Business and Technology Issues in Corporate-Owned Life Insurance

A Novarica Research Partners Program™ Report

Underwritten by Andesa Services, Inc.

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Executive Summary

Corporate-owned life insurance and bank-owned life insurance (COLI/BOLI) product lines are an important niche of the overall US-life insurance industry for 2016. These products, which provide a key funding mechanism for employee benefit programs, including executive compensation plans, tend to be underwritten by a limited number of carriers, leading to a high market share concentration.

Bank-owned life insurance (BOLI) assets held by commercial banks, savings banks and savings associations surpassed $154.5 billion at the end of third quarter 2015, reflecting a 4.5% increase from $147.8 billion at the end of third quarter 2014.The largest portion of BOLI assets was held in separate account (46.4%), followed by general account (42.9%) then hybrid account (16.7%). While hybrid account assets had been growing most quickly in recent years, that slowed somewhat in 2015 with the fastest growth for the period being in general account assets (8%). Due to different regulatory considerations and competitive concerns, comparable COLI data is generally not available.

For carriers in the COLI / BOLI markets, the issues, challenges and opportunities are somewhat different than what is currently being experienced for the larger, and more traditional, units focused on Individual and Group Life insurance.

Through this study, which included **eight carriers that are currently actively selling new business**, we are able to illustrate priorities for these important units as they plan for future growth and client support. The information contained in this report can be instructive for strategic planning, particularly in a line of business in which results appear to be very closely correlated to fundamental economic activity.

This report presents and discusses the findings of a survey of 8 large L/H insurers (annual premiums over $1B).

This report is a product of the Novarica Research Partners Program, which enables industry sponsors to underwrite surveys on topics of interest. These surveys are conducted using the same methodologies and with the same respect for participant privacy as Novarica's independent surveys and reports.

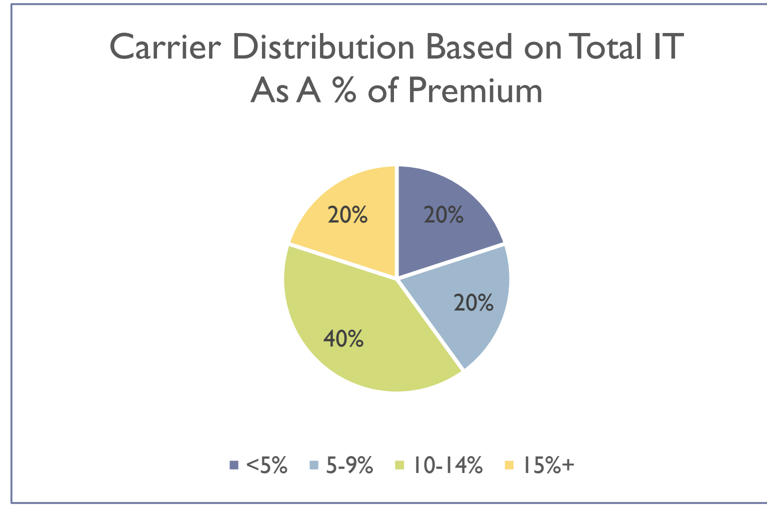
Underwriting sponsors have input on question design and general characteristics of target respondents only.

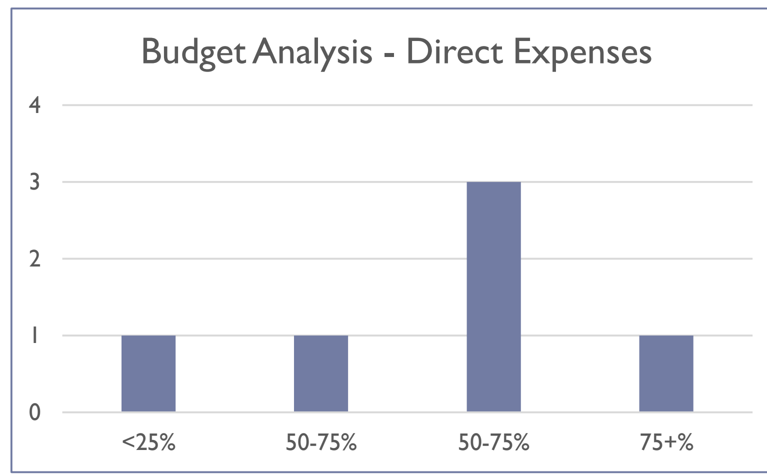
Novarica conducts the survey and analyzes the results independently. Underwriting sponsors do not have draft approval or other ability to influence content of the final report.

