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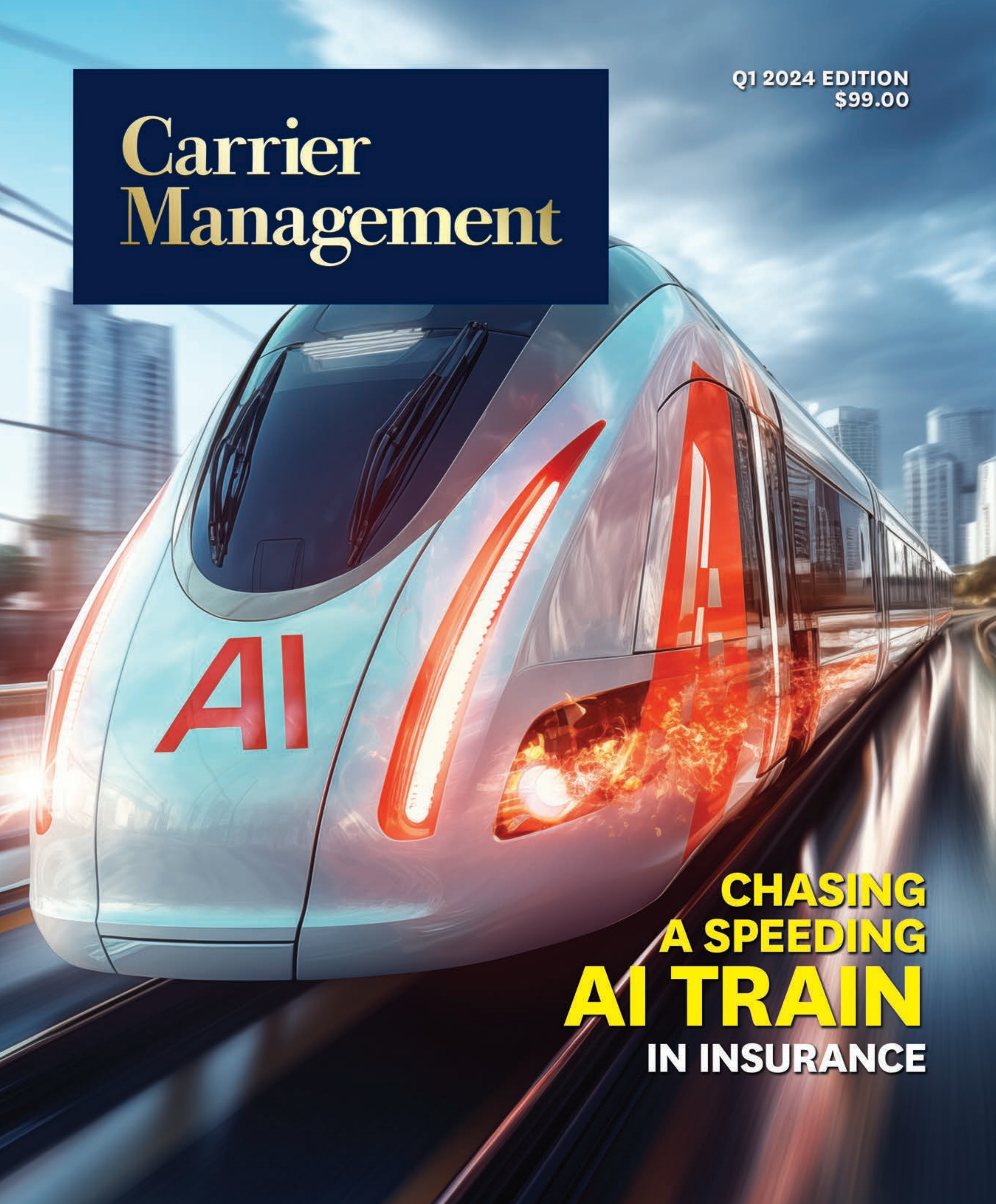


CHASING A SPEEDING AI TRAIN IN INSURANCE

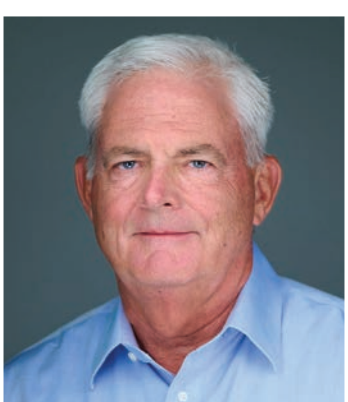
Meet CM's Guest Editor: SAS Institute's Fitz Fitzgerald

If you ask *Carrier Management's* Guest Editor Michael (Fitz) Fitzgerald to describe his career path to his current role as Insurance Industry Advisor for SAS Institute, he'll likely offer an analogy to a Swiss diplomat.

Once an insurance technologist for Royal & Sun Alliance and Zurich North America, and later an insurance technology analyst for Celent and CB Insights, Fitzgerald explains the reference: "My background is a hybrid background. I've worked in IT; I've worked in business operations. I have my CPCU as well as my PMP, the project management designation. So, I've actually had a foot in both the core insurance world as well as the IT automation world."

The dual perspective, "at times, has really caused me to feel a bit like the Swiss diplomat who can speak many languages, seeing many sides to the same problem," he told *CM* in a 2019 interview.

Earlier in his career, Fitzgerald worked on many "change-the-business assignments" for the P/C insurers—the longest lasting four years when he was in charge of the area that revamped the legacy automobile system at RSA in the United States. Shorter carrier assignments included a stint at Zurich NA, serving as VP of Enterprise Underwriting Solutions, where he led the evaluation of technologies to support a new product development process, and earlier work at RSA to develop the first global online technical insurance learning platform, delivering claims and underwriting training.



Michael (Fitz) Fitzgerald is Insurance Industry Advisor for SAS Institute Inc., an analytics and software solutions provider. He is also a guest editor for this edition of *Carrier Management*.

Those experiences, he believes, gave him a unique perspective to take on subsequent roles as an analyst for Celent and CB Insights, where he was involved with researching the application of technology for business value in insurance.

"I imagine a lot of people have experienced the fact that the business side of insurance speaks one language and the technical side speaks another," Fitzgerald said during a webinar hosted to the RiskStream Collaborative of The Institutes last November, titled "Overview on AI usage in Insurance," again explaining his career-long role as a "go-between" straddling the roles of IT and business professional.

With advanced analytics and AI taking on greater importance, Fitzgerald continues to add "go-between" value at SAS, an analytics and software solutions provider. His day-to-day work connects him to P/C insurance leaders ranging from the head of analytics at the department level all the way up to the board level, addressing questions they have about their preparedness for an AI future: "What do we have? What do we need? What should we do? What shouldn't we do? How do we prepare ourselves personally? Professionally? How do we prepare our company?"

The idea for the featured content in this edition, "Leading the AI-Powered Insurer," connects directly to that work, he said.

SAS has solutions for insurers grappling with concerns about AI. "On the more traditional side, we have data solutions which allows them to get control of their data."

In addition, SAS has also "been in this AI world for a long time"—with deterministic predictive models and also offering the types of non-deterministic natural language processing and machine learning tools that give rise to the trust, bias and data issues that make carrier executives fearful.

"The company understands those issues. And we have tool sets which help our customers manage them," Fitzgerald said. He noted, for example, that he has been mapping SAS features and functions directly to items that will be requested by regulators, such as information on data lineage and bias analysis, which will be part of insurer audits in states that pass AI regulations based on the NAIC's Model Bulletin on the Use of Algorithms, Predictive Models, and Artificial Intelligence (AI) Systems by Insurers, adopted in December. (See related article, p. 30)

Returning CM Guest Editor

Although he doesn't officially include this on his extensive resume, Fitzgerald became an award-winning journalist when he served as guest editor for a series of *Carrier Management* articles and videos titled "Eyes in the Sky: Geospatial Information Systems." The featured content, published in November 2021, was recognized by the American Society of Business Publication Editors with a National Azbee Award of Excellence for Overall Multi-Platform Package of the Year, honoring Fitzgerald along with *CM's* editors, video production team and designers.

A frequent contributor to *Carrier Management*, Fitzgerald also served as the guest editor for a section of *CM's* May/June 2019 magazine, titled "Innovation How-to-Guide." In addition, in 2020, he moderated *Carrier Management's* Virtual Roundtable—"Is Insurance Innovation Overrated?" CM

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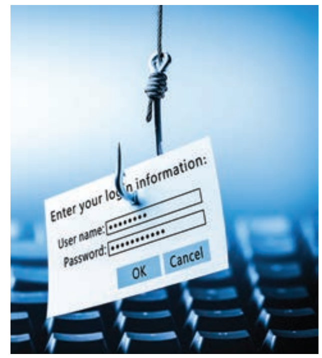

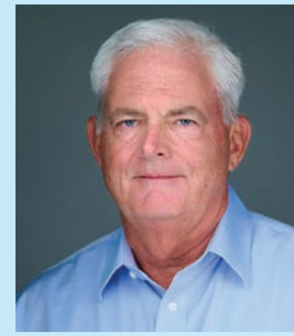

Mike Fitzgerald

Mike Fitzgerald, Insurance Industry Advisor for SAS Institute Inc., served as a guest editor for this edition of *Carrier Management*. In addition to conceiving the idea for the featured topic "Leading the AI-Powered Insurer," Fitzgerald developed the individual article topics and interviewed a variety of participants serving on boards, in executive roles and in middle management positions of P/C insurers, as well as a legal advisor and an investor devoted to the insurance space.

A frequent contributor to *Carrier Management*, Fitzgerald also served as the guest editor for a section of *CM's* 2019 magazine, titled "Innovation How-to-Guide" and an award-winning section of *CM's* 2021 magazine, titled "Eyes in the Sky: Geospatial Information Systems."

In 2020, he moderated *Carrier Management's* Virtual Roundtable—"Is Insurance Innovation Overrated?" (available on demand on the *Carrier Management* channel of InsuranceJournal.TV).

In addition to the articles listed on p. 4, for which Fitzgerald interviewed industry participants, he authored the articles on pages 17 and 20, and conceived of the articles on pages 22 and 48. He also participated in the interview of Jonathan Kalman of Eos Venture Partners for the profile article on p. 52

Read more about Mike on pages 3 and 21.

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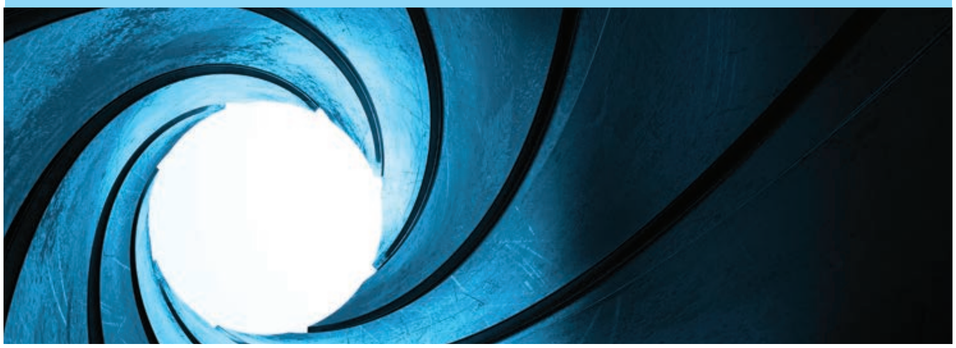

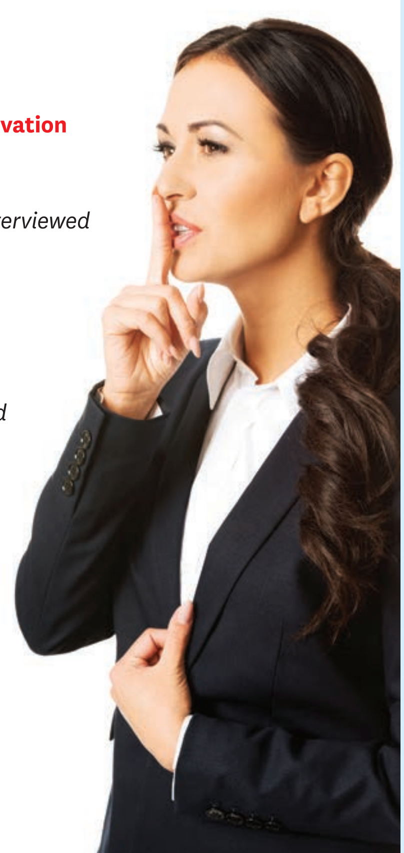

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From the Editor

AI Whisperers and Shouters

When *CM*'s guest editor wrote an article last year suggesting that industry talent and technology officers should team up to build company-specific HR programs for advanced AI, I thought it was one of the most interesting ideas we ever printed.

The article by SAS Institute's Mike (Fitz) Fitzgerald, republished in this edition (p. 20), tees up questions that he proposed we ask during talent officer interviews for this magazine: How can performance reviews be applied to generative AI engines? How do you infuse company values into AI? How do you onboard AI to learn "how we do things around here"?

As intriguing as the idea of applying typical HR processes to AI tools sounds, I couldn't imagine that CHROs had gotten too far along with any of that. On the other hand, activities preparing human professionals to work with AI were likely well underway. Upskilling and change management programs for underwriters, claims handlers, product developers, and tasks of redefining human roles and responsibilities, have likely been on the HR agenda for some time.

And there are new positions that carriers are probably starting to fill. An AI Prompter, aka "AI Whisperer," is one of the hottest new job titles, mainstream media reports say.

Still, when Deputy Editor Elizabeth Blosfield contacted carriers to interview talent leaders, she struggled to get any other than InsurTechs to talk. Maybe it was just the usual reluctance to talk to the media, I proposed. Fitz worried that the lack of interest meant HR departments aren't thinking about AI—not even to prepare their workforces.

"That's exactly the sense I'm getting," Blosfield reported, noting that carriers either said they had no one to speak to our questions, or that they hadn't invested in the HR aspects of AI.

"With all of the money and mindshare being invested in AI, with all of the risks and opportunities, why isn't AI upskilling a Q1 2024 priority for HR?" Fitzgerald asked. "If there aren't programs in place to either teach [people] how to use it responsibly or [explain] what it is," then carriers also cannot "combat some of the fear that's out there about what it's going to do to them."

Fitzgerald noted an idea for AI training put forward by VC Jonathan Kalman in this edition (p. 41). "The first thing I would do is I would say every employee gets a $500 stipend to take a course," said Kalman, a partner with Eos Venture Partners. Fitzgerald also referenced an observation from insurance technologist-turned-board member Ursuline Foley, who noted that many insurers mandate cyber training for employees. He envisions similar training for AI, explaining how popular AI tools work, identifying which tasks to use them for and which are absolutely off limits. "It will happen. It's just a question of time."

Still, Fitzgerald is troubled by the perceived delay. "The technology piece, a lot of the governance pieces are being worked on. Those were places where I was focused when we started. But when we ended, it's the HR piece. That's the biggest gap," he said, reflecting on his editor experience.

This regular *CM* editor was skeptical that there is any gap, suspecting instead that carriers are doing their own brand of "AI whispering"—that reticence to share operating secrets explains why they declined interview requests. Then, just before we were set to go to print, I spied an announcement about a cross-industry survey of HR and internal communications professionals from Gallagher. It found that 71 percent of respondents' firms do not have guidance on when, where or how to use AI.

The survey actually doesn't include insurance industry participants but suggests that the HR gap is real across industries.

Clearly, our own industry can't yet be accused of "AI shouting," or what one insurance industry participant describes as "AI washing." Kevin LaCroix, author of the D&O Diary blog, referenced the term "AI wash" from remarks delivered by SEC Chair Gary Gensler last year. Gensler drew an analogy to greenwashing as he warned that companies should not mislead investors by exaggerating AI capabilities.

That's a risk that may not even be on the radar screens of carrier CROs interviewed for another article in this edition (p. 48) but may be one to watch for D&O underwriters.

Read more:
"AI ChatGPT Chatbot Related Prompt Engineer Jobs Pay Up to $335,000," Bloomberg, March 29, 2023

"Rise Of The AI Whisperers," Forbes, May 11, 2023

"Nearly Three-Quarters of Employers Do Not Have AI Protocols for Internal Communicators, Gallagher Study Shows," PR Newswire, Feb. 8, 2024

"SEC Chair Warns Against 'AI Washing,'" The D&O Diary, Dec. 6, 2023

Send your feedback to Susanne Sclafane at ssclafane@carriermanagement.com

Fortifying the Future:

Mastering Offense and Defense to Combat the Risks of AI

Executive Summary: AI's integration into the insurance industry has introduced a range of sophisticated threats: deepfakes in insurance claims, advanced phishing attacks, the rapid spread of misinformation, the evolution of malware and IP risks.

Here, Celent Analyst Andrew Schwartz outlines offensive and defensive strategies for P/C insurers to adopt to combat multifaceted, AI-driven threats and leverage the power of AI in their operations.

By Andrew Schwartz

Andrew Schwartz is a Senior Analyst on Celent's North American Property & Casualty team. He spearheads the team's coverage of Generative AI/LLMs, InsurTechs and all claims-related topics.

In today's rapidly evolving landscape, property and casualty insurers find themselves at a pivotal juncture, akin to a digital battlefield. Echoing George Washington's wisdom from 1799 that "offensive operations, oftentimes, is the surest, if not the only means of defense," this sector stands at the forefront of a new era.

The advent of generative artificial intelligence (Gen AI) and large language models like ChatGPT brings both unprecedented opportunities and formidable challenges. This article explores the essential defensive strategies P/C insurers must adopt to combat the multifaceted threats in this AI-driven environment, while also examining the power of AI as a tool in their arsenal.

The Evolving Threat Spectrum

AI's integration into the insurance industry has introduced a range of sophisticated threats. These include deepfakes in insurance claims, advanced phishing attacks, the rapid spread of misinformation, the evolution of malware and intellectual property (IP) risks. Each threat demands a strategic and well-considered response.

Deepfakes: The New Frontier in Fraud

The advent of deepfake technology, capable of creating hyper-realistic digital fabrications, has ushered in a new and challenging frontier in insurance fraud.

These sophisticated deepfakes can convincingly mimic voices, facial expressions and even the mannerisms of individuals, making them a potent tool for fraudulent claims. It's now possible for a policyholder to employ a deepfake to fabricate a car accident scene, for example, making it appear as though their vehicle was significantly damaged—resulting in a financial loss to the insurer.

The challenge for insurers lies in distinguishing these high-tech fabrications from genuine claims.

To combat this, insurers are increasingly turning to advanced AI-driven detection tools that analyze patterns and inconsistencies invisible to the human eye. Additionally, specialized training for claims officers is crucial. This training focuses on the nuances of deepfake technology, enabling them to spot subtle anomalies and inconsistencies. By integrating these cutting-edge tools and training, insurers can fortify their defenses against this emerging form of fraud, ensuring the integrity of the claims process and safeguarding against financial losses.

Phishing: The Art of Deception

In the digital age, phishing attacks have evolved into a sophisticated art form, now further enhanced by AI technologies. These AI-powered phishing schemes are capable of crafting highly personalized and convincing deceptive communications, often mimicking trusted sources with an alarming degree of accuracy.

The challenge for insurers in this scenario is twofold. First, there is the need to protect their own organizational data from such attacks. This necessitates the deployment of advanced email filtering technologies that can discern and intercept these deceptive communications before they reach their intended targets. Second, there is a critical need for comprehensive employee training programs. These programs are designed to educate staff on the latest phishing tactics, sharpening their ability to identify and effectively respond to these threats.

By strengthening their defenses on both technological and human fronts, insurers can better safeguard their sensitive data and maintain the trust of their customers in an increasingly deceptive digital landscape.

Misinformation: The Battle for Truth

In the current digital era, the rapid spread of information is a double-edged sword, particularly when it comes to AI-driven misinformation campaigns. These campaigns, powered by sophisticated AI algorithms, can fabricate and disseminate false information at an alarming rate, posing a severe threat to the reputation and trustworthiness of brands, including those in the insurance industry. The potential for AI to generate convincing but false narratives or to distort facts can lead to widespread misinformation, significantly impacting customer trust and brand integrity.

Consider this scenario: An organized group uses Gen AI to create a false narrative around a major insurance company, claiming it is on the brink of bankruptcy due to poor management and risky investments. This misinformation spreads rapidly across social media, causing panic among customers and shareholders. As a result, the insurer's stock prices plummet, impacting their financial stability and the overall market.

To combat this, insurers must establish specialized teams equipped with advanced AI tools for real-time monitoring and analysis of online content. These teams play a crucial role in identifying and counteracting misinformation across various digital platforms. By proactively managing and correcting false narratives, insurers can protect their brand's integrity and maintain public trust. This approach is not just about damage control; it's about asserting a commitment to truth and transparency in an age when misinformation can spread unchecked.

Malware: The Invisible Threat

The evolution of malware, now increasingly powered and enhanced by AI, represents a significant and evolving threat to data security in the insurance sector. AI-driven malware can adapt, learn and evolve to bypass traditional security measures, making it more difficult to detect and counter. This new breed of malware can infiltrate systems, steal sensitive data and even disrupt operations, posing a serious risk to insurers, who manage vast amounts of personal and financial data.

To address this, insurers must invest in state-of-the-art cybersecurity solutions, including AI-driven threat detection systems. These systems can analyze patterns, predict potential threats and respond to breaches more efficiently than traditional security measures.

Additionally, insurers must ensure that these cybersecurity solutions are continuously updated and evolved to keep pace with the rapidly changing landscape of cyber threats. By doing so, they can safeguard their digital assets against the invisible but ever-present danger of AI-enhanced malware, ensuring the security and confidentiality of their customer data.

IP Risks: A Legal Perspective

In the realm of AI, navigating IP risks has become a critical concern. A striking example is the lawsuit filed by Getty Images against Stability AI, the creators of a cutting-edge AI program. This case revolves around Stability AI's alleged use of Getty's copyrighted images to train its AI model without proper authorization.

The implications of this lawsuit extend far beyond a simple copyright infringement issue. It highlights a complex challenge where AI can replicate and disseminate copyrighted material, potentially undermining the rights of original content creators.

For the insurance industry, this case serves as a cautionary tale. It emphasizes the importance of insurers not only ensuring their own compliance with IP laws but also understanding the risks associated with insuring AI-driven businesses.

On the underwriting front, insurers should include clauses in insurance policies that cover intellectual property risks associated with the use of AI technologies, or specifically exclude them.

To safeguard their own IP, insurers must develop robust data governance policies, implement strong encryption methods and maintain strict access controls to protect against IP infringements. Regular audits and compliance checks become indispensable in this new landscape, where

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the line between AI-generated and original content is increasingly blurred.

This case is a bellwether, signaling the need for heightened vigilance and proactive measures in IP management within the AI-augmented insurance sector.

AI as a Defensive and Offensive Tool

The strategic use of AI often serves as the best defense against the threats it poses. Leveraging AI in risk assessment, fraud detection and predictive analytics allows insurers to stay a step ahead of malicious actors.

AI's ability to analyze vast amounts of data and identify patterns is crucial in preempting and mitigating risks before they materialize.

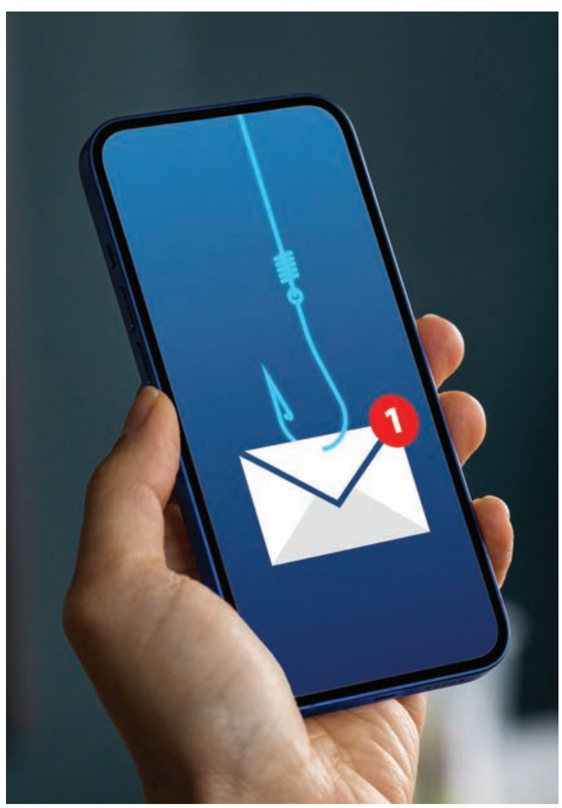
Below, we outline strategic responses for three C-suite executives: CEOs, CROs and claims officers.

- **CEOs: Cultivating a Risk-Aware Culture.** For chief executive officers, the primary task is to foster a culture that is acutely aware of and responsive to these emerging risks. This involves integrating risk management into every facet of business decision-making and establishing collaborations with technology partners to stay informed of the latest defensive technologies.
- **Chief Risk Officers: Architecting Comprehensive Risk Mitigation Frameworks.** CROs should focus on developing holistic risk mitigation frameworks that encompass both internal vulnerabilities and external threats. This includes deploying advanced AI monitoring tools and establishing rapid response protocols for security incidents.
- **Claims Officers: Specialized Training in AI-Related Fraud Detection**. Claims officers must receive specialized training in detecting AI-related fraud, particularly in identifying and investigating claims involving deepfakes and other AI-generated content. This training is crucial in maintaining the integrity of the claims process.

The Regulatory Landscape: Navigating New AI Standards

October 2023 marked a pivotal moment for AI with the U.S. government's issuance of an Executive Order on the Safe, Secure, and Trustworthy Development and Use of Artificial Intelligence. This directive, a significant milestone in defining the regulatory landscape for AI, calls for responsible AI practices with a strong emphasis on fairness, transparency and accountability. For the insurance sector, this order serves as a crucial guidepost, urging insurers to align their AI strategies with these emerging standards. This alignment is not just a regulatory compliance issue but a strategic imperative to leverage AI's potential for enhancing efficiency and customer service while adhering to ethical principles.

