

Annuity Operations
Book of Metrics
Executive Summary



Dear Colleague:

Since 1995, Deloitte specialists have conducted extensive research on annuity back-office operations through a benchmarking study known in the industry as the Annuity Contract Expense Study (ACES).

This study provides comparative analysis on metrics that are widely used by insurance executives to benchmark expenses for operations, administration, and information technology (IT). Our analysis covers a variety of topics, including efficiency, effectiveness, key trends, use of technology, and business performance.

This report, summarizing results from our latest study, provides insight in areas critical to insurance executives:

- Marketing, product, and distribution
- New business
- Customer service
- Information technology
- Corporate overhead

We hope you find this summary report of interest and value, and invite you to contact our specialists for further information about our research.

Sincerely,



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All study data referenced and presented in this report as well as the representations made and opinions expressed, unless specifically described otherwise, pertain only to the participating organizations and their responses to the Deloitte Global Benchmarking Center study of annuity performance conducted in 2009.

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Major findings

Structured discipline — in all functions — is a critical part of effectively managing costs.

Despite their best efforts, annuity executives still struggle to manage their expenses and gain meaningful unit cost reductions, according to our study (Figure 1).

Figure 1: Adjusted line of business expense (ALOB) per in-force contract

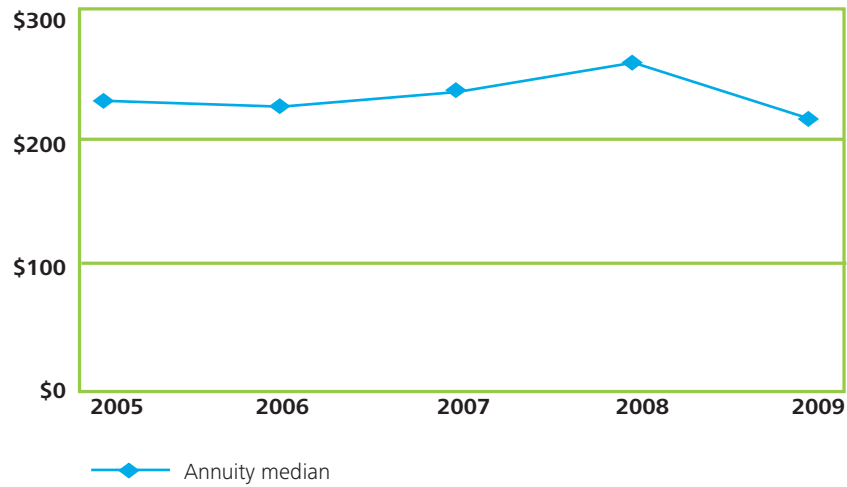
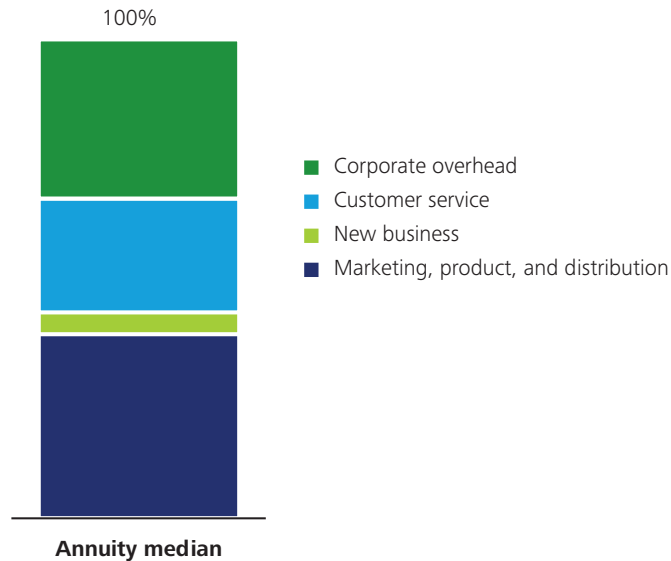


Figure 2: Components of ALOB expense



Marketing, product, and distribution expense has continued to grow and represents the largest share of adjusted line of business (ALOB) expense at 38%. While some companies have been successful in reducing costs, the ALOB expense among business functions (Figure 2) underscores the need to manage the entire business and apply structured discipline in all functions, not just the traditional focus areas of new business, customer service and related IT.

Over the last 5 years, total annuity new business unit costs have increased at an annual rate of 1.8% (Figure 3). Compliance and regulatory costs have challenged executives, along with the complex processing of 1035 exchanges (which allow for annuity transfers without tax penalties) and variable annuity guaranteed living benefit riders. High not-in-good-order (NIGO) rates also continue to plague insurers with excessive manual work.

