VIEW POINT

DISTRIBUTION MANAGEMENT SYSTEMS

A boon for insurance carriers in India

Abstract

With the Indian insurance industry registering double digit premium growth year-on-year, the market share battle is fierce. The insurance carriers in the market have been increasing their share of the distribution pie through strengthening distribution channels. Yet, the insurance penetration rate — the ratio of insurance premiums paid and the GDP of the country — is only 3.6%, which is quite low compared to the 6.13% globally.

With the tremendous scope for growth, the market is expected to quadruple in size over the next decade. This will require strengthened distribution capabilities, use of technology in distribution, and better developed distribution networks.

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Distribution channels in India

Indian insurance companies use the multiple distribution channels shown below to increase new business, based on need, targeted customer segment, and changing customer demographics.

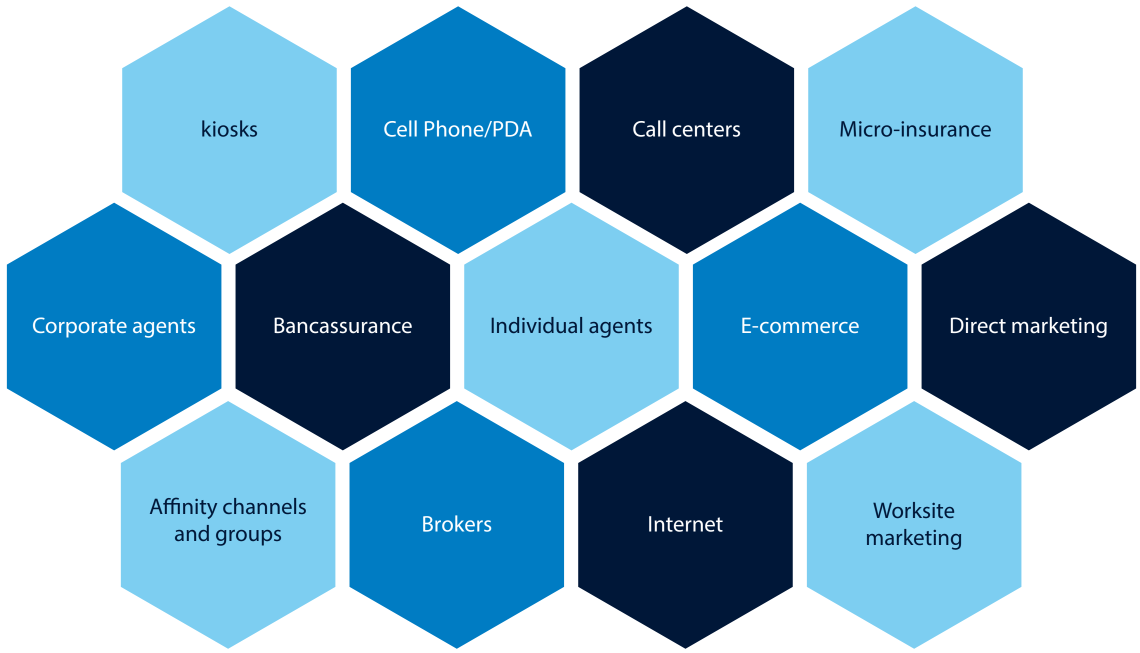

Figure 1: Distribution channels to increase new business

Yet, "insurance is often sold but rarely bought" is a quote that holds good even in today's digital world. Because of insurance's intangible nature, difficulty in understanding policy terms, the long-term financial commitment involved, and the necessity of service throughout the policy tenure, an advisor's guidance and support cannot be undermined.