* *Source: Equias Alliance/Michael White Bank-Owned Life Insurance (BOLI) Holdings Report™, 12/14/2015*

IT Investments Correlate to Block Size, With Shared Service Costs Impacting Expense Ratios

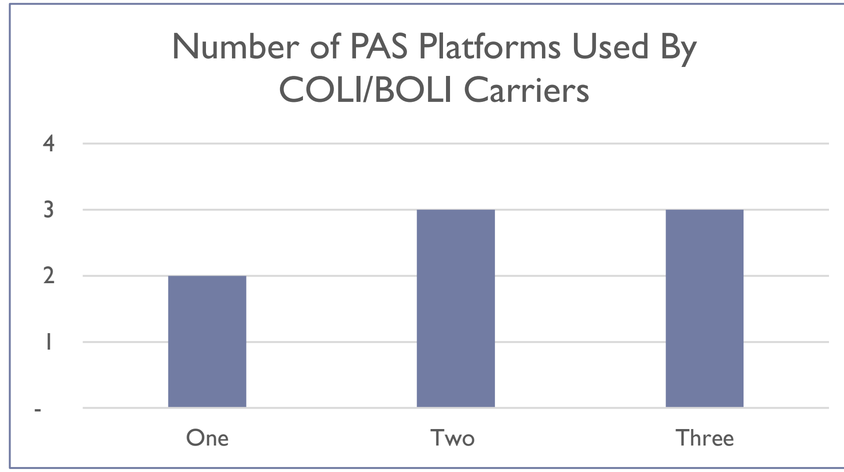
- For participant study carriers reporting premium data, Inforce Premium averaged approximately $340M.
  - The average number of contracts / carriers was approximately 1,020.
  - The approximate number of lives / carrier was 57k.
- IT budgets tend to correlate closely to the overall size of the block.
  - IT expenditures for the line of business averaged 3.9% of inforce premium.
  - The study identified a high degree of variability in the IT expense ratio, influenced by shared services / overhead allocations.
- For most COLI/BOLI organizations, more than 50% of the IT spend is an allocation rather than under direct control.
  - High percentages of control **can** mean reduced reliance on shared services. This can also reflect an expectation that capabilities designed for the specific line of business in question can be used rather than a unit being required to use generalized capabilities.
  - Somewhat unusual for life carriers, however, there's an **inverse** correlation between the percentage of IT allocated to the COLI/BOLI units in this study and their expense ratios.

