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ADVISORY CONSULTING

AI GOVERNANCE IN P&C INSURANCE

ADDRESSING CONCERNS IN A RAPIDLY EVOLVING AI LANDSCAPE

A ReSource Pro Research Report

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ABOUT THIS RESEARCH REPORT

Welcome to ReSource Pro's report on AI governance, covering enterprise AI management and responsibility in the evolving P&C insurance landscape. The report is based on ReSource Pro's observations and a survey of carrier executives.

For more insights, read our companion reports "Artificial Intelligence in P&C Commercial Lines," "Artificial Intelligence in P&C Personal Lines," and "Generative AI in P&C Insurance: Promise and Perils for Personal and Commercial Lines." Contact us to learn more.

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ReSource Pro Insights offers a broad range of research and observations on the insurance industry. We provide substantial studies, analysis, and perspectives on business and technology strategies and plans across the P&C ecosystem, covering retail agencies and brokers, MGA/wholesalers, carriers, and tech vendors. Our coverage includes distribution, underwriting, policy servicing, billing/payments, and claims business areas, as well as cross-enterprise areas such as strategic initiatives, digital transformation, innovation, customer experience, and talent.

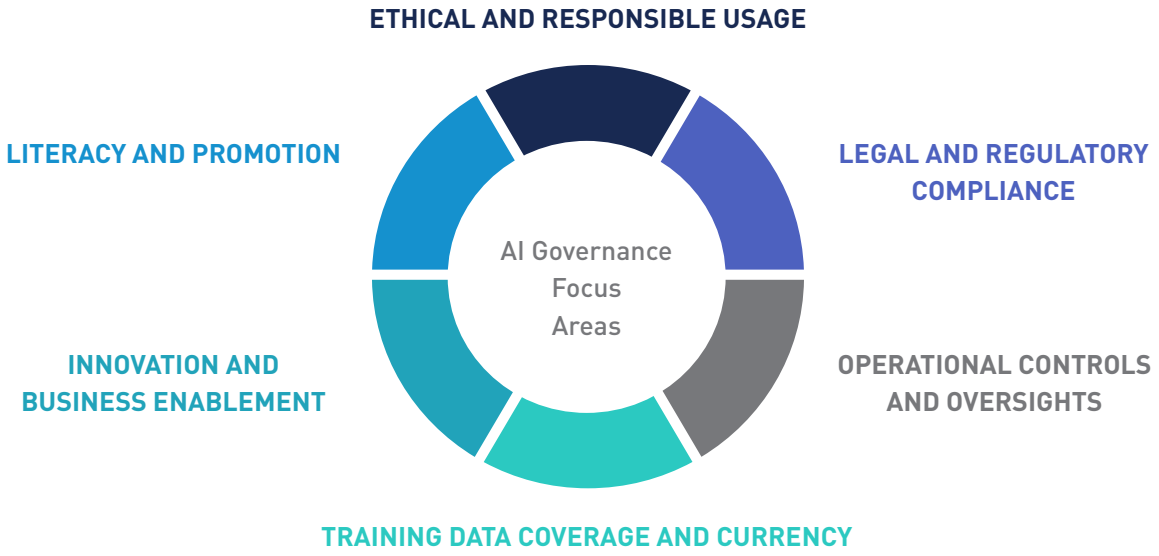
ARTIFICIAL INTELLIGENCE GOVERNANCE: KEY CONSIDERATIONS

Artificial intelligence (AI) is advancing at a rapid pace, bringing with it tremendous opportunities and challenges across the insurance industry. While the insurance industry has been using AI tools for many years, the democratization of AI through the recent emergence of new tools based on generative AI (GenAI) has accelerated the potential for broader use. This widespread transformation requires insurance businesses to create robust governance frameworks around AI development and implementation.

AI governance is a set of processes, protocols, guidelines, directives, tools, and frameworks to foster business innovation while ensuring the legal, ethical, transparent, and responsible use of AI throughout its lifecycle from development to deployment, evolution, monitoring, and eventual retirement.