Customer service unit costs have risen steadily — despite an increase in self-service for variable annuities. The level of in-force contracts has been declining, and organizations have not achieved comparable expense reductions, in part because customer service management has had to deal with new tax shelter annuity (TSA) administrative requirements, high surrender transaction volumes, and other expense pressures.

Total IT costs have been relatively flat over the five-year period. While some companies have embarked on strategic modernization initiatives, they have yet to see reductions in customer service unit costs.

Figure 3: Total new business expense per contract written

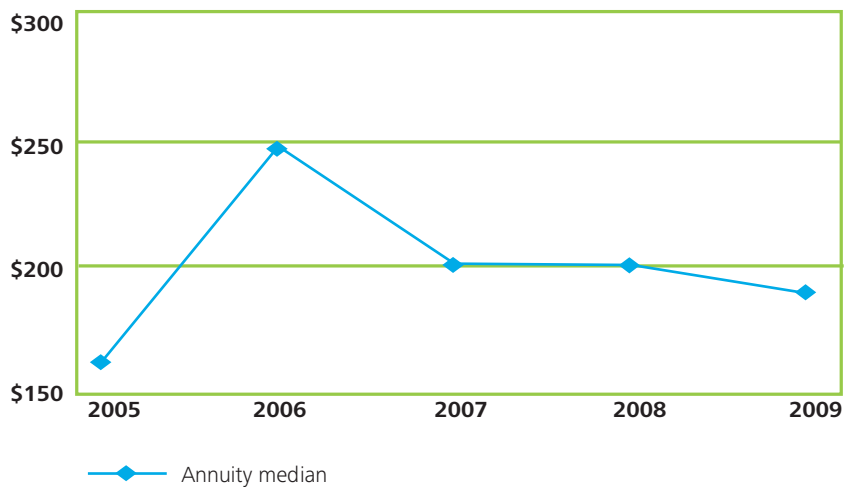
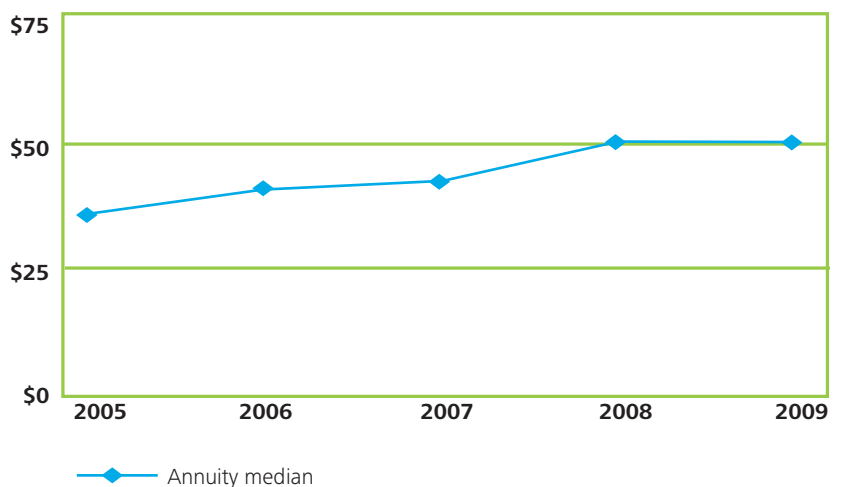


Figure 4: Total customer service expense per in-force contract



Marketing, product, and distribution

As a percentage of expense, low-cost performers spend five times more than the median on developing/maintaining products.

Historically, executives have not managed their marketing spend, product management and development, and distribution effort (MPD) with the same structured discipline as with their new business and customer service functions. With the downturn in the economy, we believe executives need to look at MPD in the same structured way they evaluate new business and customer service expense.

According to our study, low-cost performers spend 11% less than the median on MPD processing (Figure 5). Much of the difference lays in operations expenses versus IT expenses, with low-cost performers spending 28% less than the median.

As a percentage of expense, low-cost performers spend five times more than the median on developing/maintaining products, but significantly less than the median on marketing (Figure 6). This may reflect low-cost performers' emphasis on guaranteed living benefit riders and other aggressive product development programs to generate sales growth.

All areas of MPD are typically high-cost areas, potentially reasonable given future intentions; ultimately, however, the sales results must match spending. In-depth analysis of high-cost areas, clarity of accountabilities (such as ensuring profit/loss statements properly reflect decision implications), and licensing practices that include ongoing reviews and just-in-time licensing are just a few of the actions that can lead to improvement.

