INSURANCE, A BUSINESS, WHICH WITHOUT A WELL-STRUCTURED INTERNAL CONTROL IS DOOMED TO FAILURE

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Abstract

In the context of insurance-fraud growth and financial-accounting and management shortcomings, as well as of the amplification of irregularities in contracting and administering insurance, and of the economic crisis in Romania, we believe that the activities of internal-control systems and foremost those belonging to the financial control management, as well as those of combating fraud and payments of unfair compensation, should all be refocused mainly by conducting measures and activities specific for the defense of funds by preventing, discovering and combating irregularities meant to affect the assets of insurance companies, the unfair-compensation payments, by combating fraud and discovering irregularities and abuse in the activities of employees.

As such, the knowledge and the discovery of these depend largely on the organizational structure of internal control, the attributions conferred upon it, organized actions and the interest and importance, which the leadership granted to the control activities.

Key words: *corporate governance, control, principles, insurance, objectives*

1. INTRODUCTION

In the new generated context, both in business and in the public sector, new directions of entity-management have appeared, based on reconsidering how these entities can manage their evolutionary new circumstances.

Knowledge, assessment, monitoring and controlling of past influences and potential future events that may have a negative impact on the activity of insurance companies, cannot be achieved smoothly without the existence of systems of internal-control and risk management.

Without the organization and functioning of the internal control, the financial-economic activity of an entity cannot be known and pursued, the irregularities of the contracting and insurance administration cannot be identified and removed and the so needed self-protection of the company's funds and cash cannot be achieved.

The achievement of the objectives and economic - financial indicators, the cost-reduction and profitability of the insurance company largely depend on the way in which the attributes and duties of the internal control systems are established and defined.

As such, in each and every insurance company there are multiple systems of internal control operating, which, in one form or another, pursue economic activities, according to the laws-in-force and internal rules that govern the insurance companies.

According to current legislation and regulations issued by the Insurance Supervisory Commission, the internal control systems, financial control, financial control management, combating fraud and improper payments of compensation, controlling, internal audit, risk management etc. are aimed mainly at: the compliance to financial - accounting and management regulations, the correct application of the rules on contracting and managing security, compliance to the methodologies investigating the claim and damage-payment files, to fraud combat and the payment of compensation undue risk management, control and compliance to business processes of the insurance companies and subordinate branches etc.

Although almost all internal control systems are regulated by legislation and internal regulations of the insurance companies, some of them, such as the financial control; the financial control management; the investigation and damage verification, and the control and the internal audit are often confused with each other, being considered to be too numerous and having the same duties and tasks.

It is set-context, it is necessary to clearly define the concept of control and to present some of the features that are specific within insurance companies.

2. INTERNAL CONTROL SYSTEM, COMPONENT OF CORPORATE GOVERNANCE

2.1. Corporate governance and its principles

The issue of governance, far from being a new problem, continues to stand in the spotlight since entities have not learned anything from the bankruptcy of companies from different corners of the planet.

The term governance derives from the Greek verb "να κυβερνήσει" (Kubernân) which means "to steer a ship or a tank." Plato used this term, and then, up to the end of the eighteenth century, it was used as synonymous with the term "government".

"Because we cannot abuse power, said Montesquieu, be that through natural arrangement of things power leads to power". This aphorism of the eighteenth century aims, without a doubt, the public institutions, but there is every reason to believe that it can and should be also applied at the level of economic entities.

The most usual definition of governance belongs to Wikipedia, according to which, governance of an entity, be it a public or a private entity, designates a mode of operation of the assembly-organs and decision, information and monitoring rules, so that to enable beneficiaries and partners that their interests are respected and their voices are heard in the entity.

The concept of corporate governance, as perceived today is Anglo-Saxon as origin and it knows several definitions, including:

- is "the system by which companies are directed and controlled" (A. Cadbury, 2002);
- is "the system of relations between directors and shareholders in a company" (Monod and Foucard);
- is "the search for the best possible balance of powers in the enterprise"

We note that corporate governance results from the need to reconcile multiple interests, often conflicting, in companies, especially those between shareholders and managers.

Corporate governance issues arise from the separation made between ownership and control of capital, certain shareholders' disproportionate power, their control over minority shareholders, employees who hold important rights separate from those that are triggered from their being capital holders.

Corporate governance is part of a perspective of the agency, i.e. a contract by which one or more persons (main) engages another person (agent) to perform some service on their behalf, involving the delegation of part of decision-making authority to the charged agent. According to D. Carassus and N. Gardes (2005), based on the findings of incomplete contracts, asymmetric information and divergences of interests, the agent relationship is problematic to the extent that the agent is likely to take advantage of these situations to the detriment of the main.