The National Association of Insurance Commissioners has been instrumental in further shaping this landscape with the adoption of a model bulletin. This bulletin outlines best practices for the use of AI by insurers, echoing the themes of the Executive Order. It stresses the importance of transparency, fairness and accountability in AI applications within the insurance sector. The guidelines set forth by the NAIC are designed to ensure that AI systems are used in a manner that is consistent with state insurance laws and regulations and do not result in unfair discrimination. Moreover, it underscores the need for ongoing monitoring and testing of AI systems to confirm their proper functioning and to prevent potential harm to consumers. (Read more about the model bulletin on p. 30.)



Together, these developments represent the creation of a coherent framework for insurers. They provide a regulatory compass for navigating the complex terrain of AI, balancing the need to harness its transformative power with the imperative to protect consumer interests and uphold ethical standards.

For insurers, this means not only adapting to a new regulatory environment but also proactively shaping their AI initiatives to be in harmony with these guidelines, ensuring a future where AI is used responsibly and effectively in the insurance industry.

Strategic Approach

As we navigate this AI-driven era, the insurance sector must adopt a proactive and strategic approach to counter emerging threats.

Understanding the nature of these challenges and implementing targeted defensive strategies is essential not only for safeguarding assets and reputation but also for leveraging AI's transformative potential for enhanced service delivery and customer satisfaction.

The path ahead is complex, but with a well-planned strategy, insurers can transform these challenges into opportunities for growth, innovation and resilience. Adopting a dual approach of using AI as both a shield and a sword will be key in navigating the intricate maze of digital threats and opportunities. CM

Leadership Tips:
How to Conduct a Layoff the Right Way

By Kimberly Tallon

Social media sites are filled with examples of layoffs gone wrong, displaying snippets of emails and other messaging to announce workforce cuts posted by some of the employees directly impacted.

But when circumstances point in the direction of a reduction in force, is there a right way for leaders to handle the action? What's the best way to deliver the news? What other options are there?

In this edition of Leadership Tips, *Carrier Management* compiles advice from talent management experts.

Consider alternatives.

Layoffs take a financial and psychological toll on both the terminated employees and those left behind—and can also be damaging to an organization's brand and reputation. Before subjecting your company to the trauma of layoffs, Gartner recommends considering alternative ways to reduce personnel costs:

- *Voluntary reduction in hours*. Many employees may willingly take a reduction in hours and commensurately lower pay.
- *Internal redeployment*. Some employees may have transferable skills that may be useful elsewhere in the business.
- *Reduce executive compensation*. Laying off staff while failing to contain executive pay is likely to damage staff morale and the wider reputation of a business.

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• *Voluntary leave of absence*. Extensive unpaid leave (typically three to 18 months) with an understanding that staff will return when conditions improve.
• *Organization-wide pay cuts*. All staff salaries are reduced by an equal percentage.
• *Benefit Cuts*. Fringe benefits cut based upon cost and impact assessment.
Source: "Gartner Says Layoffs May Ultimately Harm Shareholder Returns," Gartner, May 10, 2023

Decision time.

You've considered the alternatives and determined that a layoff needs to happen. How do you choose which employees to terminate?
• *Seniority-based selection*. The last employees to get hired become the first people to be let go. This method can help protect against age discrimination suits, since it protects older workers who usually have longer tenure with the organization. However, it may be overly simplistic. Just because someone was hired recently doesn't mean they are not an asset to your organization.
• *Status-based selection*. Contingent workers at your organization, such as contractors and part-time workers, will be laid off, while your workers with full-time employee status are given preference in keeping their jobs. Since your organization doesn't have the same legal obligation to contingent workers as it does to full-time employees, this method is great for organizations looking to protect their legal liabilities. However, it fails to consider worker productivity and efficiency.
• *Merit-based selection*. This method helps managers weed out poorly performing employees while retaining high-performing talent they could potentially lose using other methods. However, performance evaluations are often subjective and may not be done regularly. Make sure managers have documentation to back up their layoff decisions, or you could face legal liability.
• *Skills-based selection*. This method chooses which employees to terminate or retain based on how impactful their skill set is to the success of the organization. The executive team will need to understand the driving force of the company's success—customer service, technology, product innovation, etc.
• *Multiple criteria ranking*. This method involves creating a list of factors that are given different weights. The formula is then applied to each individual in a ranking system. Those who rank the lowest are laid off in that order until the company meets its financial goals. This method is customizable but difficult to set up.
Source: "How Do You Choose Which Employees to Layoff?" Careerminds, March 5, 2018

Don't just target remote workers.

Numerous factors go into determining who to terminate in a layoff, but proximity bias could lead managers to look at remote employees as easy targets.

The work of remote employees is often invisible. Newer remote hires also lack deep-rooted, face-to-face relationships with managers and leadership. And, of course, people naturally favor those whom they see regularly. Many leaders also still believe that at-home employees are less productive.

However, consider the optics of targeting out-of-office employees. For example, letting remote employees go might unintentionally communicate low support for certain populations (potentially caregivers or workers with health conditions), not to mention a willingness to lay off high performers. It might also contradict formal policies about remote work.

Managers should be conscious of their instincts to favor in-person workers. This includes asking oneself about biases against remote employees, and being honest about one's own feelings about in-office time.
Source: "Layoffs: Will Remote Workers Be the First to Go?" Korn Ferry

Conduct a disparate impact analysis.

Before implementing a layoff, employers should conduct an analysis to ensure the decision doesn't result in the disproportionate dismissal of older employees, employees with disabilities, or any other group protected by federal employment discrimination laws, advises the Equal Employment Opportunity Commission.

The EEOC recommends making a list of employees who would be laid off under the company's criteria and determining

whether certain groups of employees are affected more than others. For example, calculating the share of female or BIPOC employees affected and comparing it with the employer's overall workforce.
Source: "Avoiding Discrimination in Layoffs or Reductions in Force (RIF)," EEOC

Communicate effectively and with empathy.

Start the layoff process by scheduling the time and place for sharing the news. It's important to notify employees live—if not in person, then on a video call.

For in-office employees, choose a private, neutral space that allows those impacted to leave the building uninterrupted if they choose. For remote workers, book a private video call toward the end of the week so employees can decompress during the weekend if needed.

Do not, under any circumstances, notify employees that they've been laid off in a group meeting, or via email or instant message.

Collect all important materials before the meeting, such as termination letter, COBRA paperwork, severance agreement and information about final paychecks.

Don't "beat around the bush" or start the conversation with irrelevant small talk. Immediately inform your employees that they're being let go, though not through any fault of their own. Express gratitude for their time and work, and allow them to ask questions and share concerns.
Source: "Laying off employees: 5 steps to conduct empathetic layoffs," BetterUp, Nov. 1, 2022

Give advance notice.

If your business has 100 or more employees and meets the qualification standards of the Worker Adjustment and Retraining Notification (WARN) Act, a 60-day notice may be required. Also check the requirements for any similar state law.

But Onwards HR recommends giving employees notice of termination before a layoff whenever possible, noting that a common rule of thumb is to give as much notice as you would require if the employee resigned voluntarily, which is typically two weeks.

The type of notice you give depends on the circumstances:

- *Non-working notice.* A non-working notice means you dismiss the employee on the day of notification, and they can go home. This provides the team member the opportunity to decompress and begin working through their emotions over being terminated. It also provides a paid jumpstart so the employee can begin looking for a new position. If the employee is hostile, you can discontinue their company access immediately while still providing the additional paid time and resources.
- *Working notice.* Business demands may make it difficult or even impossible to offer employees a non-working notice period. If you have to provide working notice instead, remember to be flexible with their time so impacted employees are able to search for a new position and schedule interviews. You also may want to consider offering more than the standard two-week notice.

Source: "Advance Notice of Termination: To Give or Not to Give," Onwards HR

Manage the transition.

Some employees designated for layoff may still be needed after notice is given to help train those who remain or to complete work on time-sensitive projects.

To incentivize employees to stay on during the transitional period, consider offering perks such as expanded severance packages or retention bonuses.

Allow employees at least a day to process the news and consider the offer—and be prepared if not everyone agrees to stay on.

It's important to offer plenty of flexibility to transitional staff, giving them adequate time to schedule job interviews and

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network.

This training period provides the company with some stability during the change, gives impacted employees longer notice periods—and may even result in the discovery that some employees are simply too valuable to let go.

Source: "Laying off employees: 6 ways to ease the transition," Insperity

Consider outplacement.

Also known as career transition services, outplacement is an employer-sponsored benefit designed to help employees smoothly transition to another position or even another industry.

While investment in outplacement comes with a financial cost, it also provides a number of benefits like reducing the risk of anger-fueled repercussions, such as workplace violence or lawsuits; increasing morale for remaining employees; and lowering unemployment costs.

Services may include:

- Career coaching
- Résumé writing and review
- Job interview preparation and practice
- Career interests and skills assessments
- Job searching tools
- Pay negotiation training
- Networking advice
- Digital presence and social media optimization

Source: "What Is Outplacement? Everything You Need To Know," Forbes, May 26, 2023

Rebuild employee trust and morale.

Employees are motivated when they believe that if they perform their duties well, their jobs and current salaries are guaranteed, and promotions and raises are possible.

Layoffs undermine this psychological employment contract, as even employees who are excellent at their jobs can be vulnerable to layoffs during organizational hardships. As a result, those who remain may question the value of committing their time and effort to the organization. This leads to decreased motivation and productivity—and often a spike in subsequent turnover.

It's time to rebuild your team's trust. Start by being transparent. Provide employees with as much information as possible about the business progress and how you are making decisions.

You also need to ensure that employees are committed to more than a guaranteed paycheck, or else they may seek more stable employment. People can be motivated by good organizational culture, a strong mission and positive job experience as much as they are by money. Remind your team about the company's mission and the accomplishments you have achieved together.

Source: "Adapting to the new normal after company layoffs," Culture Amp, Feb. 1, 2024

Manage your team's workload.

In the wake of a layoff, the remaining employees may feel lack of trust in leadership and anxiety over the safety of their own jobs. Added to these psychological impacts, they are also expected to take on many of the responsibilities of their former coworkers. To avoid burnout, it's essential to evaluate your team's capacity after a layoff and right-size their workload.

Identify projects and initiatives that can be postponed. Start by creating a comprehensive list with your team of all ongoing initiatives and projects and discussing what each one solves, creates or improves. Rank these initiatives based on their expected impact and each project's potential benefits to the organization.

Determine which initiatives can be postponed but easily resumed later versus those where a temporary pause might be difficult to reverse.

Source: "How to Manage Your Team's Workload After Layoffs," Harvard Business Review, June 26, 2023 CM

Doom and Gloom
on Talent Exodus Overstated, Says Aon Exec

By Susanne Sclafane

Discussions of talent in the property/casualty insurance industry often focus on the advancing average age of the workforce and the idea that the looming departures of retiring professionals will leave carriers shorthanded.

But an analysis that executives at Aon shared late last year paints a different picture.

There's been "a little bit of Benjamin Button effect," Charlie Gall, an associate partner and P/C practice leader for Aon's Ward Benchmarking Group, said recently, drawing an analogy between industry professionals and a character in an F. Scott Fitzgerald short story who aged in reverse.

Speaking during Aon's U.S. P/C Performance Outlook webinar in late December, Gall revealed that the average age of P/C insurance professionals actually declined to 45.7 in 2022, down from 46.1 in 2020. The average age figures come from a study of 68 P/C insurers that Ward published in April last year in a report titled "Human Resources and Employee Benefits Practices."

As people leave the industry, "we're backfilling with younger, less experienced talent. So, it has brought the average age down," he said.

"For the last 10 years, it feels like there was going to be doom and gloom of this mass exodus of talent and people out of our industry. But I don't think that's ever really been a problem for us. And it doesn't look like it's going to be," Gall said during Aon's webinar.

Supporting his view, Gall displayed a pie chart indicating that the percentage of carrier professionals falling in different age ranges is well distributed with about one-fifth in their 30s, about one-quarter in their 40s and a little over a quarter in their 50s.

"And then you have 60s and people even working into their 70s. We're having more people working longer in their life. And we have a pretty good [age] distribution."

"I do think we aren't going to see that kind of doom and gloom of a mass exodus. That's not to say we can sit back and just not plan forward. But it definitely feels better than it has," he said.

Gall went on to point out that employees over age 60 represented 12.3 percent of the workforce in 2022, according to Ward's 2023 analysis, down from 12.7 percent in 2020. A slide he displayed showed that the most recent figure is more than 5 percentage points higher than a 7.1 percent

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figure from 2008, confirming his assertion that people are working longer. The slide also revealed that the over-50 age cohort dropped from 42.7 of the carrier workforce in 2016 down to 40.6 percent in 2020 and 39.6 percent in 2022.

"We're starting to see a little bit of shift in this age distribution," he said, again noting that the average age has gone down.

That said, carriers are still worried about talent. Earlier during the same webinar, Jeff Rieder, partner and head of Ward Benchmarking, shared results of Aon's Global Risk Management Survey, showing insurers' "failure to attract and retain talent" among their top 10 risks, putting it second—behind the No. 1 risk of "cyber attacks" and ahead of "weather and natural disasters"—in 2023. Looking out to 2026, the same insurers still ranked the talent risk in the top 10, but this time in fourth place with "climate change" taking over the second-place ranking.

Referencing earlier reports, Gall noted that average tenure in the industry is falling—coming down nearly a full year—to 9.4 years in 2023 from 10.3 years in a 2021 study. But like average age, tenure was well-distributed on a pie chart, although the 0-3 years category was the largest segment, making up one-third of the total pie. "As we've had a lot of turnover, we haven't been able to replace with experience, and we have had to go into less experience," he noted.

Strategic Workforce Planning

Gall said that carriers are tackling talent challenges with "strategic workforce planning." A more robust approach than just paying attention to headcount, such planning means considering skill sets needed for the future, where and how work gets done, and employee rewards and recognition, among other factors, he said.

In terms of the "where" factor, the January 2024 edition of the Jacobson-Ward Insurance Labor Market Study (released after the webinar) revealed that 84 percent of carriers (P/C and life/health combined) anticipate no change in the number of days they will require employees to come into the office looking six months out. Rieder said that the most typical hybrid model—for 46 percent of carriers surveyed—anticipates one or two days in the office, with 30 percent requiring three or four days. (See related sidebar for more results from the first-quarter 2024 Insurance Labor Market Study.)

Offering some information pertinent to the "rewards and recognition" aspect of strategic workplace planning, Gall said that Aon projects base salaries will rise about 4 percent in 2024. "That's about what it was before the last economic downturn in the early 2000s," Gall said, referring to the 2007-2008 downturn.

Beyond base pay increases, Gall said that the majority of merit increases will be in the 3.5-4 percent range, with promotional budgets adding another half a percent point.

Rieder noted that "pay compression" will become increasingly problematic for carriers. In particular, he explained that over the last few years, at smaller companies, "senior contributors are being paid near the levels of executive leadership, in some cases even more." He also noted that more and more states are adopting pay transparency laws, which will shine the light on this trend. CM

Additional reporting by Allen Laman

Survey Shows 'Significant Pause' in Industry Job Growth

By Allen Laman

More than half of insurance companies expect to increase staff in the next year, according to the latest labor market study from Aon and the Jacobson Group.

The research shows that 52 percent of carriers plan to increase staff, while 38 percent plan to maintain their numbers and 10 percent plan to decrease in size.

While the 52 percent figure may appear promising, Greg Jacobson, CEO of the Jacobson Group, explained that, not counting 2020, it represents "the lowest that number has been since 2012," when the country emerged from the financial crisis. "So, there's been a significant change in thought process as it relates to companies looking to expand their hiring," he explained. "And it's slowed down fairly significantly. That said, this does not mean—and we have not seen this—that there are going to be mass layoffs that are going to be impacting the industry."

Aon and the Jacobson Group have conducted labor market studies biannually for the past 15 years. They focus on analyzing the market within the insurance industry, specifically with insurance carriers. The latest study covered about 275,000 employees, or about 17 percent of the market.

Jacobson acknowledged that layoffs have affected the insurance space recently. He shared that the 10 percent of companies with plans to reduce staff size in the next 12 months is comparable to recent years.

"I think that overall, what this is saying is that there's a significant pause, at the very least, in terms of the amount of growth that's going to be taking place in the industry," he said. "But not necessarily mass layoffs, as 38 percent of companies are planning on just keeping the same number of staff that they had over the last 12 months."

According to the labor market study, last year, 67 percent of companies planned to increase staff, but only 54 percent of companies did. Jacobson said this marked "probably a bigger difference than we've seen in the past."

The difference, especially over the last six months, is more companies are choosing not to fill positions. CM

A longer version of this article is published on the Carrier Management website.

Organizing for Action:
The Board of Directors in the AI-Powered Insurer

Executive Summary: Banks learned the hard way—with online banking—that setting up separate, standalone organizational structures is an inefficient and costly way of propagating new technologies. SAS Institute's Insurance Industry Advisor Mike Fitzgerald advises insurers not to make the same mistake with AI, urging them to include AI considerations in existing processes.

Here, he offers a logical place to start—the board of directors—outlining some of the changes AI-powered insurers will make to standing committees of their boards to address the opportunities and risks associated with AI.

Michael (Fitz) Fitzgerald is Insurance Industry Advisor for SAS Institute Inc., an analytics and software solutions provider. He is also a guest editor for this edition of *Carrier Management*.

By Michael (Fitz) Fitzgerald

Financial services technologies come and go. Useful shiny objects become standard operating procedure. How quickly and effectively an insurer makes this transition varies. Faster and better yields more business value.

Online banking is a classic case. Many banks initially set up their online banking as a separate, standalone unit. This was costly as it required parallel management structures, duplicated existing business processes and localized knowledge about digital banking in a specific group of employees.

With time, online became part of the core banking business and just another "way we do business around here." Costs were reduced and processes streamlined.

Insurers that use existing organization structures to propagate new technologies are examples of faster and better. AI is no exception. Insurers have an opportunity to speed and improve AI implementations by including AI considerations into existing processes.

The place to start is the standing committees of the boards of directors. This article outlines adjustments AI-powered insurers are making to board committees in order to address both the opportunities and risks of AI.

Board Committees

A board of directors sets an insurer's strategy and policies, hires and oversees the performance of the company's executive officers, and ensures that the company complies with legal and regulatory requirements.

Importantly, the board is the last line of defense for the brand of the insurer. It ensures that its strategy and values further the agreed purpose of the organization. AI has the potential to bolster or destroy a brand. Boards are working to protect their firms while harvesting full value from the tools. To accomplish both goals, they will adjust their existing committee structure.

Insurance board committees vary but usually include groups that deal with nominating and governance, compliance, audit, risk, investment, underwriting, investment, and compensation. The key committees involved in AI implementation will make the following adjustments:

- **Nominating and Governance.** This committee recruits board members. It identifies individuals qualified to become directors and recommends nominees for the next annual meeting of shareholders. These nominees are traditionally recognized experts in insurance (underwriting and claims), finance and legal. In the past, skill sets around technology were not a focus of recruitment.

  Going forward, recruiting board members that understand AI to a level that allows them to make sound strategic decisions will be necessary. Nominating and governance committees in AI-powered insurers will add recruitment of individuals with these skills as a priority.

- **Compliance.** Compliance committees monitor the regulatory environment, review compliance reports, and oversee the company's ethics and compliance programs. Traditionally, this has been around addressing the aggregated results of market conduct studies, responding to existing and pending insurance legislation, and funding operational compliance areas.

  Recently, insurance regulators in multiple jurisdictions have been taking action on AI. In the U.S., the NAIC adopted

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a model bulletin on AI; in Canada the Office of the Superintendent of Financial Institutions (OSFI) published its expectations around model risk management; in Europe, the EU Parliament is in final stages of enactment on its Artificial Intelligence Act.

Board compliance committees will add AI regulation to the list of laws they monitor and evaluate. Their work will inform other committees what needs to be done and what may be coming in the future.

- **Audit.** This committee works with internal and external auditors to ensure standards are met across the organization. They establish and update their expectations for executive management to ensure that the risks of the organization are identified, eliminated and mitigated. When effective, their reach extends to every critical part of the organization without being overly burdensome or bureaucratic.

Existing standards related to the integrity of the firm and compliance with laws and regulations will be updated to include AI. For example, the audit committee will publish expectations concerning the frequency and depth of AI use audits, data security and privacy reviews, and legal agreements with AI providers.

- **Risk.** AI democratizes data access, allowing unprecedented access to data that was previously guarded by programmers, data scientists and other technicians. This exposes an insurer to reputational, liability, bias/discrimination, ethical, intellectual property and trust risks.

The risk committee has existing processes to measure and monitor corporate risks. For AI, the committee will use these same processes to ask management to report on the type and extent of AI use, measure the risks involved with this use, and provide updates to them on risk management activities related to AI exposures.

- **Underwriting.** Underwriting committees serve as a critical oversight and governance function, ensuring that the company's underwriting activities are conducted in a prudent and responsible manner and that underwriting risks are managed effectively. Approving and monitoring underwriting guidelines, tracking underwriting risk exposures, and approval of large or complex risks and reinsurance treaties are common tasks.

Going forward, this committee must ensure the **intentional** use of AI in underwriting. Does the firm want to use AI only to recommend actions? Where and when should this be extended to underwriting decisioning? Are there lines of business for which AI will not be used, or lines where AI application should be aggressively pursued? The committee will review and approve AI underwriting guidelines, evaluate AI underwriting performance, and ensure that AI underwriting activities are aligned with the company's risk appetite.

This is a great deal of change for the board. Every insurer has its own experience to draw on when it comes to successfully making such broad change happen. One approach involves the appointment of a leader by the chair and CEO who would work with the committees and adjust their operating models to incorporate AI. As these committees then begin to ask carrier operating units to provide input into their deliberations, this same leader would assist the operating units to satisfy the board's request. For example, the underwriting committee will ask the chief underwriter officer to provide them with the AI underwriting guidelines. Through this process, AI is incorporated into the business process through the insurer's existing governance and control procedures.

Including AI in existing board committee processes will not eradicate the AI learning curve. But it should flatten it a bit and ensure that effective results are achieved faster and at lower cost. CM

Talent Management for AI?
In a related article, Fitzgerald offered reasons for insurers to apply standard human resource processes to advanced forms of AI as they onboard, train and periodically review the performance of the new technologies. (See p. 20.)

AI Leadership at All Levels

By Susanne Sclafane

"I've seen a good amount of coverage on implementing AI. But what I haven't seen a lot about is leading" AI programs.

That's how *Carrier Management's* Guest Editor Michael (Fitz) Fitzgerald started a conversation brainstorming the focus of this section of our magazine—"Leading the AI-Powered Insurer"—a theme that fits squarely within *CM's* overall mission of providing content about management and leadership of property/casualty insurance carriers.

The idea for the theme "came out of work that I was doing with boards of directors around controlling and governance," said Fitzgerald, referring to his work as an Insurance Industry Advisor for SAS Institute Inc., an analytics and software solutions provider.

The theme evolved as Fitzgerald and *CM's* content team interviewed executives like Pina Albo, the chief executive of Hamilton Insurance Group, Matt O'Malley and Steve Stabilito, two underwriting leaders at AXA XL, as well as Henna Karna and Ursuline Foley, who both serve on the boards of directors of P/C insurance and reinsurance organizations.

"As we talked to more people and we went through the interviews, this idea that I'd been coached on, that I'd heard of in the past—that leadership exists at all levels of the organization—really came up," Fitzgerald said. "I hope what this [magazine] issue does is to draw out exactly that fact—that the leadership of the AI-powered insurer is at the board level, it's at the executive level, but it's also [at] the middle management level" where people like the AXA XL executives "are working really hard on data and incorporating that into the business. That's very, very important. And how do you support those efforts?" he asked, offering a question for P/C insurers reading the article, "How Underwriters Win Business With Data and ML at AXA XL" to ask themselves.

Fitzgerald continued: "I feel really good about the issue in terms of teasing out what board members and executive teams need to be focusing on. And I think largely they are. I feel very good about the middle management piece..."

"Look for the people who are trying to push these efforts forward, and especially the supporting efforts around data. Recognize those efforts and celebrate those wins," he advised.

"But there's a big hole in the majority of most organizations," he said, noting that he was troubled by the fact that talent leaders at traditional insurers seemed to be out of the loop on AI-focused activities.

Another theme of this edition of *Carrier Management* is talent management, and when *CM* Deputy Editor Elizabeth Blosfield tried to blend the "Leading AI" theme together with the talent theme for her article, "Are Carrier Talent Leaders, Workforces Prepared to Wade Into the AI Tidal Wave?" (p. 22), she could only find one representative of a traditional carrier to interview.

"Most of the carriers I reached out to thought it was an interesting topic but said they didn't have anyone who could speak to it or haven't invested in AI in that capacity," Blosfield reported.

"With all of the money and mindshare being invested in AI, with all of the risks and opportunities, why isn't AI upskilling a Q1 2024 priority for HR?" Fitzgerald asked, highlighting a "troubling gap" that may exist in the leadership of AI programs of P/C insurers. *(Read more about the gap on p. 7.)*

Fitzgerald said he was surprised in a positive way to learn about the diligence of the nominating committees of boards of directors of insurers in adding members with technology skills to their ranks. "Who would think that people looking for board members would be touched by AI?" They are. "They recruit with this whole idea of diversity in mind," Fitzgerald said, referring to a focus on diversity of thought and experience described by Hamilton's Albo as she spoke about the selection of Dr. Karna, a technology entrepreneur with advanced degrees in applied mathematics and business administration, as well as broad industry experience at Verisk Analytics, AIG, AXA XL and Google.

The elevation of AI to the board nominating committees "really drives home" the fact that "there are going to be very few places" within insurance companies that won't feel the impact of AI.

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Meet Your New Employee: Advanced AI

Executive Summary: Because advanced forms of AI have characteristics that set them apart from other technologies—including the fact that they can make recommendations and decisions on their own that may not reflect corporate values—insurers need to apply standard HR processes to advanced AI to keep them in line, advised SAS Institute's Insurance Industry Advisor Mike Fitzgerald.