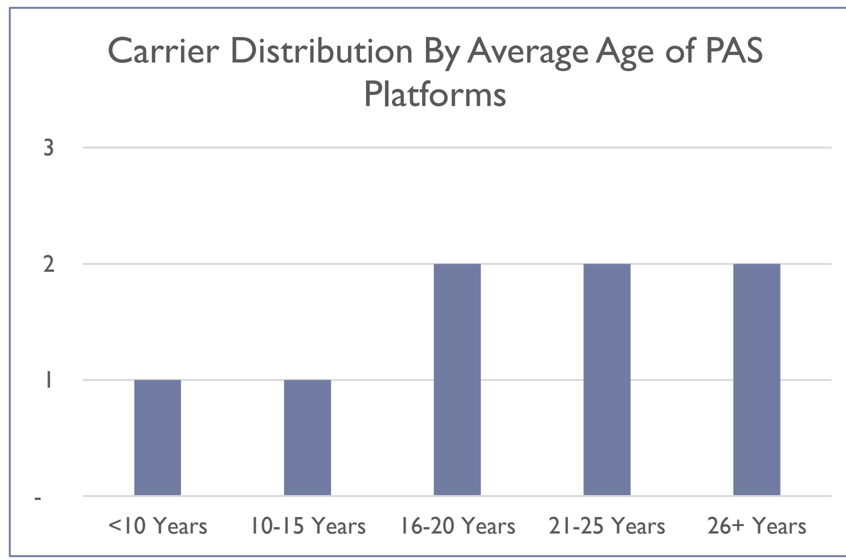




Technology Environments are Generally Diverse … and Aging

- **For carriers in any line of business, time to market for new products can be a critical performance metric.** The age and diversity of the underlying technology platforms for a carrier are frequently inversely correlated to the flexibility needed to get new products and enhancements to market in a timely fashion.
- **For this line of business, core PAS diversity is the norm.** Participants reported using, on average, 2 platforms for COLI/BOLI. This somewhat masks another underlying issue, however, with the average age of these systems at slightly more than 19 years old. Almost 25% of the systems in production are greater than 30 years old.
- **Multiple PAS platforms have a variety of origins.** In some instances it may be the result of acquisitions. In other cases, insurers use different systems for different purposes. Irrespective of the source for multiple platforms, unless architected well, the added complexity can create an impediment to both flexibility and market responsiveness.