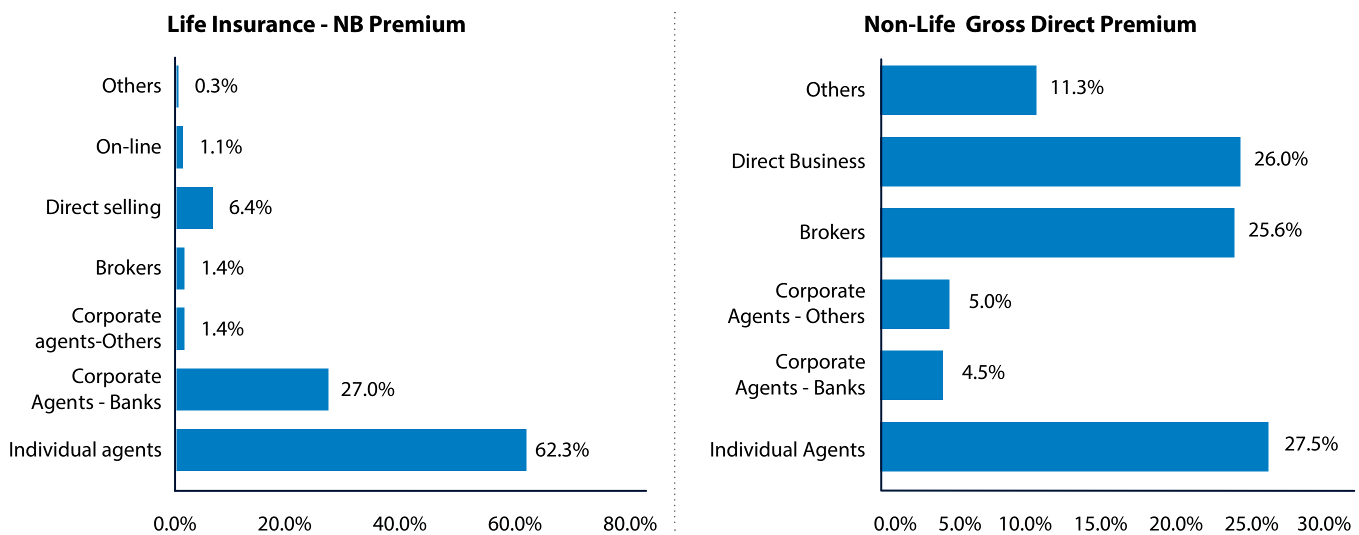

Figure 2: Distribution channels share in the Insurance sector

Source: IRDA Handbook FY18-19

Today, customers research and compare products online, but prefer to have face-to-face interactions with an advisor before signing on the dotted line. The data shows that more than 98% of new business premium in India was procured through face-to-face sales in FY'18-19 with agencies, bancassurance, and brokers as the dominant distribution channels.

Need for DMS solutions

Many carriers use policy administration systems (PASs) for commission calculations, and spread sheets for incentive and rewards and recognition (R&R) calculations. However, when it comes to growth, these systems impede insurers' ability to manage and compensate distribution channels well, with inadequate system support creating difficulties in launching innovative compensation plans. Manually using spread sheets for complex calculations leads to errors and in turn, disputes and complaints from agents. Further, legacy systems neither enable easy management of the ever-changing compliance rules, nor provide the required flexibility for scaling up across distribution channels and geographies.

To overcome these challenges, it would be a prudent idea for insurers to implement a dedicated Distribution Management System (DMS) solution that offers the following advantages:

- **Effective channel management:** Data on distribution channels and producers can be systematically organized and managed
- **Speed to market:** Commission and incentive plans can be easily configured to match dynamic market changes, with the system tracking agent performance, managing payouts, and generating MIS reports
- **Seamless integration:** Out-of-the-box integrations with various upstream and downstream systems can help with batch processing of high transaction volumes or real-time processing via web services or API
- **Error reduction:** With the system making manual processes redundant, human errors in calculations will be reduced, thereby reducing complaints and disputes from the field force
- **Cost reduction:** With automation of data maintenance and processes, human effort and in turn costs will be reduced
- **Regulatory compliance:** Rules configured in the system will ensure compliance with regulatory requirements preventing huge fines

The figure below shows the core components of a DMS and integration with upstream and downstream systems. We will next look at each of these components in detail.