By Michael (Fitz) Fitzgerald

Much of the discussion around how to manage advanced forms of artificial intelligence—machine learning, generative AI, large language models—deals with them only as technologies. This is a mistake.

There are characteristics of these tools which require insurers to apply some of their traditional human resources tools to ensure adequate governance and to maintain an acceptable risk exposure.

Advanced AI Is Different

The fundamental problem in treating advanced AI as only another technology is that these tools can:

- Learn on their own.
- Generate output on their own.
- Make recommendations or decisions on their own, which may—or may not—reflect corporate values and also may create—or destroy—trust with customers and employees.

Unlike traditional technologies, AI can perform these activities without the direct involvement of a human. There is no programmer or manager to act as a stopgap, ensuring that corporate guidelines are being followed, that bias and discrimination are not present, that reputational risk does not take place, etc.

Insurers can address this by applying some standard human resource processes to advanced AI. Three examples are technical training, cultural norms and performance reviews.

- **Technical Training.** Like any employee, AI must be onboarded to learn "how we do things around here."

> "Like any employee, AI must be onboarded to learn 'how we do things around here.'"

There is a great deal of discussion around using vast quantities of data to train large language models, tapping unstructured corporate information sources, bringing in third-party data in order to establish a base understanding of the business. However, for AI, training is not only standard system testing where test scripts are written and defined outputs are identified. AI technical training also should test for understanding, identify what inferences are made, and highlight answers which are correct but not desired.

Once initial training is performed, an AI training plan must also address the need for ongoing, continuous learning.

All of these objectives are addressed in a robust HR training approach. Their use needs to be expanded beyond human and to AI application.

- **Cultural norms.** AI must be aware of, understand and reflect the values of an organization in its outputs.

Just as employees receive regular reminders of "what our company is all about," AI must also have this understanding to guide its actions. As humans know, giving an answer is only half the challenge; how it is communicated is the other. HR programs such as values training, nondiscrimination in the workplace, company history can help here.

- **Performance reviews.** Once AI has been trained and imbued with the appropriate corporate "way," it's important to recognize that conditions change. AI activities must be monitored for quality results as well as to ensure that its output still meets current business needs. AI activities must also be reviewed continuously to make sure that unwanted bias and discrimination are not part of its output.

Just as humans receive feedback on how they are doing, the best applications of AI will include some type of performance review approach.

How to Start

Insurers can bring together their IT technical team members and HR experts to exchange their knowledge and design possible applications of company-specific HR programs to advanced AI. Objectives of these sessions include:

1. IT outlines how advanced AI learn and apply that learning.
2. HR identifies the programs that they use to guide employees in their jobs.
3. The group proposes where the two realms intersect and initiatives to include in the advanced AI development plan.

Defining AI

This article uses the definition of artificial intelligence used in the NAIC Surveys on Automobile and Homeowners: "AI/ML describes an automated process in which a system begins recognizing patterns without being specifically programmed to achieve a pre-determined result. This is different from a standard algorithm in that an algorithm is a process or set of rules executed to solve an equation or problem in a pre-determined fashion. Evolving algorithms are considered a subset of AI/ML."

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Not Everything Is Advanced AI

As Fitzgerald and *CM* editors pulled together the content for this edition, he stressed the need to drive home another point. "People are calling everything AI," but he believes the focus of leaders' risk management efforts should be on the types of advanced AI called out in a definition offered by members of the NAIC Big Data and Artificial Intelligence (H) Working Group when they surveyed auto and home insurers on their use of AI in 2022 and 2023. (See accompanying textbox at the top of this page.)

Paraphrasing the definition, he said, "It's the use of technology in a way that doesn't require the intervention of a human. In other words, a computer that can program itself, a computer that can find insights in data without the human pointing to it."

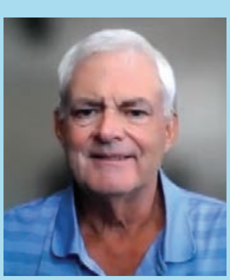
"To me, that [definition] gets you away from some of the simpler and less risky issues or discussions of the technology," he said. "Using AI, even if it's a natural language processing ChatGPT-like large language model, to do the submission intake summarization" doesn't fit that definition. "You're not going to get goosebumps thinking about what could go wrong."

Fitzgerald confirmed that the definition in the Model Bulletin on the Use of Algorithms, Predictive Models, and Artificial Intelligence (AI) Systems by Insurers crafted by the NAIC Innovation, Cybersecurity and Technology (H) Committee and adopted by the NAIC in December, encompasses both types of AI. In states that adopt the bulletin, regulators will be expecting insurers' risk management and governance programs to address predictive algorithms and advanced AI. (See p. 32 for the definition in the Model Bulletin.)

Still, insurers need to appreciate the difference. "We've lived in the world of predictive modeling since the 90s, and while it is mysterious and magical in its own way, it still is very statistically based. You start at A, and you get to B, and you can tell how you got there," Fitzgerald said. In the new world, "you start at A, and you end up at C, and it's not always evident or even explainable to say how the machine got there."

"That's the piece that people need to focus on when they think about Leading AI," he said. "[It's] not something that's deterministic."

"You're talking about something that you might not even ever be able to explain…It might be absolutely the right answer, but you don't know why."



"The leadership of the AI-powered insurer is at the board level, it's at the executive level, but it's also at the middle management level."

Michael (Fitz) Fitzgerald, SAS Institute

Are Carrier Talent Leaders, Workforces Prepared to Wade Into the AI Tidal Wave?

Executive Summary: Talent and tech officers of P/C insurance operations spoke with *CM* Deputy Editor Elizabeth Blosfield about the benefits of AI for their companies' workforces and their own jobs. They discussed the fears that are holding some companies back and the best steps to guide human talent forward. Employment lawyer Holly Goodman also described risks for carriers as the use of AI tools becomes more common in human resources departments.

By Elizabeth Blosfield
Guest Editor Michael (Fitz) Fitzgerald
Insurance Industry Advisor for SAS Institute Inc.

In an August interview with Bloomberg, Microsoft CEO Satya Nadella referenced a 1995 internal memo from the company's then-CEO Bill Gates titled "The Internet Tidal Wave," saying he believes the impact of artificial intelligence will be just as profound. And while experts say benefits await those who are brave enough to test the waters of AI, many insurance carriers still seem cautious about the risks.

"Those fears are real," said Gordon Wintrob, co-founder and chief technology officer at Newfront. "It goes back to how difficult it is to change or to do things differently."

Newfront is an insurance brokerage that markets itself as a modern business insurance company, and Wintrob said he sees AI as the next computing revolution.

"Mobile phones brought a wave of innovation. The movement from mainframe computing to the cloud was another breakthrough revolutionary change. I think AI is doing the same thing across the entire economy," he said. "To think of it as this limited thing that's only going to maybe impact a limited number of products or services is the wrong way to think about it."

Wintrob believes insurers and brokers should be asking themselves, "How do we train and arm our employees to be able to take advantage of all this innovation and think of things through the AI lens?"

The challenge, he said, is conquering fear. "It's a lot of change," he said, "and change is always hard."

Blair Kamrass, vice president of people at Coterie Insurance, also pointed to the early days of the Internet to address the fear of using AI in carrier operations.

"You know, the same fears held true just from the people and operations perspective of automating employee files back in the day," she said. "I know in some places, there were these massive filing cabinets of employee records and the thought of making them digital just really scared a lot of people. But again, it's almost like these baby steps of getting people to understand that this is the new world we live in."

Coterie is an insurance technology company with a focus on small business insurance, and Kamrass said AI is in the early stages of implementation across company operations.

"It's on our road map for 2024 to really start just analyzing: What do we want to do? What do we want to start with? And then what will we build on from there?" she said.

Humans vs. AI: Preparing for Innovation

Training employees and arming them with knowledge about AI starts with human resources, which is one area of focus for AI implementation at Coterie. Kamrass oversees the company's operations regarding benefits, compensation, payroll and employee engagement.

"I think from the HR perspective, we know that AI's goals are to increase efficiency, improve accuracy and just really enhance the employee experience," she said.

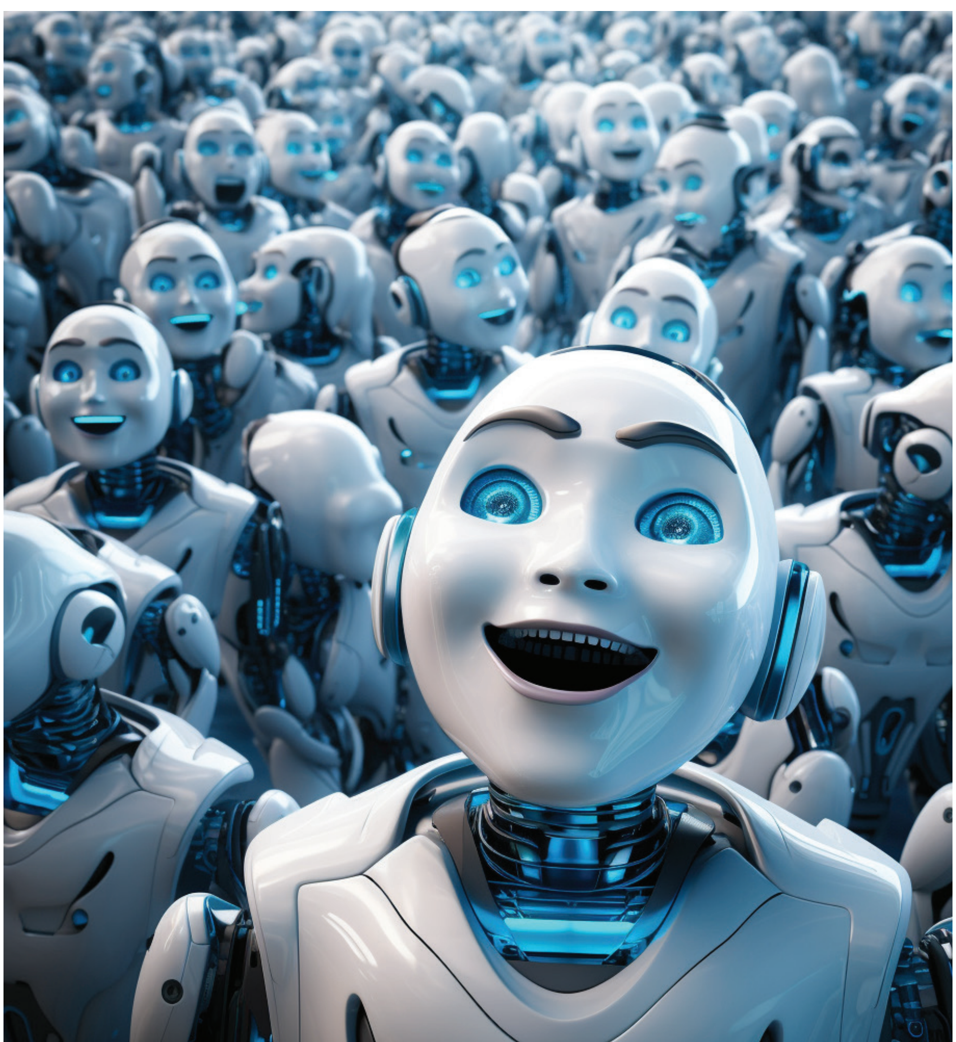
Ken Gregg, founder and CEO of homeowners insurance company Orion180, said his company has used large language models—an AI program that can recognize and generate text—to refine job descriptions, create companywide policies, summarize documentation or create presentations.

"Outside of customer service and some claims intake, most of the applications of AI thus far have been tools that greatly assist our professionals in performing their jobs more efficiently," he said. "While this may slow the rate at which companies need to add headcount, it does not replace the existing talent. It enables them to leverage their critical thinking and creativity."

If concerns about AI replacing human jobs are holding carriers back from embracing it fully, Gregg said he's navigating these fears by emphasizing his company's intent to maintain personal human interaction as a core value.

This is also true at Nationwide, where Chief Human Resources Officer Vinita Clements sees AI as introducing new efficiencies into the employee management process.

"One of the most impactful benefits of AI we've seen in HR is the ability to connect employees to information more quickly and efficiently," she said. "We believe the strategic integration of generative AI offers a powerful way to create a bionic workforce that can drive greater value and impact in the marketplace. Humans lead in a bionic workforce because humans are accountable for decisions and outcomes, not the machines."



Blair Kamrass, Coterie Insurance:
"When you think of just your average tech tool, they're typically depreciating assets of the company, whereas a person should be an appreciating asset where you're investing in their development and their growth."

Clements added that by combining the empathy and judgment of human workers with the speed and efficiency of machines, human workers can focus on higher-value tasks that require a relationship-based approach while AI models can take on repetitive, lower-value work.

"Our HR team is preparing employees to use and experiment with generative AI by helping them understand the potential, educating on known risks, and creating learning opportunities that include self-guided trainings and outside speakers," she said.

Kamrass said it's also helpful to position AI as another employee to be trained and integrated into a company's culture rather than a simple tech tool.

"When you think of just your average tech tool, they're typically depreciating assets of the company, whereas a person should be an appreciating asset where you're investing in their development and their growth," she said. "And I think AI needs to be thought about in the same way where it's not going to sit on the shelf and you use it once a year. It's something that will be eventually integrated into the very fabric of an organization and will constantly need to be evaluated to make sure that it's producing the appropriate output to properly support the organization."

(See related sidebar, "Meet Bob, Cover Whale's AI Employee.")

This work will likely be ongoing as the technology evolves, Nationwide's Clements said, and insurers will need to be deliberate with their workforce and

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training strategies going forward.

"We anticipated the need for a continuous learning culture many years ago," she said. "We have already implemented specialized training into our comprehensive upskilling program. In addition, we have a thoughtful governance program in place aimed to educate and create awareness, train and develop, test and learn, and manage risks as well as opportunities."

Big Benefits Pose Big Risks

Beyond training employees to work alongside AI, human resources teams are also navigating how to incorporate AI into their own work. Kamrass sees benefits in the recruitment and onboarding process, as well as with performance reviews.

"We're actually in a performance review cycle right now at Coterie, and wouldn't it be so great if we had an AI platform that could pull that together?" she said.

She sees AI as having the ability to pull documents and notes about employees from various platforms into a package for leaders to write performance reviews, adding that AI can also be useful in crafting employee policies or job descriptions and helping new hires sort through and understand onboarding documents.

Holly Goodman, a board certified labor and employment attorney and shareholder at law firm Gunster, said she also sees AI as being useful in crafting employee policies or job descriptions, as well as helping new hires sort through and understand onboarding documents. However, the use of AI in these functions is not without risk.

"The [functions] that are becoming more common are the ones that pose the most risk," Goodman said, pointing to bias and discrimination as "the big issue" with including AI in HR.

"Just because it is artificial intelligence doesn't mean that it's not going to also potentially create scenarios where a business could be violating the laws or could be inadvertently discriminating against someone," she said.

She said examining blind spots can go a long way.

"Perhaps it's something as simple as using AI for recruiting processes, and you input that you want to eliminate any candidate who had a six-month or greater gap in their resume," she said.

While this input may appear neutral on its face, she explained this AI prompt could inadvertently affect those who have taken parental or medical leave. She encouraged insurance companies to include bias training for AI into any discrimination and harassment training they're already undertaking, especially if AI is going to be doing some of the tasks human employees are trained to do.

"What employers really need to be worried about and what HR departments need to be worried about is making sure they're vetting those information points that they're putting into the AI, and then also on the back end, evaluating outcomes to determine whether or not there's any evidence of that kind of a negative or disparate impact," she said.

This is where a healthy amount of skepticism comes in, Newfront's Wintrob said. "Always have some steps where you ask a large language model to explain its reasoning and walk you through how it came to an output," he said.

Kamrass at Coterie added it's important to be mindful of language and data used to train AI models to avoid introducing bias and to implement company core values. "We want to make sure that we are supporting a diverse, equitable, inclusive environment in every facet of everything that we do, and sometimes these AI tools, if they're trained with biased data, they're going to produce biased output," she said. "Test different language to see what might stick."

Beyond concerns of discrimination, insurers should also be thinking about data privacy risks, she said.

"Data privacy is enormous," she said. "We don't want to be uploading employee personally identifiable information because once it's in some of these systems, we're not always 100 percent sure where it's going to go."

This means thinking through current data governance practices and updating security protocols when necessary.

"As technology grows, so too do the threats," Goodman said. "Businesses have a lot of personally identifiable information—insurance companies in particular, where you have people's names, you have their addresses, you have their date of birth, possibly their Social Security numbers, you have a lot of personal information about individuals. You need to make sure that you have protections in place and limitations on the use of that data."

She said insurers should be careful about the information uploaded into AI models because it could mean giving ownership of their data to the platform. She cautioned them to revisit their policies around the use of data and what can be uploaded into AI products.

Vinita Clements, Chief Human Resources Officer, Nationwide: "We believe the strategic integration of generative AI offers a powerful way to create a bionic workforce that can drive greater value and impact in the marketplace. Humans lead in a bionic workforce because humans are accountable for decisions and outcomes, not the machines."

Gordon Wintrob, Co-founder and Chief Technology Officer, Newfront: "At the end of the day, I do think there will be a lot of change, and [the successful ones] will be the folks who are able to embrace doing things differently and think about how AI plus humans can be much better than the sum of the two parts."

"What's really important here is that all of the laws—the existing laws that deal with employment matters, that deal with even privacy outside of the HR space—those laws and those regulations are still going to apply even in the AI use case," Goodman said. "They were passed long before we ever even thought about something like artificial intelligence."

Insurers should also examine any third-party vendors they might be working with to supply their AI models, she said.

"Even if the artificial intelligence that [carriers are] using isn't their own, if they have a third-party vendor that they have outsourced a decision point to or that they have outsourced data analysis to and that third-party vendor is violating some of these regulations or laws, then that business who hired that vendor can also still be liable," she said. "So, it's really important to make sure that the business is aware of that third-party connection and is really vetting some of the policies and the use practices of third-party vendors."

Two Better Than One

Kamrass said she believes despite some challenges, the insurance workforce will be prepared for the changes ahead as humans and machines learn to work together.

"You know the workforce has seen so many changes over the years, and like anything else, it takes time and education," she said. "There have already been a lot of tech advancements over the years. We're already living through it. And the sooner that you can embrace that and of course ask questions along the way to make sure that you're comfortable, then it will just take everyone further. It will take our companies further. It will take us as individuals further as we grow and develop. And I think it will be an exciting ride."

After all, Wintrob said, two is better than one. "At the end of the day, I do think there will be a lot of change, and [the successful ones] will be the folks who are able to embrace doing things differently and think about how AI plus humans can be much better than the sum of the two parts." CM

Meet Bob, Cover Whale's AI Employee

At Cover Whale, an InsurTech for commercial trucking insurance, an employee named Bob on the artificial intelligence team is actually an AI-powered chatbot.

"Bob is our friend. He is an incredible partner that we have here," said Erica Wood, Cover Whale's chief people officer, noting that Bob's name stands for bundle of bots.

Bob's goal at Cover Whale is to streamline communication with agency partners to improve response times and support customers. "Bob handles all sorts of inquiries that come from the market, like claims processing, quoting and binding, status and loss runs, underwriting guidelines, and all sorts of inbound questions," Wood said. "And he does it in under two minutes."

The company issued a media statement last year announcing Bob's employment. "Bob is built to outpace the industry-standard wait time..., while maintaining Cover Whale's brand voice," the statement said, adding that Bob is also enabled with optical character recognition to read inbound communications with embedded images.

Bob officially joined Cover Whale's AI in October 2023, four months after the InsurTech hired a human leader for its artificial intelligence team, Chief AI Officer Darien Acosta.

Acosta, Wood said, "has really supported us and is driving our harnessing of all of the transformative capabilities of AI models and advanced algorithms with not just looking at task automation but also, how do we enhance? How do we get quicker at making better decisions? And how do we foster innovation? How do we really spread that through the culture?"

Wood works alongside Acosta to incorporate the use of artificial intelligence into the company's human resources functions.

Acosta has worked with his team to facilitate the adoption of AI, machine learning and generative AI across the company, according to Wood, who noted that the rest of the AI team includes a solutions architect, a data scientist, a senior AI engineer, and an AI automation and customer opportunities specialist.

Wood said she expects to see more AI-specific roles pop up at insurance companies in the future, adding that Cover Whale itself is also in the process of mapping out a data architect role for its AI team.

"In the future, I think it's going to be happening more and more," she said. "The candidates that we bring in have to not just demonstrate that they have the talents and the skills for the role, but more importantly, that they're willing to evolve and adapt really quickly and run very fast alongside us."

While Wood believes many insurers are at the beginning stages of getting comfortable with AI, she sees it as an exciting time for the industry.

"The more that we bring on these roles that enhance efficiency and really liberate the human intellect to concentrate on the really fun problems, the really deep problem solving and really deep critical thinking, this could be a dynamic partnership holding hands between human creativity and AI's incredible computational power," she said. "It's there. There's unparalleled possibility here. So, it's just about leaning into the curiosity part a little bit at a time."

(Related article, p. 41, "'Critical Thinkers' Needed for AI-Powered P/C Insurers")

Reporting by Elizabeth Blosfield

How Underwriters Win Business With Data and ML at AXA XL

Executive Summary: A machine learning model that flashes stop-and-go signals to underwriters in AXA XL's environment unit and a distribution tool that fills the U.S. business pipeline with carrier-selected accounts are two of the successes that underwriting leaders Matt O'Malley and Steve Stabilito attribute to a cross-functional focus on insights hidden in decades of insurance data. Here, they provide *CM* Guest Editor Mike Fitzgerald with a high-level view of what it takes to win with data—curiosity, simplification, funding outside of business units, bite-size proofs of concept and communication.

By Susanne Sclafane

Guest Editor Michael (Fitz) Fitzgerald Insurance Industry Advisor for SAS Institute Inc.

Imagine being able to tell a broker prior to a submission, "I can take this account in my underwriting portfolio," instead of giving a broad appetite listing for the distributor to puzzle through.

A grassroots effort by underwriters to incorporate data in their decision-making has turned the vision into reality at AXA XL, according to Matt O'Malley, AXA XL's U.S. country manager and East zone manager, who described the benefits of a machine learning tool for pipeline management that was created from predictive relationships buried in the carrier's data.

"The aha moment has been realizing what the conversion ratio has turned out to be," O'Malley said. There's "a difference between telling someone specifically, 'I can really perform on this account based upon our data and analytics' versus describing to a broker that this is generally what I want, and then leaving the broker trying to figure out as things come across their desk, 'Does this fit what that person told me?'"

"Now, we're able to do that across multiple lines of business," O'Malley continued, explaining that the machine learning tool is able to identify where AXA may have interest in offering different lines of insurance to the same client. "This really brings an additional client lens to AXA.

There are lots of places where we can engage and solve needs for clients that we hadn't been addressing in the past. And it's all coming from the data," he said.

Steve Stabilito, underwriting manager for the construction professional and pollution teams, agreed. "By being proactive—not reacting to a submission that comes in but being proactive in seeking that business—we can have a better sense of ownership of those opportunities within our teams. Then we can come to a faster, more confident decision when it comes time to make the decision."

In addition to the distribution tool, AXA XL has developed a machine learning model that is literally "greenlighting" the best business with flashing signals built into existing tools used by AXA XL's environmental underwriters, according to O'Malley.

Data Networks

The starting point for both machine learning tools was a decade-long effort to understand, clean and harvest the insights hidden in the company's data, the two underwriting leaders stressed during an interview with *CM* Guest Editor Michael (Fitz) Fitzgerald, Insurance Industry Advisor for SAS Institute.

Stabilito led off, noting that he has taken on a role within his team to be a "steward of data and data analytics," essentially bringing data into every conversation underwriters have about planning strategies or individual risks. "On our monthly calls, I incorporate elements of data to give different insights that maybe team members have not seen before."

Stabilito has also created a dashboard for his team, which serves up the right information at the right time for his underwriters to make a decision, according to O'Malley, who reported that AXA XL is looking to roll that out more broadly across the organization.

Beyond his team, Stabilito started a data network throughout the company. "That network is essentially a dozen or so people

"One of the really important pieces in terms of how we use the data was making sure that we had alignment not only within the underwriting teams but with our actuarial team, with our claims team.

Matt O'Malley, AXA XL

who have similar backgrounds throughout the company who are interested in bringing data insights to their teams," said Stabilito, whose education in geological engineering confirms a lifelong interest in unearthing information beneath the surface. "We get together once a month and talk about data. We share experiences —the knowledge and the tools that we're using for analytics," he said, noting that the group includes members from actuarial, claims, underwriting and finance—"those of us that live in the numbers every day."

While the current group has been getting together for about six months, the network started two years ago as a two-man operation—Stabilito and one of his peers in a risk engineering group at AXA XL. "He and I have both started using a lot of the tools that are available...to analyze our books and build dashboards that can deliver insights to our internal and external customers," he said. Recognizing that the effort should move beyond the two of them, they "put feelers out" to see who else was interested.

"The real theme around the data network is empowering the use of data analytics in our business," Stabilito said. "Just by demonstrating to everyone, showing what some of these tools are capable of doing, it sparked an interest among the group [members]. And then it went from there. We had a curiosity about our business—segments that might be profitable or what class of business are we more successful in pursuing."

From Data to Model Building: Green Means Go

O'Malley, who previously led the North America environmental practice, recalled how that business started to look for ways to improve the underwriting results using machine learning back in 2014.

"We had a lot of stakeholders at the table," he said, noting that a separate strategic analytics unit, as well as the environmental unit's pricing team and underwriting managers, were involved at the outset, working with 10 years of existing data. "We needed to make sure that everybody understood the mission and what some of the critical values were," he said, reporting that the task initially involved identifying some 350 or 400 key variables that were key drivers of desired outcomes and building a multivariate model.

"But at the end of the day, we turned our analytics model into a red, yellow, green [signal]. So, underwriters could understand, without needing to understand the mechanics, 'Is what I'm doing at the desk level making an improvement to the book or not?'"