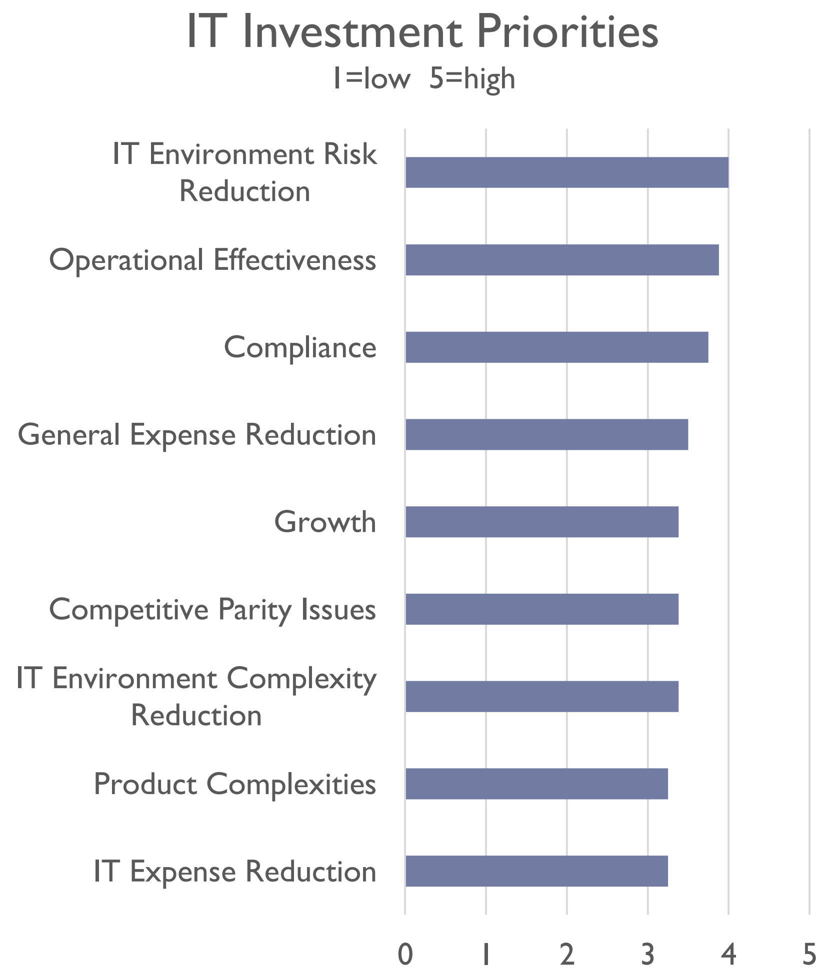


Time to Market is Less Critical Than in Other Life Insurance Lines

- **Product changes take place at a modest frequency and pace for carriers in this sector.**
- **Carriers report, on average delivering slightly less than one new product to market per year.** In no case does a carrier in this study introduce more than one new product per year to market. Looked at another way, on average, these carriers deliver a new product to market every 14 months.
- **Speed to market varies considerably by carrier.** While the study shows that it takes an average of 11 months to deliver a new product, one carrier reports that new product delivery requires approximately 21 months in their environment. Not surprisingly, their multi-PAS environment now averages 24 years old, including a 30+ year old platform.
- **Enhancements take place more frequently … and more quickly.** Enhancements take on average 5 months to deliver, with 75% of the participants reporting a consistent 6 month window for delivery.
  - 38% of the participating insurers deliver 3 or more enhancements a year.
  - For those delivering more than one enhancement, the number of months to deliver an enhancement is 4 or more.

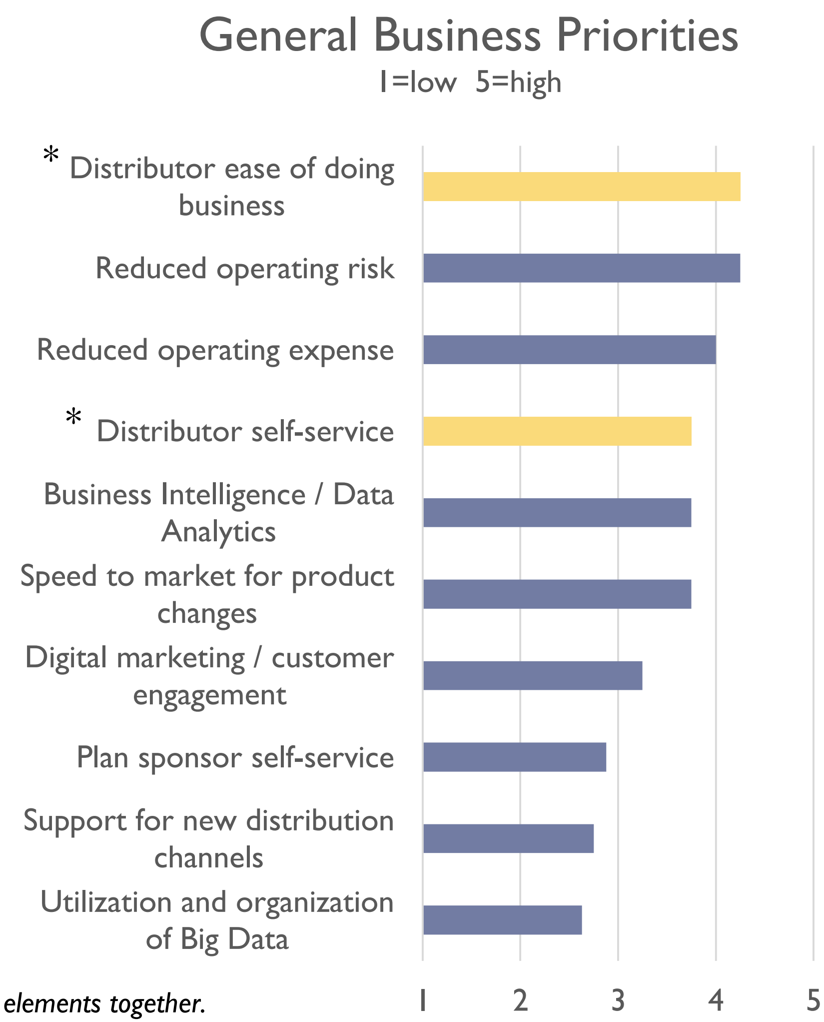
IT Environment Risk Reduction and Operational Effectiveness are Top IT Investment Priorities

- More than half of the CIOs in the study group cited IT risk reduction and operational effectiveness as the highest priorities for IT investment.
  - Compliance is also a high priority with half of the group giving it a ranking of 4 or 5
- There is wide diversity of priority level for growth and environment complexities:
  - About half of insurers cited high priority for these areas while the other half cited low
  - Growth and product complexities are tied to a company's IT environment.
- The ability to develop product features and bring products to market quickly require an environment that is flexible and configurable.
  - All insurers are running the COLI/BOLI business on legacy systems that are at least 10 years old, with only one noting that a system less than 10 years old was part of their current IT portfolio.