Effective AI governance aims to address six core areas of focus, as listed in Figure 1 below.

Figure 1. AI Governance Considerations



Concerns about ethical violation, transparency, and explainability, along with the introduction of bias, were the early considerations regarding the use of AI in insurance processes. Legality and regulations specific to AI use are still being formulated. In the interim, the industry has focused on the Unfair Trade Practices Act and laws for consumer protection, which address these concerns. With the introduction and explosive growth of generative AI use, considerations arose around the technology, including issues with improper or offensive content output, hallucinations[1], and accuracy of results. AI technologies are dependent on the currency of the training data along with how the model approaches content creation, with oversight of the process required to ensure accuracy. Insurance companies must also consider innovation and how AI use cases can transform current insurance processes. At the center of these considerations is the role humans have in all aspects of AI development, use, and monitoring. Governance of the AI process is key to addressing these concerns by providing guidelines and structure to use the technology while maintaining the active role of humans in the loop.

[1] According to IBM, AI hallucinations is a phenomenon wherein a large language model, such as GenAI, perceives patterns or objects that are nonexistent or imperceptible to humans, creating outputs that are nonsensical or altogether inaccurate.

The scope and influence of AI permeate the organization and touch all aspects of the business, including operations, technology, data, legal, regulatory compliance, and risk management. Accordingly, the scope of AI governance must be seen in conjunction with other existing organizational governance models, such as corporate governance, portfolio/program governance, technology governance, and data governance.

AI REGULATIONS

The US government and other regulatory bodies have released several orders and guiding documents in recent years to establish the standard of AI use in the insurance industry and across society as a whole, including the following:

- The NAIC's Principles on Artificial Intelligence document in 2020 and the formation of the NAIC Big Data and Artificial Intelligence (H) Working Group.
- President Biden's Executive Order released in October 2023 established new standards for AI safety, security, privacy, and equity.
- The NAIC Model Bulletin on the Use of Artificial Intelligence Systems by Insurers, published in December 2023, recommends that insurers establish an AI System (AIS) Plan to "address governance, risk management controls, and internal audit functions."

CARRIER APPROACHES TO AI MANAGEMENT

Insurers have been experimenting and using AI tools for decades. Data and analytics teams at leading carriers have developed advanced AI expertise, with many deploying AI in underwriting and distribution functions in addition to other business areas. Now, with the recent rapid expansion of AI and GenAI, AI tools are being considered for a much broader set of use cases across insurance enterprises. This has led to complexity in managing AI tools and models and a greater focus on developing governance and management of AI use.

