



## DST Invests \$9M in New Annuity, Insurance Unit

By Jackie Noblett

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**DST Systems** will invest up to \$9 million this year to launch DST Insurance Solutions, a new business unit focused on serving insurance companies and variable annuity providers.

The back-office technology provider disclosed April 19 that it formed the unit to provide payout processing and client servicing to insurance and annuity policyholders.

The unit is not expected to generate revenue until 2012. The firm is using this year to adapt the technology to the North American annuity structure as well as hire staff with specialized insurance expertise.

The firm intends to roll out the service beginning with annuity payout processing, but will also offer capabilities in servicing the new business accumulation and reporting functions of annuitant services, in the same vein as its transfer agency business for mutual funds, officials say.

DST Insurance Solutions aims to capitalize on what is expected to be increased pressure on annuity providers' back offices in the coming years, as large numbers of baby boomers use annuity payouts for retirement income. In addition, many of DST's existing clients are also looking to get into the annuity business in order to keep clients that are moving from an asset accumulation phase to spending down those savings, said CEO Thomas McDonnell in the company's most recent earnings conference call.

While mutual funds, DST's main line of business, have almost universally accepted outsourcing and third-party back-office servicing, insurers and VA providers have traditionally kept control of their operations. DST estimates upwards of 95% of annuity providers keep processing in-house.

But the timing of the annuity service's launch coincides with a changing view on back-office operations among annuity providers, says Bonnie Wasgatt, president of DST Insurance Solutions. "Cost is certainly a driver, but in addition to cost, they are looking at what are they good at and what are they going to focus on."

The launch also coincides with a period of declining mutual fund accounts for DST. During the first quarter, three fund clients informed the firm that they were dropping DST as a service provider. Those three firms represent 1.6 million registered accounts and 8.4 million subaccounts.

While variable annuity assets reached a record high of \$1.5 trillion in 2010, the real stress for annuity back offices will come if retirees increasingly look to roll over defined contribution assets into annuities and begin payouts.

"At a high level, the stage is set for more payouts and for a need to scale up a capability for annuitization of policies and payouts," says Clark Troy, research director at **Aite Group**. "It's fair to say that most, if not all, areas of life insurers' back offices are opportunities for the outsourcing and upgrading of many core functions."

In addition, the arms race among insurers to meet retirement income needs with new annuity products and features may also be stretching operations resources thin.

"It's all about product proliferation," says Karen Pauli, research director in **TowerGroup's** insurance practice. "The new retirement products, particularly the ones that have an income payout, and the fact that retirement products are way more complex now than they ever were makes the carriers really need to find efficiencies wherever they can."

More processing options, fund options and guarantees inside annuities, combined with a demand for speedier product manufacturing and launches, are causing the operations and technology infrastructure to show its age. Not only is the technology aging, but so are the staff running those systems and servicing annuitants, analysts say.

Key to DST's new business offering is new payout processing and recordkeeping technology acquired in June by **International Financial Data Systems** — a United Kingdom-based joint venture between DST and **State Street**. The more modern, rules-based technology along with integration and communication capabilities will make product introduction faster and less costly, Wasgatt says.

DST will license the software from IFDS and ultimately be able to integrate it with DST's other technology platforms for insurance companies either on a hosted basis or, in conjunction with **Boston Financial Data Systems**, in a business process outsourcing agreement. Wasgatt says different annuity providers have different operational strengths and capabilities, which is why it is important to offer different delivery methods for the service.

Indeed, analysts say one of the greatest opportunities for service providers is to act as a bridge while annuity providers scale up their servicing capabilities. In that process, a carrier can test the technology and people capabilities of the service provider to see whether they want to continue the relationship on a permanent basis, says Pauli of TowerGroup.

DST declined to comment specifically on client interest or opportunities in the U.S., but some 15 insurers use the recordkeeping platform with IFDS in Europe, Wasgatt says. In the conference call, McDonnell said the firm's focus is carriers with more complex products, particularly variable annuities.

"The revenue characteristics in this are substantially better and more attractive than what we see in the mutual fund arena," he said.

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