Distributor Ease of Doing Business and Reduced Operating Risk are High Business Priorities

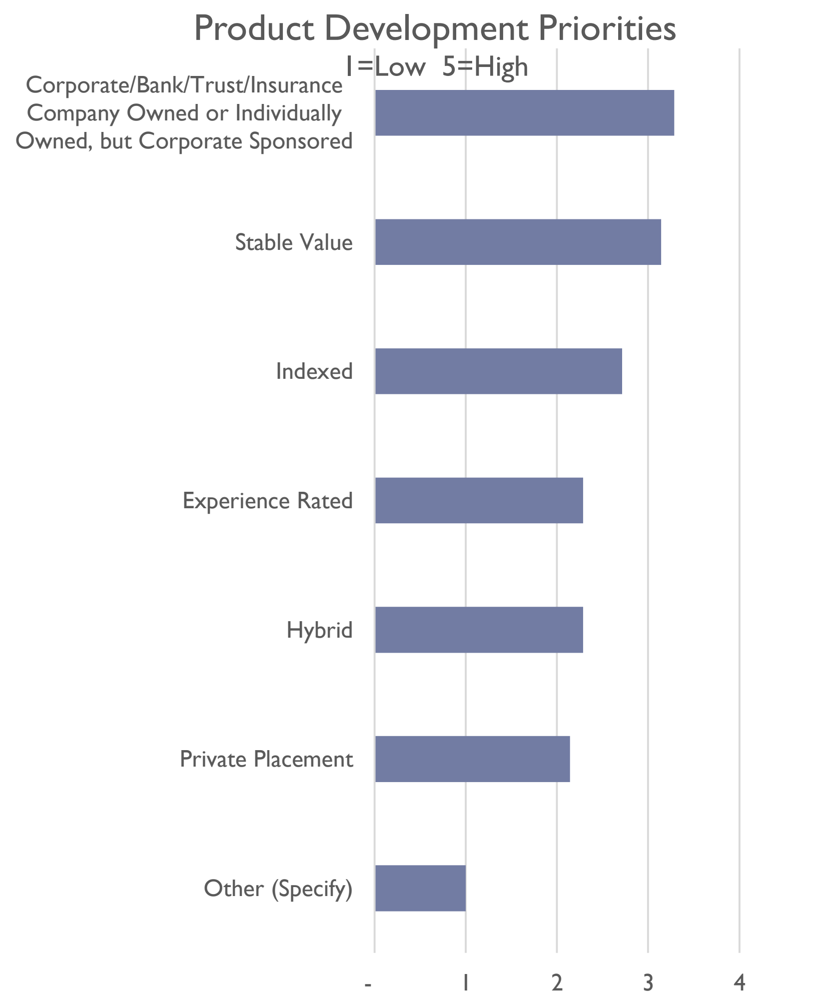
- Like the rest of the industry, COLI/BOLI insurers are focused on customer experience.
- For COLI/BOLI insurers, this means distributors more than anything else.
- Reducing operating risk and operating expense are constant priorities for insurers, reflecting both the competitive market for this business and the transparency that companies purchasing these products expect.
- While a small number of participants cited Big Data, new distribution channels, and plan sponsor self-service as high priorities, most are not considering these areas in their current period business planning.



* *The focus on Distributor-related issues is best understood when tying these elements together. Ease of doing business and self-service are frequently highly correlated.*