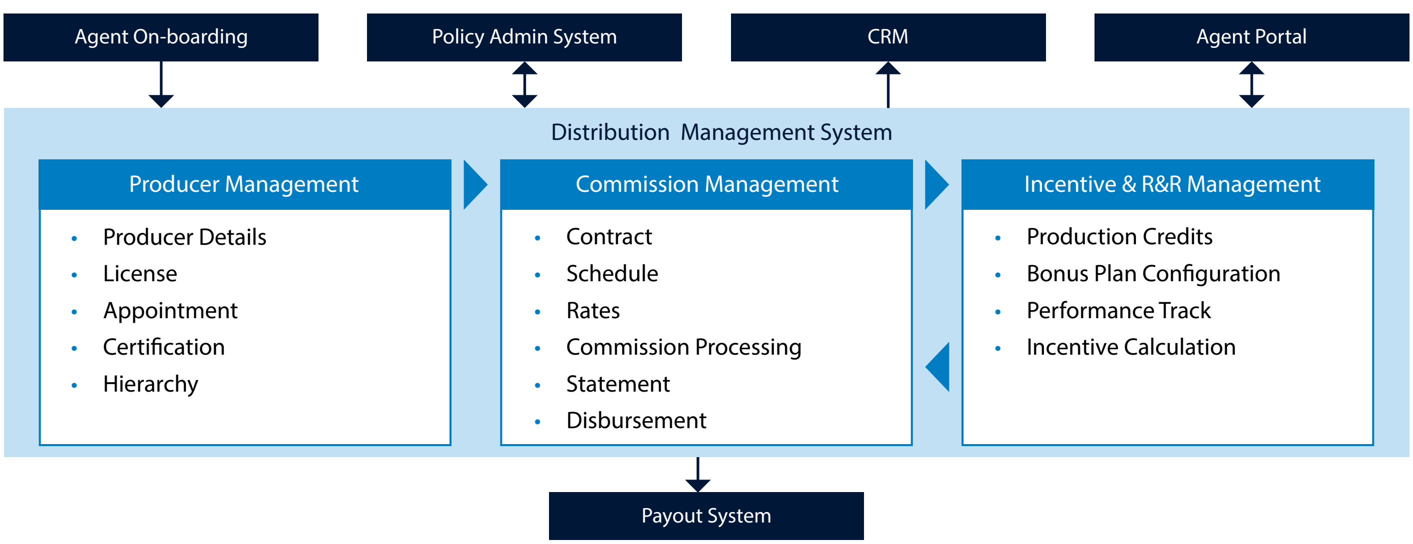

Figure 3: Core components of DMS solution

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Producer management

The producer management component of a DMS automates many functions of producer maintenance including adding or updating producer data, managing licenses and appointments, handling hierarchies, and so on. This makes it easier to ensure licenses are in force, appointments are processed, and demographic data is accurate.

The producer management component should offer:

- **Audit trails:** Updates made to producer records must be auditable with the complete details of the updater, update time, and nature of the change
- **User security:** User access rights must be differentiated based on their roles, permissions, and security levels
- **Date tracking:** Historic, current or future dated business rules should be configurable based on start and end dates. Similarly, licenses, appointments, hierarchy, and contracts should be trackable based on dates
- **Configurability:** Users should be able to easily configure the data, rules, static tables, and drop-down values by themselves without programmer dependency
- **Online help:** Detailed online documentation must be available for users to understand the application functionality

In general, the system should support maintenance of the self-explanatory producer details mentioned in the following diagram. Some rules specific to India are as below:

Maintenance of Producer Details

Basic Information

- Address, Phone, Email
- Bank Account
- Background Investigation
- Distribution Channels
- Product Classes
- External Numbers
- Tax Number
- Status Information
- Mis-Selling Indicator
- Suspend Process Indicators

Relationships

- Contacts
- Office Affiliation
- Territory Affiliation
- Group Affiliation
- TPM Affiliation
- Club Membership
- Nominee Details
- Sales Office Hierarchy

Compliance

- License Details
- Appointment Details
- Training & Certification
- Authority Details
- Minimum Business Guarantee
- Eligibility for Ren. Commission
- Exempted from MBG Norms
- Vesting Rules

