms of revenue, depth of capability, and breadth of delivery footprint.
- ✓ Offshore majors have the highest average headcount and witnessed the fastest growth in average revenues as well as new accounts in the last three years.
- ✓ Within BFSI, the insurance vertical has larger and longer duration transactions
- ✓ Transaction-intensive functions (policy administration and claims processing) are the most mature insurance functions from a BPO perspective. More complex processes, such as actuarial analysis, underwriting and analytics support are increasingly getting outsourced.

Insurance Outsourcing Services:

Insurance BPO represents one of the most mature offerings within the BFSI BPO market. Notwithstanding some challenges, the value proposition around managing growth and cost pressures, addressing changing consumer behavior needs, and effectively dealing with operational pain points increasingly drives insurance companies to adopt Insurance BPO. This has led to the revival of the Insurance BPO market which saw a dip post the financial crisis. However, with the adoption pattern across geographies and insurance segments changing, change is observed BPO solutions as well. This is reflected across multiple dimensions, such as scope of services, technology requirements, global sourcing, and pricing structures, among others. Service providers need to align their offerings and make the necessary investments to address these changing requirements and capture the significant untapped potential. Insurance BPO is not the only service which can be outsourced but a variety of other services in Insurance domain. These are highlighted below:*

*Source: Cymatric

Life Insurance:

Life insurance is a contract between an insurance policy holder and an insurer, where the insurer promises to pay a designated beneficiary a sum of money upon the death of the insured person. The proceeds are typically paid as a lump sum but may also be paid in installments according to the terms of agreement. We discuss the common types of insurance available in market.

- ✓ **Term Life Insurance**: This provides coverage at a fixed rate of payments for a limited period of time. After that expiry period, coverage at the previous rate of premiums is no longer guaranteed and the client must either forgo coverage or potentially obtain further coverage with different agreement.
- ✓ **Permanent Life Insurance**: This is a form of life insurance such as whole life or endowment, where the policy is for the life of the insured, the payout is assured at the end of the policy and the policy accrues cash value.
- ✓ **Whole Life Insurance**: This is a life insurance policy that remains in force for the insured's whole life and requires premiums to be paid every year into the policy.
- ✓ **Universal Life Insurance**: This insurance is based on a cash value i.e. the policy is established with the insurer where premium payments above the cost of insurance are credited to the cash value of the policy.
- ✓ **Variable Life Insurance:** This type of policy provides lifelong protection. Also, allowed to make choices about where the premium is invested within the insurance company's portfolio.
- ✓ **Variable Universal Life Insurance:** This is a type of life insurance that builds cash value. In a VUL, the cash value can be invested in a wide variety of separate accounts, similar to mutual funds, and the choice of which of the available separate accounts to use is entirely up to the contract owner.
- ✓ **Survivorship Life Insurance:** This type of insurance covers two people on the same policy and the death benefit is not paid until the second person's death.
- ✓ **Joint Life Insurance:** This type of policy is intended to provide a benefit upon the death of the first spouse or business partner.
- ✓ **Convertible Life Insurance:** This allows one to enjoy the savings of term life premiums today, and can convert to a pricier permanent policy when one can afford it.
- ✓ **No Medical Exam Life Insurance:** This type of policy does not require a medical exam for approval. This is highly desirable for those looking for instant approval, without the waiting time involved when a medical exam is required.
- ✓ **Child Life Insurance:** Child life insurance is a form of permanent life insurance that insures the life of a minor. It is usually purchased to protect a family against the sudden and unexpected costs.
- ✓ **Senior Life Insurance:** This type of policy is especially important if one is nearing the age of retirement. People need to compensate for their loss of income and sustain similar lifestyle when they were employed.
- ✓ **Group Life Insurance**: This is basically one plan usually taken by employer to cover for life insurance of all employees working in a particular firm.
- ✓ **Military Life Insurance:** These are specially designed for Veterans and Military professional by the Government Department in order to cover for their life.
- ✓ **Key Man Life Insurance**: Key Man Life Insurance protects the business of the insured. Many small businesses are dependent on one or two key members of the company who have specific knowledge, resources, or client relationships that are irreplaceable. Should the business lose this member suddenly, this Policy can help to keep the business afloat in the face of significant financial losses that may be incurred.

Health Insurance:

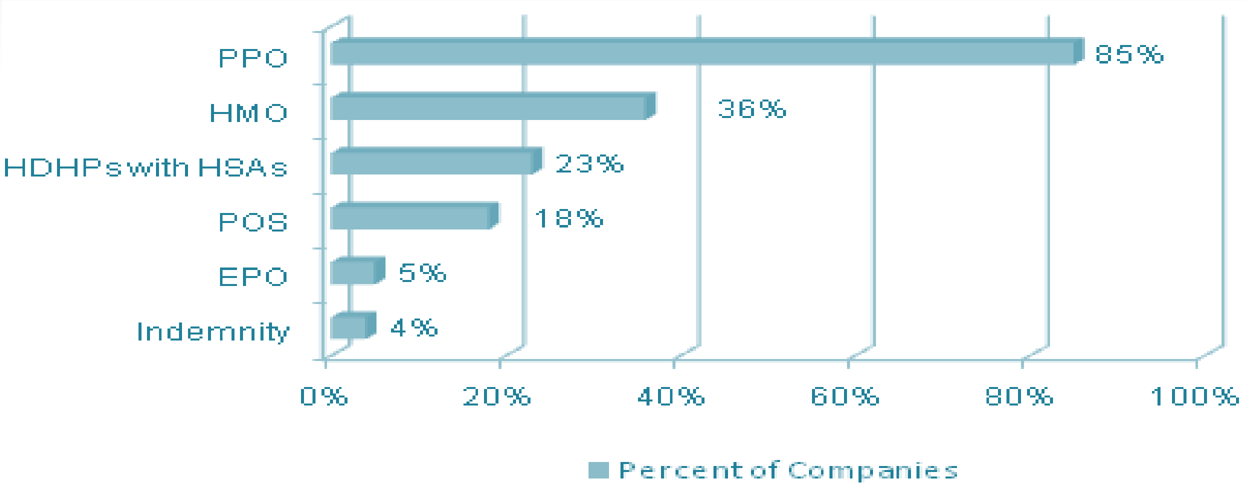
Health insurance is an important coverage that protects people from the devastating financial effects of unexpected health problems or illness. Health coverage can be issued to individuals, to employees of an employer offering health coverage, or to individuals that are members of association groups.

