NAIC National Association of Insurance Commissioners & The Center for Insurance Policy and Research
CIPR newsletter

When Innovation Meets Regulation

By Shanique ("Nikki") Hall, CIPR Assistant Director; and Julie Sherlock, Head of Insurance Strategy, Boost Insurance

◆ Introduction

Innovation in the insurance industry (and the world) is happening at a pace much quicker than most of us can keep up with. Fueled by recent technological advances, an exponential growth of data, changing consumer expectations, and a tremendous amount of capital, insurance technology start-ups ("InsurTechs") are redefining the fundamentals of insurance, including the way insurers communicate with policyholders, measure risks and process claims. As the InsurTech sector continues to emerge, and the use of new technology becomes more prevalent, state insurance regulators are moving quickly to ensure they are equipped with the tools to oversee this changing marketplace. They are also taking a more active role in understanding InsurTech.

The NAIC established an Innovation and Technology (EX) Task Force in late 2016 to monitor new InsurTech developments and help state insurance regulators stay informed of emerging technology. The Task Force is currently studying different ways in which the U.S. insurance regulatory framework can respond to and foster innovation. It has formed a small group of state insurance regulators to compile information on what states are doing with respect to innovation. The Task Force is also looking into several regulatory areas where innovation may be facing obstacles and has identified three specific areas to study. They are anti-rebating laws, cancellation and renewal regulations, and states' implementation and interpretation of Uniform Electronic Transactions Act or UETA.

To better understand some of these obstacles, I've partnered with Julie Sherlock, Head of Insurance Strategy at Boost Insurance, on this article. Boost is a technology-enabled MGA that streamlines the go-to-market process for innovative insurance products and distribution platforms by providing Insurance Infrastructure-as-a-Service to InsurTech startups and digital distribution partners. Julie was a panelist at our CIPR event held during the 2018 Summer NAIC National Meeting titled, "Can Regulation Keep up with Innovation?" and provided valuable insights on the regulatory challenges she has seen impacting InsurTech start-ups. This article will begin with an update on the current InsurTech landscape and initiatives by state insurance regulators to advance innovation. Julie will then provide her perspectives on some of the regulatory hurdles to innovation in the insurance industry.

◆ The InsurTech Landscape

While there is no one definition of InsurTech, the broadest definition involves the use of new technologies with the potential to bring innovation to the insurance sector. The term InsurTech is most commonly used to describe new start-up ventures, such as Lemonade, Slice Labs and Hippo, that were launched over the last five years. These InsurTechs are harnessing the latest technology—for example, artificial intelligence, cloud computing, blockchain/distributed ledger technology (DLT) and smart contracts, and the Internet of Things (IoT)—to develop and deliver new and innovative customer-centric products and services. Moreover, these InsurTechs are active in all major insurance products and all lines of business, with concentrations in the property/casualty business and in the marketing and distribution areas of the value chain.

Although the InsurTech "movement" is still in its early stages, it has become a global phenomenon, with well over 1,000 start-ups in more than 60 countries.[1] The United States is the biggest destination for InsurTechs due to its large base of sophisticated consumers and vast pool of venture capital. According to Deloitte, there were 1,516 InsurTechs globally as of the first half of 2018, with the U.S. accounting for a little over half of all start-up launches since 2008. While the majority of InsurTech launches still take place in the United States, the United Kingdom, Germany, Singapore and India are now significant markets and many other countries are following suit.[2]

More than $7 billion has been invested in InsurTech companies globally since 2014, with a record $2.5 billion raised across 101 deals in the first three quarters of 2018, according to FinTech Global (Figure 1 on the following page).[3] Moreover, there are a number of InsurTech accelerators and bootcamp programs helping InsurTechs attract capital and attain scale. For example, Startupbootcamp, Plug and Play Tech Center and Global Insurance Accelerator all provide InsurTechs access to investors and mentors.

InsurTech is said to now be entering its second wave as investors are channeling additional money towards more mature InsurTechs. In an InsurTech study led by Deloitte, it was noted "investor activity is expected to remain robust as investors shift their attention to maturing entities. More established InsurTechs will likely focus on gearing up

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Figure 1: Global InsurTech Investment (USD, Number of Deals)

Source: Fintech Global.

their solutions to scale, but we may yet see a second wave of new startups not too far down the road in areas where innovation has lagged." [4]

InsurTechs are also driving a new era of collaboration with incumbent insurers. Many incumbents have acquired technology from InsurTechs and incorporated it into their own ecosystems, or they are partnering with InsurTechs that provide software-as-a-service (SaaS) or licensing solutions. A recent World InsurTech Report by Capgemini[6] found insurance executives across the industry believe InsurTechs will be a major catalyst to redefine the customer experience, deliver widespread efficiencies, and create new business models. Of the 140 insurance executives surveyed, almost 96% of them said they were looking to collaborate with InsurTech firms in some way.