Commission Admin

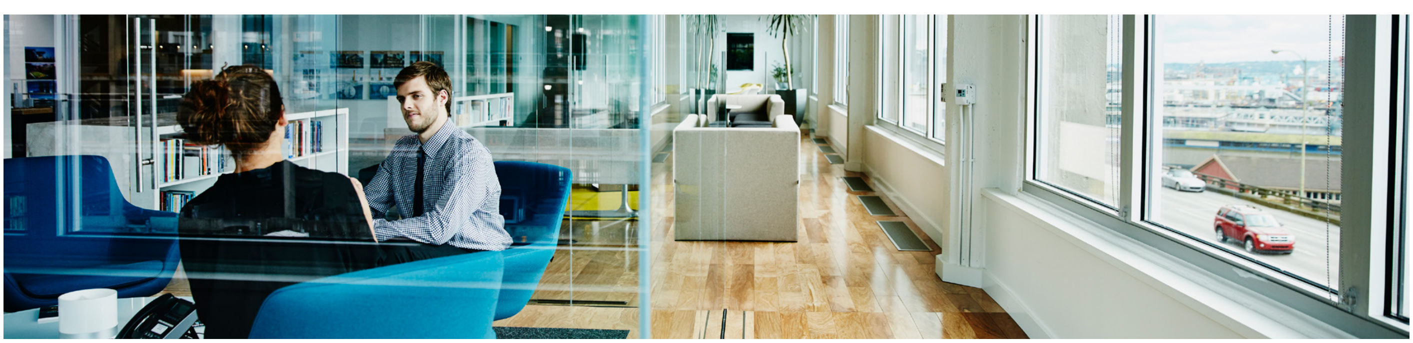
- Contracts
- Hierarchy
- Alternate Payee

Miscellaneous

- Profile Notes
- Profile Alerts
- Work Items

Figure 4: Maintenance of producer details

- **MBG (minimum business guarantee):** Agents need to fulfill minimum new business requirements each year to keep their appointments active
- **ERC (eligibility for renewal commission):** Agents are eligible for renewal commissions only if they have fulfilled MBG to keep their status active
- **EMBG (exempted from minimum business guarantee):** Agents fulfilling certain requirements can be exempted from MBG requirements
- **Vesting Rules:** These rules relate to payment of various kind of commissions when the agent status is terminated



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In addition, features helping with critical producer management operations on a daily basis are elaborated below.

Operational Abilities

Inquiries

- Agent Find
- Policy Find
- Maintenance History
- Commission History
- Adjustments History
- Tax Deduction Details
- Disbursements History
- Journal Entries
- Production Credits

Mass Update

- License Update
- Appointment Update
- Hierarchy Update
- Status Termination
- Profile Transfer
- Club Membership
- Office Affiliation Update
- Territory Update

Administration

- Accounting
- Commission Rates
- Commission Schedules
- Carrier
- Product/ Plans
- Edit List Tables
- License Control
- User Security
- System Setup

Correspondence

- Reports
- Letters
- Producer Data Warehouse

Adjustments

- Balance
- Miscellaneous

Figure 5: Operational abilities

- **Inquiries:** Querying and filtering of the database for details relating on events, history, tax deductions, journal entries, and so on, with exporting of the results to Excel spreadsheets for further analysis
- **Mass update:** Bulk operations such as, a mass profile transfer, to transfer all producers under an agency that have been terminated to a new agency
- **Administration:** Maintaining various system configurations relating to data on producers, commission processing, accounting, licensing, reporting, and so forth
- **Correspondence:** Out-of-the-box reports and letters with the ability for report scheduling or creating of ad-hoc reports by categories such as territory, wholesaler, or distribution channel. Many DMSs offer bundled data warehouses as well, as central repositories for production data that is generated as producer information is processed and made available to the entire organization.
- **Adjustments:** Enables adjustments to correct existing transactions by minor amounts for agent balances or miscellaneous amounts.

Commission management

The commission management component encompasses the calculation and disbursement of commissions to producers as well as the associated accounting. Unlike the commission capabilities inherent in their PAS or billing system that are usually limited to simple and transactional commission plans, a robust DMS can handle complex commission and bonus plans.

The diagram below shows the high-level components involved in commission management