Figure 5: Marketing, product, and distribution per \$1,000 first-year deposits

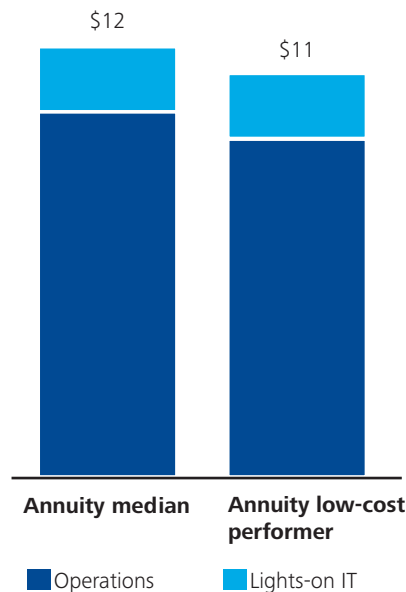
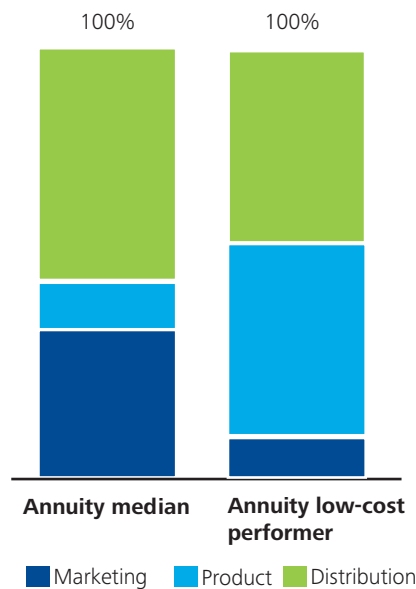


Figure 6: Distribution of marketing, product, and distribution processing expense



Customer service

Call center staffing models and tools are the heart of efficient customer service.

Lowering in-force expenses continues to be a challenge, though some companies are finding success. Variable low-cost performers spend 17% less than their median counterparts (Figure 12).

In fact, variable low-cost performers are doing well in leveraging self-service opportunities; our study shows that they are utilizing e-service at much higher levels than the median (Figure 13). We believe this partially compensates for — and perhaps creates — greater transaction volumes.

The challenge facing executives is to balance business objectives with the lowest possible cost when choosing an annuity service delivery model with a mix of the following elements (listed in order from lowest to highest cost):

- Eliminate the transaction
- Self-service (IVR, Web)
- Call center (once and done versus repeat calls)
- Service center (transaction, nonreferral, auto-index)
- Service center (referral or manual index)
- Expertise area (e.g., subject matter experts)

Annuity providers have significant opportunities for improvement through enhancements to call centers, which are typically the most important producer and customer interaction point. Though turnover and tenure challenges can be a concern, staffing options have evolved in the past few years, yielding more part-time and remote employment options.

Evaluating call center models as part of the overall service plan can provide direction for important trade-off decisions, such as skill groupings, service levels, tools, training, and performance management. By assessing the organization's current state and tools, organizations can more effectively align their chosen model properly and equip it with the necessary functionality.

Figure 12: Variable in-force administration processing expense per variable in-force contract

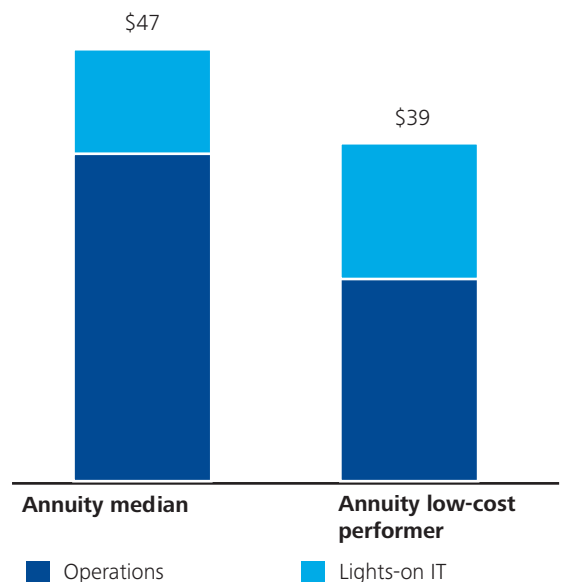
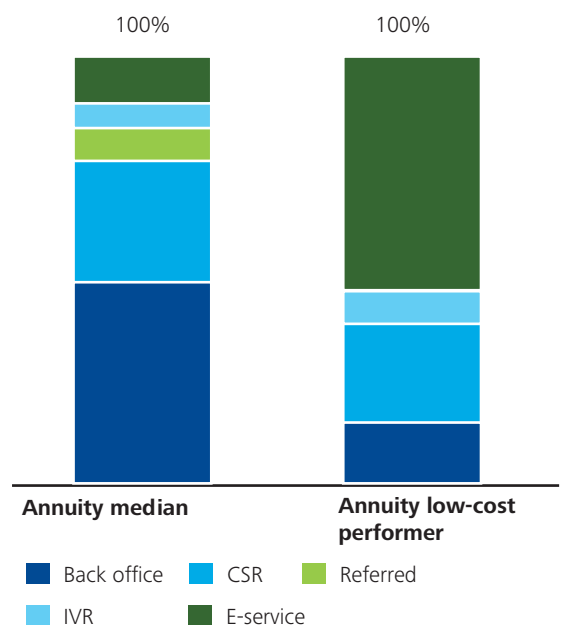


Figure 13: Distribution of variable in-force transactions



New business

In a number of organizations, fixed annuity growth exceeded 200%.