Product Development Priorities Vary

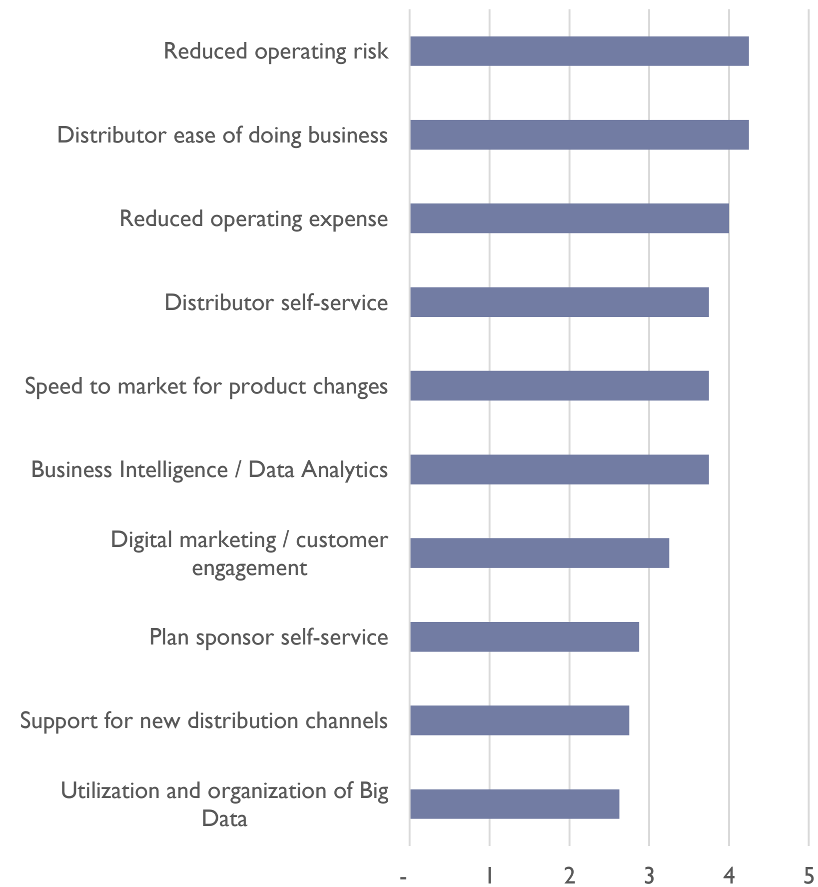
- The pace of new product development for this line of business is modest, averaging less than one new product per year.
- Underneath that pace, however, rest a varied set of planned portfolio enhancements or extensions.
- Fully half the participating carriers identified Corporate/Bank/Trust/Insurance Company Owned or Individually Owned, but Corporate Sponsored products as high priorities.
- Stable Value and Indexed products were also cited as higher priority initiatives, on average, by the participating carriers.



Almost All Insurers Agree: Tools to Support Distribution is a Top Priority

- Technology investments on the front end to support sales – such as tools for distribution, document management, and portal for plan administrators – are clearly high priorities.
- Other capabilities focused on Distributors, including Distribution and Compensation Management, reflect high prioritization.
- Exposing functionality and information access for plan administrators, typically through a form of portal, is considered high priority for the participants in this study.
- Conversely, exposing functionality for plan sponsors / participants is a universally low priority.

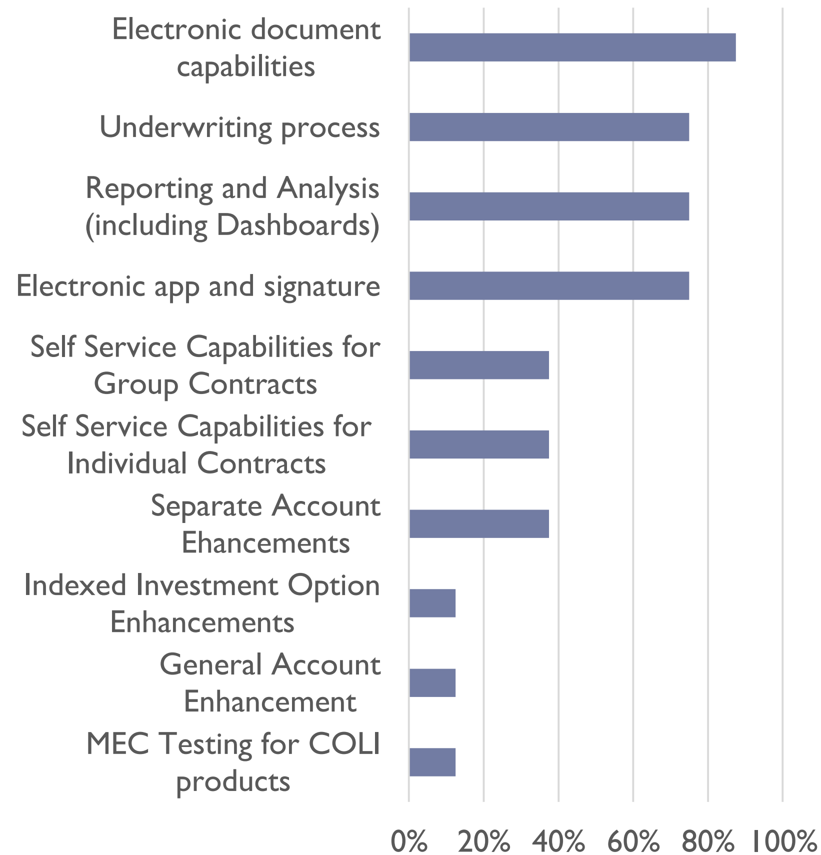
Marketing / Distribution Priorities For IT Investment