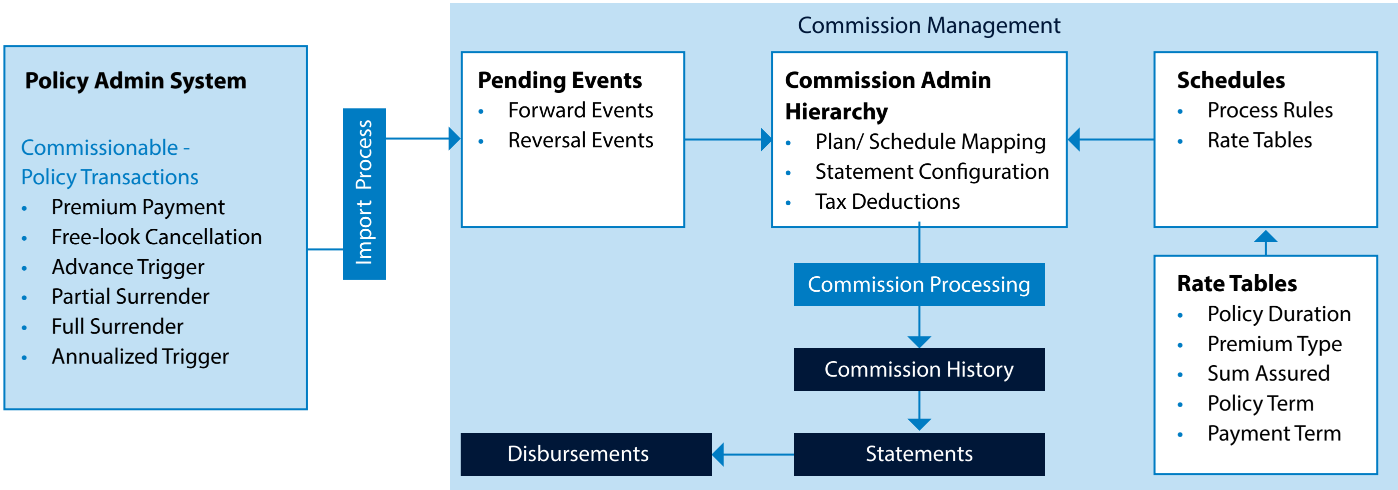

Figure 6: Commission management

Commission and bonus calculations need to be performed for each event based on the agent on the event and the hierarchy structure, and the product, plan, commission rate, schedule, and contract set ups. Following are a few examples of variables impacting these calculations.

- **Policy information:** Policy number, issue age, product/ plan code, premium paying term, policy term, agent code, agent type (writing or servicing)
- **Policy event information:** Transaction code, premium, premium type (regular or single or top-up), issue date, effective date of transaction, duration (first year or renewal), event type (premium based or asset-based trail or charge back)
- **Producer information:** Hierarchy (for override commission), club-membership, contract, schedule process rules, commission rate table, vesting rules

After a commission history is generated for all successfully processed commission transactions, the DMS needs to support various error correction scenarios as listed below:

- Users should be able to review and correct pending events that are errored out during commission calculation processes to be processed in the next batch cycle
- Users should be able to correct through reversal, correction, and reprocessing the mistakes identified after the commission was calculated and the history created. For example, a commission rate that was wrongly applied for a transaction
- The system must enable the users to create manual adjustments such as for agent balances or other miscellaneous items

A commission statement is a consolidated report of commission transactions made at each agent level during the statement period defined under the agent contract and includes details such as methods and frequency of payouts. After applicable tax deductions such as income tax, professional tax, and GST are deducted from the statement total, the net amount is disbursed to agents. Journal entries need to be created for all commission history transactions and statement history transactions.

For disbursements, the DMS should provide – disbursement extracts which can be consumed by the enterprise payout system, and accounting extracts which can be consumed by the enterprise GL system.

Incentives and R&R

The Insurance Regulatory and Development Authority (IRDA) has stipulated 40% as the maximum first-year commission for regular premium term plan, with lower caps on other product types. But carriers are allowed to pay incentives up to 20% of the first-year commission. This has facilitated the design of bonus plans focused on performance targets and the quality of business procured. While commission rate structures do not vary from agent to agent, a lot of customization is possible while designing incentive programs which can take into account many quality parameters including persistency targets, policy churn, early claims ratios, and complaints about agents.

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The diagram below shows the high-level DMS components involved in incentive and R&R management.

