

## Fraudsters Love Digital

### An Emerging Threat Missed on Many Insurers' Digitization Roadmaps

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#### ABSTRACT

In most financial services companies and at almost every conference, there is a real buzz around digital transformation programs and digital disruption initiatives that will significantly impact, if not reinvent, many insurers and their business role today. This is all seen as positive and good, helping to deliver new and improved service levels, broaden appeal, and potentially reduce servicing costs.

So, for the vast majority of customers this is good news. But it is also good news to the small minority (perhaps up to 10% of claimants) who are looking to actively defraud the insurer. In this presentation, we explore the need to build in suitable safe guards to ensure that the rise of the armchair fraudster doesn't go unchallenged. The presentation illustrates how insurers are embracing real-time fraud analytics to help them in this fight—but without compromising the good that such programs deliver for the majority of customers.

#### INTRODUCTION

Looking back to the 1960s, the most common way of buying and servicing insurance customers in the UK was via the visit from the “Man from the Pru” to collect the monthly premiums for life, motor, and home insurance. Indeed, an old Prudential advertisement claims that they regularly visited some six million British homes. This face-to-face approach was there to provide helpful and practical financial advice—from a family friend.

Times change, and in most countries, there has been a gradual removal of this “home service” distribution channel. It was relatively expensive, hard to manage, dealt in cash, and offered poor value to customers. Ultimately, Prudential got caught up in a major pension scandal in the 1980s, which was almost certainly the last nail in this channel's coffin.

Moving into the 1990s, we saw the rise of telephone direct insurers, which helped put the emphasis on reducing the policy premium specifically for motor and property insurance through its lower operating cost model.

At the turn of the millennium, insurers started to replace their “brochure websites” with the ability to solicit take out new business directly online. And, more recently, we have seen the rise of the insurance aggregator in many countries, enabling customers to load their insurance needs once into a website and in seconds receive quotes for their insurance from potentially hundreds of insurers.

Fast forward to today, and the trend for many insurers is to digitize more of the insurance process including allowing mid-term policy adjustments, claims notifications, and claims updates through their corporate web interfaces and mobile apps.

#### DIGITAL TRANSFORMATION AND DIGITAL DISRUPTION

For most insurers, and at almost every insurance conference, there is a real buzz around digital transformation programs and digital disruption initiatives that will significantly impact, if not reinvent, many insurers and their business role today.

As with many new paradigms, it's hard to firmly pigeon hole exactly what this means for each insurer (and each program), but we can summarize this move as follows:

- Moving beyond just a digital distribution channel to incorporate a range of digital technologies within and across the insurance process
- Seeking out new opportunities outside the standard insurance business model—for example, becoming “risk managers” for their clients and not just the insurer
- Mapping out and managing the customer journey across the lifecycle of the engagement with the insurer

The emergence of the second wave of motor telematics, the bundling of home insurance with sensors for fire, smoke, water, escape, and so on, to truly protect the home and the provision of mobile apps that can help marry a customer’s health and fitness to lower premiums for health insurance, are all great examples of digital transformation and disruption programs now in place with many insurers.

Digitization and digital disruption programs are now engrained in the insurance culture – with an overall positive impact for both the insurer and the insurer’s customers.

## PUTTING THE CUSTOMER AT THE CENTER OF THE INSURER

In this evolving new world of insurance, it is a clear priority for every insurer to both retain and grow their customer base. That is, the insurer is to “look after” the customer in ways that can only seem like a return to the values of the old home service agent, but without the operational cost.

Terminology such as “managing the customer journey,” “enriching the customer experience,” “a customer-centric view of the organization,” and “an outside-in view of the organization,” all fit within this nomenclature around this key business topic. Many insurers are now investing heavily in their websites, operational systems, processes, and, of course, their people, to make this happen.

But what about the fraudster?