The economic climate and consumer concerns, as well as attractive fixed annuity interest rates relative to certificate of deposit (CD) rates, have driven a significant shift in sales volumes from variable to fixed annuities. Fixed annuity growth for the median was more than 150%, and in some organizations, the growth exceeded 200% (Figure 7). The move to fixed annuities is not a result of new organic growth, but rather due to significant turnover of existing portfolios.

Variable low-cost performers spend 11% less than the median on new business, partly due to their higher percentage of new issues and lower percentage of costly assets-in transfers (Figures 8-9). Inefficient processes for 1035 exchanges burden the industry and improvement efforts have been relatively unsuccessful to date.

Figure 7: New business contracts written

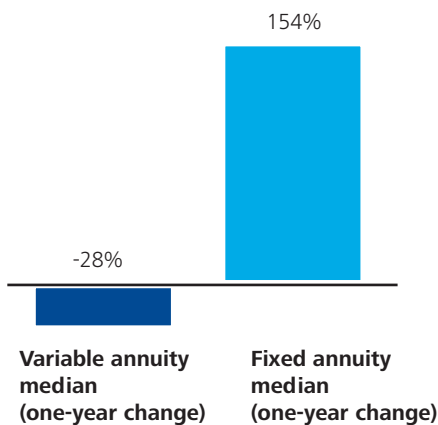


Figure 8: Variable new business processing expense per contract written

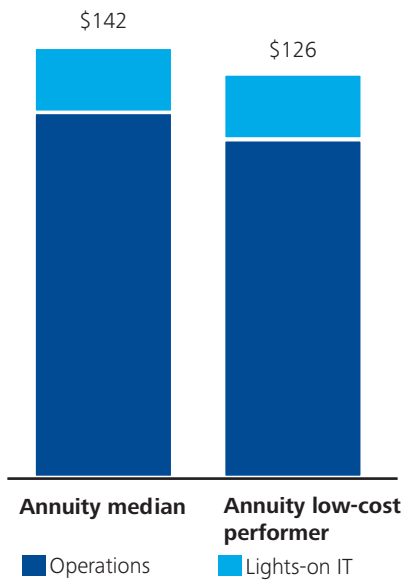
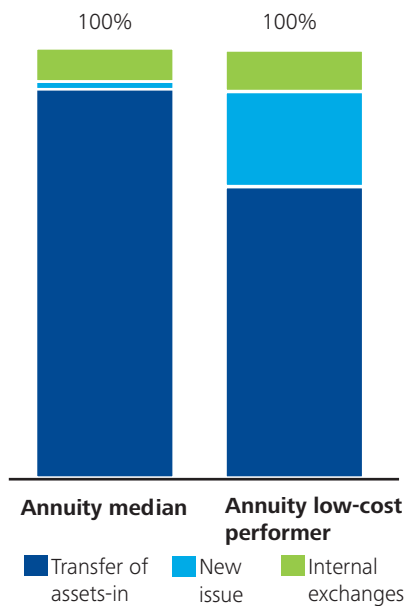


Figure 9: Distribution of variable issues by type



Fixed low-cost performers spend 38% less than the median on new business. Like the variable side, this also is partly due in part to their high percentage of new issues versus incoming transfer of assets (Figures 10-11). The study suggests that smaller companies can overcome scale disadvantages and reduce unit costs through strong management techniques, such as improving not-in-good-order (NIGO) rates (generally running above 40%).

Figure 10: Fixed new business processing expense per contract written

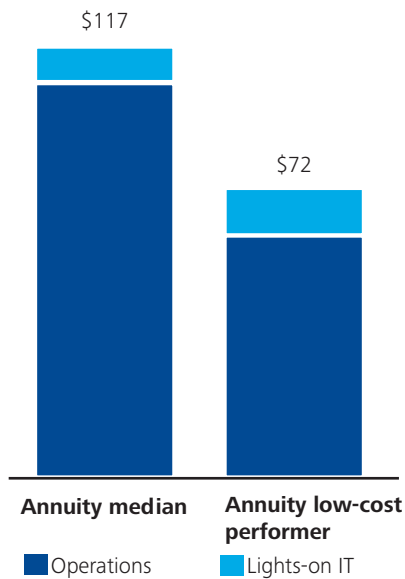
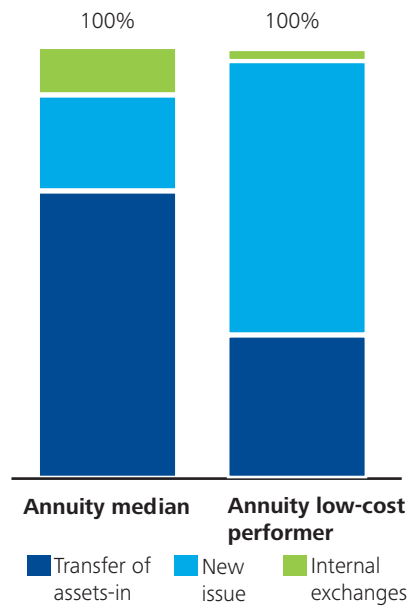