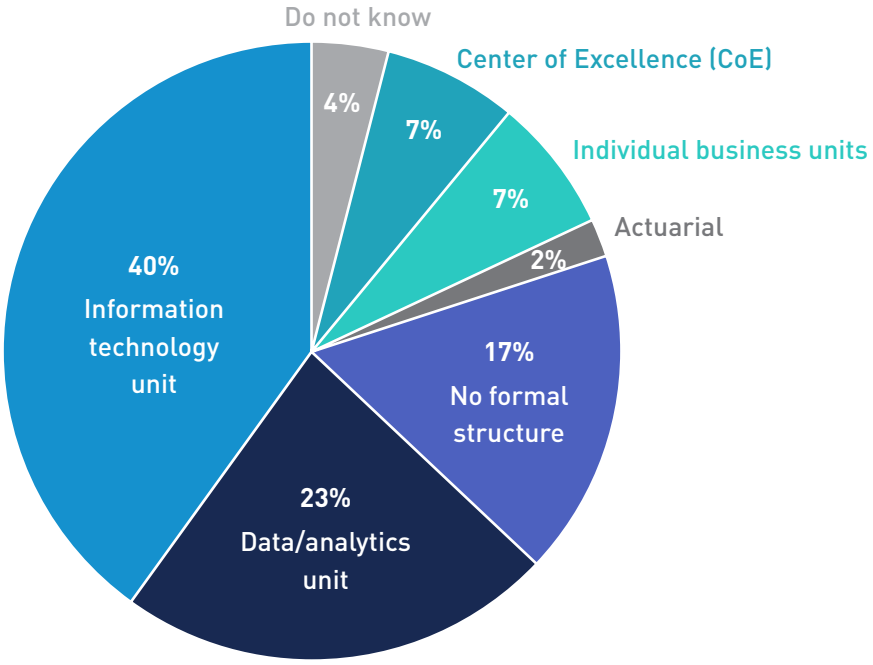
AI MANAGEMENT RESPONSIBILITY

For most insurers, planning and management functions are incorporated into current management and governance functions – primarily IT and data/analytics (Figure 2). Since these are established governance frameworks, they provide a readily available structure by incorporating AI as a technology or as part of the data and analytics strategy. It should be noted, however, that more personal lines carriers direct AI responsibility to their data/analytics units, with slightly fewer granting IT units responsibility. This is reversed on the commercial lines side, with more carriers delegating AI planning and management to IT units, followed by data/analytics teams.

However, 26% have no formal structure or rely on governance at the actuarial or business unit level, with 4% stating "do not know." A lack of clearly defined roles, responsibilities, and governance models for AI across the enterprise (including business units, IT, data & analytics, actuarial, compliance, risk management, etc.) can lead to inconsistencies around decision-making and challenges in keeping up with innovation and regulatory changes.

AI planning and management needs will extend to stakeholders across the enterprise. While current governance responsibilities may be seen as a subset of IT or data management, governance may require participation beyond what is needed for these areas. Some insurers (7%) have approached AI governance with a centralized CoE approach, which can better assure participation from all functions in the organization.

Figure 2. Business Areas Responsible for AI Planning and Management at P&C Carriers



Source: AI in P&C Insurance in 2023 and Beyond (n=53)