Explaining further, O'Malley said, "When it's time to bring [something like this] to market, when you're going to take those new insights and build a strategy around it, it needs to be executable. We tried to break it down into bite-size pieces for the underwriters. So, instead of understanding that we worked on 300 variables, which we told them at a high level, we basically said the way the model works is you use your pricing tool the same way you did, but now you have these icons of red, yellow, green [to indicate] how that modeling layers into what we're trying to accomplish in the market."

By taking out the complexity for users of the tool, you avoid the prospect that they will try to "reverse engineer" the process, he said.

"When it is different than we have done in terms of go-to-market strategy for the past 20 years, you want to make sure that people are focused on using the tool as it's designed versus trying to figure out why this shouldn't work," he said, noting that another desired outcome is driving efficiency.

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Engagement Strategy Matters

O'Malley confirmed that while the signals flash account by account, the underwriters also were able to see portfolio results at monthly meetings. "Our actuarial team would come in and actually present the results for the portfolio to the [underwriting] team. So, they could see how we were driving loss ratio improvement over a month-to-month basis, which then became a year-to-year basis..."

"At that team meeting, we had our entire underwriting staff, our assistant underwriting staff, our claims, our risk engineers. Everybody heard the same message. People could see the actions that underwriters were taking every day were turning into the results that were being reported out," he said.

Stabilito re-emphasized the importance of showing the underwriters the loss ratio impact at a portfolio level. "Underwriters are looking at their individual risks—the individual risk that is right in front of them at that particular time. They may or may not be thinking about how that affects the whole portfolio. They may not even know how it affects the portfolio."

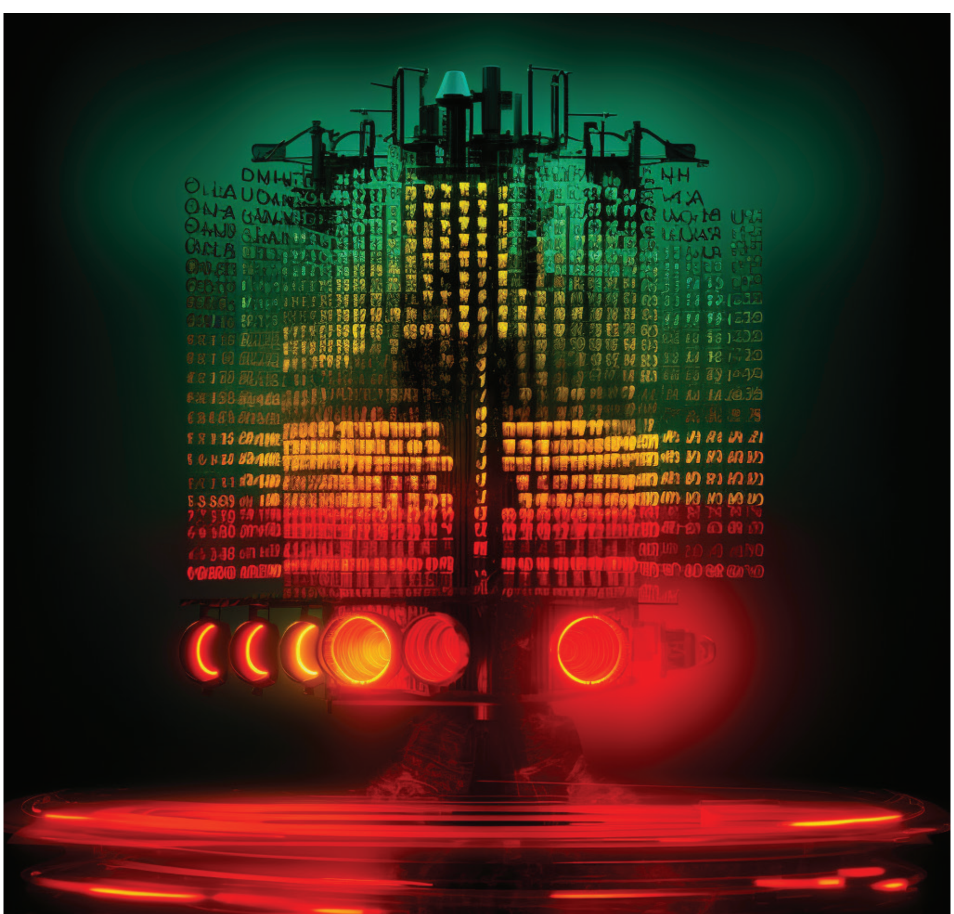
He also described similar tools that his team uses for pricing. "We have models that will allow us to input our targeted pricing or what we anticipate offering for an account. The tools show us what impact that has on our individual results, team results and the portfolio as a whole," he said, adding that an unfavorable indication overall could prompt the underwriter to "go back to the well and think about making some adjustments."

O'Malley added, "I think one of the aspects that people overlook [is] how important change management is as we implement new ways to incorporate data into our everyday [work]," explaining that an engagement strategy needs to involve everybody—"from the senior leaders who were sponsoring the investment in the models all the way down to the underwriters."

"Using the data is bringing us to faster, more confident decisions."

Steve Stabilito, AXA XL

He continued: "There needs to be an entirely different way that you think about that end-to-end execution [and] communication...because it's easy to just go back to what you're comfortable with—and that's usually not using the data in the way we're looking to use it today."



Making Data Exciting

Stabilito reported that his team isn't quite as far along as O'Malley's in the adoption of machine learning or AI technologies. "We're in the infancy of incorporating data into our regular conversations, with the goal of taking advantage of those technologies as they are built more and more around our business."

In Stabilito's view, "It really starts with making data exciting, getting everybody involved in what's going on—maybe not in the weeds and the mechanics, but at least incorporating data into conversations" that normally didn't draw upon data insights.

"We get together and we talk about our book profile. We talk about specific accounts or specific risks. My intention on this is to incorporate an aspect of data analysis in every one of those conversations, and ultimately end the conversation with 'I took this approach' or 'I went in this direction with this opportunity because that is what the data is telling me.'"

"We have not had that as part of our culture until very recently," he said.

The process of becoming a data-focused insurer is not without challenges, Stabilito confirmed. "I don't think any company's data is ever 100 percent clean. In fact, probably not even close to 100 percent. And we're certainly not an exception to that. But what we're really trying to do within our group—and this is one of the goals of the data network, too—is we're trying to get away from the apathy that comes from knowing that the data is not always clean."

Now, instead of saying, "It's somebody else's job to fix that. I know it's not right, so I'll just ignore it for now," Stabilito is encouraging a proactive approach. "If you see something that's consistently wrong, let's fix it so that we can use the data," he said.

"It's our responsibility to ensure the accuracy of this. It's not IT's responsibility; it's the business' responsibility," he stressed.

As more teams adopt data-driven approaches and use models based on the data, there's a payoff in the marketplace, O'Malley believes. "It allows us to be much more consistent across a significant number of variables so that when we execute in the market, our distribution channels see us being more consistent than we would have been in the past," he said.

Fitzgerald observed a sense of satisfaction coming across as the two underwriting leaders spoke about their data-driven approaches to targeting profitable business.

"Absolutely," that's another benefit, O'Malley said. "Being an underwriter is kind of like being a baseball player. Nobody bats 1,000, but if all of a sudden you can bat 400, you feel really good about that. [With the data insights], you win—and you win together."

"You're a Hall of Famer," Stabilito added. CM

Ground Up or Top Down?
Tips on Building a Data-Driven Insurer

When Matt O'Malley and Steve Stabilito, underwriting leaders from AXA XL, described a ground-up process for transforming their teams into data-driven businesses recently, *Carrier Management* had questions about activities in the C-suite.

"Was there any top-down messaging?" asked *CM* Guest Editor Michael (Fitz) Fitzgerald, after hearing Stabilito describe the growth of a cross-functional data networking group that started at the grassroots level, and after O'Malley described the development of machine learning models to improve underwriting and distribution processes. "Is there anything from leadership that's either helpful or not helpful?" Fitzgerald asked.

"From a senior perspective, particularly when we did our machine-learning driven model, that comes with the budgetary ask," O'Malley said, highlighting the decision of AXA XL leaders to put modeling teams in a corporate center as a key ingredient to success. "One of the challenges is when you ask a business to pay for the project upfront," he told Fitzgerald, an insurance industry advisor for SAS Institute, who has had his own experiences with transformation projects at insurers Zurich and Royal Sun Alliance. As a business unit leader, "it's hard to take the leap that I'm going to spend this money when I'm not quite sure what the benefit is going to be. Intuitively, I believe there will be a benefit, but until I've spent a significant amount of money, [I can't really] determine whether these models are actually going to generate the outcomes we're hoping for," O'Malley said.

"With AXA setting up those modeling centers as centers of excellence, we've done proofs of concepts around what we think will work. We've tested them and then launched them," he said.

Fitzgerald also asked the two underwriting executives to offer recommendations to other insurance leaders "that are now faced with all of the noise around AI and leading their organizations from this point forward."

Test and learn, they said.

"We are fortunate to be one of Microsoft's pilot companies for Copilot, and we have a small group that is testing what can AI do within our organization, and then reporting back on what those outcomes could be," O'Malley said. "We're going to learn as we go along. And I think we'll actually learn quickly just how much has advanced in the last year-and-a-half. But I would say: build a core team, experiment and then figure out where do you want to place your bets."

Stabilito endorsed the idea of a team effort and reiterated the need to understand your data. "To understand AI, you have to understand what's underlying that. You have to understand the data."

"That's what we did with the data network. We started our group as a very targeted initiative in a very low-risk and low-cost environment, ...where we tested and we explored some of our curiosities before we tried to scale them across the organization or even across our individual teams."

He likened the network approach to forming a think tank that tests theories in a very controlled environment to start an AI journey. "You might not necessarily have the quality of the data or the quantity to use AI in an effective manner," Stabilito said.

"Charging into this saying 'we're going to adopt AI' may not be the best approach. It might be best to proceed a little bit more slowly or more cautiously in a lower risk environment—but knowing that starting small can really deliver big results in the long run." CM

Regulators Run Alongside Speeding AI Train:

What the NAIC Model Bulletin Means for Insurers

Executive Summary: Bruce Baty, a lawyer with nearly 40 years of experience assisting insurers in regulatory matters, gave an overview of a model bulletin adopted by the NAIC late last year, setting forth regulators' expectations about how carriers will govern the development, use and acquisition of AI technologies.

At a high level, what regulators rushed to accomplish in crafting the bulletin was to deliver a reminder that laws about unfair trade practices, unfair discrimination, corporate governance disclosure, P/C rating laws and market conduct surveillance laws apply to the use of AI systems as well, and to convey expectations about written documentation regulators expect carriers to produce during regular conduct exams regarding AI governance, risk management and scrutiny of third-party providers of AI systems.

By Susanne Sclafane
Guest Editor Michael (Fitz) Fitzgerald
Insurance Industry Advisor for SAS Institute Inc.

In an industry where the pace of regulation is often described with references to snails and turtles, the NAIC's adoption of a model bulletin on carriers' use of Artificial Intelligence Systems resembles the blur of a bullet train.

"This was overnight, comparatively speaking," Bruce Baty, a partner with the law firm Norton Rose Fulbright U.S. LLP, said during a January interview with *Carrier Management* Guest Editor Michael (Fitz) Fitzgerald, describing the development and adoption of a "Model Bulletin on the Use of Algorithms, Predictive Models, and Artificial Intelligence (AI) Systems by Insurers" by the National Association of Insurance Commissioners.

The bulletin, adopted at the Fall National Meeting of the NAIC in early December last year, outlines guiding principles for governance, risk management and internal controls for AI systems, with an entire section delineating what insurers should include in an "AIS Program"—a written program that regulators "expect" insurers to develop in order to document their "responsible use of AI Systems that make or support decisions related to regulated insurance practices."

A final section addresses what might happen going forward as regulators carry out their oversight responsibilities during market conduct exams or other investigations to address AI usage:

"[A]n insurer can expect to be asked about its development, deployment, and use of AI Systems, or any specific Predictive Model, AI System or application and its outcomes (including Adverse Consumer Outcomes) from the use of those AI Systems, as well as any other information or documentation deemed relevant by the Department."

The first section of the bulletin starts with a simple statement: "AI is transforming the insurance industry." Baty, who has been advising insurance industry clients on corporate, reinsurance and regulatory matters for 38 years, agrees. He likens the use of AI in insurance to "a really fast-moving train that is speeding down the tracks." That kind of speed, he said, "always is a great concern to state regulators, and the NAIC, in particular," he said, highlighting the NAIC's desire to get out in front of innovative ideas. "They like to study and to understand what is happening, what they are regulating, and how best to regulate that to protect consumers."

The legal adviser, who has specialized in insurance merger and acquisition deals over the years, contrasted the NAIC's slower work on insurance business transfers (moving blocks of insurance business from one carrier to another) with its rush to get in front of insurer's AI usage. With IBTs, the NAIC is carefully watching the process go forward in Oklahoma and other states and considering how this will impact consumer rights and state guaranty fund coverage, among other things. "With AI, and the use of AI in marketing, underwriting and claims, it's too late to start early. And that's the NAIC right now. We can't stop it. But what we can do is tap the brakes on the speeding train."

Baty described activity at the National Meeting in Orlando, where the bulletin was ultimately adopted, to support his observation about its "overnight" incarnation. Usually, by the time a proposed model gets to a national meeting, "all of the important stuff is already cooked. It's already baked in by the time it gets to an airing by the committee in that public forum," he said. But this time around, "regulators were still wrestling with concepts. There was a discussion and a debate among the regulators as to the meaning of the word 'bias.'"

"They were still drafting it on the day that this bulletin was adopted in Orlando," he reported.

Anatomy of a Model; 'Bias' Undefined

The NAIC effort to craft the model bulletin started just about a year ago, with discussion at the previous Fall National meeting in December 2022. Two drafts created by the Innovation, Cybersecurity and Technology (H) Committee were subsequently exposed for comment—one on July 17, 2023, and a second draft on Oct. 13, followed by a virtual public meeting on Nov. 16 last year. Sticking points raised by commenters during draft exposure periods included the phrasing of definitions that make up a section of the bulletin, as well as issues related to the use of third-party data and model providers and the corresponding obligations of insurers to comply with insurance regulations when they use such providers. Revisions along the way included the removal of definitions for the terms "bias," "big data" and "model risk," as well as the introduction of definitions for "adverse consumer outcomes" and "degree of potential harm to consumers"—both of which are considerations for how insurers tailor their AIS programs in the language of the final bulletin.

Preliminary minutes of a Dec. 1 meeting of the H Committee posted on the NAIC website describe the last-minute back-and-forth over the bulletin's references to "bias" in some detail. The word appears in an overarching statement about regulatory encouragement of "the development and use of verification and testing methods to identify errors and bias in Predictive Models and AI Systems" and in more specific recommendations for insurers to engage in—and document—data governance practices related to "bias analysis and minimization" in their AIS programs. According to the minutes, after hearing an insurance carrier trade group representative advocate for the removal of all of the bulletin's references to the undefined term bias, a consumer advocate advanced the idea of replacing the word "bias" with "unfair discrimination." Then regulators weighed in.

North Dakota Commissioner Jon Godfread motioned for the "unfair discrimination" terminology, Iowa Commissioner Doug Ommen supported the idea of removing the word "bias" in the

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five instances where it appears, and Colorado Commissioner Michael Conway suggested a new term—"statistical bias."

Although Godfread then agreed to endorse the "statistical bias" phrasing, other commissioners raised concerns about whether the change would necessitate a new round of comments and about whether "statistical bias" was the right term for all pages of the bulletin. The H Committee's Chair Kathleen Birrane, Maryland's insurance commissioner, stated that the goal was to conclude discussion at the December meeting. After more debate, Godfread retracted his motion, and another motion to approve the bulletin with existing bias references unchanged (and the term remaining undefined) was passed through the committee, with Ommen abstaining from the motion to adopt.

The NAIC Executive Committee and Plenary adopted the model bulletin a few days later.

'Subtle Reminders'

There was one instance of wordsmithing made at the 11th hour, according to the minutes draft, which reveals that a phrase about insurers' "performance of audits" of third-party data and AI models to confirm their compliance with regulatory requirements was amended to read "performance of contractual rights regarding audits." Concerns about vendor rights of confidentially and about exactly what insurers can contractually require of third-party vendors to gauge their conformity with an insurers' standards of practice or compliance with regulatory requirements were raised by some of the 37 commentators that offered a total of 275 pages of reactions to the first and second drafts.

The sheer breadth of the commentary that the H Committee had to wade through supports Baty's sense of an accelerated pace of activity from start to finish. Rushed or not, the intent of the bulletin was realized, Baty believes.

"It [is] a reminder to the carriers that with this use of artificial intelligence, you still have to comply with the unfair trade practices laws, you still have to be mindful of your claims practices. Do they adhere to the Unfair Claim Settlement Practices Acts?" Baty asked, paraphrasing the introductory paragraph of the bulletin and the first section, which lists those two laws, along with market conduct surveillance laws, P/C rating laws and the regulatory disclosures requirements of the Corporate Governance Annual Disclosure acts that already exist.

"It's an effort to tap the brakes of this speeding train down the tracks, to tell carriers that we already have laws on the books that address so many of these issues. We adopted CGAD to understand how you're managing yourself. [And] AI, because it has such an impact on consumers, needs to be addressed in your CGAD reports. It's got to be an important aspect of CGAD."

In the end, what the committee created is a "subtle reminder that we have market conduct laws on the books and that we fully intend to utilize those market conduct tools to come in and investigate how are you using AI so that you are mitigating the risk to consumers with respect to unfair discrimination," Baty said, summarizing the last of the bulletin's four sections, "Regulatory Oversight and Examination Considerations." (See related sidebar, "NAIC's Model Bulletin in Brief," for more details of the bulletin, on the *CM* website)

Definitions, Definitions: Advanced AI vs. AI

Definitions of artificial intelligence and machine learning used in the NAIC Surveys on Automobile and Homeowners over the last few years differ from the definitions set forth in the Model Bulletin on the Use of Algorithms, Predictive Models, and Artificial Intelligence (AI) Systems by Insurers."

The surveys, with a focus on "advanced AI" or post-year 2000 models, say: *"AI/ML describes an automated process in which a system begins recognizing patterns without being specifically programmed to achieve a pre-determined result. This is different from a standard algorithm in that an algorithm is a process or set of rules executed to solve an equation or problem in a pre-determined fashion. Evolving algorithms are considered a subset of AI/ML."*

Multi-item lists provide examples of what are considered AI/ML systems for survey purposes, and what are not. Excluded from this definition, for example, are "static ratemaking and/or predictive-modeling methodologies, including linear regression, generalized linear modeling (GLM), or generalized additive modeling (GAM)."

The model bulletin, which includes predictive models within its scope, says: *"Artificial Intelligence (AI) refers to a branch of computer science that uses data processing systems that perform functions normally associated with human intelligence, such as reasoning, learning, and self-improvement, or the capability of a device to perform functions that are normally associated with human intelligence such as reasoning, learning, and self-improvement."*

Noting that machine learning is a subset of artificial intelligence, the model bulletin says: *"Machine Learning (ML) refers to a field within artificial intelligence that focuses on the ability of computers to learn from provided data without being explicitly programmed.*

According to the bulletin: "*Predictive Model refers to the mining of historic data using algorithms and/or machine learning to identify patterns and predict outcomes that can be used to make or support the making of decisions."*

Also defined in the bulletin are the terms "algorithm," "AI System," "Generative AI" and "Model Drift."

Principles Not Enough

"Not so subtle," in the view of *CM's* Guest Editor Fitzgerald, an industry advisor for SAS Institute, who notes that firms like his offer tools allowing carriers to deal with recommended "data lineage" and "bias analysis" and audit activities referenced in the bulletin.

None of that is required, however. "The goal of the bulletin is not to prescribe specific practices or to prescribe specific documentation requirements," the language of the model clearly states. "Rather, the goal is to ensure that insurers...are aware of [their] Department's expectations as to how AI Systems will be governed and managed and of the kinds of information and documents about an Insurer's AI Systems that the department expects an Insurer to produce when requested," the model bulletin says.

So, why put out a document that is not prescriptive? Why do carriers need a reminder of any of this given that CGAD, ORSA and Form F requirements already exist and that the NAIC already adopted "Principles in Artificial Intelligence" around fairness, accountability, compliance, transparency and security commitments of "AI actors" in 2020? (AI actors are "insurance companies and all persons or entities facilitating the business of insurance that play an active role in the AI system life cycle, including third parties such as rating, data providers and advisory organizations.")

"It's an effort to tap the brakes of this speeding train down the tracks, to tell carriers that we already have laws on the books that address so many of these issues."

Bruce Baty, Norton Rose Fulbright U.S. LLP

"It was clear that that statement alone was not going to be enough to bring accountability to the companies using AI," Baty said, referring to the Principles. In fact, when the NAIC has directly asked carriers whether they are adhering to the Principles, most simply ignored the question, Baty reported, referring to a survey of auto insurers using advanced AI conducted by the Big Data and Artificial Intelligence (H) Working Group in 2022.

"What was really remarkable and caught

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the attention of the regulators was the number of companies that just left that [governance] question blank," he said.

According to the Working Group's auto survey report, 169 out of 193 carriers reported using advanced AI or machine learning in some part of their operations, with the highest percentage using AI for claims, 70 percent. Yet, while 135 carriers surveyed reported already using AI for claims, 45 said they hadn't documented the first principle (fairness and ethics) in their governance program and 81 left the question blank.

The Working Group report pointed out that regulators expected the number of "blanks" to be less than or equal to the 58 who are not using or planning to use AI for claims. The report writers offered the same observation for all of the other functions and principles where the unexpected pattern repeated. (See related textbox, "Definitions, Definitions: Advanced AI vs AI," p. 32 for more information on the surveys.)

"In other words, maybe they have adopted those principles, but they haven't incorporated them formally as part of their governance program. That was a real eye opener to the NAIC," Baty said, during a video interview with Fitzgerald posted on the SAS website last year. (Video series: Insurance Analytics at Scale Video Series | SAS website)

A more recent survey of home insurers tallies only yes and no answers for survey questions about whether each of the Principles is documented in carrier governance programs. Tables in the report reveal that 104 of 194 homeowners carriers say they are already using advanced AI for claims (still the top function for AI usage) and 174 said they did not document fairness considerations related to the use of their AI claims tools in their governance programs—again, with similar response patterns for other functions and principles. (Editor's Note: 65 respondents said they documented fairness considerations "companywide," across all functions)

Looking Ahead

Baty anticipates states with regulators who were on the H Committee in 2023—15 of them—will move forward to adopt the model bulletin in 2024. "The bulletin talks about a written AI program that carriers should adopt. That's something that is not currently required, but I think the carriers are going to have to [recognize], whether your state of domicile adopts the bulletin or not, this is going to become a best practice.

Already, some states are moving to craft their own unique guidance documents. On Jan. 17, New York's Department of Financial Services released a circular letter aimed at preventing unfair discrimination in carriers' use of AI and external data sources specifically in underwriting and pricing. (Related sidebar, "What's in the Latest New York AI Circular?" available exclusively on the *CM* website)

"I don't know that we need to have all 54 jurisdictions adopt the bulletin for this to have impact," Baty said. "What this [NAIC bulletin] is going to do is establish that best practice. So, when the market conduct examiners come in and they say, 'I want to see your written AI program, whether your states adopted it or not, they're going to be looking for your AI program. And I think, prudently, you better be able to hand that over. You better have one," he said. CM

MGU-Carrier Relationships and AI

The NAIC's bulletin model bulletin on carriers' use of Artificial Intelligence Systems, adopted in December 2023, specifically sets out expectations that insurers will describe their processes for acquiring, relying on and performing due diligence on third-party AI systems in written programs for the responsible use of AI Systems.

Is an MGU or a broker considered a third party by the NAIC drafters?

"I think it could be," said Bruce Baty, partner with the law firm Norton Rose Fulbright U.S. LLP. He noted that provisions related to third parties were being discussed—and changed "on the fly"—in the final minutes before the vote for adoption at a December 1 meeting of the committee that drafted the bulletin. "One regulator raised his hand and said that licensees [insurers] can go out and audit these third-party providers of data only if there's a contractual right to go out and audit these companies," Baty said.

"It was a very good point," Baty said, alluding to a reference in the bulletin to carriers' auditing protocols with respect to third-party providers of AI systems or data. "If they are not a licensed entity, neither the carrier nor the regulator has the right to come in and look behind the curtains to see what what's in the sauce," he said.

"But a lot of what we're seeing now are MGUs that are developing out their own systems, purchasing their own datasets, and packaging that and selling them to carriers. And so, it's both. It's third-party vendors that are not licensees, but also MGUs that are licensed and subject to audit."

Asked whether there might be another model on the horizon aimed specifically at brokers, agents and MGUs, Baty said he doesn't think so. Instead, the NAIC will remain focused at the carrier level—"if you contract the third party to supply these data, you have to have the following terms. You must comply. These terms have to be in the contract. That's what we'll likely see coming out of 2024."

Baty said that Maryland's Insurance Commissioner Birrane, the chair of the NAIC committee that drafted the model bulletin, has indicated that in 2024 the relationship between carrier and third-party data supplier is one of the things the NAIC will be examining more closely. CM

All Aboard:
What's Next for Executives and Directors Riding the AI Train

Executive Summary: A year after ChatGPT exploded onto the scene, and a month after the NAIC's adoption of a "Model Bulletin on the Use of Algorithms, Predictive Models, and Artificial Intelligence (AI) Systems by Insurers," *CM* Guest Editor Mike Fitzgerald asked industry participants and observers what all this means for property/casualty insurers. Here, we summarize portions of the individual interviews, highlighting some of the topics addressed in other articles in this special section—"Leading AI-Powered Insurers," which was conceived by Fitzgerald, an industry analyst for SAS Institute.

By Susanne Sclafane

**Guest Editor Michael (Fitz) Fitzgerald
Insurance Industry Advisor for
SAS Institute Inc.**

Some are standing in the station. Others are already on board. Property/casualty insurance carriers are mapping out itineraries as the AI train speeds across this industry and the ones they insure.