Figure 11: Distribution of fixed issues by type



Corporate overhead

Corporate overhead represents the second largest share of ALOB expense at 33%.

Corporate overhead can be difficult to align with the business size, as finance, legal, and compliance work are largely driven by external requirements rather than organization size or volumes. Sarbanes-Oxley requirements, market changes and regulatory issues all contribute to higher spend in these areas. However, significant improvement opportunities remain and underscore the need to manage the entire business and apply a structured discipline in all functions (Figure 14).

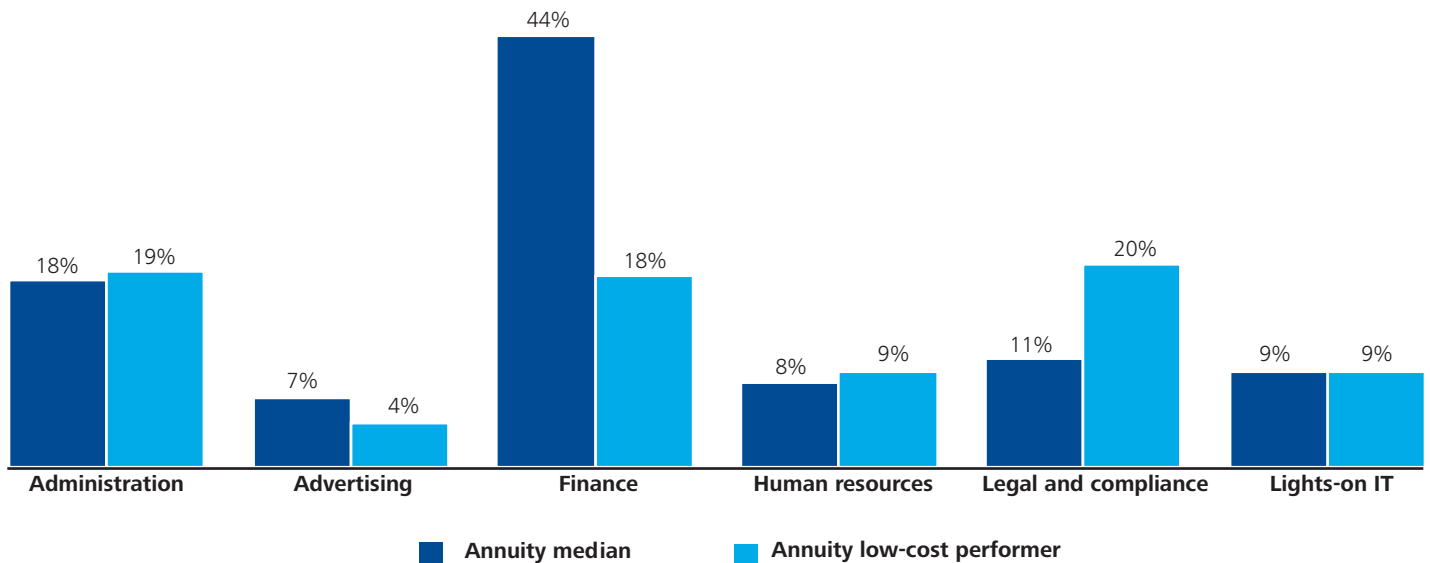
Costs may simply be a factor of scale and business focus areas. A comprehensive, ongoing management process has the potential to help by:

- Prioritizing areas of focus (e.g., statutory compliance)
- Decomposing costs into areas and services
- Ensuring that accountability is clear (supply and demand)
- Flushing out choices and alternatives that are built into the cost structure
- Taking stock of progress and making mid-course corrections

In addition, a structured compliance strategy can enable improved risk and cost trade-off decisions.

Lastly, outsourcing still provides great promise. Selective pursuit of third-party services — not necessarily offshore — can enable scale, deliver capabilities, and limit capital investments.

Figure 14: Percentage of corporate overhead spend by business function



Information technology

Enhanced technology decision-making processes could enable better competitive value.

