

# Successfully Navigate the Consolidation Trend



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*The driving forces behind consolidation are to expand offerings and reduce expenses—and to ultimately achieve new levels of earnings growth. To succeed, there are five basic steps companies should follow:*

1. Assess
2. Build the vision
3. Plan
4. Execute
5. Review and refine

### **The trend toward consolidation**

The insurance industry is riding a wave of consolidation. To thrive within this market dynamic, companies must implement the appropriate strategies and tools that allow them to create efficiencies of scale and to increase their competitiveness.

As many industry tales demonstrate, the road to a successful merger or acquisition involves a lot more than accounting and legal matters. Therefore, this paper explores the driving forces behind consolidation and provides tips on how to successfully navigate consolidation and ultimately achieve new levels of earnings growth.

#### **Driving forces**

During the consolidation process, companies are primarily focused on achieving two outcomes:

1. **Reduce expenses:** consolidate internal operations to achieve economies of scale
2. **Expand offerings:** increase client wallet share through acquired operations or books of business

It is also important to note that there are specific drivers for both the property and casualty (P&C) and life insurance sectors.

- **P&C-specific drivers** include both growth and diversification. The market for clients to buy insurance is not growing. To grow, insurers must capture business competitively through mergers and acquisitions or by purchasing specific books of business. In addition and in the aftermath of recent catastrophes, companies are feeling pressure to diversify their books of business. One way to do this is to acquire other operations with additional lines of business or geographies.
- **Life-specific drivers** revolve around growing consumer demand, globalization and overcapacity. The increased demand for universal life and variable annuity products is requiring larger surpluses. At the same time, the desire among insurers to expand into a virtually untapped global market creates a need for additional capital. There is added pressure to reach critical mass to compete and remain profitable in a highly competitive and crowded market. In addition, banks are divesting their life and annuity operations in lieu of co-marketing agreements with life insurers.

#### **Key issues within consolidation scenarios**

With these driving forces in mind, there are three primary ways in which consolidation plays out.

1. **Companies acquire smaller operations:** Critical issues within this scenario include retention of the smaller organization's key staff and typical concerns such as profitability and consolidation of systems, which need to be addressed within all acquisition scenarios.
2. **Merger of equals (or near-equals):** Key issues within this scenario include retention of employees across both organizations, as well as the political realities of merging or consolidating two sets of senior management. Unlike the acquisition of a smaller organization, the cultural fit needs to be carefully evaluated from an organizational change perspective. Many decisions become more political since there is no dominant organization to impose its will.
3. **Acquisitions of a book of business:** This scenario can play out in a variety of ways, from the acquisition of an entire division to the acquisition of policies only.

*There are many functional areas to consider when transforming from disparate organizations into a unified company. To align all internal and external forces toward success, each function should be unified under a cohesive plan that benchmarks and measures success.*

### The consolidation roadmap

Within each of these scenarios, there are five basic steps that companies should follow to build, execute and continually refine a successful consolidation roadmap.

#### Step 1: Assess

During this step, conduct a full assessment of the situation's biggest issues that must be addressed. Some issues that should be considered during the assessment phase include:

- Where do profitability issues reside?
- How many staff members need to be merged? Where are they located? What is their culture like?
- What political issues could arise during the merger? Who will make up senior management of the new company? What decision making power will they have?
- How will we retain agents and clients?
- How will we consolidate operations and systems? Where are the best opportunities for economies of scale or reductions in expenses?

#### Step 2: Build the vision

Having a clear vision of the end-state company is critical. Whether it's a merged or expanded company, a new mission or vision statement—as well as a plan for the end-state organization, systems, locations and operations—may be in order. Some key questions to consider include:

- What will the culture of the new organization be?
- Who should lead the organization?
- Where will we do business?
- What products will we write?
- What is our competitive differentiator?
- What do our agents and clients expect?

#### Step 3: Plan

Develop a holistic plan to address the transformation from disparate organizations to a unified company. Also define the "exit criteria" that benchmarks and measures the plan's success. Some items to consider are provided under the functional headings below.