A year after ChatGPT exploded onto the scene garnering 1 million users in just five days, and a month after the NAIC's adoption of a "Model Bulletin on the Use of Algorithms, Predictive Models, and Artificial Intelligence (AI) Systems by Insurers," *CM* Guest Editor Mike Fitzgerald asked industry participants and observers whose opinions he values what all this means for property/casualty insurers.

How will generative AI and advanced analytics impact the insurance industry?

Pina Albo, chief executive officer of Hamilton Insurance Group, the newest

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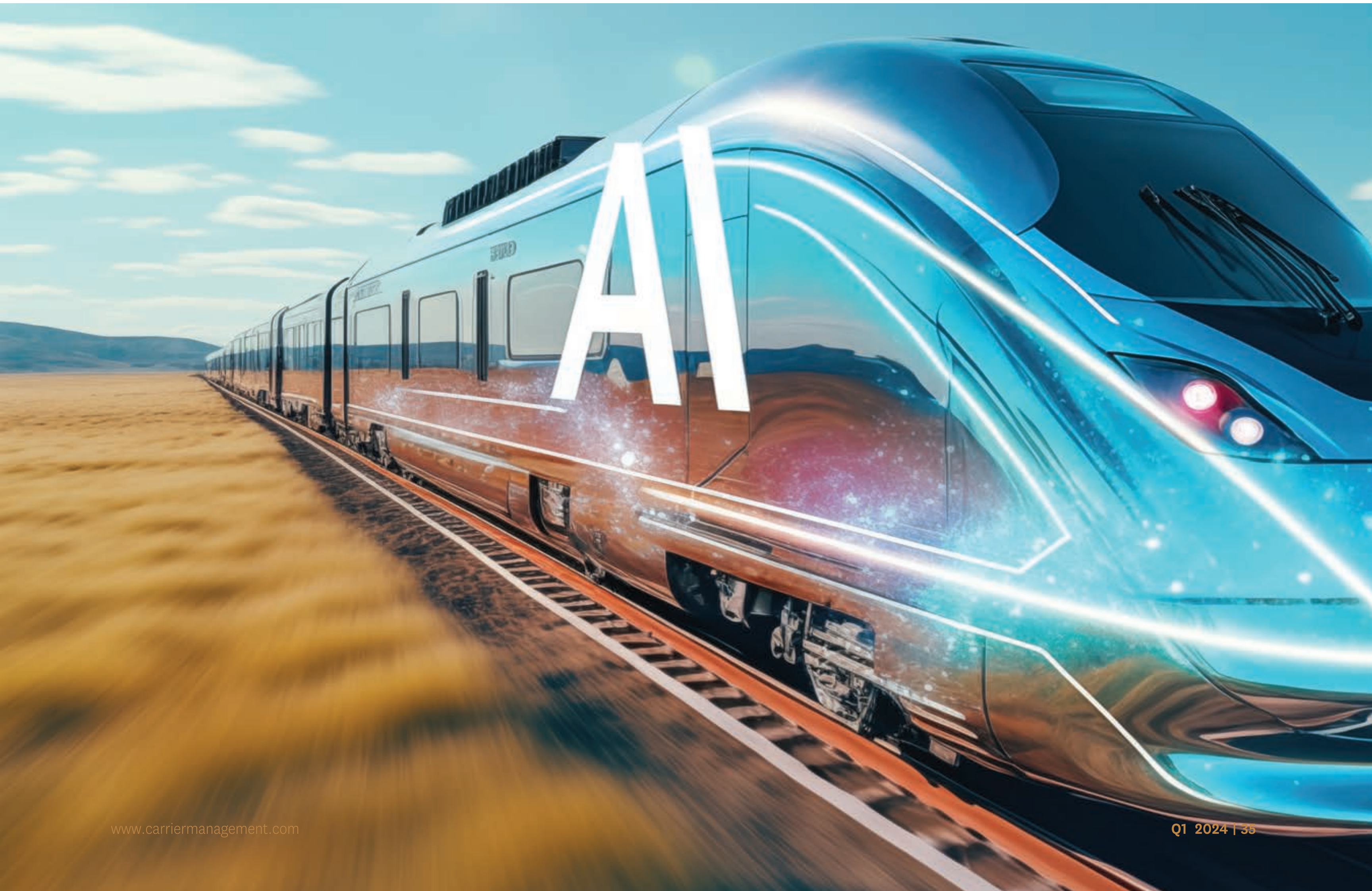

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public insurance company in the P/C insurance industry, revealed that her company is already using generative AI to streamline underwriting workflows. “But you don’t have to invent every mousetrap yourself,” advised Albo, who confirmed that embracing technology and analytics has been a core tenet of Hamilton’s strategy since inception.

“Everything we do, we think about how can technology and data make us better, make us stronger, make us faster. And over the years we have both invested in proprietary technology tools to enable our business, specific to our business, but we’ve also partnered with some vendors,” she said.

In particular, she noted that Hamilton teamed up with an AI vendor a few years ago to provide a tool specific to the property insurance area. Hamilton insures Fortune 500 and Fortune 1000 companies that have very complex buildings at multiple locations. “We use AI there to read the very extensive and complicated engineering reports and provide us scores. We humans could not do that at the speed and actually at the accuracy that this tool does for us. So, there we find it a real competitive advantage,” she said.

“Every single function will be touched by AI, generative AI and advanced analytics. Every single function,” said Jonathan Kalman, a partner with Eos Venture Partners, a venture capital firm exclusively focused on the insurance industry.

“On a simple level, it could just be using those analytics to develop customized workflows that better serve segmented populations.” AI has “an ability to create

micro-optimization of processes in ways that are infinitely scalable," he said. Contrasting the days of pasting stickers on whiteboards and rearranging them to simplify main core workflows with the new world that's opened up through AI, Kalman said, "There is technology right now that has the capability to essentially watch a workflow, reflect on a workflow, understand a workflow and optimize the workflow in ways that we can't even imagine." Insurers can leverage this ability "to surface and extract data, organize it and make meaning out of it, and when directed through appropriate prompts, to create ways to synthesize improved outcomes," he said.

"The mid-market carriers and the smaller carriers that feel they have got to jump on this fast-moving AI train if they're going to remain competitive don't have the infrastructure and the processes built out to develop and to write up a robust AI program. They don't know what that looks like."

Bruce Baty, Norton Rose Fulbright US LLP

This will reverberate through "every aspect of the business"—even the finance function, he said. Giving a heads-up to finance executives, he said, "It will impact reserving. It will impact treasury. It'll impact investment management. It will impact your balance sheet allocations. It'll impact your understanding of trading patterns if you're a public market."

"When you look across the entire business, it will be impacted. It won't be impacted this week or next week or at the end of 2024, but we are in the midst of the most profound shift of the last 50 years," he said.

Albo, a Canadian lawyer by training, who went on to work as a casualty underwriter and leader of businesses around the world for Munich Re before signing on to head up Hamilton in 2018, recalls that one of her first hires was Chief Technology Officer Venkat Krishnamoorthy. "He's always thinking ahead" and observing what's on the horizon, she said, revealing that she moved ahead to greenlight a pilot of an internally designed tool derived from Open AI after Krishnamoorthy pulled her aside to demonstrate it last year.

Rather than a vendor partnership, "this is our *own* AI project," she said, explaining that the tool essentially reads emails to populate Hamilton's workflow system.

"Insurance submissions come largely in the form of email. They don't all come looking the same way. Normally you have humans who will extract that data and populate it into your workflow system," she said. The in-house tool does that automatically. "We use AI to read the emails, read the submissions, populate [our] workbench and then take it from there. We did it in a very specific area just to pilot it, to test it, to see if it works. And now that we've proven that proposition, we will expand it more broadly across our operations," she said.

"We're building a global diversified specialty insurance and reinsurance

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company that's enhanced by data and technology and focused on producing sustainable underwriting profitability," she told Fitzgerald.

What should executives of P/C carriers start thinking about today as they move ahead to embrace advanced analytics and AI in their operations? What should be on the boardroom agenda?

According to Bruce Baty, a partner with the law firm Norton Rose Fulbright U.S. LLP, regulators have sent a clear message, both with the adoption of the NAIC's AI Principles in 2020, and now through the adoption of a model bulletin on carriers' use of Artificial Intelligence Systems, that carriers need to address AI in their Corporate Governance Annual Disclosure (CGAD) reports, which have been required to be filed by all carriers to state regulators since 2015.

The board of directors needs to understand the processes for control over the use of AI within the company. "This is now going to call for a separate AI program for executives to develop out and present to the board that addresses, 'How are we mitigating risk to the consumers? How are we complying with unfair trade practices acts? [Are we] rooting out implicit bias in the system so that we're not going back to the days of redlining? And how are we complying with unfair claims practices?'"

"This is a new level of inquiry for the board: 'Have we developed out our AI program? What does it look like?' And we want to talk to the executives at the board level to find out, 'Are we complying with the laws that are already on the books?'"

Said Albo, "I think that board members should be asking us—and they are, quite frankly—'How are you embracing this technology?' Clearly, there are risks involved, and you have to be conscious of this risk and mitigate the risk. But there is an immense amount of opportunity now, particularly with OpenAI."

Explaining why that is the case, she said that vendor models trained on specific datasets cost money to build. "With ChatGPT, the barrier to entry has just been lowered significantly."

"So, our board members are asking us, 'What opportunities do you see here for using this OpenAI? How can you improve what you're doing or service your clients and brokers better by embracing it?' We're getting questions on both sides: 'What are the risks and how are you managing those risks? And what bets are you placing?'"

Are P/C insurance company boards and executives well-positioned to take this on? What areas would you encourage them to work on?

Baty offered one example of a client of his firm that is in better shape than most insurers. A team of lawyers, he said, will be meeting with senior U.S. executives of a very large international group to present ideas on best practices—on what a robust AI program should look like. "That group is then going to be making a presentation to their board of directors. But we're not starting out from scratch with this group. They already have a framework that they've worked at. We're just tweaking that to make sure that we're hitting all of the marks in terms of the model laws that apply. They're far ahead of the game. They've got their written procedures in place. They're already in communication with the board..."

"That is not the norm," Baty said.

"The mid-market carriers and the smaller carriers that feel they have got to jump on this fast-moving AI train if they're going to remain competitive,...don't have the infrastructure and the processes built out to develop and to write up a robust AI program. They don't know what that looks like. They're going to be catching up and trying to figure this out [at] the executive and the board level."

"We do it bite-sized. Let's take a pilot project. Let's see if it works. If it doesn't work, let's pivot. Let's move and fix it. And then once it does work, how do we leverage that more broadly across our organization?"
Pina Albo, Hamilton Insurance

Shoud P/C insurance and reinsurance company boards appoint technologists as directors? When discussions turn to finding bias in a machine learning algorithm that looks at huge datasets, do boards understand that?

"They do not understand that, and there is a gap," said Baty, who called out the boards of nonpublic PE-backed companies, in particular.

"As you think back over the activity in the industry in the last 10 years or so, with private equity coming in and buying up insurance companies, primarily life insurance companies to take advantage of the large reserves on the books of those carriers,...you don't find a lot of insurance expertise on these boards. You don't find technology people on the board. These are all business and finance people that are driving the companies that they purchased.

What about traditional players, not the newer PE- and VC-backed entities? Who sits on those boards? Does board composition need to change? Is there a technology skills gap at the board level?

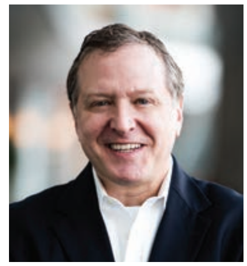
Before CGAD, "there was not a lot of deep thought going into the question, 'Why is this person sitting on the board of directors of this insurance company?'" Baty reported. "It was because 'I've known them for years' or 'I went to school with them,' 'I played golf with this person...And CGAD now told us that we need to stop and sit back and think about, 'Why do we think this person is capable of overseeing our insurance operations? And here are her credentials...'"

"Now we need people on the board who are not dinosaurs like me but rather who are well-versed in this kind of technology that can really contribute to the organization."

At Hamilton, Albo is proud to talk about the recent appointment of Dr. Henna Karna to the board of directors. Karna, who earned both a master's and a Ph.D. in applied mathematics from the University of Massachusetts, and a master's in business administration from MIT, has also designed and developed patent-pending technology and applications in the fields of AI, genetic algorithms, behavioral analytics, deep neural nets and advanced data technologies.

"When I was introduced to Henna, the first call I made was to my board chair and said we've got to get her on our board...We were so thrilled not just [with] her particular expertise in this area but coupled with insurance. It just was too good to be true," Albo said, referring to the fact that Karna has led digital services, technology and data businesses at Verisk Analytics, AIG and AXA XL. Her more than a dozen years of experience working in the P/C insurance industry culminated in a position as managing director, Global Insurance & Risk Management Solutions at Google Cloud from 2020-2023. (Read more about Karna in the online article, "CM Exclusive: Google's Insurance Strategy Could Be a Game Changer.")

Albo said Hamilton's nominating committee is "always very deliberate about looking for diversity of experience, of backgrounds, of knowledge that's specific to our business and will help us...We have a very well-rounded and diverse board, and several board members do have an affinity to technology or knowledge of technology," she said. (Editor's Note: Other Hamilton board members include Russ Fradin, a partner with the PE firm Clayton, Dubilier & Rice, who served as president and CEO of software and IT provider SunGard Data Systems until the company's 2015 acquisition by FIS in November 2015, and Marvin Pestcoe, CEO of Langhorne Re, who previously served as chief risk and actuarial officer at PartnerRe, where he was responsible for overseeing risk, capital modeling and reserving functions.)



"There is technology right now that has the capability to essentially watch a workflow, reflect on a workflow, understand a workflow and optimize the workflow in ways that we can't even imagine."

Jonathan Kalman, Eos Venture Partners

"Putting a board together is a conscious, deliberate process, and if you go about it the right way, you will be able to have all the skills that you need to run a business as complicated as ours...Technology and AI, any emerging technology is core to our business and should be represented around the table at the board level," Albo said.

While Albo helped push Karna's appointment forward, unlike Baty, she believes boards without technologists are capable of asking the right questions. Agreeing with Fitzgerald, who hypothesized that boards have technology gaps, on the other side of the coin, she said, whether as a board member for other entities or just as an executive and a board member of Hamilton, there's not one continuing education seminar that I attend, not one newsletter I open up that hasn't got AI and technology top of mind. So, I think boards are turning their attention increasingly to this topic," she said.

"What opened that door was the whole area of cyber attacks. That in and of itself has opened boards' minds" to start paying more attention to technology, she believes.

At Hamilton, we very specifically thought about this, and we have that expertise both around the executive table with our CTO and chief data officer but also on the board."

Who's responsible for AI governance at the board level? Should the compliance, the risk and the nominating committee, for example, all be raising questions about AI? Or should there be a separate AI committee? What about the management team—a committee of people from underwriting, claims, product development, etc.? Or a chief AI officer and his group?

Boards have really struggled with these questions, Baty said. "If it's the entire board, then that's not a robust oversight of your AI activity. So, boards have been looking at either creating subcommittees or assigning the audit committee to be in charge of this to embrace their oversight of AI."

Baty encourages insurance company boards to take a cue from how the NAIC settled on a regulatory team responsible for crafting the recently adopted AI model bulletin. (See p. 30 for more about the bulletin.) Regulators identified the issue that sat at various committees within NAIC until they ultimately settled on the H Committee on Innovation, Cybersecurity and Technology. "Just as the NAIC came around to [deciding] we need a dedicated committee to address these issues with its own specialized working groups, that's how I think [carrier] boards of directors need to evolve. [From] the various established committees we have on the board, I think we need to establish a new innovation, cybersecurity committee of the board that is focused on these issues."

"And they will draw [input] from all elements of the company—accounting, underwriting, legal, compliance," he said. (See also, Fitzgerald's view on p. 17, "Organizing for Action: The Board of Directors in the AI-Powered Insurer.")

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How should small and midsize carriers be preparing for the new world of AI?

Baty asked Fitzgerald, insurance industry advisor for SAS Institute, for his own answer to the question.

"The most fundamental thing I would say is you have to find resources to put at this rather than giving them some specific project," Fitzgerald said. "They need to look at their balance sheet and [come to the conclusion that] if we're going to survive, we have to invest in an area that we traditionally never have before and then see where that goes. I'm talking about a material impact—a $300 million carrier is going to need to put millions in, especially at the beginning to get up to speed if they're going to be around in 25, 30 years."

Baty honed in on the governance and risk management tasks ahead. "This is not a knock on the people who currently head up IT, but that's not their area of expertise. So, you've got the head of IT, you've got the CISO, but you don't have anybody that's really grounded in AI principles and really understands that technology. And if you're going to play in this market—and you have to as this train keeps speeding down the track—you're going to have to get on board with this because this is how product is going to be sold. This is how product is going to be developed. This is how claims are going to be managed in the future. And you have got to embrace this technology."

Albo framed her advice for leaders of AI-powered insurers by reflecting on Hamilton's approach. "First and foremost, we look at what is necessary to execute the strategy for our business and what we are trying to achieve."

"This involves thinking not only of the here and now, but more importantly, thinking about the future and what it's going to take to be great," she said, drawing inspiration from hockey legend Wayne Gretzky, who attributed his success in the game to an unwavering focus on where the puck was going.

"We use that same kind of mentality—always trying to think, 'What is out there? What should we be thinking about? What new technologies can we embed in our business?'"

"A $300 million carrier is going to need to put millions in, especially at the beginning, to get up to speed if they're going to be around in 25, 30 years."

Michael Fitzgerald, SAS Institute

In addition, Albo advises, "We're not trying to boil the ocean. We're not playing buzzword bingo here. We're looking very specifically at what do our underwriters, our operations staff—what do they need to make their lives more efficient, more effective, [and] to make us more responsive."

"And then we do it bite-sized. Let's take a pilot project. Let's see if it works. If it doesn't work, let's pivot. Let's move and fix it. And then once it does work, how do we leverage that more broadly across our organization?" she said.

What are carrier leaders most worried about as they grapple with boarding the AI train? What missteps have they made?

Kalman said: "The carriers that are at the forefront are the carriers who started investing in a data infrastructure a decade ago, hands down. Those are the ones that listened when the advisers from McKinsey and Accenture and other firms said, 'Look at your data today. Not only is it siloed, but some of that data is embedded in departmental solutions or even embedded within an application. And what you need to do is really develop a sophisticated technology architecture specific to the use of information, separate from the transaction processing systems underneath it. And you need to save the data and leverage the fact that the cloud economics are fractional from what it would cost historically. You need to start creating that environment, especially so that you can focus on the issues around cleansing the data.'"

For carriers that have already taken those steps, "it's easy to step into a proprietary large language model. It's been easy for them to say we already know where [the data] is. We already have governance policies. We already have invested in teams to do it. They will accelerate ahead of other carriers that do not have the economies of scale to make those investments."

Kalman answered no with a head shake when asked if he sensed that most of the industry had done that data and governance work. Then, he offered that "most everybody has done something."

"It's not like it's new, but they haven't necessarily made it a priority that's risen to the board level, where you're having people say, like, 'Are we doing this fast enough?'" Over the past 20 years, the P/C industry has spent the most money retrofitting core policy admin systems—and they spent a fraction of that on analytics," he stated. "But optimizing the core processing platform isn't competitive differentiation. It's competitive parity. You need the analytics to get differentiation because every insurance company has a different underwriting box, different expectations and a different approach," he said.

Carriers that don't have the resources to move in the right direction will see their financial performance impacted over time, Kalman believes. "The rate of change in this industry is going up by order of magnitude every year. Every part of the industry is being touched," he said. CM

All hope is not lost for lagging carriers, however, Kalman said. He went on to offer some sage advice about winning the AI talent war. See related article, "'Critical Thinkers' Needed for AI-Powered P/C Insurers," p. 41.

'Critical Thinkers' Needed for AI-Powered P/C Insurers:
Building AI Leadership Across the Enterprise

Executive Summary: Leadership happens at all levels of the organization. How will insurers infuse AI leadership across the entire enterprise? P/C industry participants shared their thoughts with *CM* Guest Editor Mike Fitzgerald.

By Susanne Sclafane
Guest Editor Michael (Fitz) Fitzgerald
Insurance Industry Advisor for
SAS Institute Inc.

Career experience in deep tech and investing in insurance industry innovation give Jonathan Kalman a unique perspective on how artificial intelligence will change the P/C insurance industry.

The impacts of AI will be felt in "every single function"—and talent management is no exception, Kalman, a founding partner of Eos Venture Partners told *CM* Guest Editor Michael (Fitz) Fitzgerald during a recent interview.

"AI will impact the talent war in [the] industry. You will see a tremendous upskilling of the workforce in insurance where people will be augmenting their work with a copilot, which will allow faster maturation of skills," said Kalman (referring broadly to assistive technology rather than Microsoft Copilot, specifically). "It will allow different skills transfer. And it will allow more efficient workloads, so you can have less people doing administrative tasks."

"But this is a point which is really lost on many of the people we talk [with] who are fearful of it impacting the jobs. It is actually going to require more people to be discerning and discriminating in their ability to understand the [AI] output," he said. Explaining why, Kalman noted that the goal of AI technology is to "always give you an answer. That's not like a person who can get stuck, who says, 'Hey, I'm stuck. I know I'm stuck. This number doesn't look right. I need help.' The computer never says that."

"That human discernment of understanding and looking at the information is important," he said.

Yes, the acceleration of AI applications also means "a great opportunity for our country to continue its focus on STEM. Those skills will be more in demand as we go through. But at the same time, it's not just STEM. It's also what is taught in often more humanities-based courses, which is critical thinking," Kalman stressed.

"Sometimes it's easier to teach someone who is good at critical thinking how to use a copilot than it is to teach somebody who is an engineer or leading mathematician how to become a critical thinker," he said.

Nonetheless, Bruce Baty, a partner with the law firm Norton Rose Fulbright U.S. LLP, who has decades of experience

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assisting insurers on regulatory matters, believes insurers will need AI specialists, and he sees well-positioned insurers casting a wide net to snag them. "They don't have to be insurance people. I work with clients all the time that bring in the head of marketing for Staples or some retail operation, and one of the first things we do is go through training on insurance advertising principles and how that is so different than anything they've done in the past. But they're smart people and they get it. They can adapt their experience to the insurance industry."

"That's what we're going to have to do with AI specialists coming in," he said, suggesting that training will go beyond claims and underwriting and production.

The new talent will need to appreciate how to build AI models that are fully compliant with insurance laws and regulations.

Kalman sees a path forward in expanding the skill sets of career insurance professionals to add knowledge of AI to the mix. "The wonderful thing about this new world we're living in is that there is so much education about it. Any employee can be upskilling. You can take a course online—many free. Many universities offer free courses."

Putting himself in the shoes of an insurance carrier executive, Kalman said, "The first thing I would do is I would say every employee gets a $500 stipend to take a course."

"And here is what I didn't say: Let's go spend $10 million and figure out how to build a data lake," Kalman added. "Educate your people. That's your biggest impact [and] differentiation," he said, suggesting with that education about AI tools, ideas about how the firm can leverage the technology to solve its problems will blossom internally.

"How do you light up your workforce to do this?" he asked, suggesting that executives who seek to answer this will move ahead of the rest.

A CEO's View

Hamilton Insurance Chief Executive Officer Pina Albo is among the leaders who believes that the best ideas about how to leverage AI will come from within. In 2019, in an article Albo posted on LinkedIn to mark the first anniversary of her role as CEO, she wrote, "The role of people versus the role of technology is not a binary question. Few would argue that machines have not and will not continue to replace human labor. The best-case scenario is for them to replace tasks, not work in the sense of the net sum of jobs."

"Modern organizations face the challenge of elegantly integrating people, processes, and technologies with desired outcomes."

Five years later, she talked about a leader's role in meeting that challenge. "It was important to me to have somebody responsible for technology at the executive table in the company," she said, referring to the fact that one of her first actions as CEO was to hire a chief technology officer. "As a result of that, technology is a standing agenda item on our weekly executive calls. We're always talking about what investments we should make. What is going to help us drive it forward?"

"The investments that we make are informed by our people," she said. "We don't think top-down: Wouldn't it be great to do this? We think about what do our employees who are closest to the business, who are transacting every day, what are they telling us that they need." Then Hamilton executives examine the "list of to-dos" compiled from listening to the workforce and decide how to prioritize those in order to make their lives easier.

"It's not some kind of blue box thinking. It is specific to the business. It's specific to the needs. It's making them better at what they do."

At least one idea came directly from the CTO to Albo—a tool derived from Open AI that extracts key information from email submissions and populates an underwriting workbench. "That was our chief technology officer actually putting me in the room and saying, let me show you something. He actually took me through what ChatGPT can do to an insurance submission that we get at Lloyd's," she said, noting that the CTO expressed a desire to pilot the tool.

"Sometimes we have to be willing to place a bet," Albo said, explaining her decision to let the pilot go forward. "That is something that I have to do—that a leadership team has to do, which maybe didn't come from our workforce. But we think there's something there" and we act, she said.

Leaders "have to be willing both to listen to their people and give them the tools that they need to be better. And then when technology comes, [employees] are embracing it because it's helping them." Then, at the same time, leaders have to be thinking about what else is possible. "What dimensions are [employees] not thinking about because they're just too much in their weeds [but] that we think might be a game-changer for the future? What bet are we going to place?"

Asked specifically to describe professional development programs that assist Hamilton in delivering on two business imperatives of the specialty insurer and reinsurer—empowering the business with technology and being a magnet for talent—Albo said that Hamilton enables attendance in various continuous education courses, which increasingly include technology-enhanced programs.

What about change management programs?

"Because a lot of our technology is response to what we're hearing [from the workforce], that change management process is a lot easier to implement—because it's not a 'top-down, we-want-you-to-do-this [charge]. It's more [that] we listened...We involve our underwriters in the process" of building technology, she said.