IT cost as a percentage of ALOB is twice as high for low-cost performers as it is for the median, and neither utilize outsourcing (Figure 15). However, in looking at the breakdown of total IT spending, we find that low-cost performers invest much less on discretionary spend than the median, and considerably more than the median on infrastructure and maintenance (Figure 16). As a result, we believe lights-on costs are a critical point of analysis for potential cost savings.

Effective value-based decisions depend on clarity and transparency of spending decisions and allocations (to products, channels, etc.). Within infrastructure and maintenance, numerous detailed value judgments drive costs and focus, and we believe improving decision-making processes (e.g., empowerment with accountability) can aid improvement efforts. In addition, linking total IT spend (not just discretionary) to strategic objectives not only can help manage expenses; it can also encourage focus.

Figure 15: Total IT expense as a percentage of ALOB expense

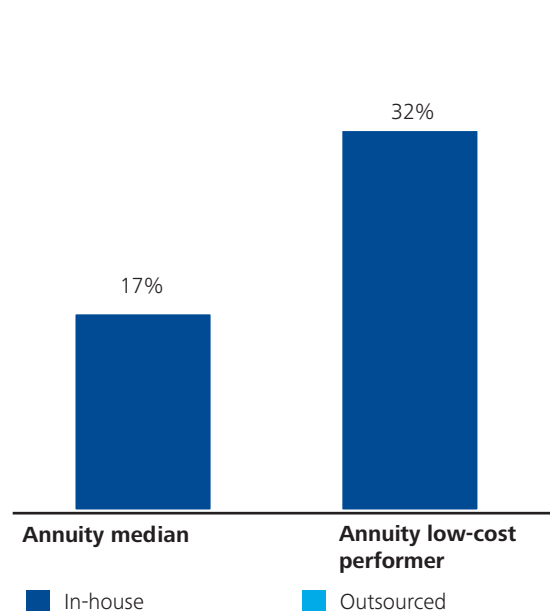
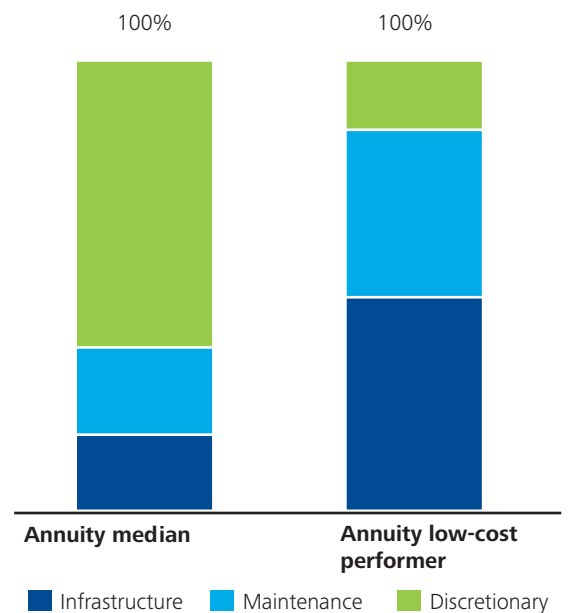


Figure 16: Distribution of total IT expense



Looking forward

Annuity executives are in the midst of a challenging business environment, where issues such as high 1035 exchange activity will continue to burden organizations.

Fortunately, many opportunities still exist to control costs, improve performance, and achieve competitive advantage:

- Executives must continue to modernize their technology infrastructure and drive toward lower unit costs and more scalable capabilities through the use of automation
- Successes can likely be achieved by emphasizing STP (straight-through processing), outsourcing, and self-service to control costs
- Companies that succeed in outsourcing will likely have sufficient benefits of scale
- Expense pressures will increase if fixed annuity sales do not continue at their current levels
- Organizations that aggressively use call centers for service handling — without referral to a service center — can meaningfully reduce costs

Executives who are able to contain costs and increase efficiencies will have their greatest opportunity to establish and maintain a leadership position in the marketplace.

Approach and methodology

Insurance benchmarking scope

The scope of the program is governed by a refined taxonomy. The taxonomy provides a standard set of definitions which guides participants in data collection and facilitates a true cost comparison to external organizations.