◆ U.S. Regulatory Initiatives

The U.S. regulatory system is unique and can be confusing to new entities. Some of the innovators and entrepreneurs behind InsurTech initiatives come from the technology sector and are not as familiar with the regulatory environment specific to insurance. While the rest of the world tends to view the U.S. market as a whole, our state-based system of insurance is regulated by insurance departments in the 56 U.S. states and territories. As such, rules and regulations may vary by state, which can be complicated for innovators to navigate. This is one reason regulation is often cited as an inhibitor of innovation in the insurance industry.

As InsurTechs have made inroads into the insurance world, it is particularly important they understand the regulated nature of the industry. State insurance regulators and the NAIC have been reaching out to InsurTechs to start a dialogue early on to promulgate a better understanding of the U.S. regulatory landscape. This dialogue also allows state insurance regulators to better understand the innovations in technology and products being developed. The NAIC has coordinated and facilitated numerous events and dialogues with InsurTechs and incumbent insurers including a "Bridge the Gap" event at Plug and Play and a "Meet the Regulator" session at the InsurTech Connect Conference in 2017 and 2018.

State insurance regulators and the NAIC also recognize there may be outdated regulations impeding the development of innovative InsurTech products and services. Many of the laws and regulations currently on the books do not contemplate technologies such as big data analytics and other recent innovations. However, their underlying purpose is often still very much relevant and important. Accordingly, it is important for state insurance regulators and InsurTechs to work together from the beginning to ensure applicable statutes and regulations are being followed. This could help bring innovative products to market more quickly and point out where regulations effective in the past, need to be modernized.

The NAIC Innovation and Technology (EX) Task Force recently compiled a list of innovation and technology contacts in each state insurance department. This will allow startups, accelerators and incumbent insurers to get in direct contact with someone in most State Departments of Insurance to ask questions regarding new concepts and ideas. The Task Force is also studying several regulatory areas where innovation may be facing obstacles.

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◆ Anti-Rebating

One area the Task Force is studying is insurance rebating, which occurs when an insurer or producer offers something of value to a customer, not specified in the policy, to "induce" an insurance purchase. Rebates can include cash, gifts, services, payment of premiums, employment, or almost any other thing of value, usually over a certain specified amount.

Historically, rebates were used in the life insurance industry by agents to induce a customer to purchase life insurance. The first set of anti-rebate laws were introduced more than 100 years ago after agents' use of rebates raised questions around unfair discriminatory practices. While the definition of what constitutes rebating may vary from state to state, nearly all states have some form of anti-rebating or anti-inducement laws on the books, most of which are substantially similar to the NAIC *Unfair Trade Practices Act* (Model #880).[7]

Although promotional items, such as mugs and pens, are often exempt from such laws, a company must be especially careful when it begins to offer—at no charge—more valuable goods or value-added services to its customers. For example, if a new entrant provided a wearable or smart home device to its customers, they should check to see if this would constitute an inducement and therefore would violate anti-rebating laws. A number of states have enacted revisions to their anti-rebating laws permitting certain value-added services directly related to the insurance policy sold.

The other two areas the Task Force is studying are cancellation and renewal regulations as well as states' implementation and interpretation of Uniform Electronic Transactions Act in the area of e-signatures. Julie Sherlock will provide more insight on these two areas in the remainder of this article.

"It Depends…"

At Boost, we have a recurring joke of "it depends" which we shout in the office after someone has identified another state-by-state variance that may stand in the way of improving the industry—both for the policyholders it should be serving as well as the companies that do business in it. There are numerous examples of this, but complex and inconsistent cancellation/non-renewal notice laws, and e-delivery and communication restrictions are two low-hanging targets we feel innovators and regulators can tackle together.

◆ Policy Cancellation and Non-Renewal Notices

Policy cancellation and non-renewal requirements are complicated and disparate across the 56 jurisdictions. These laws can be frustrating because they differ significantly by state and by line of business. Whether it's understanding and tracking policyholder notice timing requirements and ensuring the reasons for cancellation or termination are compliant in each respective jurisdiction, the administrative costs associated with this issue are enormous. Creating the technology to track and support this can cost hundreds of thousands of dollars, sometimes millions depending on the company size and the number of lines of business they support. Hundreds of hours are spent configuring and maintaining the systems needed to track these inconsistent rules.