As an example, she noted that Hamilton is currently starting to build a workbench for its newest business, Hamilton Select, a U.S. E&S operation. "Who's involved in the process? Our chief underwriting office; our heads of business lines. They're involved because this is what they're going to use every day," Albo reported. CM

Stick to Purpose: Why Carriers Need to Cooperate on AI

Executive Summary: Henna Karna, a technology entrepreneur who has led digital services, technology and data businesses at Verisk Analytics, AIG and AXA XL, as well as an insurance solutions business at Google Cloud, believes that building basic AI models is not a competitive advantage for any P/C insurance carrier. Karna, who describes her career without reference to those well-known employers but instead by focusing on her missions to solve the complex problems of closing protection gaps and using data to deliver customer-centered products, believes that understanding how to manage and mitigate risks are the skills that set carriers apart from one another. She recommends they collaborate rather than try to compete to develop basic AI tools.

By Susanne Sclafane
Guest Editor Michael (Fitz) Fitzgerald
Insurance Industry Advisor for
SAS Institute Inc.

An industry consortium or other form of coopetition may be the best way for carriers to jump into the fast-moving world of AI, a tech entrepreneur who has held executive roles at major carriers suggested recently.

During an interview with *CM* Guest Editor Michael (Fitz) Fitzgerald, Henna Karna suggested that building basic AI models is not a competitive advantage in the property/casualty insurance industry. Instead, understanding the nuances of different types of existing and emerging risks and how to manage them are the skills that set the industry apart—and set carriers apart from one another, she said, recommending that insurers focus their energies on innovations that align with those core skills.

"I would love to have a consortium in our industry where we're producing AI models that are base layer. They're not the IP layer. They're just the base that everybody needs to have—because we shouldn't be inventing ZIP code 500 times," she said, referring to the use of geocoded data. That "ZIP code invention" is something that Karna, who engaged with hundreds of insurers around the world in a prior position at Google, has heard executives inaccurately call out as technology that sets their firms apart.

"Things like that, those sorts of fundamental AI models could be very

continued on next page

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useful for everybody across the insurance value chain. And they're not the secret sauce. Even though we might think so right now, they're not," Karna said.

"How do we now change that mindset?" she asked. "I'm looking forward to that change."

Karna's work as general manager of Global Industry Solutions in Insurance at Google, creating an open-source offering of a layer of net-new data and analytics for the insurance industry, gave her a broad view of the P/C industry's progress to date and opportunities to come. Prior to Google, she spent more than a dozen years leading digital services, technology and data businesses at Verisk Analytics, AIG and AXA XL, igniting personal passions centered on dual goals of helping insurers become more customer-centric by leaning into data and digital experiences and closing protection gaps around the world.

(Read more about Karna's career and her previous position at Google in prior *CM* articles, "CM Exclusive: Google's Insurance Strategy Could Be a Game Changer" and "Google's Champion of Holistic Insurance: Karna's Journey Continues")

"It's going to be super-exciting to be able to take all [available] information at a point of decision, at the point of underwriting—[to have] a 360-degree view of risk," she said, referring to industry opportunities ahead that are being fueled by the "multimodality of everything." In other words, models that pull together data from text, video, images and sensors are increasingly giving carriers a better understanding of what their customers are experiencing, whether commercial enterprises or consumer.

Still, Karna has questions about how everything will come together.

Outside the insurance industry, "we talk about Open AI all the time now. We talk about these organizations that are looking at generating content." The content generators are focused on what information can be used to train AI models going forward, "and our industry is not able to catch up with that yet," Karna said. "We have to find a way to think about how do we as an industry [move on to] generation of information that is new, and not lean onto every other area."

At that point, Karna, who holds a master's and a Ph.D. in applied mathematics from the University of Massachusetts and a master's in business administration from MIT, offered her vision of an industry consortium.

"Consortium may be the wrong word. It's collaboration or coopetition," she said, prefacing her explanation of a joint effort for the P/C insurance industry that might allow individual companies to move forward to breakthrough risk management innovations using data, advanced analytics and AI.

"One of the learnings I had going from AXA to Google was [that] companies that are not AI bread-and-butter companies should not be AI bread-and-butter companies...Our expertise in our industry, the business we know is risk mitigation and risk management...For us to spend energy and time and focus on that is key."

"For us to reinvent a [data] cloud or reinvent an AI model that's going to fix my autogeneration of clauses—that isn't the game-changing world. It's a very short-term [win]. It can help us go faster today, but it won't scale and it won't sustain us going forward," she said.

"We didn't invent APIs as an industry," she continued, referring to application programming interfaces (that allow two or more computer programs or applications to talk with each other). "We're using them. But if there was a best practice for APIs, we would just take that and go. We don't have to create a new version of that."

"If there was a best practice for telematics, we would take that and go. And then our competitive advantage would be how do we do more beyond the base layer," she said.

Karna continued: "It still surprises me when I go into an executive meeting and the discussion is about how different we are because we do location monitoring

"For us to reinvent a cloud or reinvent an AI model that's going to fix my auto-generation of clauses—that isn't the game-changing world...It can help us go faster today, but it won't scale and it won't sustain us going forward."
Henna Karna

differently. But that actually just means [using] location-specific data, geocode or something like that. It's not actually location monitoring" via sensors or real-time data.

"Transparency about what we actually are good at, and then what we think is not our competitive advantage, that I think is going to be pretty important."

"Fundamentally, what is our business? Let's get very good in that business and use the ecosystem to do everything else with us—lean on the ebbs and flows of the ecosystem to get us all the ingredients that we need, and then we focus on what we think is going to be our biggest game-changing, value-add differentiation for the market that we're in," she said.

"We tend to do all of the above, and we lose a lot of momentum that way."

Describing Karna's vision as a collection of AI microservices sitting above the technology infrastructure level, Fitzgerald drew an analogy to the work of the industry standards organization ACORD. "Nobody has their own workers compensation application anymore, right? They just pick up the ACORD data and format" and add to those.

Been There, Done That

Building on Karna's idea, Fitzgerald

suggested the P/C insurance industry might take a cue from the telecommunications industry. Twenty-five years ago, pre-3G, telecoms were "building their own protocols," he said. Eventually, "they standardized on a common approach. So, when they went to 3G, 4G and now 5G, they don't build their own network protocols anymore."

Fitzgerald asked Karna, who was recently appointed to serve on the board of Hamilton Insurance Group, if it would make sense for nominating committees of insurers to consider former telecom executives—or executives from other industries "who have seen this before from outside"—on their slates of board director candidates.

Karna agreed that the idea makes sense. "Not only have they [telecom executives] understood what normalization is [but also] the fear of it. There's a concern, right? We always spend so much energy thinking that we're different that we perhaps have to step back and say, 'OK. Actually, this isn't what differentiates us because that's just base core.' And then leaning into what that difference is."

"The CPG [consumer packaged goods] industry is similar. At some point, they had to normalize also," she said, referring to the process to reorganizing data in consistent formats from disparate sources.

"Executives that have been there, seen that and have seen technology take a different course of action to create relevancy, and [seen that] that relevancy is good for the end customer, can bring a little bit of grounding to [insurance] boards" by sharing their journeys. They might also offer perspective for gathering good questions.

"At the board level, I think that's the most important thing—[that] we are thoughtful about the questions we ask and sincere about what we hope is a good outcome," Karna said. CM

Related article, p. 46: Dual Skills Needed to Sit on Boards of Tech-Savvy P/C Insurers

A longer version of this article, which includes Karna's thoughts on building internal collaborations to move innovation forward, is available on Carrier Management's website.

Dual Skills Needed to Sit on Boards of

Tech-Savvy P/C Insurers

Executive Summary: Tech professionals who will make the biggest boardroom contributions will be those who pursue risk management designations, according to Ursuline Foley, a technologist turned independent board director for financial services companies. Foley, who led tech transformations for XL Group during a 35-plus-year career, sees the potential for AI to impact insurers beyond tasks such as data ingestion and customer support.

By Susanne Sclafane
Guest Editor Michael (Fitz) Fitzgerald
Insurance Industry Advisor for SAS Institute Inc.

With titles like global chief information officer, chief data officer and chief platform operations officer marking an accomplished career in financial services, Ursuline Foley is well-positioned to peer into the P/C insurance industry's future with AI.

But when *CM* Guest Editor Michael (Fitz) Fitzgerald selected Foley to interview as part of a series of articles about leadership tips for AI-powered insurers recently, it wasn't just her experience in leading multiple global business transformations for XL Group (and later AXA XL) that pointed him in her direction.

Fitzgerald was also interested in her view from the vantage point of a member of boards of directors of multiple companies in and outside the insurance industry. In particular, Fitzgerald wondered about the composition of boards. Do they have enough technologists like Foley? In what ways do the skill sets of directors need to be broadened as the opportunities and challenges of AI rise to the boardroom agenda?

Foley purposefully left her last executive role in the insurance industry to focus her full attention to serving on various boards of directors. Having served on the boards of not-for-profits like the Society for Information Management, Pace University and the National Association of Corporate Directors, and in advisory board member roles for private equity firm Blumberg Capital LLC and Accenture's Insurance Innovation Executive Board, Foley landed her first public board role in 2019 with Provident Financial Services, where she serves on the Risk and Technology committees. Then about three years ago, she was appointed to the board of Greenlight Capital Reinsurance, serving as chair of the compensation committee and a member of the audit committee.

Foley doesn't "believe for one second" that she garnered those two public board appointments based on her technology skills alone. Noting that a typical board is composed of between eight and 15 people, she said, "They can't really afford to bring on an individual that just represents one skill set. Boards want to manage their size. Otherwise, it can become a bureaucracy and not an oversight body."

She believes boards "are looking for technologists—but technologists that have a very strong business acumen." She encourages fellow technologists, even those who have "managed risk and business continuity in a big way [and] have had to understand the business operations of companies end to end," to "round off" their risk management skill set with certificates in enterprise risk management.

Highlighting areas like liquidity risk management, credit risk management, investment risk management, geopolitical risk and third-party risk management, she noted that the DCRO Risk Governance Institute offers programs such as Qualified Risk Director, Certificate in Risk Governance and Certificate in Cyber Risk Governance designations (all three of which she holds).

A diversity of skills represented among directors enriches the conversation in the boardroom, Foley said. "It forces questions to be asked that are outside of the box." The questions encourage broader thinking on topics. Board members who were more likely to lean one way initially, might move "more toward the middle on a particular topic" as a result, she said.

Fitzgerald also asked Foley what boards should be asking executive management about the use of AI.

"They should at least be asking their technology officers, 'Is it something we're considering as a company? And how are we providing some oversight and guidelines on that—and education?'" she said, reporting that her boards are educating directors on the capabilities of AI.

Foley pointed out that boards of P/C insurers and reinsurers are confronted with many issues—AI opportunities and risks being just one of them. She listed catastrophe risks, convective storms, interest rate risk and geopolitical risks as items also consuming boardroom mindshare. There's a lot to navigate in addition to the speed of technological change. "Never have we lived through such an uncertainty on so many fronts," she said.

Tips for Fast Followers

Still, Foley said carriers can't afford not to embrace the prospects of using AI tools to bring efficiencies to support desks and to activities like data entry and memo writing. "Those are low-hanging fruit." But AI "should never be used totally on its own. I see it as an enabler," she said. "If you're using external information, [then] you can't totally trust that it's factual."

Foley also emphasized the importance of governing internal data—ensuring it is current and validated using good analytics. "If you've got all of that right now, you can basically embrace AI and take it to the next level," she said. "For companies that are more advanced in their data governance and analytics, then they are in a great position to leverage AI in the more valued business processes of underwriting, claims management, risk management, etc. AI will be a game-changer long-term, but those companies that educate and prepare their teams now about the possibilities and the risks of AI so that they can start to embrace it in their solutions and culture are the companies that will reap the big benefits over the long run."

The prospect of an AI-enabled future "really reinforces the topic of data even more than ever before, which in turn reinforces the topic of good analytics as a means to validate data," she said. "If you don't have those two check marks going well in your company, then you are far away from using AI well."

She continued: "Everybody is worried about the black box for AI, and the only way you can peel back the black box is to know that you've got good confidence and ownership in your company's data, and understand the analytical tools that you can rely on to validate your own data."

Foley also cautioned insurers to move slowly as they incorporate AI tools into their operations. "You want to be a close follower. You don't want to be the laggard. You can't afford not to do it. You want to be in there, but you don't want to be the leader either," she said, explaining that leaders will stumble through early issues. "Having lived in the world of technology for 35 years-plus, I would say that about any technology when it's first introduced. It's going to evolve and it's going to become even better," she said.

"One positive thing that AI is doing is that it's opening up employees' and business leaders' minds, and especially society's minds even more to the current capabilities of technology. Even if you're not going to use AI—[if] you use blockchain or you use e-commerce or some traditional method—the fact is that society and employees and business leaders overall are much more aware now of the possibilities and capabilities of technology."

"Their eyes have been opened," she said. CM

"The only way you can peel back the black box is to know that you've got good confidence and ownership in your company's data, and understand the analytical tools that you can rely on to validate your own data."

Ursuline Foley

Executive Summary: Generative AI's remarkable productivity and untamed risks encouraged four CROs to establish early rules, build governance structures and commence pilot tests. Insurance Journalist Russ Banham spoke to CROs of QBE NA, Cincinnati Insurance, Church Mutual and United Educators.

Chief Risk Officers Take on Gen AI

By Russ Banham

Guest Editor Michael (Fitz) Fitzgerald Insurance Industry Advisor for SAS Institute Inc.

When Generative AI burst onto the scene at the end of 2022, users gushed about the automatic content creation, greater productivity, and some funny or disturbing anomalies. Within days, it seemed, people who had not given Gen AI a try were outliers. Few technologies had captured the public's imagination so quickly.

These developments were closely watched by chief risk officers across diverse industries, given their responsibility to identify, assess and mitigate significant risks to operations. This was especially the case in the insurance industry, where many CROs either took it upon themselves or were tasked by other senior executives and board members to balance the perceived benefits of Gen AI with its opaque risks.

Concerns centered on the accuracy and source of the underlying data used by different Gen AI models to detect commonalities, patterns and anomalies. Biased, inaccurate, fake or copyrighted information can result in compliance violations, intellectual property infringement, breach of contract, erroneous fraud alerts, harmful customer communications, third-party exposures and reputational damage. These risks and others are only half the story, of course.

Gen AI's ability to process large sources of unstructured data on behalf of user prompts and turn it into images, speech, text, video and other content is of enormous benefit to insurance carriers. Gen AI offers the opportunity to enhance operational processes in underwriting, claims, fraud detection, customer interactions, risk assessment and regulatory compliance, as well as in traditional business functions like marketing, customer service, accounting, financial reporting and so on.

Carrier Management reached out to four CROs to discern their role in establishing sound rules and governance practices to constrain potential abuses without eliminating Gen AI's obvious value. Their efforts suggest the high-priority status of the new technology. As CRO Adrian La Forgia at QBE North America put it, "Of all the opportunities out there, this is the time for the risk function to really shine. You either stand on the sidelines and observe, or you help shape the direction."

Test and Learn

La Forgia began his insurance career at AIG, eventually becoming chief operating officer in the commercial underwriting office. In 2016, he migrated to QBE NA to lead Enterprise Risk Management, before becoming deputy CRO and then CRO in June 2022. La Forgia is a member of the executive management board for QBE NA and part of the large insurer's global risk function, leading Risk and Compliance for North America.

"I became involved with Gen AI as it exploded across the world, initially thinking we'd need to quickly build a governance framework around its use with sensible and flexible risk guardrails," said La Forgia.

In February 2023, employees had begun dabbling with Gen AI tools like ChatGPT. "Boards were concerned about the implications and how we were seeking to protect ourselves," he said. "Early on, we issued a set of 'dos and don'ts,' mindful of our existing acceptable use policy, data management guidelines and the broader cybersecurity infrastructure. We wanted to ensure rigor and the application of our subject matter expertise."

Once the restrictions were in place, the spotlight turned to the opportunities presented by Gen AI. "We were at an inflection point, where the risk of embracing it and getting it wrong was starting to converge with the risk of being left behind. We either needed to get behind it and address the risks or insulate ourselves from the opportunity," said La Forgia. "We decided to get behind it through a very measured 'test and learn' methodology."

The CRO was part of a cross-functional and global team overseeing the development of the governance framework to identify and manage Gen AI use cases and potential pilot projects. Once in place, the first use case, focused on the insurance broker submission intake process, was undertaken. "Gen AI was used to test how various forms of unstructured data provided by brokers could be parsed into the different elements needed for underwriting, pricing and risk selection," he said.

Once a use case demonstrates confidence in the specific use of Gen AI, the next stage is to launch a pilot for further testing and refining. La Forgia commented that the submission intake use case is now in the pilot phase.

In this methodical test-and-learn process, the opportunities of Gen AI are carefully weighed against perceived risks. "What sounds good on paper may not provide the benefits and efficiencies touted," he explained. "We're mindful of the 'hallucination effect,' the risk of inaccurate conclusions drawn from nonexistent patterns and correlations."

He provided an example of a public case study in the legal arena. "In one case, Gen AI cited case law that didn't actually exist," La Forgia said. "We're thoughtful in not rushing toward a fully autonomous platform, as the technology is still emerging and volatile."

Other use cases are in the works, La Forgia said, adding that it is premature to discuss them in detail. "What's most important in choosing use cases is to pick the big opportunities that align with the strategy," he said. "With any use case, we review the implications of which data will be used, how it will be used, and the conclusions that may be drawn from this use. This is a long journey."

As CRO, La Forgia said he "needs to monitor Gen AI-driven regulations on a state-by-state and international basis, as some states are taking a regulatory

"We were at an inflection point, where the risk of embracing it and getting it wrong was starting to converge with the risk of being left behind."
Adrian La Forgia, QBE North America

"My role is as the executive sponsor, making sure everyone has the right goals in mind, we're all moving in the same direction, and we're thinking about our members in everything we're trying to do."
Johnny Gilbert, United Educators

"We did a lot in just three quarters. We all knew Gen AI was a game-changer and didn't want to be late to the party."
Stephanie Lynn, Church Mutual

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approach to Gen AI, whereas others are looking at legislation."

Having demonstrated the early value of Gen AI usage, La Forgia said that board members have "fewer questions about protecting [the company] from the downsides and are more engaged in how we can harness the upside."

Stay Calm and Carry On

The sea change represented by Gen AI has compelled QBE NA and other large insurers to be deliberate in their approach

"We're fortunate the early work on our predictive models was done inside the actuarial group, which is governed by a very strict code of conduct. A lot of ethical requirements come with being an actuary."

Teresa Cracas,
The Cincinnati Insurance Companies

to implementing the tools, the case at The Cincinnati Insurance Companies. "We're looking at both sides of the sword, making sure we're taking advantage of a new technology that will be transformational for every industry but also making sure we do it in a safe, ethical and governed way," said Teresa Cracas, CRO at the property and casualty insurer, which serves customers in 46 states and the District of Columbia.

Cracas manages enterprise strategy and risk, which includes oversight of the carrier's analytical and actuarial teams. She is a member of a three-person steering committee responsible for the governance of Gen AI and AI-based predictive models (the other members are the company's chief information officer and chief legal officer).

In 2018, the committee put together a governance framework to manage the use of early predictive models for fraud detection and spatial imaging, giving it a leg up on managing Gen AI. "Like Gen AI, the predictive models use open source algorithms, but Gen AI is a big nut to crack," Cracas said. The committee decided to enhance the governance framework specifically for Gen AI and tasked the head of compliance (Kelly Chasteen) with developing it. "It's in her wheelhouse and she's passionate about the topic."

The more robust framework will include an ethical statement crafted by the actuarial group defining appropriate and inappropriate Gen AI use. "We're fortunate the early work on our predictive models was done inside the actuarial group, which is governed by a very strict code of conduct. A lot of ethical requirements come with being an actuary," Cracas explained. "We want to be very clear in what Gen AI will and won't do, how to vet the tools, and how to manage them."

Several professionals in the insurer's IT organization are already using Gen AI in their work, and both traditional and newer vendors are embedding the tools in the solutions provided the company. "One of the things we struggle with is how to vet every Gen AI vendor to see what's under the hood," she said.

Other concerns include the safety of open source models, properly vetting them to ensure they don't infect the carrier's network and systems; emerging regulations; and hiring people skilled in using Gen AI models. "They're in very high demand, since every company on the planet has made Gen AI a focus," Cracas said.

Like QBE NA, Cincinnati Insurance has commenced a Gen AI pilot project, which is aimed at pushing information more quickly to underwriters. "We're in the early days of it, and are still working on security," said Cracas. "We recently hired a Gen AI expert from Google, who is inspirational when he talks about all the things Gen AI can do. Now our problem is keeping everybody patient."

The Game-Changer

In April 2023, then-CEO Rich Poirier at Church Mutual Insurance Company asked CRO Stephanie Lynn to marshal a Gen AI strategy and a formal Gen AI governance committee to govern its use across the business. "I assembled a group of eight people from legal, data analytics, IT, InfoSec and other functions, and asked them to find as much information as possible on what other businesses are doing as far as governance," said Lynn. Church Mutual provides specialized insurance to religious organizations, schools, colleges, nonprofits and other service organizations.

Armed with this information, the committee evaluated other companies' governance processes, insofar as "what made sense and what didn't," Lynn said. "We examined the use cases for Gen AI at these organizations to see which ones actually succeeded in managing the risks against the potential."

Instead of scrambling, Lynn and the committee took a few months in developing the insurer's Gen AI strategy before presenting it to the board of directors. "I had previously met one-on-one with one board member, who had extensive technology experience, to show him what we were thinking," she said. "He helped us expand some areas. Ultimately, the board approved and away we go."

The committee's next actions included crafting a charter detailing the scope and objectives of Gen AI implementation, drafting a policy requiring employees to solicit permission for using Gen AI to the governance committee, and creating an intake form template for this purpose. The form is subsequently submitted to the committee for review. "We evaluate the proposals from a data perspective—why and how the tool will be used, who owns the outputs, will we be masking proprietary information—and then have the legal team takes a look" before it is approved or denied, Lynn said.

Like many insurance carriers, Church Mutual a decade ago was wary about the influx of new insurance technology solutions. No longer is this the case. "We're at the forefront in innovation in using emerging technologies across the business, but we realized very quickly that Gen AI had a much bigger footprint, as it can be used by every single person in the organization," she said. "At the same time, it's still the Wild West."

She pointed to her overflowing email box, which is inundated with emails from Gen AI vendors specializing in insurance operations. "There's a 'spaghetti map' of different tools competing against each other. To control the chaos, we've tasked a single group to evaluate [the vendors] to avoid the potential for duplicative tools being brought into the organization."

Three Gen AI pilot tests are underway at Church Mutual. "One is for marketing to enhance our social media presence; another is for customer service, instantly and correctly summarizing communications between our CSR's and customers; and the third is more of an operational efficiency tool, like ChatGPT but not quite," the CRO said. "They're just getting started." Altogether, some 40 people across the organization are engaged in the three pilots and several use cases, including HR, claims, compliance, legal and information security.

Looking back, Lynn said, "I was a little intimidated at first to take this on. At the outset, I knew next to nothing about Gen AI. But I just poured myself into it and got the right team around me to help. We did a lot in just three quarters. We all knew Gen AI was a game-changer and didn't want to be late to the party."

Executive Sponsor

At United Educators (UE), a risk retention group and licensed liability insurer owned by 1,600 member schools and colleges, CRO Johnny Gilbert was a natural to lead the Gen AI governance effort—he's also UE's chief actuary, in charge of data analytics and modeling.

"I'd worked on earlier versions of Gen AI like machine learning that were more passive and less generative, but when the news came out that everyone was using this new tool called ChatGPT, I realized we needed to quickly get out in front of it," he said.

Like other CROs, Gilbert was alarmed by the possibility that employees might use Gen AI to develop content from their emails and other proprietary data. "I was concerned about the lack of control, so we immediately developed a policy requiring everyone before using Gen AI to receive explicit permission from the CFO and corporate counsel," he said. "We then paused to think about more long-term sustainable governance."

Gilbert has assembled a committee that includes business leaders and UE's IT, actuarial and analytics teams to consider how Gen AI may change work across the enterprise from a competitive standpoint. "My role is as the executive sponsor, making sure everyone has the right goals in mind, we're all moving in the same direction, and we're thinking about our members in everything we're trying to do," he said. "We're still in this exploration phase."

One possible benefit of Gen AI to member schools and colleges is in risk management, given the potential to take a huge volume of claims data and quickly recycle it into knowledge helping members improve their risk profile. As Gilbert put it, "Using Gen AI, an enormous amount of claims data and text can be summarized into useful themes. It's not a magic bullet, but it does give researchers a lot more breadcrumbs to think about." CM

Russ Banham is a Pulitzer-nominated business journalist and best-selling author.

Executive Summary: "How do we make the insurance industry better than we found it?"

That's the mission of Eos Venture Partners, according to Jonathan Kalman, a founding partner of the venture capital firm, who told Guest Editor Mike Fitzgerald about some of the portfolio companies that reflect the mission, and about a strategy of turning loss-making companies into profit-making ones by providing capital, relationships and know-how.

Kalman also shared views on the impacts of AI and advanced analytics on P/C insurance and how carriers can prepare their workforces for an AI future.

See related articles, "Critical Thinkers Needed for AI-Powered Insurers" and "All Aboard: What's Next for Executives and Boards of AI-Powered Insurers?"

VC Insights: Putting the Focus on Insurers, Not Silicon Valley

By Susanne Sclafane
Guest Editor Michael (Fitz) Fitzgerald
Insurance Industry Advisor for SAS Institute Inc.

When Eos Venture Partners invested in a cyber recovery firm, it was losing money.

But Fenix24 has since had a "meteoric rise," according to Jonathan Kalman, a founding partner of the venture capital firm that is exclusively focused on the insurance industry. Kalman, who would go on to explain that the essence of venture capital is investing in loss-making businesses, said his firm's relationships with insurance carriers helped put Fenix24 on the radar.

Specifically, it was relationships with cyber insurers, "who said that their payouts were moving from being just ransom to business interruption." Eos sought out ways to reduce the financial impact that business interruption claims were having on the insurers. Then VC discovered Fenix24, a business that is built around what happens after a business experiences a cyber attack.