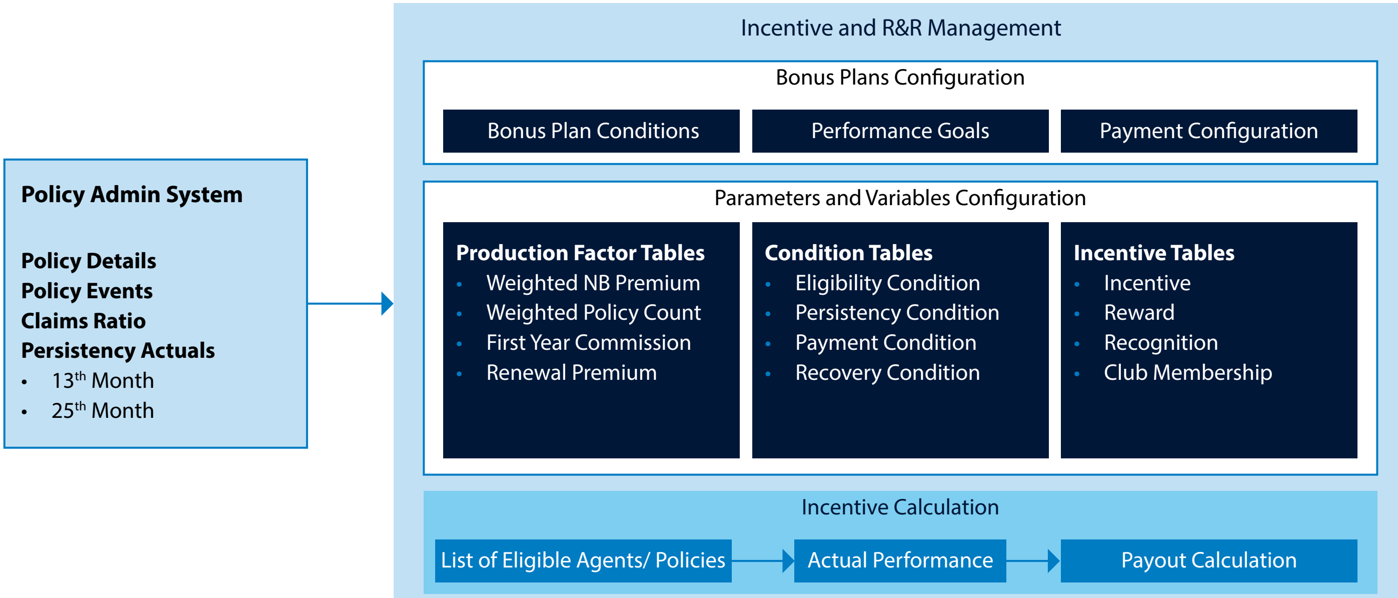

Figure 7: Incentive and R&R management

Incentive programs use weightage factors as a basis to measure the performance of an agent. The weightage factor is based on multiple variables like product type (traditional or ULIP or annuity), premium type (single, regular, or top-up), territory, premium payment term, or agent appointment date.

Incentive programs generally have conditions such as:

- **Exclude policy conditions:** While computing the performance basis, policies which are churned, cheques dishonored, or free-look cancelled and so on need to be excluded
- **Entry conditions:** Agents whose persistency targets are above a certain %age only need to be considered
- **Agent exclusions:** Agents who are having complaints from customers need to be excluded
- **Payment conditions:** Production targets that need to be fulfilled for agent payment eligibility
- **Recovery conditions:** At the time of payment, if certain conditions are not fulfilled then payment has to be reduced according to the recovery percentage defined.

A DMS should be able to handle these complex calculations in an efficient manner and generate timely MIS reports on a daily basis through batch jobs. With performance goals measured on individual or team target achievements, the DMS should also provide for uploading of targets from excel spread sheets, with actual performance tracked and reported on a daily basis.

At the end of the incentive plan period, payouts need to be calculated based on the incentive table configuration and process rules. A payout type can be either a cash payment incentive, a reward such as a gift or a gift voucher, or a recognition such as a promotion or convention sponsorship. These payouts should be reflected in statements and applicable taxes need to be deducted.

Conclusion

There is tremendous scope for spreading insurance coverage in India, considering the massive amount of untapped potential. The recent amendment to allow 100% FDI in insurance intermediaries will lead to more innovations happening in distribution landscape and use of technology in distribution. While carriers are trying to increase sales through various distribution channel strategies, DMS solution will bring in synergies to achieve their marketing objectives, and stay ahead of competition.

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Naresh Kumar is Principal Consultant in McCamish account of Infosys BPM. He has over 16 years of experience in the Life and Annuity domain consulting. His experience includes managing insurance operations, product development and delivery management. Naresh is leading the PMACS® (Producer Management & Compensation System) product development initiatives, platform modernization and new opportunity pursuits.

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Focused on enhancing digital experience and improved customer service, Ganesh is leading teams of Product enthusiasts who bring innovative ideas to the Infosys McCamish Insurance platforms.

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