Even if an insurer, managing general agent (MGA) or InsurTech start-up is only focused on a single line of business in a single state, they will still deal with several hundred configurations, which for a technology-savvy company is not terribly taxing. However, what about an MGA supporting multiple lines of business in multiple states or country-wide? They will have to configure thousands upon thousands of disjointed and varying rules and requirements—a massive undertaking.

Consider these challenges: different cancellation reasons, notice timing, notice delivery methods—all varying by line of business, by state, by reason. Does this state require a 90-day policy cancellation notice? A 60-day notice? Can we mail it? Can we email it? Will we be allowed to cancel/non-renew for this reason or do we need to change our policy form? Boost feels there should be greater consistency on this relatively simple issue across the states.

◆ E-Delivery and E-Communication

Currently 38 states allow for policyholders to receive all insurance transaction documents and insurer communications over the internet—if the consumer has given their consent.

Despite e-signatures being more efficient, it isn't the default method. Delivering a policy electronically is pretty simple these days. It's also definitely the modern consumer's preferred method of receipt. This simple change would instantly save billions of dollars across the industry—not to mention however many trees that get tossed into the trash, unopened.

Another challenge is "policy delivery" which is far from the only communication between an insurer and its policyholders. Depending on the state, certain notifications—like the cancellation and non-renewal notices discussed earlier—need to be sent via postal service. Consider the reliance on proof of mailing—this can be purchased at a physical post

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office or, to avoid that trip, you can upgrade to certified mail at a higher cost. In the age where online communication is the rule, not the exception, and everything has a digital footprint, this "postal service certification" seems entirely unnecessary, unless the policyholder expressly communicates it as their preference.

There have been incremental changes made to adjust to our new digital world. For example, 49 states now allow electronic proof of personal auto insurance for drivers—so let's take this next step forward and make electronic document delivery and communication of all types the default.

Boost Insurance is excited to work with the NAIC and other entities to tackle these issues later this year. Some of the critical issues we are trying to solve for, in addition to those mentioned in the article, include: improving the go-to-market process for start-ups, improving products and notice requirements to better support the on-demand/gig/sharing economy, modernizing the declination requirements and marketing restrictions in non-admitted business, and many more.

◆ Summary

The rise of InsurTech along with technological advances is having a profound impact on the insurance industry. State insurance regulators want very much to smooth the way for innovative products and services, but, need to make sure the consumer is protected, insurance laws are not violated, and they do not create unintended consequences. State insurance regulators will continue to work with innovators to identify obstacles that may need to be reviewed for relevancy as the world of technology evolves.

Endnotes

[1] *Source: Innovators Edge.*

[2] *"InsurTech entering its second wave," Deloitte Center for Financial Services, 2018. Retrieved from: www2.deloitte.com/content/dam/Deloitte/us/Documents/financial-services/us-dcfs-insurtech-entering-second-wave.pdf*

[3] *"InsurTech funding on track for a record-breaking 2018 with $1.7bn in capital raised," FinTech Global, August 22, 2018. Retrieved from: http://fintech.global/insurtech-funding-on-track-for-a-record-breaking-2018-with-1-7bn-in-capital-raised/*

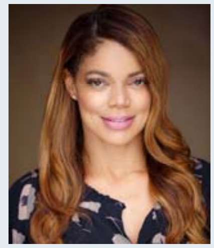
[4] *"InsurTech entering its second wave," Deloitte Center for Financial Services, 2018. Retrieved from: www2.deloitte.com/content/dam/Deloitte/us/Documents/financial-services/us-dcfs-insurtech-entering-second-wave.pdf*

[5] *Ibid.*

[6] *"The World InsurTech Report," Capgemini, Oct. 2, 2018.*

[7] *Parson, J., Marlette, D., and Powell, S., "Time to Dust off the Anti-Rebate Laws," Journal of Insurance Regulation," 2017. Retrieved from: https://www.naic.org/prod_serv/JIR-ZA-36-07-EL.pdf*