Months after the venture capital firm put $5 million into Fenix24 last year, "Fenix24 restored MGM in nine days," Kalman reported, referring to work to restore the systems of the Las Vegas-based resort after a breach in September. "Fifty thousand people were locked out of their hotel rooms. They were losing over $10 million a day, and they estimated it was going to take them eight weeks to be restored to functioning," he said. "That's independent of someone's going to pay a ransom. That is, 'My business is interrupted, costing me way over $10 million a day.' So, when you look at the finish line, in fact they estimated it was going to be over $500 million," he said.

Fenix24 is relevant to carriers for another reason, Kalman continued. When carriers think about cyber, they typically think, "'How am I going to underwrite this line? What are the product features?' But they [also] have to look at themselves as potentially being the target of a threat event," he said, noting that a sister company of Fenix24, known as Grypho5, checks a company's defenses in advance. Grypho5 uses information from current threat behaviors to help look for areas of vulnerability and eliminate them, he said.

Cyber attacks, Kalman said, are the risks that keep his friends, who are chairs and CEOs of insurance carriers, up at night. "The bad guys have realized that they get inside and they can then read the policies. That gives them a road map to attack the customers of insurance companies," he said, referring to the breach of Reinsurance Group of America reported in October last year, and recently reported breaches of title insurers.

In Kalman's mind, this makes companies like Fenix24 and Grypho5 "very relevant to the insurance industry. In fact, he described the investments as "the most important" ones he's made in a 23-year investing career.

Funding Losses

"We are investors who are looking to enable the industry to be more effective—to be better at serving policyholders, to be more cost-effective in servicing the business," Kalman told *Carrier Management*. "And this is a key motivation of our firm: How do we leave this industry better than we found it? That has served us very well. It attracts fantastic entrepreneurs to work with us because they see that we're about co-creating successful businesses that will impact this industry," he said, citing portfolio companies like Fenix24, Champ Titles and Family First (discussed below).

International in scope, with offices in the UK, in New York and in Los Angeles, Eos Venture Partners invests into technology and data-enabled insurance businesses. The firm's four partners are investors in roughly 20 companies. "Our capital comes from insurance companies," Kalman said, noting that some of the portfolio companies provide services to the insurance companies that are providing the capital, and others are acquired by the insurers. "It's really creating a virtuous cycle," he said.

Kalman doesn't have a background as insurance professional himself. "I'm a physicist by training and have worked in deep tech. Subjects like AI are very familiar—and databases and cloud computing," he told *CM* Guest Editor Michael (Fitz) Fitzgerald, an Insurance Industry Advisor for SAS Institute. In the late 1990s, Kalman helped build a company that created datasets used by the credit card industry to make underwriting decisions before he moved into the world of investing. He went on to found Katalyst Venture Partners, which focused on investing in the fintech industry and payments industry, and ultimately embraced the insurance industry.

Eos Venture Partners, in a sense, brought something unfamiliar to the insurance industry when it launched in 2016. "Venture capital is a very interesting business because it hasn't really been part of the insurance world for the last 50-100 years," Kalman said. The reason, he said, it that "the essence of venture capital is funding losses."

"Insurance is not that industry, right?" he said. "Financial services understood 20 years ago that I'm going to fund a business that's losing money because it's going to

Jonathan Kalman

"Venture capital is a very interesting business because it hasn't really been part of the insurance world for the last 50-100 years."

make money someday. And It's going to create a competitive advantage. That math and calculus is not in the insurance industry."

Explaining why Eos has been able to attract insurer capital, he said that prudent investing and specialization sets the firm apart. "We're known as specialists who know the industry and who look at the ability of a company to go from loss-making to profit-making. We're not going to sit there and assume that you're going to keep raising money again and again and again, which is what happens in Silicon Valley. That's not how we invest."

Kalman said there's "a bit of alchemy and art" involved in being able to understand whether or not a business can make that transition to become profitable, and whether the company's product or service will scale to have significant growth. As an example, he highlighted another portfolio company, Champ Titles. "When we invested in 2021, they were pre-revenue, and now they ended last year having signed $300 million of contracts."

Like Fenix24, Kalman believes Champ Titles has "extraordinary implications" for the insurance industry—and three others. "Champ Titles has developed a fully authenticated digital automobile title," he said, noting that beyond insurance, it impacts the automotive industry, government municipalities, and financial services and lien holders.

He explained that a large

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percentage of automobiles are purchased via a loan from a financial institution. The financial institution and the car owner are both listed on the title. When the vehicle is involved in a crash and totaled, "there is a very paper-intensive, arduous, inefficient, rusty, old, dinosauric process for getting the approvals, the titles, getting the money in the policyholder's hand, and getting the insurer to salvage the asset and getting reimbursed for that."

Insurers say "there are billions of dollars of friction in that process," he said.

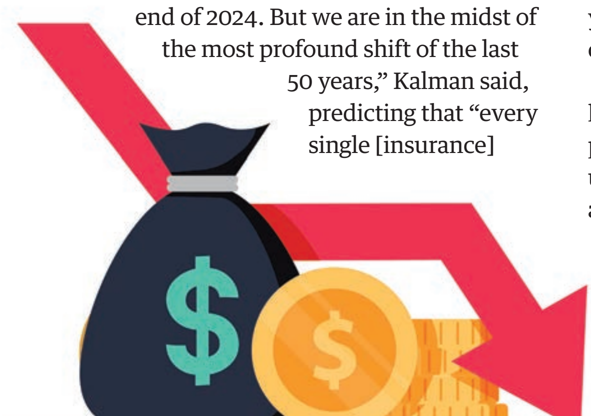
Eos Ventures co-invested in Champ Titles alongside WR Berkley and The Institutes. "It's been a fantastic example of a partnership. That's how we work with the industry...We are not a Silicon Valley investment shop that's looking to disrupt the insurance industry," he said.

What About AI?

Kalman partnered with Fitzgerald last year to co-host a video series called "Insurance Analytics @ Scale" posted on the SAS website—a series in which the two men posed questions like the ones presented on these pages. They asked executives and directors about best practices and lessons learned that can help peers as the industry moves forward to embrace advanced analytics and AI.

Fitzgerald gave Kalman an opportunity to weigh in with his own thoughts on the industry impact of AI, as well as the AI investment opportunities he sees for Eos.

"When you look across the entire business, it will be impacted. It won't be impacted this week or next week or at the end of 2024. But we are in the midst of the most profound shift of the last 50 years," Kalman said, predicting that "every single [insurance] function will be touched by AI, generative AI and advanced analytics."



Eos continues to focus on insurance-related technology as AI opportunities emerge. "We are looking for those investments whose predominant value is within the industry," Kalman said. "Many of the companies that are being invested in are applicable across industries," he said, referring to companies developing AI and advanced analytics tools.

"Some of those companies are better served by investors in the Valley. But when they see businesses that require insurance domain expertise, they come to us because that's what we bring to the table. Then you create an investing consortium," he said, noting that Silicon Valley investor Andreessen Horowitz and Eos are coinvested in a business. (Editor's Note: Andreessen Horowitz is the lead investor in CYGNVS, a Silicon Valley-based guided cyber crisis response platform. Eos and Stone Point participated in a $55 million Series A round last year, funding CYGNVS services, which can be purchased directly by commercial business or accessed as a benefit of cyber insurance policies.)

"They bring the cross-industry expertise, and we bring the [knowledge of] how this will be effectuated to impact what we think about as a $7 trillion industry on the P/C side," Kalman said.

Focusing on takeaways for tech company founders, Fitzgerald asked how the current surge in interest in AI changes the thinking of investors like the Eos partners. As a founder, "how does AI technology change the value proposition I need to present to you, or eventually to the end insurance customer?" Fitzgerald asked.

Kalman responded with a description of how Eos recently took a profit-making portfolio company called Family First and urged the company to invest in building analytics that hadn't been part of the strategy before. "Just like an insurance company is going to be touched by AI across the business, [a tech startup's] business is going to be touched by AI in many cases. What we help the founders do is understand how to build a road map to leverage the technology in a way that's going to create an extraordinary impact."

> **"The essence of venture capital is funding losses."**

Eos added Family First to the portfolio in 2023. Kalman explained that Family First addresses the problems of caregivers who are juggling tasks of caring for spouses, special needs children or parents while also continuing to work. Family First is "an employee benefit purchased by the chief HR officer for their employees to help them be present"—to get the resources they need in the most efficient way, so that they can really be effective, said Kalman.

"It's becoming a mandatory benefit," he said, going on to explain why it meets Eos' criteria for investable opportunities. "This is a trillion-dollar problem," he said citing information in a white paper published by the Society of Actuaries last year.

"Family First serves thousands and thousands of lives, and has collected data on that," he continued. "It was a business that was profitable. But we said we're going to actually invest money, [and] you're going to go unprofitable because we're going spend on R&D...We're going to actually invest to build the analytic engine to sit on top of this information and to use that to accelerate the ability for an employee to get access to information they need to impact their loved ones," he said.

"That's something that lights up Eos because we know that we are impacting millions of lives through our capital, relationships and know-how. In this case, we helped the organization bring together the analytics team and skills and technology to be able to leap to an entirely different level," he said.

"We're specialized investors in the insurance industry...We'll look at over 1,000 companies this year. We'll invest in four...At the end of the day, we bring our capital, which is from the industry, our relationships within the industry, and our know-how in building technology that can solve problems in the industry." CM

Insurers in All Coverage Layers, Insurers Must Collaborate to Get Ahead of Social Inflation

Tony Rai was appointed Group Chief Claims Officer of Aspen in January 2022 and is based in London. Rai joined Aspen in January 2021 as head of International Claims. Previously, he had been Hiscox's head of London Market Claims since 2009, where he was responsible for the management and leadership of claims for London market business, both direct and reinsurance. Prior to that, Rai worked as an insurance and reinsurance lawyer at Clyde & Co.

Executive Summary: Setting up mock jury trials, taking cases to trial and refraining from issuing "hammer" letters to lower-layer insurers are just three of the strategies Aspen's Chief Claims Officer Tony Rai suggests that insurers start undertaking—in concert with their insureds—to rein in social inflation.

Although nuclear verdicts can't be eliminated, they can be better managed, he writes, also advocating for appropriate claims handler caseloads that recognize the growing complexity of claims.

By Tony Rai

Insurers need to take a comprehensive and collaborative approach to stem the rising tide of social inflation. This approach should be one that involves not only assessing corporate risk and developing and implementing strategies with their insureds and co-insurers but also, collectively, working with lawmakers to help eliminate its root causes.

However, insurers need to acknowledge that the risk of a nuclear verdict is one that needs to be better managed by the industry but can never be eliminated.

Aside from the financial and reputational damages for insurers and insureds, social inflation can lead to inadequate or

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unaffordable insurance for consumers, resulting in more expensive or unavailable services. More broadly speaking, its consequences can lead to a ripple effect that is beyond insurance—impacting societal, economic, legal and behavioral norms.

Nuclear Verdicts and Settlements

Social inflation is leading to so-called "nuclear verdicts" where plaintiffs are receiving awards in the tens of millions and, in some cases, hundreds of millions of dollars. In these cases, the non-economic damages of the case far outweigh its economic damages.

This has spawned "nuclear settlements," which are driven by the fear that a nuclear verdict will be in excess of the defendant's available insurance policy limit. With insureds increasing pressure on insurers to settle within the available limits, this has resulted in settlement values being driven up as insurers are rightly concerned with the potential risk of bad faith.

The insurance market's understandable response to increasing verdicts and settlements has been to increase rates, reduce capacity, increase attachment points, and tighten terms and conditions. However, that only increases the pressure on carriers to settle within the tower of coverage as the insured's primary focus is to avoid an excess exposure.

Drivers of Social Inflation

There are multiple factors driving social inflation and increasing claims costs in the U.S. For example, an increase in third-party funding enables cases to be run for longer and more aggressively. Additionally, there is what appears to be a jury's desire to "punish" insureds for perceived bad practices, especially where it relates to safety issues that have led to entirely avoidable serious injury or death. We have seen extremely large jury awards and settlements in auto accident claims, particularly where an insured was aware of poor practices within its facilities (such as depots) but took no steps to stop such practices.

The composition of jury panels is tending to be younger citizens who can hold anti-corporate stances and unrealistic views of appropriate product and workplace safety standards, causing larger consumer/ plaintiff verdicts. Therefore, it is critical that insureds understand the potential consequences of bad practices that could lead to injury or death, and insurers need to look to limit or restrict coverage in circumstances where an insured tacitly accepts such practices. In that event, if a jury believes that an insured should be punished for their behavior, the financial impact is materially impacting the entity that was at fault.

Social inflation not only adversely affects insurers and their liability accounts, but it also affects insureds more broadly. Social inflation is one of the leading factors in the deterioration of reserves on back years, as awards by juries in the U.S. continue to increase. Indeed, this is one of the main reasons insurers have looked to mitigate their risk by reinsuring their back years through loss portfolio transfers. So, what can insureds and their insurers do to stem the tide of increasing jury awards?

Here are six tactics insureds and insurers can employ to help mitigate the impact of social inflation and, as a consequence, nuclear verdicts and settlements:

- Insureds and insurers should participate in mock jury trials to better understand how juries will react to a specific and factual scenario, and which types of arguments will likely resonate well in front of a jury. While claims handling costs will continue to increase, driving up the average value of claims, mock jury trials can help reduce the impact.
- "Anchoring" should be used to highlight the appropriate value of compensatory damages. Many individuals sitting on juries are desensitized to large sums, especially when they regularly see press coverage about large sums paid to sports and entertainment stars. The real focus should be on what that individual needs to support themself and to compensate them fairly for the loss that has been suffered, rather than making them extremely wealthy.

"'Nuclear settlements' are driven by the fear that a nuclear verdict will be in excess of the defendant's available insurance policy limit."

- It is important to help the jury understand the amount that plaintiff's counsel will take from any award. This is almost always a material percentage of the ultimate jury award.
- It is critical to employ experienced and technically competent counsel. It is equally important to ensure that the claims handler caseloads are appropriate for the level of complexity of the claims under management. Given increasing awards and settlements, more claims are under active monitoring than previously, and appropriate caseloads will make sure cases are managed effectively.
- Be willing to take cases to trial and take a verdict rather than fearing a jury trial as it will be key to getting good case law on the books for the future, accepting that some cases will need to go to appeal. Yes, some cases ultimately may be lost, but it may be a price the insurance industry will need to pay to mitigate the impact of social inflation.
- Insurers should take lessons learned from verdicts and settlements driven by social inflation to partner with their insureds to assist with creating better practices to mitigate against the risks. This would be a value-add activity to look to reduce the litigation life cycle—looking to protect the insured, not just defend the insured. Insureds need to act when they are aware of possible poor practices, rather than ignoring the situation.

Insurance Industry Best Practices

Insurers and insureds in the coverage

layers need to work together more closely to prevent fear from driving up nuclear verdicts and settlements. Here are five best practices the industry needs to consider, which involve a great deal of collaboration:

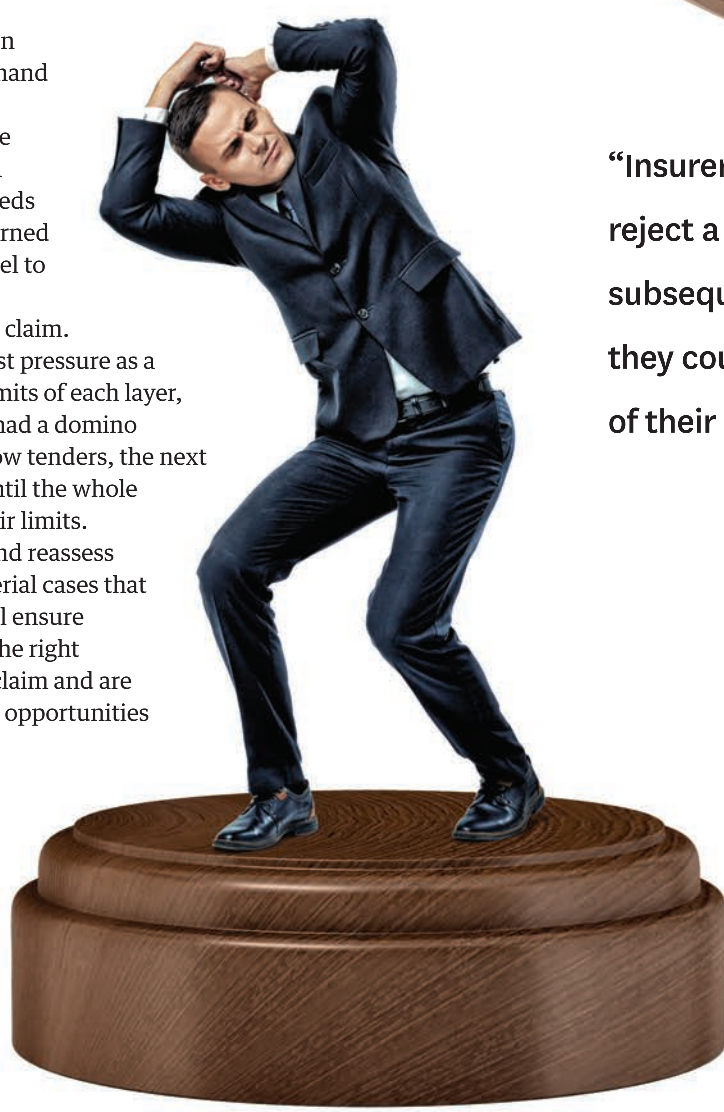
1. Collaborate on excess placements, rather than taking an adversarial approach. This includes resisting issuing "hammer" letters to the layers below, where a settlement can be achieved in that layer but where the settlement value is not reflective of the injury or damage suffered. Those insurers that are prepared to reject a settlement in their layer subsequently carry the risk that they could be liable for in excess of their policy limit. This is a consequence that few insurers are prepared to take, and one critical factor that pushes up settlement value and drives social inflation.

2. Avoid panicking when plaintiffs' counsels demand tower limits before settlement demands are made. To mitigate such demands, the tower needs to work jointly with learned and experienced counsel to fully understand the settlement value of the claim. Together, they can resist pressure as a market to tender the limits of each layer, which historically has had a domino effect—as the layer below tenders, the next layer folds and so on until the whole tower has tendered their limits.

3. Constantly review and reassess the value of those material cases that have volatility. This will ensure carriers stay on top of the right settlement value for a claim and are ready when settlement opportunities arise.

4. Drive an early settlement, particularly where liability is unlikely to be in question. The old adage is true: The best claim is a closed claim.

5. Ensure tort reform is on the agenda. The insurance industry should use lobbying firms to drive these issues onto the agenda of legislators in the various states.



"Insurers that are prepared to reject a settlement in their layer, subsequently carry the risk that they could be liable for in excess of their policy limit."

Do Your ERM Practices Need Updating?

Executive Summary: "Nothing stays static over a number of years. Companies change internally, and so does the external operating environment," writes Carol Williams, a risk management and strategy consultant for P/C insurers, reminding carriers not to wait to be backed into a corner before they update their ERM programs.

Carol A. Williams is the CEO of Strategic Decision Solutions, a consultancy that has helped numerous P/C insurers address unique challenges to their success. Williams started her career in insurance and risk management with the Florida Office of Insurance Regulation nearly 20 years ago, more recently holding various ERM leadership positions for Citizens Property Insurance Corporation. At Strategic Decision Solutions, she focuses on helping carriers move beyond putting out fires to achieving strategic goals. Reach her at Carol@strategicdecisionsolutions.com.

By Carol A. Williams

Immediacy or necessity has a way of sneaking up on us and getting our attention.

This principle is true across the board. Nobody rushes to the front of the line to get a colonoscopy or root canal, but when circumstances force us, we'll take action, albeit grudgingly.

Some examples of how this may look for an insurance carrier include:

- Ratings agencies like AM Best, Demotech, or Kroll say your current program is insufficient for the size or complexity of the company. Without drastic action, the company could see its rating downgraded.
- State insurance agencies and other regulators are asking more questions about risks, modeling, controls and mitigation verification, expressing concerns that the company will be unable to protect itself.
- The company is nearing the $500 million threshold for ORSA regulations and is nowhere near ready.
- Significant changes to corporate governance result in a misalignment between the board and the executive discussions and expectations regarding risk-taking behavior.
- Haphazard meetings create internal chaos and gridlock, leaving the company with missed performance goals; extended projects cost more money than budgeted and larger than expected financial losses overall.
- Premium growth creates more volume to maintain, leading to expensive changes in technology and employee costs.
- Expansion into new geographic markets makes the company subject to additional (new) regulations.
- Antiquated assessment and analysis methods generate reports that regurgitate what is commonly known already.

Enterprise risk management is a prime example of this principle in action in the insurance industry, or any business. ERM is a subject many executives would prefer to avoid. Admit it, you'd rather spend your time talking about operations, rates, products, claims and even systems. However, there are certain situations where you will have no choice—where, as a company, you are backed into a corner and focused into action: either adopt ERM or updates practices to reflect not only where the company is now but where it's going.

Although there are many reasons or triggers that can back a carrier into a corner, prompting action, there is one overarching principle that drives these situations to come about. Nothing stays static over a number of years. Companies change internally, and so does the external operating environment.

Therefore, the question has to be asked: What makes an ERM practice or program any different? A carrier may be prompt in adapting its underwriting or claims processes based on current events and trends, but when it comes to ERM, many leaders expect practices, implemented five, 10, even 15 years ago, to still meet the company's needs today.

Think of it like a new suit for a fast-growing teenager. When a parent buys the suit, it fits perfectly (or even a little big) at first. But the teenager doesn't stop growing. As his height and body changes as part of the normal growth process, the suit will eventually not fit anymore.

Much the same can be said for an insurance carrier and its ERM program.

The company itself keeps growing and changing, while the ERM program remains static. What results is an outdated ERM program that is unwieldy and provides little to no value to the company.

Surveys like the State of Risk Oversight Report from North Carolina State's ERM Initiative show this to be a challenge not just for insurers but all types of companies. According to the latest report released in June 2023, only around 35 percent of respondents believe their risk oversight to be robust, while only an astonishing 12 percent felt their ERM practices provide unique competitive advantage.

It's clear that ERM needs to catch up to the needs of today's companies.

In his book, "Risk Management in Plain English: A Guide for Executives," author and former Chief Risk Officer and Chief Audit Executive Norman Marks states the ultimate goal of ERM is anticipating what might happen, assessing whether that would be OK, and acting as needed—all so you can increase the likelihood and extent of success.

This is the ideal, but unfortunately very few companies get to this point. They get stuck in the past.

Like our teenager who has outgrown his clothes, these situations and similar ones outlined earlier necessitate changes to the company's ERM and risk practices. Continuing to ignore this reality could negatively impact the company's strategic goals, day-to-day operations or even its very survival.

The next question that naturally arises is: How do the risk practices need to change? Are only some minor, strategic tweaks needed? Or are practices so out-of-date that a complete overhaul is required?

When considering this and making changes, carriers should establish practices and routines that the company can grow into, like kid's clothing. It would be unwise to buy clothes that are a perfect fit now but will soon be too small. Instead, clothes and shoes should be purchased with the future in mind, so the child can grow into them.

A similar approach should be taken with ERM. Any new or updated ERM practices should be able to adapt and mature as the company continues to grow and change.

Before determining where ERM needs to go, you have to first determine where it currently is. This is the first step in an ERM Maturity Assessment. The purpose of this type of assessment is not about checking all the boxes on some checklist but about the effectiveness of ERM practices relative to your company's needs.

Carol A. Williams is a regular contributor to *Carrier Management*. Her prior articles include:

- Why Strategic Implementations Fail and the Counterintuitive Way to Address It
- Transforming Enterprise Risk Management From 'Have To' to 'Want To'
- What Does an Ideal Strategic Planning Process Look Like?
- Taking a Growth Pause: Preparing for Long-Term Success
- Stop the Deluge: Why P/C Leaders Should Rethink Project Management

Many tend to compare (or benchmark) their ERM practices to what their competitors or peers are doing, but this is dangerous. What matters is how effective your ERM practices are for your company's needs.

- Is ERM providing you and other executives and decision-makers with information and insights you didn't already have?
- Is this information easy to use?
- What's working well?
- What could work better?

These are a sampling of questions that should always be top of mind since ERM practices are iterative, meaning the refining and improvement process should be ongoing. After all, the company's needs are always changing.