**Profitability:** Investigate the acquired or merging organization's loss history and premium trends. Assess the use of credits, discounts and other discretionary factors, and review the loss reserves against the type of business being written. Audit the underwriting files to ensure that the business being written is consistent with the underwriting rules. Use loss control techniques to assess whether the account can be rehabilitated or if it should be non-renewed as it cannot be made profitable. Review claims processing practices for appropriate reserving, payment and settlement, and review reinsurance treaties to ensure that the correct treaties are in place. Use business process engineering techniques to streamline existing processes and to reduce redundant processing. Also consolidate and update IT systems to reduce system maintenance costs and to manage the costs of licensing, product support and other vendor-related agreements. Apply spend management techniques to reduce costs of procurement for daily business needs. Finally, outsource non-core processes to a qualified third-party provider that can process the business less expensively, allowing flexible pricing models based on volume.

*Throughout the consolidation process, it is critical to manage the "human factors." If agent and employee expectations are managed and consistent levels of customer service are maintained, mergers and acquisitions have a high probability for success.*

**Actuarial and product development:** Conduct a profitability assessment for both existing and newly acquired lines of business. Conduct an analysis of loss reserving practices and review the risk spread and diversification. Create recommendations for new products and the reduction or elimination of old ones based upon the profitability and risk assessments. Also review the reinsurance treaties.

**Sales and marketing:** Create strategies for agent and client retention and develop the appropriate communications plan. Review the market positioning for the products. Create brand positioning for the newly merged organization and build the resulting marketing plan to raise awareness of the new brand.

**Underwriting:** Implement new rates or underwriting guidelines and plan for the non-renewal of business for eliminated lines. Review the customer and agent service systems, such as call and processing centers, to identify economies of scale. Cross-train underwriters and processing staff and re-underwrite existing risks to rehabilitate loss ratios.

**Claims:** Plan for changes to geographic territories or training for adjusters handling new lines of business or coverages. Review the customer and agent service systems, such as call and processing centers, to identify economies of scale. Review reserving practices and workflow processes and time service to reduce the cost of claims. Implement new tools for claims adjusters to reduce fraud and improve efficiency.

**Billing:** Plan carefully for changes to billing. Disruptions in billing are the most common cause of client dissatisfaction in system consolidation. Billing representatives are likely to have the most frequent contact with the customer, so it is critical to maintain continuity.

**Accounting and finance:** Determine whether to consolidate the financial systems or simply merge them. Review the financial reporting practices.

**Human resources:** Plan for the retention of key employees by evaluating who will be critical to operating the new company. Consider using techniques such as retention bonuses to ensure that key staff remain in place throughout the transition. Coordinate the merger of acquired employees onto the main HR system. Train employees on the new benefits structure and coordinate enrollment for acquired employees. Evaluate job titles and the promotional structure for acquired employees and align salary structures between the companies. The human resources department needs to act as a consultant for organizational realignment and employee communications surrounding the merger. Retaining and growing a high-quality staff is vitally important to the new organization. Plan for training initiatives that support the new vision and hire an organizational change expert to help if needed.

**Facilities and support services:** Prepare for employee moves and review the use of the company fleet. Create a central document processing center or enterprise content management system. Review the rerouting of mail and internal document flows. (This is a good candidate for outsourcing if mail handling is not considered to be a key function.)

**Information technology and systems:** Achieve economies of scale and reduced cost of maintenance by consolidating disparate systems. Incorporate an enterprise technology standard and establish a project management office and other best practices to ensure the success of projects. Redesign infrastructure and networks and review data protection and security procedures.

**Other associated businesses:** Many insurers have other associated operations such as mortgage lending, banking operations or credit card issuance that need their own consolidation plans.