Therefore, the issue of control is linked to a delegation of responsibility, thus involving the control of the one receiving this delegation. Control aims to limit deviant acts and to maximize the benefits of the shareholders, when the manager is managing information (Figure No. 1)



Figure 1. The operation of corporate governance

For the last ten years, several principles are outlined, principles that underpin corporate governance, as cited by Michel X. et al. (2009 pag.211-212) as follows:

- **prevention principle** - principle including actions to eliminate or reduce the hazards of a risk. This principle applies only where scientific certainty or probability of risk is known and objectively accepted;
- **precautionary principle** - discusses use of a product or a service when there is an assurance that there is no danger for the user or consumer;
- **principle of respect for laws** – bringing laws and regulations and their implementation in companies. The legal system allows the proper functioning of the entity and the strong impact of preventive and precautionary principles;
- **principle of responsibility** - develop better communication and training thus different actors at all levels become aware of their responsibilities;
- **principle of transparency** - provides access to information. This principle consists in giving spontaneous information, of general interest, to the public in order to pursue an active policy of information;
- **principle of solidarity** - involves participation in a common, rewarding cause and the acceptance of the fact that there is the right to access and use their natural resources without compromising the sustainability of future generations;
- **the principle of participation** - involving all actors of civil society, as part of governance and therefore in the decision-making process;
- **the principle of integration** - calls for hiring a global approach rather than sectoral one and forces a simultaneous and interactive reckoning of various economic, social, societal, environmental and organizational dimensions;
- **the principle of economy and sound management** - aimed at saving non-renewable resources and using the most advanced techniques possible at an economically acceptable cost.

D. Bakkour (2013, p.11) points out that these principles give an impression of completeness, but in reality they are not enough, which is why additional principles are needed, such as the principle of sustainable development and risk management.

2.2. The concept of internal control, its models and the types of control

Internal control has its origins in history of accounting, dating back to ancient times and it has evolved with it. We are making this statement because, along with the development of accounting principles and methods, a series of means and measures had to be settled for, measures, which ensure the reliability of information and records.

Looking into history, cross control was one of the most used means in accounting clearance (comparing information from two sources independent from each other). If the Sumerians were checking the number of bags of wheat entering the warehouse with the number of wheat-bags delivered by farmers, Pope Nicolas requested a duplicate of record revenue and expenses to verify the correctness of his own accountant.

Therefore, shared responsibility is a principle known since Roman times obliging Quaestors to take account of public funds and justify them to the Senate.

Intended to prevent the risk of fraud, these were the first forms of control that gave rise to what was later called, internal control and financial accounting.

The evolution of societies along the time had an impact on the management of enterprises, which has become increasingly complex and launched the struggle for competitiveness, context in which we can talk about the stakes for performance, the number revolution (the emergence and development of information systems), the emergence and development of communication systems, the development of legislative requirements, the increasing development of the organizations in an increasingly globalized world, the power of media.

In such an economic environment, increasingly competitive, globalized and at an accelerated pace, enterprise management has become increasingly complex while operational, legal, financial and strategic risks, to which they are exposed more and more, are on the rise. Therefore, it is obvious that the management of concerns raises the issue of a number of control devices, which are called by some "security", which ensure a certain level of mastering the activities and the risks that threaten the enterprise.

If the above emphasize the reason why the concept of internal control emerged, it is necessary to put into question the various ambiguities and confusion arising in connection with it.

Paradoxically, the term internal control is not as old as the concept which it defines as, in reality, it is a literal translation of contemporary English term "internal control".

In French theory and practice, the word control comes from the Medieval Latin "contrarotulus" (counter and rotulus) defining two registers for checking the markings of the second on the first. Hence the purpose of verification (e.g. fiscal control).

Currently, given the developments of the term, control has two different meanings:

a) one of: lawful and regular verification of something;

b) a notion of moral material or political domination, to which a country, a region is subjected, which can be equally perceived as the organizing and managing of a company or companies, which is why the word "dominion" is the closest synonym to defining control in this context.

In English, unlike French, the meaning of the term control refers rather to the concepts such as authority, direction, command, government, influence and generally speaking, possession of a thing. However, although the roots are ancient Latin, and the word control may correspond to the notion of verification or audit, in modern English it is used for the definition of internal control, a rather archaic notion.

Literary translation of the term "internal control" was unfortunate because it contributes to the perception of the concept only from the appearance of verification and less of mastery that better describes the real purpose of internal control.

Thus, the desired understanding of the term and concept of internal control must always be interpreted as meaning "dominion over activities".