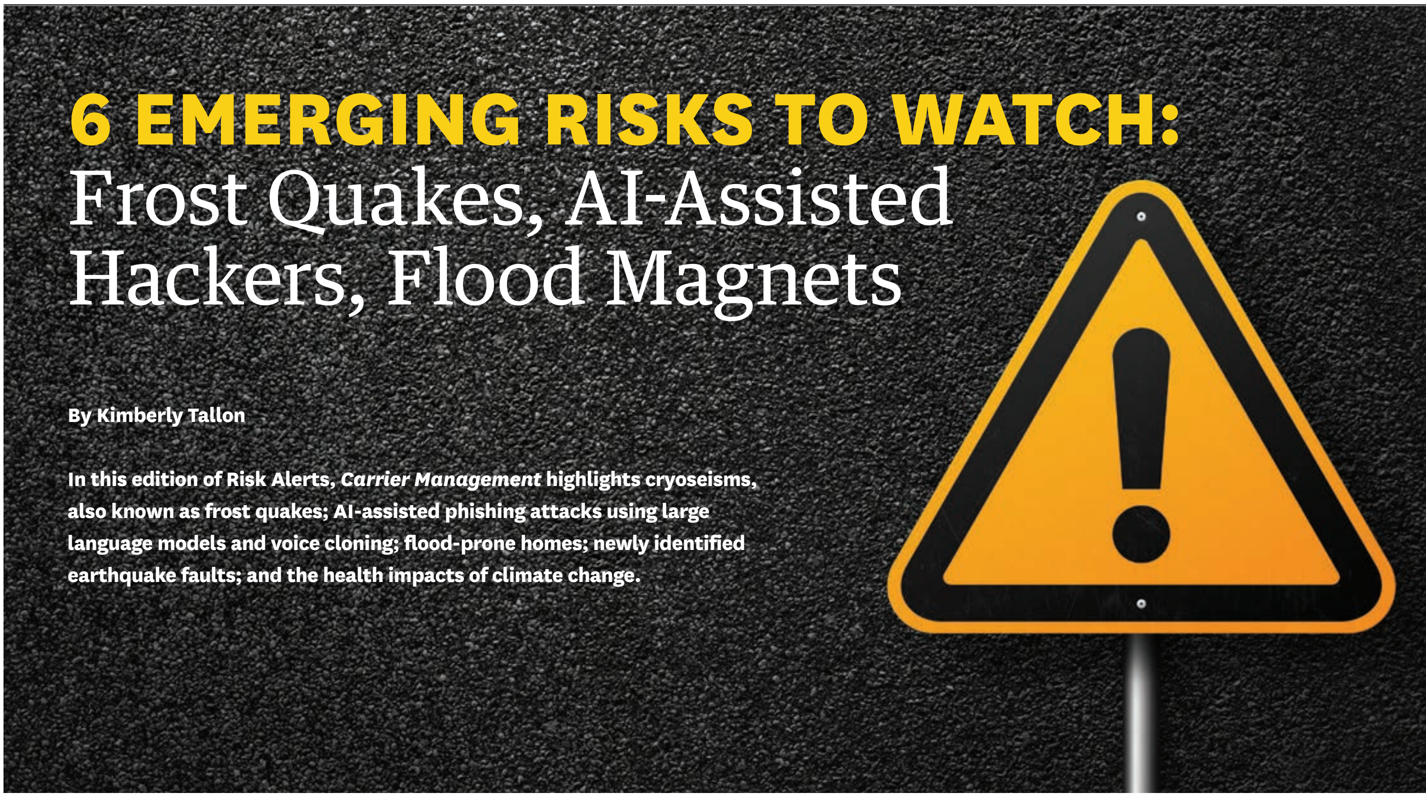
The important thing is to get started. Imperfect action is better than perfect inaction.

Second to that, realize that to get to the ideal that Marks describes in his book can take time. Immediate results may be the norm for project management or other areas, but ERM sometimes requires a bit of trial and error to find out what works best now and for the longer term.

Similar to how good companies become iconic brands as discussed in the Jim Collins book "Good to Great: Why Some Companies Make the Leap and Others Don't," there is no single point or action that will get your ERM program to where it plays a valuable role in helping the company achieve its goals. Like pushing a "Good to Great" goal flywheel, it will happen "...turn by turn, building momentum until a point of breakthrough and beyond."

Once it does though, you as an executive will be free to focus on the things you really want to focus on, with ERM helping you know how much risk is acceptable in certain areas and situations.

The question you have to answer is: Do you want to wait to act until you're backed into a corner, or do you want to get ahead and address this underlying issue before it blows up into yet another crisis? CM



6 EMERGING RISKS TO WATCH: Frost Quakes, AI-Assisted Hackers, Flood Magnets

By Kimberly Tallon

In this edition of Risk Alerts, *Carrier Management* highlights cryoseisms, also known as frost quakes; AI-assisted phishing attacks using large language models and voice cloning; flood-prone homes; newly identified earthquake faults; and the health impacts of climate change.

1. Frost quakes. A new study published in the journal EGUsphere has identified a potentially growing natural hazard in the North: frost quakes. Also known as cryoseisms, frost quakes occur due to rapid freezing of water in the ground, which can cause cracks accompanied by tremors and booms. Ground motions during frost quakes are comparable to those of other seismic events, such as more distant earthquakes, mining explosions and vibrations produced by freight trains.

While frost quakes are generally not dangerous, they can cause damage to infrastructure such as buildings, basements, pipelines and roads.

Roads and other areas cleared of snow in winter are particularly vulnerable to frost quakes, but they can also occur in swamps, wetlands and other places where water accumulates.

"With climate change, rapid changes in weather patterns have brought frost quakes to the attention of the wider audience, and they may become more common. Although their intensity is usually low, a series of relatively strong frost quakes in Oulu, 2016, which ruptured roads, was the starting point for our research," said Kari Moisio, a senior researcher at the University of Oulu.

Frost quakes have been reported in the Midwest and New England in the U.S., as well as Canada and parts of Scandinavia.

Source: "Frost Quakes: a new earthquake risk in the north?" University of Oulu, Dec. 11, 2023

2. Phishing bait. Generative AI can make it more difficult to detect cyber threats such as phishing emails, warn two cybersecurity experts from Southern Methodist University.

"In the past, signs such as misspelled words or the awkward use of language could often be used to detect the use of emails or web ads to trick users into providing sensitive information... But with the high quality of human language generation provided by these new AI-based language generators, detecting such emails and fake ads is much harder than it used to be," said Eric C. Larson, an associate professor in the SMU Lyle School of Engineering's Department of Computer Science.

Larson and Mitch Thornton, executive director of SMU's Darwin Deason Institute for Cybersecurity, are particularly concerned about hackers using large language models (LLMs), which made popular programs like OpenAI's ChatGPT possible. LLMs use algorithms and AI to mimic human intelligence, and it can be difficult to determine the difference between an automated AI-based LLM and something written by an actual human.

Hackers can also use AI-generated images created on programs like DALL-E or

Midjourney to make phishing emails look even more authentic.
Source: "AI Could Make Cyber Threats Harder to Detect," Southern Methodist University, Jan. 18, 2024

3. Voice cloning. Cyber criminals are also turning to AI tools to clone the voices of individuals they target on social media to place panicked calls to their family or friends in a bid for money or access to sensitive information, said Mike Scheumack, chief innovation officer at IdentityIQ, in an interview with Fox Business.

They just need to record a person's voice or find an audio clip on social media or elsewhere on the Internet. "All they need is as little as 3 seconds; 10 seconds is even better to get a very realistic clone of your voice," he said.

The audio sample is then run through an AI program that replicates the voice, allowing the scammer to make it say whatever they type in addition to adding laughter, fear and other emotions.

Scheumack noted the voice clone calls from scammers are typically fairly short and may try to cut off a potential conversation by saying something like, "I can't talk right now."
Source: "AI voice cloning scams on the rise, expert warns," Fox Business, Sept. 23, 2023

4. Flood magnets. Thousands of homes in the U.S. have flooded again and again—many with little or no efforts for flood mitigation, according to a new analysis by the Natural Resources Defense Council.

NRDC used data from the Federal Emergency Management Agency to identify the most flood-prone properties covered by the National Flood Insurance Program. The analysis revealed that 44,616 homes meet the criteria to be considered "severe repetitive loss properties"—the most flood-prone homes covered by the NFIP. SRLPs have an average of 5.1 NFIP claims, but NRDC noted that the actual number of claims may be even higher.

These homes account for 0.8 percent of all NFIP policies but are responsible for 12.8 percent of the claim payments.

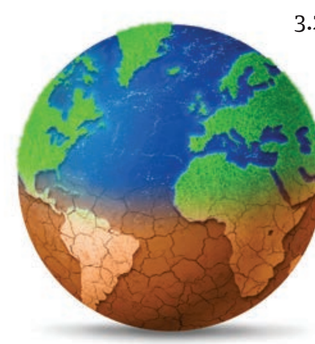
Fewer than 25 percent of the repeatedly flooded properties have received assistance to mitigate flood risks, NRDC said, and many homeowners have just dropped their flood insurance altogether.

About 1 in 5 SRLPs are located outside FEMA-designated flood zones.
Source: "Losing Ground: Flood Data Visualization Tool," NRDC, Jan. 9, 2024

5. Shake it up. Nearly 75 percent of the U.S. could experience potentially damaging earthquakes and intense ground shaking, putting hundreds of millions of people at risk, according to a recent U.S. Geological Survey report.

A team of more than 50 scientists and engineers in the latest USGS National Seismic Hazard Model created a color-coded map that pinpoints where damaging earthquakes are most likely to occur based on insights from seismic studies, historical geologic data and the latest data-collection technologies.

The NHSM update identifies nearly 500 additional faults that could produce a damaging quake. The latest iteration is the first 50-state comprehensive assessment.



Changes in the new model show the possibility of more damaging earthquakes along the central and northeastern Atlantic Coastal corridor, including in the cities of Washington, D.C., Philadelphia, New York and Boston. There is also a chance for greater shaking in California and Alaska. The new model characterizes Hawaii as having greater potential for shaking because of observations from recent volcanic eruptions and seismic unrest on the islands.

The full findings were published in the journal Earthquake Spectra.
Source: "USGS: Nearly 75% of U.S. Could Experience a Damaging Earthquake," Claims Journal, Jan. 19, 2024

6. Climate crisis. A new World Economic Forum report warns that by 2050 climate change may cause an additional 14.5 million deaths and $12.5 trillion in economic losses worldwide.

The report, "Quantifying the Impact of Climate Change on Human Health," developed in collaboration with Oliver Wyman, quantifies the health consequences of climate change, both in terms of the health outcomes (mortality and healthy lives lost) and the economic costs to the healthcare system, estimated to be a further $1.1 trillion in extra costs by 2050. The analysis is based on scenarios developed by the Intergovernmental Panel on Climate Change (IPCC) on the most likely trajectory for the planet's rising average temperature, 2.5° to 2.9° Celsius over pre-industrial levels.

WEF analyzed six major climate-driven event categories: floods, droughts, heat waves, tropical storms, wildfires and rising sea levels. Floods were found to pose the highest acute risk of climate-induced mortality, accounting for 8.5 million deaths by 2050. Droughts are the second-highest cause of mortality, with an anticipated 3.2 million deaths. Heat waves take the highest economic toll at an estimated $7.1 trillion by 2050 due to the loss in productivity. Excess deaths attributed to air pollution, caused by fine particulate and ozone pollution, are expected to be the largest contributor to premature death with almost 9 million deaths a year.

The report also found that by 2050 an additional 500 million people may be at risk of exposure to vector-borne diseases due to climate change.
Source: "Climate Crisis May Cause 14.5 Million Deaths by 2050," World Economic Forum, Jan. 16, 2024

Trade Secret Insurance Could One Day Protect 'Trillions' in Assets

Executive Summary: Everything that can make a company "different and better than your competition" can now be covered by insurance, according to Mary Guzman, the founder of Crown Jewel Insurance. She was referring to trade secrets, including algorithms, designs, business processes, recipes or formulas—assets that could be worth trillions. While underwriters previously pushed back on covering the assets, Crown Jewel's own secret sauce to make underwriters comfortable includes an independent valuation by outside experts.

By Allen Laman

Mary Guzman already has helped develop a new insurance coverage once in her career.

Now, she's leading the charge of another.

In the early 2000s, when she worked as a regional practice leader at Marsh & McLennan Companies, Guzman flew across the country, teaching companies about cyber risk and why it wasn't covered by existing insurance. It was challenging. Not as challenging, though, as her current effort: launching Crown Jewel Insurance, a company that bills itself as the world's first trade secret insurer.

"Very few people understood cyber risk at the time," Guzman said. "Very few people understand trade secrets. And so, to say that we're coming in, covering something that most people didn't even realize was an inherent risk, is a hard thing to do."

But she sees the potential.

Guzman worked as a broker for more than 25 years. The common threads of her path during that stretch were the professional liability and errors and omissions spheres, and near the end, she focused almost exclusively on cyber and intellectual property risks. Intangible risks that don't fit well into existing forms of insurance piqued her interest.

She could explain to clients that cyber policies covered losses stemming from leaked personally identifiable information and protected health information and that markets had become comfortable with business interruption losses resulting from attacks that sent systems offline.

But what about innovation assets that drive competitive advantages? What if an employee discloses that information? What if hackers steal it?

Guzman didn't have an answer. For years, she and senior leaders in the cyber insurance sphere tried to get markets to pick up the exposure in cyber policies. The markets didn't budge.

Guzman listened to the underwriters' pushback. She heard that the valuation was misunderstood, and she began planning. Crown Jewel Insurance was officially formed in early 2021. After careful planning, the company (a Lloyd's coverholder) is now writing and binding insurance.

"I just see it as a massive opportunity," Guzman said, noting that "trillions and trillions" of dollars of assets could qualify as trade secrets, and none of them are currently insured to their actual values.

Examples of trade secrets that Crown Jewel insures include algorithms, designs, business processes, recipes and formulas. Everything that can make a company "different and better than your competition," she explained. "And none of that is being insured right now. So, the opportunity is staggering once we can get this thing to take off, and once we get sort of a grassroots movement on the carrier side to understand and want to write this."

> **"The opportunity is staggering once we can get a grassroots movement on the carrier side to want to write this."**

Crown Jewel's primary product, Crown Jewel Protector, covers first-party loss of the value of a trade secret as an asset and provides the crisis management expenses a company would incur to try to figure out what happened and stop the bleeding. In follow-up correspondence, Guzman explained that Crown Jewel Insurance pays out a pre-agreed amount if it is not successful "in stopping the bleeding/putting the genie back in the bottle with an injunction or other method that would prevent them from using the asset."

Crown Jewel defines trade secrets broadly, but they must meet certain criteria to qualify for coverage. They must be independently developed, not known in the industry, inherently valuable to organizations and have reasonable protections in place. Trade secrets must pass a six-factor test established by the American Law Institute.

The Google search algorithm, for example, is a trade secret, and so is just about everything in a company's R&D pipeline. Once brokers contact Crown Jewel, Guzman and her team help identify these secrets and verify they qualify for coverage. Crown Jewel then examines the potential insured's information security policies, procedures and legal protections.

A panel of law firms, security firms and experienced valuation firms helps with this process. Underwriting culminates in the independent valuation of secrets. In addition to providing the fair market value of misappropriated trade secrets, Crown Jewel helps clients ascertain the source and scope of the loss and stop the bleeding using trade secret attorneys and forensics teams.

Establishing credibility was key to Crown Jewel's creation. Guzman believes the independent valuation of trade secrets by outside firms, combined with the storage of their metadata on blockchain technology, demonstrates this focus. "That's [how] we were able to convince the market that this could be done profitably," Guzman said. "A lot of companies aren't doing some of these steps yet themselves. I hope that three to five years from now, this will be the method that people follow—or something close to it."

Cyber policies might cover some of the crisis management expenses if the theft is through a breach as opposed to just former employees or vendors behaving badly, but cyber policies do not cover the value of IP or the cost of R&D the insured expended to develop its innovation and know-how. "That's what is so different about this," she said. "We cover trade secrets like they are buildings, essentially."

In addition to Crown Jewel Protector, Crown Jewel offers a standalone crisis management response product and a product that offers crisis management and reimburses the expenses incurred for R&D and product development.

Intellectual property insurance products are similar, but the market's products are almost exclusively liability products, Guzman said. They'll cover organizations if they're alleged to have infringed on someone else's intellectual property, but they don't cover an organization's own product development and asset values. Meanwhile, the cyber market does cover stolen corporate confidential information, she said, but it excludes the future value of any asset and excludes the value of intellectual property, too.

Feedback from brokers has been positive. Guzman has been told her offerings are timely and important. The SEC's new cyber disclosure rule and the FTC's potential ban on non-compete clauses are raising awareness and causing consternation for brokers and clients, she said. She explained that if the FTC bans non-competes at the federal level, then all companies will need to amend the way they protect their trade secrets when employees leave. The new SEC rule requires companies to share what they're doing to protect material that could have an impact to earnings if breached.

> "We cover trade secrets like they are buildings, essentially."
>
> **Mary Guzman, Crown Jewel Insurance**

When asked about AI, Guzman said she believes trade secret protection will be "almost exclusively the only IP protection that can be garnered for artificial intelligence." She explained that the output generated from AI tools will likely be challenged to garner other types of IP protection, namely either patent or trademark, because the courts appear to be saying the inventor has to be "human" for either of those to apply.

"The No. 1 thing that companies [and] people need to realize is that if they have an excellent idea and an innovation asset that is going well and they think has a lot of opportunity, that patents are not the only way to protect that asset," she said. "A lot of companies believe that if you don't have a patent for something, then it's not valuable. That could not be further from the truth."

Guzman believes that creators and inventors desperately need to be incentivized to keep innovating, and that protecting R&D is crucial as experts work to solve massive environmental and social problems.

"People are going to have to feel like, 'If we're going to put the time and energy into developing something, we need to be able to protect it,'" Guzman said. "And so, I feel very passionately that, as an industry, we owe it to ourselves and owe it to the world, really, to solve for this problem." CM

On the Same Side: How Legal Finance Adds Value to Judgment Preservation Insurance

Executive Summary: Although casualty insurers often voice opposition to legal finance professionals, linking their roles in funding litigation to rising plaintiffs' verdicts and settlement costs, the insurance industry is also in the business of putting its capital at risk to help plaintiffs through a relatively new coverage: judgment preservation insurance.

Here, Andrew Lundberg of Burford Capital explains how firms like Burford add value to the emerging specialty insurance class with premium advances and expertise.

This article was originally published on the Burford Capital website in early January 2024: "Legal Finance & Judgment Preservation Insurance | Burford Quarterly (burfordcapital.com). It is republished here with permission.

By G. Andrew Lundberg

Successful litigants holding trial-court judgments have traditionally found themselves positioned similarly to mountaineers atop Mount Everest: After a long, brutal and costly ascent to the summit, they are only halfway home, as their opponents vow to appeal and take their victory away.

Legal financiers and other financial professionals have for years offered some peace of mind to such litigants in the form of claim monetization—advancing a portion of the judgment on a non-recourse basis in exchange for an entitlement from the judgment if and when it is affirmed and ultimately collected.

Recently, insurers have offered another financial product—Judgment Preservation Insurance, or JPI—that doesn't advance funds against the eventual collection of the judgment but does mitigate the risk of reversal on appeal.

Legal financiers can help litigants access the JPI market and enjoy the mitigation of appellate risk that these policies offer by working with them both to fund the purchase of JPI policies and to optimize legal finance products to maximize returns and minimize risks on their insured judgments. In addition to its customary roles of advancing cash to the successful plaintiff pending a final decision and financing legal expenses on appeal, legal finance can enhance the benefit of JPI coverage by tapping legal financiers' capital, experience and expertise.

What is JPI?

Judgment preservation coverage is simple in concept and, ideally, in execution. For a premium, the insurer agrees to assume the risk that a final trial-court judgment does not survive the defendant's appeal, agreeing to pay, up to the stated policy limit, the difference between the trial-court award and the amount the plaintiff ultimately recovers post-judgment.

Unlike the claim monetization offered by legal financiers who advance funds against judgments on a non-recourse basis, JPI provides only judgment protection, not collection protection. JPI does not guarantee the judgment holder that some or all of the judgment will be recovered in all events. It covers only the legal risk of an adverse judicial outcome, not the risk of being unable to collect following a successful one.

Thus, JPI insurers do not cover either the duration risk of the post-judgment proceedings (they do not pay interest on any portion of the trial-court judgment accruing after it is entered) or the credit risk of the defendant (i.e., the risk that the judgment, even if affirmed in whole or in part, cannot be enforced against the defendant). And, of course, JPI does not advance funds to the judgment holder to use pending decision of the appeal; rather, the judgment holder pays the JPI insurer an upfront premium.

The underwriting diligence performed by JPI insurers on post-judgment cases mirrors that done by legal financiers, who evaluate claims all along the timeline, with the obvious difference that a post-judgment risk will generally present far fewer variables that a pre-filing or pre-trial one.

JPI insurers have the benefit of looking at the risk on a record that has, by definition, been developed to the point where a court has deemed it sufficient to finally adjudicate the claim (whether by trial or on motion), and thus in the context of a judgment that, by definition, reflects at least the trial court's validation of the plaintiff's position. With that record in hand, JPI insurers typically will engage outside counsel with special expertise in the subject matter to opine on the likelihood that the judgment will be upheld on appeal. That opinion, together with the plaintiff's declaration that it has provided all other information the insurer may deem material to the risk, provides the basis for the insurer's decision whether, and at what price, to provide coverage.

Given their very specific and limited scope, JPI policies are considerably shorter and simpler than most commercial insurance forms. Unlike all-risk property policies, comprehensive general liability policies and other familiar forms of commercial insurance written to cover a broad landscape of unknown future events, JPI forms cover a single, well-defined risk: reduction or reversal of a particular existing judgment.

Such policies have no need for the laundry lists of exclusions and conditions addressing a universe of imagined and yet-to-be imagined scenarios. Accordingly, in theory they should present a minimal degree of legal risk themselves.

Funding Steep Premiums

That's the good news. The bad news? Primarily, cost.

JPI is expensive. Premiums run between 10 and 20 percent of the amount insured, whether that be the whole judgment or just a portion of it. Accordingly, a plaintiff looking to insure $100 million of potential judgment proceeds will need to find a low-eight-figures quantity of cash to put JPI coverage in place. (See, for example, Wall Street Journal, Oct. 17, 2023, "The Niche Insurance Policy Behind a Software Company's Big Legal Payout" by Kristin Broughton, describing a software company with $2 billion judgment insuring a $500 million portion of the judgment for $57.3 million.)

Related CM Articles

• An Innovator's Journey: From Star Litigator to Litigation Finance *(January 2022)*

• Commercial Litigation Funding and Social Inflation: A Non-Sequitur *(March 2022)*

Andy Lundberg is a Managing Director and a member of Burford's Commitments Committee who helps evaluate, approve and finalize Burford's litigation finance investments.

Legal financiers are an attractive source of that cash, as well as of additional financing secured by the judgment. Many plaintiffs, of course, can't or won't pay such a premium out of their own funds. Some are suffering the effects of the wrongful conduct of the defendant that produced the judgment they now hold. Others would rather spend the cash they do have on building their business rather than hedging their bets on their not-quite-final judgment. And many may be loath to borrow from banks or other conventional lenders even if traditional debt is an option for them.

Meanwhile, unsurprisingly, JPI insurers have little interest in financing the premiums for their would-be policyholders: Having already taken on the litigation risk of the defendant's appeal, they aren't disposed to tack on the credit risk of the plaintiff being unable to pay the premium if the judgment is ultimately reversed.

How Legal Finance Enhances JPI

Legal finance offers a solution by providing an alternative that is not only risk-free but also credit-enhancing.

Legal finance applied to the premium for a JPI policy—like legal finance applied to the cost of prosecuting the claim to judgment in the first place, or to the monetization of a claim prior to the affirmance and collection of the judgment—is generally non-recourse. The funder recovers its deployment and its profit only from the proceeds of the case (if

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the judgment is affirmed) or the JPI policy (if it isn't). If the financier recoups its investment and expected profit, it's only because the plaintiff has obtained a recovery and will enjoy the balance of the proceeds. Meanwhile, the plaintiff's other assets remain unencumbered.

In the JPI environment, moreover, although the legal financing follows the same structure, the economics of financing the further legal proceedings or of monetizing a portion of the hoped-for recovery are generally more plaintiff-friendly given the additional collateral provided by the JPI. The financier's return, normally paid only out of the ultimate proceeds generated by a successful claim, may now come either from the payment of the judgment by the defendant (if the judgment survives and is enforced) or payment under the policy by the insurer (if the judgment is reduced or lost).

Outside of the JPI environment, legal finance providers are accustomed to underwriting appellate risk, whether as an element of the overall risk profile of a claim presented to them pre-judgment (or even pre-filing), or as the core legal risk of a case looking for expense funding or monetization after a trial court award. But where an insurer is willing to cover some or all of that risk, the financier is well-positioned to finance the premium for that coverage, as well as potentially to advance a portion of the expected proceeds, and can make its capital available at a lower rate, reflecting the security provided by the JPI (of which it will be a beneficiary alongside the plaintiff holding the judgment).

Thus, in theory—that is, assuming the JPI insurer's timely payment of the policy proceeds without dispute—the financier's legal risk in a JPI-insured transaction should, to the extent of the covered portion of the judgment, be zero. Of course, it continues to bear legal risk on the uninsured portion, as well as the duration risk of the case (how long it takes to resolve all appeals and their sequelae), the collection risk of the defendant (will it pay, and be able to pay, when the day arrives), and the collection risk of the JPI insurer. But the insurance, properly done, should produce a material reduction in the cost of capital it provides compared to capital deployed in the absence of such insurance.

Additional Security Through Legal Finance

Besides the capital flowing to the plaintiff and its insurer, legal financiers provide an important additional benefit: reduced risk of collecting under the JPI policy. JPI is still a relatively new class of insurance, and new insurance products are notorious for giving rise to payment disputes. An unfamiliar subject matter can put underwriters in a learn-as-you-go posture that leads to misunderstandings about the intended terms or conditions of coverage. When previously untested language proves ambiguous, insurers may resist payment to which the insured believes it is entitled.

Unlike all-risk property policies, comprehensive general liability policies and other familiar forms of commercial insurance written to cover a broad landscape of unknown future events, JPI forms cover a single, well-defined risk: reduction or reversal of a particular existing judgment.

Consider, for example, potential disputes over what constitutes material information that a policyholder has a duty to disclose during the underwriting process, and whether a failure to disclose constitutes a breach that voids coverage. These novel policies require careful review and sometimes material revision by experienced insurance professionals, including qualified brokers and savvy legal counsel.

An eight- or nine-figure insurance policy should not be a placebo or a mere ticket to a fight. Sophisticated legal financiers have the expertise needed to reduce those risks to the minimum—and they bring that expertise to bear in both their own and the judgment holder's interest. An experienced legal finance provider can work with the insurance broker to review and revise policy language to avoid coverage disputes.

Adding Value

JPI is a significant new feature of the legal environment, giving litigants the ability to leverage their courtroom successes—whether gained at their own expense or with the aid of third-party capital—to achieve certainty, liquidity and security that can enable their businesses to grow. Legal financiers are uniquely positioned to make those benefits available, affordable and reliable, adding new value to the litigation landscape. CM


From the Desk of
Patrick Wraight
Cough medicine is the worst tasting thing I have
ever tasted, so I avoid it.
But when the cough is out of control, I'll do
anything to get it to stop. Even take the medicine.
Sometimes what you need is not something that you
would ask for, it's not something that you want,
and to be honest, it usually tastes awful.
But it helps.
If there's someone trying to speak truth to you,
they're doing it to help you.
Exactly what you need. Even if it tastes bad.
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