## INSURANCE FRAUD – IT DOESN’T SEEM TO BE GOING AWAY

Statistics published in the Netherlands in 2013 by the Verbond Van Verzekeraars<sup>1</sup> suggest that insurance fraud has increased by 25% in the last five years, adding €150 to the average policy. Figures released from the Agence pour la lutte contre la fraude à l’assurance (ALFA)<sup>2</sup> suggest that in France alone insurance fraud is a €2.5 billion per annum problem. There seems to be broad consensus across similar organizations like the VvV and ALFA that globally 10% to 15% of all insurance claims include an element of fraud. And the FBI estimates that fraud costs US insurers as much as \$40 billion per year<sup>3</sup>.

Added to this an increased concern for many insurers over the level of application fraud where customers play the system to reduce the premium that they pay (and sometimes to have risk accepted), and the rise of new fraud types such as “Ghost Broking.”

Fraud remains a big issue.

## FRAUDSTERS LOVE DIGITAL

There is no doubt that some of the significant transformation programs that are ongoing on within insurers will help combat some insurance fraud types. So for example, the second wave of motor insurance telematics including the regular monitoring of where the vehicle is, how it is being driven, the speed it is going, and so on, will make it significantly harder for some fraud types to happen such as car theft and staged accidents.

But the concern is that increasing focus on digital technologies seems to further remove experienced insurance staff from the customer, where they would normally be introducing, holding, and managing that relationship, and replacing staff with easy-to-use web pages. Digital technologies seek to remove the ability for “human interaction” within both the new business stage and the claims process. While from a

cost-benefit aspect this makes sense, not many insurers have thought through the potential impact on fraud rates.

We've called this paper "fraudsters love digital" because we know that organized criminal gangs and individuals or households who deliberately invent or expand claims will invest their time and experience to understand how best to exploit any perceived weaknesses in the insurer's ability to defend itself against fraud. Once this is understood and fraudsters have worked out how best to do this, expect them to quickly act—velocity of fraud is on the rise. Some insurers underestimate the sophistication of these fraudsters and their dedication to crack the system.

## THE RISE OF THE ARMCHAIR FRAUDSTER

With digitization the key question is: Are we making it too easy for premeditating fraudsters to make claims or introduce new business from non-existent clients or from those who have had their details significantly changed, possibly from their armchair, but almost certainly from their laptop or tablet?

Digitization also makes it easy for opportunistic fraudsters. For example, it's now easy to manipulate a motor insurance quote when sitting in your armchair. So, for example, changing rating factors such as annual mileage, or kilometers driven, or where a vehicle is kept overnight can significantly reduce the quotation. Similarly, when there is a real claim, it's easy from the comfort of an armchair to add a few additional items to a property claim, or to increase the value of a damaged or stolen item.

A number of claims managers have expressed concerns that their digital programs are not looking at the full spectrum of clients. And we have heard a number of reports from insurers, that after going through a digitalization program, the claims incidence has increased significantly. They can't be certain that this unwelcomed uplift is due to fraud, but it seems likely that this could be a significant factor.

But let's be clear: For the 90% of genuine and honest customers who file a real claim, we want to ensure that they get the very best service possible. And many digitization programs are looking to address exactly this and should be applauded.

But what about the 1 in 10?

## TACKLING FRAUD IN THE DIGITAL AGE

Insurers are already embarking on some ground-breaking projects such as identifying the IP address of an applicant or claimant's laptop or tablet and looking for repeats. And this has helped stem some of the tide.

But what if we could use the data that exists within the insurer to progress the claimant or new business applicant down a specific path? Straight Through Processing (STP) has been around for many years now, but what if we could have real confidence that those claimants who were going down an STP route were part of the 90%, not the 1 in 10?

Fraud analytics can be used to help steer the customer journey. We can use real-time analytics to work out which claimants should go through the STP channel, or be automatically accepted as new business, and which claimants or new business applicants we might want to have an experienced insurance person talk with.