Marketing, product, and distribution (MPD)	New business	Customer service	Corporate overhead	Information technology
<ul style="list-style-type: none"> • Marketing <ul style="list-style-type: none"> – Pre-sale prospectuses – Post-sale prospectuses – Marketing materials – Marketing administration • Product <ul style="list-style-type: none"> – Develop new products – Maintain existing products • Distribution <ul style="list-style-type: none"> – Manage distribution channels – Compensation management – Appointments and licensing support 	<ul style="list-style-type: none"> • Operations <ul style="list-style-type: none"> – Capture applicant data – Evaluate suitability – Issue contract – Receive initial deposit – Support 	<ul style="list-style-type: none"> • In-force processing <ul style="list-style-type: none"> – Call center – Back office <ul style="list-style-type: none"> • Disbursements • Administration – Remittance – Print and send billing notices – Update records for deposits remitted – Reconciliation • Contract statement <ul style="list-style-type: none"> – Confirmations – Tax reports – Account balances 	<ul style="list-style-type: none"> • Administration <ul style="list-style-type: none"> – Stock options • Advertising • Finance <ul style="list-style-type: none"> – Accounting – Actuarial – Auditing – Reinsurance – Tax – Treasury • Human resources <ul style="list-style-type: none"> – Communications • Legal and compliance 	<ul style="list-style-type: none"> • Lights-on <ul style="list-style-type: none"> – Maintenance – Infrastructure • Discretionary <ul style="list-style-type: none"> – New development – Enhancements
Operations			Technology	

Methodology

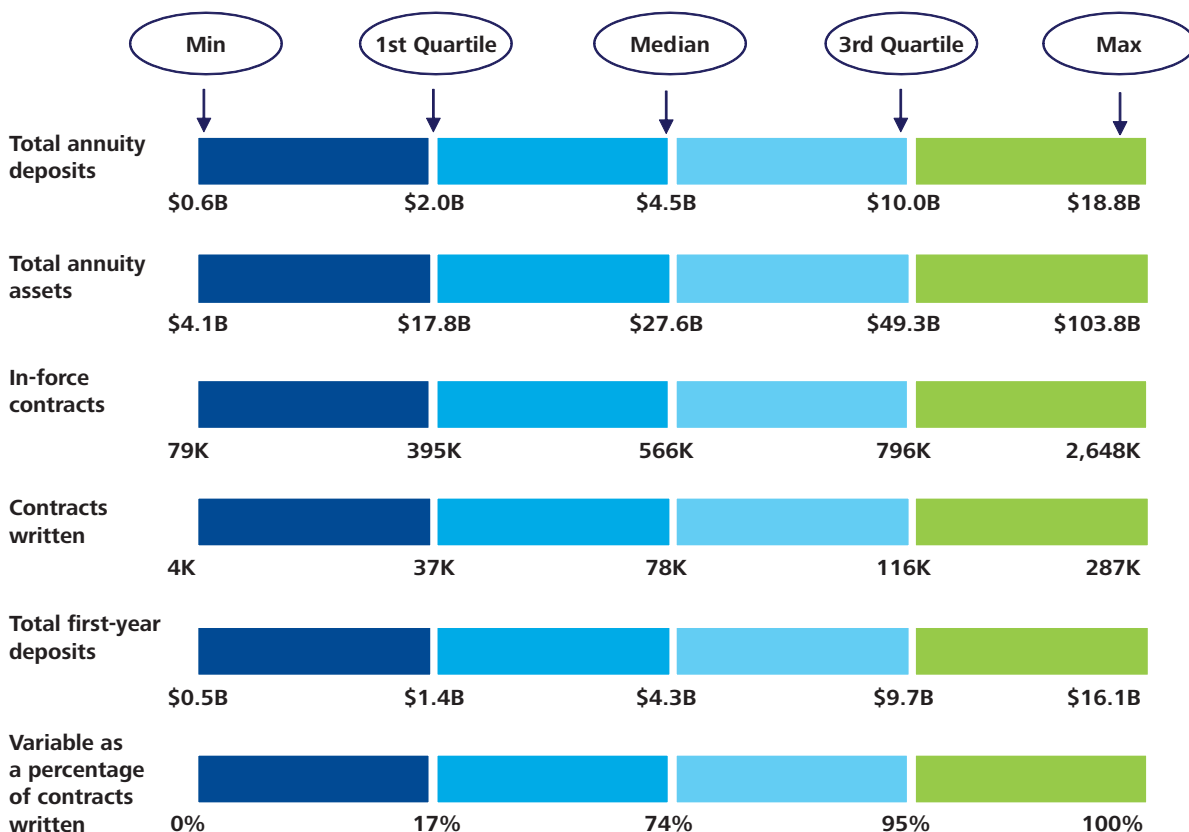
The 2009 Annuity Contract Expense Benchmarking Study (ACES) is based upon year-end and full-year 2008 data from 13 insurance companies.

The study comprises 378 questions on all aspects of performance and expenses for insurance back-office processes within new business; customer service; marketing, product, and distribution; and corporate overhead. Reports to participating companies include

185 data tables with detailed metrics on unit costs, service levels, processes, and use of technology.

The study was initiated in February 2009, and initial results were provided to participating companies in June 2009. Individual company reports with charts, comparisons to low-cost performer and appropriate peer group, and explanatory narrative were provided in August and September 2009.