About the Authors



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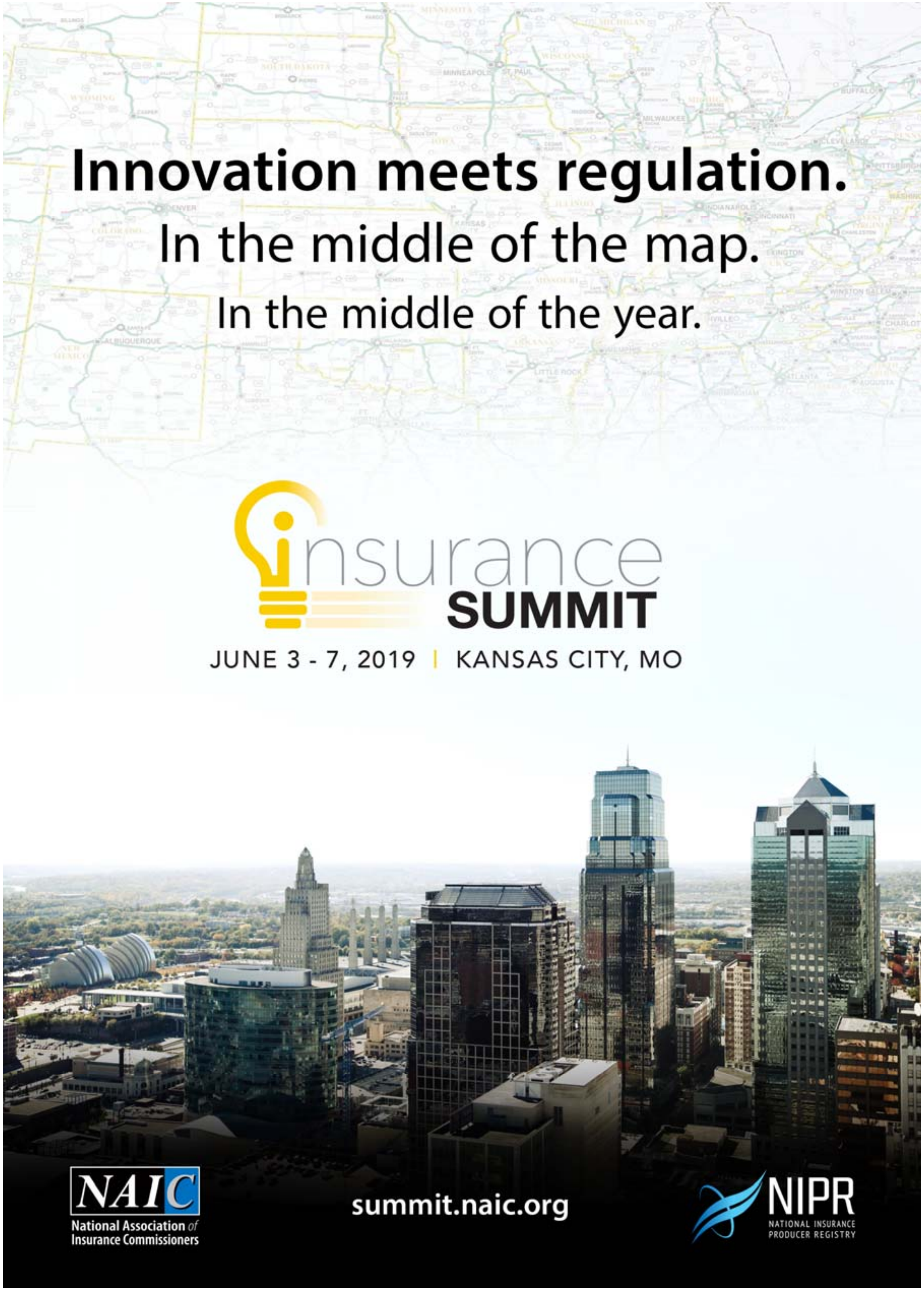
Julie Sherlock is the Head of Insurance Strategy at Boost Insurance. She is responsible for executing Boost's Insurance Strategy with oversight on underwriting, product development, and claims; additionally she serves as an underwriting resource for Boost's Insurtech Partners. Sherlock has an extensive insurance background, with over 13 years of experience in high net worth personal lines. She has expertise in complex programs, fine art insurance, and has underwritten for multiple lines of business, including Non-Admitted Solutions. She also has reinsurance experience, handling both facultative and treaty solutions for one of her prior carriers. In her last role she led the Underwriting Department for an Insurance carrier, responsible for all aspects of underwriting execution and underwriter development. Sherlock has a BA from Villanova University and an Art Business Certification from NYU.



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