COLI/BOLI Insurers are Digitizing Processes

- Almost all insurers cite electronic document capabilities (production, delivery, access) as one of their five top priorities.
- Complementing the electronic documents capabilities is a high prioritization on electronic application and signature functionality, including the capture and tracking of consent data.
- These are also a key component to helping to reduce both operational expense levels and risk. Digitization of these aspects of business processes are increasingly an expectation of producers and clients alike.
- 75% of participating insurers report investing in the underwriting process; reporting and analysis tools are top priorities.

General Administrative Priorities for IT Investments



Concluding Thoughts

- **This is a niche market constrained by regulations, but players are growing.** A specialized line of business that has undergone notable change over the past decade. It is also a business that appears to be highly correlated with broader economic performance. As the US economy has strengthened recently, growth in this business has been notable for many of the participant carriers.
- **Distributor functionality is top technology priority.** For participating carriers, the key focus for investments now appears to be on improving/enhancing distributor facing functionality. Given the sales model, carriers are competing for attention from producers and focused on making themselves easier to do business with, as well as enhancing their product offerings.
- **Speed to market for new products is less important than other lines of business … today.** Current speed to market with new products appears to be, at best, modest. The specialized nature of this market may not require the level of innovation increasingly being expected in more consumer-oriented lines of business, but that may not be true as labor markets continue to evolve and the nature of employment, even for more senior employees, evolves.
- **Aging systems create risk.** The underlying technology supporting a majority of carriers engaged in this study would best be described as "mature," with environments that may be more complex or difficult to manage than they would be in an idealized state. The focus on addressing IT Risk and Complexity is a clear reflection of this concern.

About Novarica and Andesa Services, Inc.

Novarica provides technology strategy research, advisory services, and consulting to more than 80 property/casualty and life/annuity insurers.

Novarica's research covers trends, benchmarks, best practices, case studies, and vendor solutions, drawing on the expertise of its senior team and relationships with nearly 400 insurer CIO members of the Novarica Insurance Technology Research Council.

Through its advisory services, Novarica's expert team becomes an adjunct member of its clients' strategy and planning functions, providing a force-multiplier that facilitates faster, better, more informed decisions.

Novarica's consulting services focus on vendor selection, custom benchmarking, project assurance, and IT strategy, leveraging its proven methodologies, extensive knowledgebase, and broad network to rapidly deliver actionable insights and recommendations.

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Andesa Services, Inc. provides comprehensive, integrated policy administration, plan administration and support solutions for life insurance and annuity carriers and producers. Andesa began as a pioneer in the field of SaaS policy administration. Today, more than 30 years later, we provide seven of the top 13 life and annuity carriers and several top brokers with a comprehensive suite of services backed by decades of proven, practical expertise in the life insurance industry. Andesa's highly experienced team of U.S.-based professionals is made up of devoted client advocates who help insurers large and small save time, reduce risk and tap unrealized value.

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