Today, broadly speaking, there are two main types of health insurance:

- **Indemnity or fee-for-service plans**: This is a traditional health insurance plan that allows access to any doctor, any hospital across the country. With this plan the insurance company pays part of invoices from doctors and hospitals.

- **Managed Care:** There are three types of managed care plans which are similar in nature but the programs differ somewhat.
  - ✓ **Health maintenance organizations (HMO):** This is the association of medical facilities that offer certain plans with a set of services at fixed prices.
  - ✓ **Preferred provider organizations (PPO):** A PPO combine elements of indemnity and managed care plans. It allows its members to choose doctors outside the PPO network.
  - ✓ **Plans under Point of Service (POS)**: The POS can be considered as the hybrid of HMO and PPO. This plan offers policyholders the freedom to choose their own doctors whether inside or outside the network while benefiting low cost visitation charge.

There is also Exclusive Provider Organizations (EPO) where an insurance company contracts with hospitals or specific suppliers. The insured members must use contracted providers or hospitals to receive the benefits of these plans.



USA Govt. Sponsored Health Insurance:

- ✓ **Medicare:** This federal program is designed for Americans age 65 and older. Medicare supplemental insurance does not cover all costs, particularly long stay in a hospital or nursing care at home.
- ✓ **Medicaid**: This insurance plan is available to people with low incomes. Obtain such insurance also may people who have reached a certain age, blind, disabled, and families who have dependent children.
- ✓ **Children's health insurance program (chip):** Children no older than 19 years are eligible for cheap or even free medical insurance. CHIP covers visits to doctors, payments for drugs, hospital stay, etc. For example, a family consisting of four people and receive up to $ 34,000.00 per year is eligible for a subsidized insurance.

Property & Casualty (P&C) Insurance:

This type of insurance provides financial protection for individuals, commercial businesses, and others against losses of property or losses by third parties for which the insured is liable. These insurance companies are classified under fire, marine, and casualty insurance. The common services which companies can outsource in this segment are as follows:

*Source: iGate-Patni

Some of the other types of insurance available in the market are briefly discussed below:

- ✓ **Auto insurance:** This is a contract between concerned person and insurer that specifies each party's rights and obligation in times of theft, vandalism, or natural disasters.
- ✓ **Homeowners insurance:** This provides coverage if property or house of an individual is damaged or destroyed. It can also provide with compensation for liability claims, medical expenses, and other expenditures that result from property damage and bodily injury suffered by policy holder or others.

There are many USA insurance companies but the following are some of the best known, the companies that have the highest ratings and the happiest policyholders. In fact, the below mentioned companies also outsource some areas of operation to domestic and foreign players:

Aetna	Global Life and Accident Insurance Company	Principal Financial Group
AIG American General	Liberty Mutual	Prudential Financial
Allstate Insurance Company	Lincoln Financial Group	Shelter Life Insurance Company
American Family Company	Mass Mutual Financial Group	State Farm Insurance

Boston Mutual Life Insurance Company	Metropolitan Life Insurance Company	The Hartford
Colonial Life	Mutual of Omaha	Transamerica
Farmers Insurance	Nationwide Insurance	William Penn

Top Insurance Outsourcing Service Providers:

A number of BPO and consulting firms have already made a mark in this sector of outsourcing but there are still opportunities for small players to make a mark in this market. The major players which constitute around 75%-80% of deals in insurance outsourcing are as follows:

Accenture	Genpact Limited	MphasiS Limited
Acclaris	HCL Technologies Limited	Softtek
Aegis Limited	Hexaware	Sparsh BPO Services Limited
Allsec Technologies Limited	HP	Sun Knowledge, Inc.
Atos	IBM	Syntel
Capgemini	iGATE Patni	Tata Consultancy Services
Cognizant	Infosys	Tech Mahindra Limited
Convergys India Services Private Limited	iProjects	Wipro
EXL Service India Private Limited	L&T Infotech	WNS Global Services Private Limited
Firstsource Solutions Limited	MindTree	ACS-Xerox

The future of Insurance outsourcing is encouraging. This is the time to make the most of the given opportunity. It is anticipated that more complex work like underwriting, actuaries and analytics are also likely to be outsourced. Though the big player will continue to prosper but SME can also contribute greatly. With the implementation of Healthcare reforms in US which aims at reducing healthcare costs, India stand to gain the most because India presents a considerable lower cost for Healthcare providers in US.

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