***There are several key success factors to consider within a merger or acquisition situation:***

- *Identify and fill culture and value gaps.*
- *Build a post-merger vision and a plan for how to get there.*
- *Achieve buy-in from employees, agents and clients.*
- *Examine systems and data and integrate them as needed.*
- *Pick a strong partner to serve as a guide.*

***Step 4: Execute***

Once the plan has been built, follow it carefully. Don't abandon the plan if things go wrong—use the outcome of assessments to help correct course and navigate through the process.

During the execution phase, it is critical to manage "human factors." Whether or not a company has acquired staff, many people issues must be considered. If agent and employee expectations are managed and consistent levels of customer service are maintained, consolidation has a high probability for success.

**Agents**

- Keep the agency force informed and involved throughout the consolidation process. The more informed they are, the better they can assist clients with any issues.
- Anticipate changes that will affect agents and solicit their involvement and feedback.
- Avoid changing too many areas at once.

**Clients**

- Minimize disruptions in service, especially in the two key areas where clients are most affected: billing and claims.
- Keep it human. Make it easy for clients to speak with a live person when seeking help with a problem. This will make even the most frustrated customer more satisfied with the outcome.
- Communicate changes that will affect clients. They may not care that the companies are merging, but they do care if it will affect their billing, policy service or claims handling.

**Employees**

- Build a clear communication plan and implement it quickly. In the absence of information, rumor will take over. Quash rumors quickly with factual information.
- Anticipate emotion. When people's work lives change, they often act in emotional—and sometimes illogical—ways. Be respectful of people's emotional reactions and provide employees with the appropriate channels in which to express them. This goes a long way toward making a smooth transition. Be positive, not punitive, and remember that new teams will take some time to form.
- If a staff reduction does occur, plan for the reaction of the staff who are leaving and those who will remain.
- Act with integrity. People will follow those who they trust; any implication otherwise will cause productivity issues and turnover. Remember that it's okay to tell people that a decision has yet to be made.

***Step 5: Review and refine***

Continue to review and refine the plan on an ongoing basis until the consolidation is complete and the exit criteria are met. Typically, this step takes place for some time after the initial plan has been completed to address any issues or opportunities that arise during the consolidation process.

**Key factors for M&A success**

In summary, there are several key success factors to consider within a merger or acquisition situation. The first involves identifying whether the merging or acquired organization has a common culture or common values. Identifying and filling culture and value gaps will make the new operation much easier to manage. Also build a vision for how the business will operate post-merger, and a plan for how to get there. Be sure to create buy-in from employees, agents and clients for this new vision.

Also important is the examination of consequences for systems and data. In insurance, data is king. Continuing to run siloed systems will hamper the team as they struggle to get a handle on the data needed to run the new, larger business.

Another key to success is to pick a strong partner to serve as a guide and extra set of hands during the reorganization process. For companies going through the merger and acquisitions process, there's no substitute for real-life experience. Beyond all of the legal work and accounting changes lies a veritable minefield of cultural and organizational change. Pick a partner that understands organizational change and has the experience needed to manage both the human factors and the business processes and technology issues.

Once the plan is created and execution begins, review and reassess at each stage. This creates a flexible plan that can quickly change course to adapt to challenging situations and to take advantage of new business opportunities. In the end, a focused vision and plan can make the difference in more quickly and efficiently achieving new levels of earnings growth.

### **About CGI**

Founded in 1976, CGI is a full-service IT and business process services provider with 25,000 professionals operating in more than 100 offices around the world. CGI's insurance practice includes 3,800 professionals dedicated to providing a full range of services, from IT infrastructure management, legacy system maintenance and systems integration and development to business process management in areas such as claims, document management and vehicle inspections. This full-service offering is combined with our deep industry expertise to provide clients with a true strategic partner that knows how to use technology to achieve business goals. This blend of capabilities and know-how has earned CGI the distinction of being one of the top-10 IT services providers to the insurance industry as identified by Insurance and Technology magazine.

To explore consolidation issues and how we can help, contact Mardee Brosh CPCU, Executive Consultant, at [mardee.brosh@cgi.com](mailto:mardee.brosh@cgi.com).