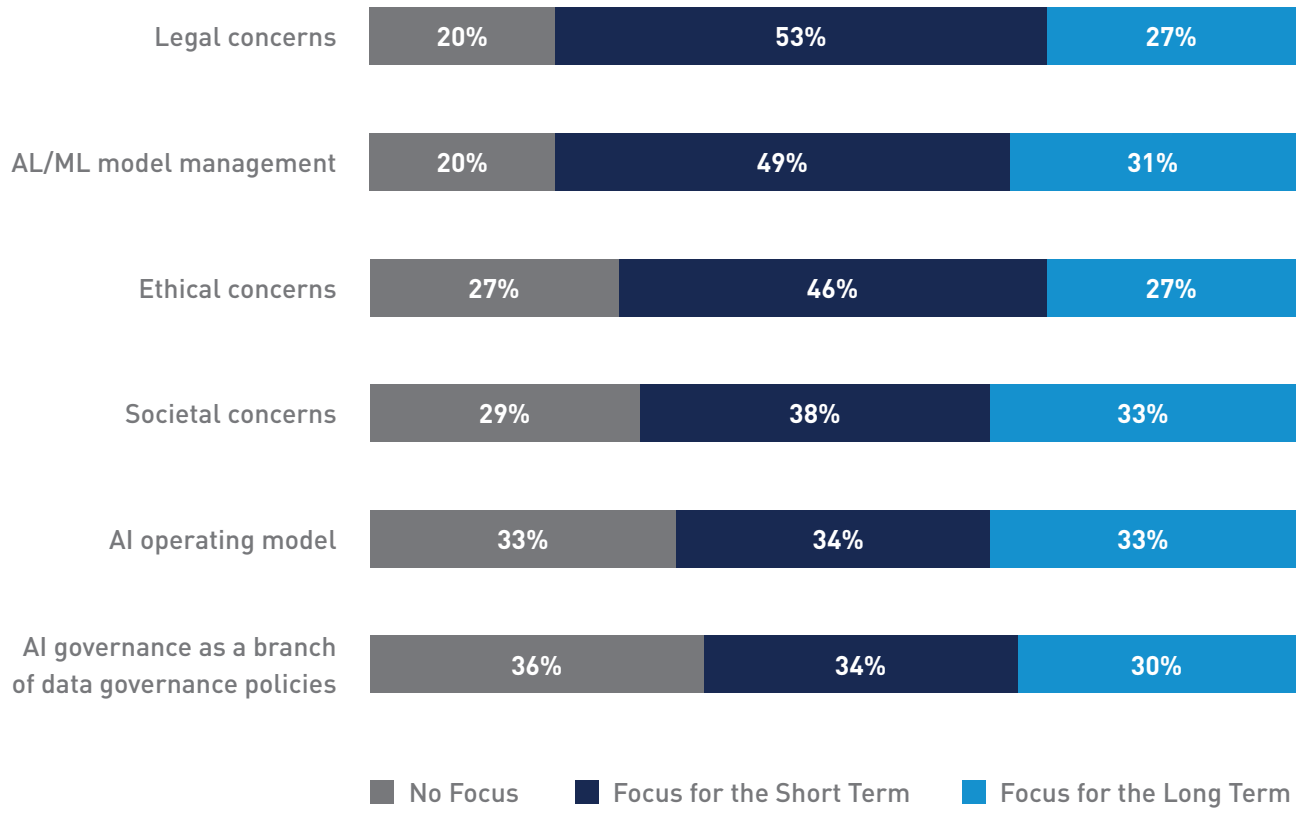
GOVERNANCE PLANS AND CONCERNS

In the short term, most carriers' primary concerns regarding AI revolve around operational areas, including legal/compliance worries and how to manage AI and machine learning (ML) within the organization, as shown in Figure 3.

Regulatory concerns and the broader use of AI are driving the need to better manage AI/ML models across functions and use cases in the organization. With the increased use of AI tools and models, carriers are facing challenges in keeping track of various regulations, including new versions, state variations (testing, regulatory review, status of state laws, etc.), and performance/results. In addition, the rise of GenAI has raised concerns around pending regulation and the expected follow-up rules and regulations to the Executive Order issued in late October 2023 and the NAIC Model Bulletin released this past December. Currently, there are few software solutions available for managing the complexity of AI model management.

Next, insurers are focused on ethical and societal concerns. These are broader and more external concerns; therefore, they are more difficult to address. However, the more practical concerns of developing an AI operating model and developing governance are not a focus for about a third of carriers. Also, carriers are paying the least amount of attention to these areas in the short term. It could be argued that developing an AI strategy, operating model, and governance are necessary to better address the concerns insurers currently emphasize for their short-term focus.

Figure 3. Carriers' AI Governance Plans and Concerns in the Short and Long Term (Ranked by Short-term Plans)



Source: AI in P&C Insurance in 2023 and Beyond (n=53)

MANAGING AI RESPONSIBLY IN A DIGITAL ENTERPRISE

Broadly speaking, insurers can consider three possible organizational archetypes to govern and manage AI responsibly.

CENTRALIZED

A centralized team is responsible for developing, managing, and supporting all enterprise-level and functional-level AI solutions.

DE-CENTRALIZED

Each functional team is responsible for developing, managing, and supporting its own AI solutions.

FEDERATED

A hybrid model with a centralized AI center of excellence team working in conjunction with various functional-level teams developing, managing, and supporting AI solutions.

Figure 4. AI Organizational Archetypes

CENTRALIZED MODEL

- Centralized team typically led by a CAIO (Chief AI Officer) or CDAIO* (Chief Data & AI Officer).
- All domain-specific and aggregated enterprise-level AI needs are supported by this centralized team or department.
- Centralized and consistent AI practices, tools, governance, and talent management.
- Simplest, least ambiguous, and easy to manage/govern.
- Tend to be more reactive, less flexible, and may lack domain/functional area-specific knowledge.