In its evolution, the term has undergone several approaches, more or less developed, but which can be considered as substantially equivalent.

The question is whether the internal control system is applicable to the insurance sector as well, a sector with multiple features.

Insurance is above all a business based on trust. Essentially, an insurance contract is neither more nor less than a promise to pay in the event of a disaster or other commitment as result of the payment of an insurance premium. The promise or guarantee materializes only in the future, at the occurrence of the disaster or event that triggers payment commitments. The mechanism, by which the policy-holder pays first and subsequently receives, is called reverse production cycle.

Therefore, any insurance company should be able to meet its commitments to the insured in a future period, ie should be solvent and not go bankrupt in the meantime. This notion of commitment in the future is specific to the insurance sector and requires care and management rules, which are more important than in a traditional activity because failures cannot be accepted unless all commitments are honored.

Thus, to protect security, the public power emerged. It controls the solvency of insurance companies in that it verifies the extent to which they maintain their commitments. Therefore, insurance companies are subject to specific legal obligations and prudential supervision.

Concluding, we can answer our own question, making the following statement: insurance companies are subject to the same management problems as all other entities, they must ensure the reliability of accounting and financial information, must master the risks and subject to specific legal duties and internal control.

The organizations and professional bodies have **an important role in** the evolution and development of internal control, as well as in implementing concepts both through models or appropriate frameworks.

In time, there have been developed a series of models of control that are used as reference systems for implementation, operation or assessment of internal control, some of the most famous are COSO, CoCo model Turnbull (Renard, 2010) model ISA 315, "Identifying and assessing risks of material misstatement through understanding the entity and its environment "model approved by the Ministry of Finance Order no. 946 in 2005 and the proposed model for Romanian managing state revenues entities (Briciu, et al, 2011).

Among the mentioned models, COSO model and CoCo model are the most common and are characterized by the fact that they are complementary, which is why a comparison between them can made and the diagram of Figure 2 reveals that the COSO model describes the components while the CoCo model groups control criteria established in COSO model components (figure no.2).

We say that the two models are complementary because the recommendations contained in the CoCo document is based on the concepts expressed in the COSO. Even if the two documents cover many of the same areas and largely in line they also involve some differences in certain dimensions.

2.3. The principles of the internal control system at insurance companies

Achieving an effective control system cannot be conceived outside a certain set of principles, as stated by the Court of Accounts (2011) for public entities as well as by JLBellado's study (2004) that

addresses the specifics of the internal control in insurance companies. We have outlined, following the same line, our view as follows:

a. The principle of formalizing procedures supposes that the company has to be rationally organized, ie its structures are to be defined by the organization chart and presented in a written procedure manual. There is no standard pattern of how to organize it, which is why every company is organized in accordance with its objectives and strategies, its size and its activities.

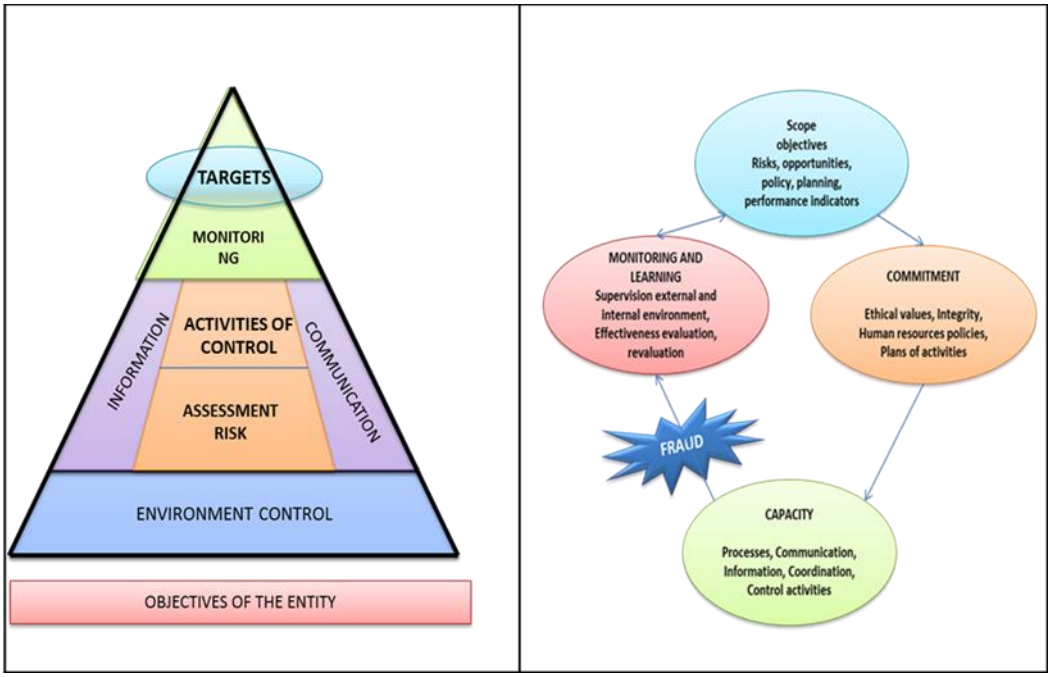


Figure 2. Comparative scheme COSO model (left) and CoCo model (right)