We can automatically look at a new business application to see if it would "fit" into a known high-scoring fraud ring, and then pass this for further action.

We can see emerging threats and trends, based on the insurer's data that would enable the insurer to be ahead of the next fraud wave.

## DOES ANALYTICS REALLY WORK?

In 2016, SAS worked with the Coalition Against Insurance Fraud on a survey of US insurers. And 61% reported that the number of suspect frauds against their company had increased over the past three years. The survey revealed that now 76% of US insurers are using fraud technology to aid them in detecting suspect claims, an increase from 65% from a similar survey conducted in 2012. More than half of insurers are now using predictive modeling, and that technology is producing more referrals and better-quality ones.

The expanding SAS global customer base shows that our customers are gaining true value from the use of analytics.

- **Allianz** in the Czech Republic identified 1.161 extra insurance fraud cases worth more than CZK 62 million in the first six months after implementation. They were able to investigate 26% more cases with the same resource and submitted 40% more proven fraud cases for criminal prosecution.
- **Alm Brand** is one of the largest motor and property insurers in Denmark. They adopted the SAS solution to complement their existing well developed SIU function, and it now makes up a significant proportion of the €5.3m saved annually due to fraud detection.
- **Ethniki** is the largest insurance company in Greece and part of the National Bank of Greece Group. With the economic situation in Greece, combating increasingly sophisticated fraud schemes was becoming a major need. So Ethniki has deployed the SAS for Insurance Fraud in real time. In the first 14 months after implementation, the company has doubled the amount of fraud detected. Heracles Daskalopoulos, Deputy General Manager, commented: "The benefits we've gained with SAS have already exceeded the cost of investment. We now have a holistic strategy to our fraud management approach. We're able to evaluate things differently and more thoroughly than before, and it's given us the momentum to modernize our operations."
- **Česká pojišťovna** is the largest insurer in the Czech Republic and part of the Generali Group. They were one of our early insurance fraud clients, licensing the software in 2011. They are making good use of all of the components of the SAS for Insurance solution, including using the solution in real time for some lines of business. "By using SAS Fraud Framework for Insurance to analyze all new policies and detect suspicious new contracts, Česká pojišťovna has saved tens of millions in Czech crowns each year," says Zdeněk Dragoun, Fraud Analyst in Česká pojišťovna's Fraud Detection Department. "Additionally, we have been able to uncover cases of insurance fraud totalling 20 million Czech crowns (\$820,000 USD) annually that would have otherwise gone undetected."
- **Sigorta Bilgi Merkezi (SBM)** is an insurance consortium providing a cross-carrier fraud detection program initially for the Turkish motor insurance market. In total, SBM has 60 members and details on approximately 20 million insured vehicles. After the first 9 months, SBM had identified 259 million Turkish lira in suspicious fraud rings, equating to \$86 million USD.

## CONCLUSION

Insurers using digital transformation programs to truly place the insurer at the center of the insurance company should be encouraged and long term will be the winners.

But those insurers who do not take the continuing threat of insurance fraud seriously and build in to their digital programs suitable safeguards will not escape the threat of increasing claims incidence and falling underwriting results due to fraud.

Digitization—it really is about the 90% of good customers, but let's not forget the 1 in 10.

## REFERENCES

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<sup>3</sup> FBI. "Insurance Fraud." Accessed January 5<sup>th</sup>, 2018. <https://www.fbi.gov/stats-services/publications/insurance-fraud>

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<sup>9</sup> SAS Institute. "Cracking down on insurance claims fraud." SBM. Accessed January 5, 2018. [https://www.sas.com/en\\_us/customers/sbm-tr.html](https://www.sas.com/en_us/customers/sbm-tr.html)

## RECOMMENDED READING

- *Fraud Analytics, Using Descriptive Predictive and Social Network Techniques*. Baesens, Van Vlasselaer and Verbeke. Wiley.

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