DE-CENTRALIZED MODEL

- Each domain/functional area has its own AI team.
- Each team is responsible for envisioning, developing, supporting, and managing its domain/function-specific AI solutions and the underlying training datasets.
- Tend to be more proactive, flexible, and specialized.
- Can be unwieldy, ambiguous, and difficult to manage/govern enterprise-wide.
- Can result in disparate and inconsistent AI practices, tools, governance, and talent management.

FEDERATED/CoE MODEL

- A centralized team establishes and advocates consistent practices, tools, governance, and talent management across the enterprise.
- Aggregated/enterprise-level AI and analytics supported by a centralized team, while domain/function-specific needs are supported by decentralized teams.
- Provides many of the advantages of both centralized and decentralized models while simultaneously avoiding some of the disadvantages inherent in both models.

**Note: Most AI solutions require access to relevant, high-quality, and reliable training datasets while in compliance with various data privacy and protection laws and regulations. The Data Governance discipline plays a critical role in ensuring that the datasets used by AI meet these requirements. It is not uncommon in other industries, and we expect it will become more common in insurance, to see this dependency between AI Governance and Data Governance reflected in the convergence of the two disciplines under the leadership of a newly emerging CDAIO (Chief Data & AI Officer) role.*

As described in Figure 4 above, each organizational archetype offers a unique set of advantages and disadvantages depending on the size, maturity, and complexity of the organization and the envisioned role of AI in the near and long term. Accordingly, insurers may find it beneficial to adopt one archetype over the others.

Given the nascency of AI and various legal, regulatory, and ethical issues surrounding AI, the centralized model is recommended, and most small and mid-size insurers would find it more appropriate. Larger organizations, or those that achieve a sufficient level of governance maturity, could consider the use of the federated model. We don't recommend the de-centralized model for most situations.

Although AI governance is distinct from data governance, technology governance, and other related disciplines, all areas should work in alignment/conjunction with each other to create and adopt principles and guidelines.

CALL TO ACTION

As AI use expands in insurance organizations, insurers need to prioritize the development of an AI strategy, operating model, and governance framework. While our research shows that AI management is currently owned by the IT or data/analytics teams at most carriers, AI governance should be developed as a separate governance domain. Some considerations when implementing AI governance include:

- **ENSURE AWARENESS AND BUILD A CASE FOR CHANGE**

  Adding a governance framework requires effort and acceptance of the change by a broad group of stakeholders. The ability to explain why AI governance is necessary and how it benefits the organization can help reduce resistance to change and build acceptance. The organization needs to consider AI governance not as an IT project but as a business-led effort enabled by technology.

- **START WITH THE MOST IMMEDIATE USE CASE**

  Beginning with a specific use case will enable an agile approach to developing the governance framework. It will also keep the scope limited and manageable in the early stages of developing governance practices.

- **BUILD OUT CORE ELEMENTS INCREMENTALLY**

  Start small but think big when implementing governance. Develop ways to measure the effectiveness of AI governance and course correct as use cases and framework elements are added. It may be helpful to introduce and utilize enterprise governance tools as the framework progresses.

- **ENSURE ADOPTION, COLLABORATION, AND BENEFIT REALIZATION**

  Ensure emphasis is placed on building trust and collaboration rather than promoting a control and compliance culture. Leverage success measures to promote the realization of expected benefits. As the framework is put into place, build maturity of the governance process by learning from experience.

As AI governance matures, keep in mind that ethical and social concerns will continue to evolve, along with regulation and innovation. Continue to monitor AI regulations and review your governance process to ensure current and future compliance. Involve both internal and external stakeholders to review and address ethical and societal concerns, which can lead to regulation and possibly affect the acceptance of AI in your organization or by your customers and other stakeholders. Stay updated on industry developments and use cases by other carriers and solution providers, not only for implementing and using AI in your organization but also to inform the AI governance process and to provide input on best practices.

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ReSource Pro

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