The organization chart should describe especially those persons who are company-representatives and eventually their own responsibility. In other words, the organization chart should provide information on the authorized persons to take a decision.

The procedures manual should explain the delegation of authority and must be unambiguous or it should facilitate certain benefits to the people who are qualified to exercise this power. The procedures should be systematically applied and have a character of permanence.

b. The principle of quality and availability of information according to which the information collected and used in the internal control system should be:

- relevant, that is adapted for use;
- neutral, i.e. not manipulated;
- useful, meaning that it must be useful for each and every recipient wishing to develop reports, dashboards, etc.;
- verifiable by means of documentation, which should be clear and accessible, so that the major transactions can be examined, this meaning that the transactions and other events are promptly and accurately recorded;

An effective internal control requires an information feedback. In some cases, managers of large companies want to obtain information that is unfiltered by officials or operational and functional intermediaries, which is why they are routed directly to the Board of Directors, such as: complaints about insurance, litigation, monitoring off - balance sheet commitments, discrepancies between

emission and collection of insurance premiums, significant differences between the payment and created reserves, damage recovery rates established judicially or amicably, other damages to be awarded.

c. The principle of staff competence and honesty derives from the text of the Treadwai Commission's communication (1992) which states that the effectiveness of internal control procedures is based on the integrity and ethics of those involved in the control.

Staff competence is ensured through relevant recruitment, ongoing training in specialized institutions and securing challenging objectives to encourage professional careers.

In our opinion, honesty is a virtue but it is not eternal, this aspect explains slippages of otherwise irreproachable conduct employees, and who after many years fail. Therefore, staff mobility and transfer of responsibilities at all hierarchical levels can prevent temptations caused by routine and habits. Effectiveness of internal control may be affected even in a highly computerized environment as a result of distraction or fatigue.

It follows that, regardless of the competence and integrity of staff, it is always appropriate to supervise the operations, be it made by those superiors responsible with it, or by outer people, internal or external auditors.

d. Providing adequate materials and sufficient human resources.

Checks must be adjusted to the right ratio to the company's situation and the risks assumed by it which means to establish appropriate personnel and appropriate tools for achieving the goals. Therefore, the costs should follow the cost-benefit rule.

As for insurance companies, if the procedures necessary to identify fraud insurance payments from the declarations and damages resulting from disasters have higher costs than the savings that allow these operations, it makes sense to give them up.

Moreover, an internal control to prevent any error or fraud would obviously be more effective if its price is not prohibitively expensive by multiplying redundancies at the expense of information processing speed.

e. The principle of function separation results from the interpretation of the IASI text, which includes measures of authority and delegation of responsibility. In this context, internal control is considered effective when the same person does not have two or more functions. In this context the following functions can be separated:

- *the decision on company's statutes realization*. If the decision is delegated to a subordinate, the decision function is related to the authorization and approval function;
- *conservation of assets function* (protection or retention) is achieved by the separation made in the assets (intangible assets, such as computer circuits vs. local financial ones). The operation of the conservation function can be implemented by means of protection and access to material resources and documents, such as entry codes, passwords, locks, access software etc. Asset preservation function requires an adequate insurance policy;
- *recording or accounting function* refers to verification of documents prior to their registration, according to programmed control procedures;
- *verification function* (control or audit) aims to monitor other functions related to the routine, systematic and permanent operations. This traditional approach does not meet the large companies that exercise their activity in a system of integrated accounting and therefore there is a separation (a) between the tasks of decision making, preserving and accounting. Therefore, the computer operator, accountant, treasurer, manager of values, must have tasks procedures, excluding thus any exhaustive description of treatments and integrated computer checks of these treatments.

f. The principle of self-control and control involves duplication of reporting and takes the following into consideration:

- duplication is to compare similar information contained in different documents or to justify information from different sources;
- mutually control involves comparing the same information recorded by at least two different people in order to see the consistency between the two amounts (e.g. purchase of a property is registered both by the technical service and accounting);
- continuous monitoring made by the managers, it is necessary to ensure the internal control objectives.