Profile of participants



All study data and statistics referenced and presented in this report as well as the representations made and opinions expressed, unless specifically described otherwise, pertain only to the participating organizations and their responses to the Deloitte Global Benchmarking Center study of annuity performance conducted in 2009.

Performance measures

General

- Adjusted line of business expense as a percent of total annuity deposits
- Total IT function as a percent of adjusted line of business
- Distribution of total IT spend

Marketing, product, and distribution

- Marketing, product, and distribution processing expense per \$1k first year deposits
- Distribution of marketing, product, and distribution processing expense
- IT expenses as a percent of total marketing, product, and distribution expense

Variable new business

- Variable new business processing expense per variable contract written
- Variable new business processing expense outsourced
- Variable new business operations expense by type of issue (%)

Fixed new business

- Fixed new business processing expense per fixed contract written
- Fixed new business processing expense outsourced
- Fixed new business operations expense by type of issue (%)

Variable in-force administration

- Variable in-force administration processing expense per variable in-force contract
- Variable in-force administration processing expense outsourced percent
- Variable in-force administration operations per variable in-force administration staff

Fixed in-force administration

- Fixed in-force administration processing expense per fixed in-force contract
- Fixed in-force administration processing expense outsourced percent
- Fixed in-force administration operations per fixed in-force administration staff

Variable remittance

- Variable remittance processing expense per variable in-force contract
- Variable remittance processing expense outsourced percent
- IT expense as a percent of total variable remittance expense

Fixed remittance

- Fixed remittance processing expense per fixed in-force contract
- Fixed remittance processing expense outsourced percent
- Fixed remittance operations expense per remittance staff

Variable contract statements

- Variable contract statement processing expense per variable in-force contract
- Percentage of contract statement processing expense outsourced

Fixed contract statements

- Fixed contract statement processing expense per fixed in-force contract
- Percentage of contract statement processing expense outsourced

Corporate overhead

- Administration and stock options per \$1k total annuity assets
- Advertising per \$1k total annuity assets
- Finance per \$1k total annuity assets
- HR per \$1k total annuity assets
- Legal and compliance per \$1k total annuity assets
- Lights on IT per \$1k total annuity assets
- IT expense as a percent of total corporate overhead expense

Participants

Since 1996, more than 50 life insurance and annuity companies have participated in Deloitte's benchmarking studies.

Companies in parentheses identify acquiring company.

AEGON Direct Marketing Group
AEGON Financial Partners
AEGON Financial Services Group
AIG American General Life Cos., LLC
AIG Retirement Services, Inc.
Allianz Life
Allmerica Financial
Allstate Financial
Ameriprise Financial
Aviva USA
AXA Equitable
Baltimore Life
Chase Life (Protective)
CIGNA (Lincoln National)
Conseco Services, LLC
Fidelity Life Insurance
General American Life (MetLife)

Genworth Financial
Great American Financial Resources™, Inc.
Great West Life & Annuity
Hartford Life
ING
Jackson National Life
John Hancock Annuities
John Hancock Life
Keyport (Sun Life Financial)
Legacy Marketing Group
Lincoln Financial
ManuLife USA (John Hancock)
MassMutual Financial Group
MetLife
Minnesota Life
The MONY Group (AXA)
Mutual of Omaha
National Life
New York Life

Northwestern Mutual Life
Old Mutual Financial Network
Pacific Life
PennCorp Financial
Ping An of China
Principal Financial Group
Protective
Prudential Financial, Inc.
Samsung Life
SBLI of Massachusetts
se2, inc.
Sun Life Financial
The New England (MetLife)
Thrivent Financial
TIAA-CREF
Travelers Insurance Co. (MetLife)
Western Southern Life
Woodmen of the World Insurance Society

About the Global Benchmarking Center

Deloitte’s Global Benchmarking Center (GBC) was established to provide executives with industry relevant metrics and insight. The GBC delivers this information through ongoing benchmark studies in areas such as sales, general and administrative (SG&A), finance and accounting, supply chain, information technology, human resources, and operations. The GBC has conducted studies with more than 600 global organizations since 2005. These studies are uniquely designed to provide industry-specific insight relevant to multiple sectors.

Industry	Function
<ul style="list-style-type: none"> • Consumer and Industrial Products <ul style="list-style-type: none"> – Aerospace and Defense – Automotive – Consumer Products – Process and Industrial Products – Retail – Tourism, Hospitality, and Leisure • Financial Services <ul style="list-style-type: none"> – Banking – Securities – Insurance • Energy and Resources <ul style="list-style-type: none"> – Oil and Gas – Power and Utilities 	<ul style="list-style-type: none"> • Finance • Information Technology • Human Resources • Sales and Marketing • Indirect Materials • Corporate Services • Legal • Corporate Real Estate • Supply Chain • Operations • Product Development

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**Participation in this ongoing study is open to all annuity providers.
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