As shown, although the jurisdiction allotted to internal control is all-inclusive, it is subordinated to internal audit reports, which appears as an over-controller and, paradoxically, at the same time, part of the internal control system.

Effectiveness of internal control system must be based on a better coordination of the device around key activities, as shown in Figure No. 3 and relates to: mapping and risk assessment, control activities definition and assessment, remediation plans, piloting and dissemination of information, permanent surveillance.

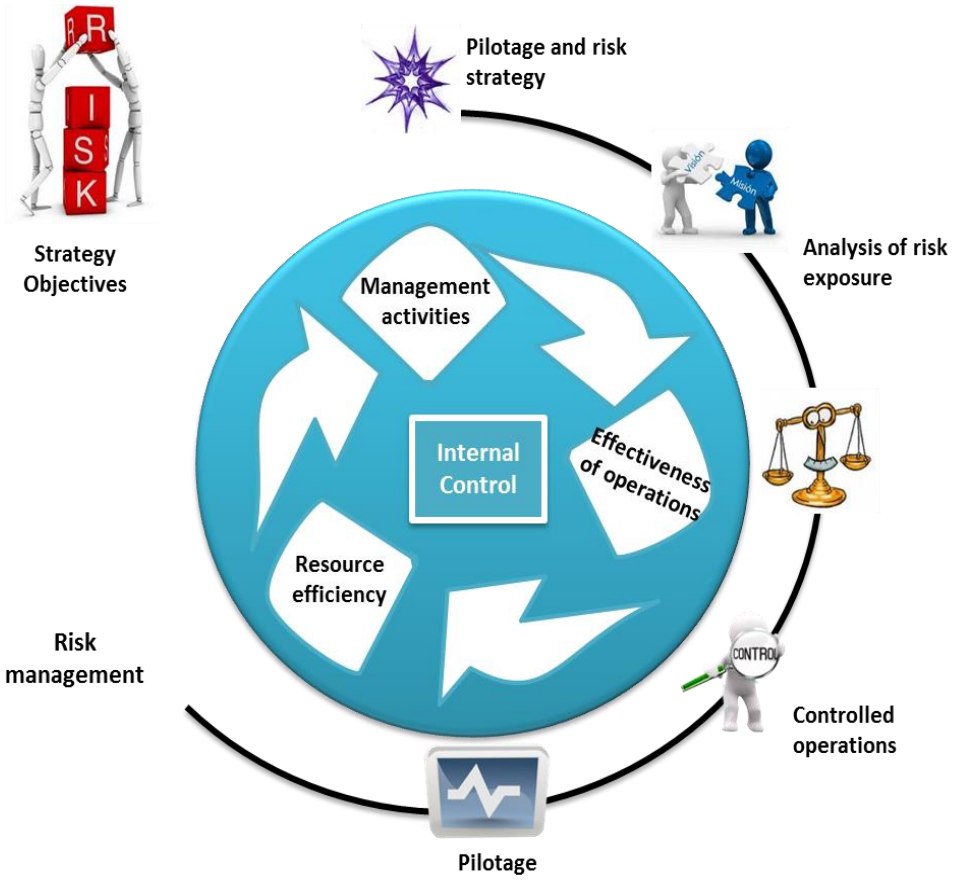


Figure 3. Effectiveness of risk management and internal control

Source: adapted from IFA, Le SUIVI de l'efficace et des Systèmes internal controls des Risques de gestion, novembre 2010, page 5

The perspective of internal control creates a double paradigm image, namely that of guardian of the temple on compliance aspects regarding compliance and fraud prevention, on the other hand being a business partner with the role of lowering the risk exposure. The flexibility of the internal control and adapting it to the requirements of efficiency of any activity is a consequence of the fact that currently, internal control is applied too mechanically – there is internal control for internal control, test for test, while its purpose is to reduce the level of residual risk.

3. CHARACTERISTICS OF INTERNAL CONTROL IN INSURANCE COMPANIES

Generally, the approach to internal control objectives, principles, certain procedures in the insurance companies do not differ from those found in other companies in the financial sector, but the application of specific procedures must take into consideration:

1. *The peculiarities of insurance operations* that materialize in:

- determining a priori price (under-pricing risk);
- risk selection (under-pricing risk);
- commitment to long-term insurance (risk of under-funding);
- correlation between life insurance contracts and investments (interest rate risk, the risk of depreciation);
- reinsurance (specific risk);
- intermediation (risk of a partner's failure);
- delegating management (risk of a partner's failure)

2. The need for policyholders protection. In this respect, internal control should focus on measuring the quality of services offered to policyholders on the basis of precise information, such as payment of redemptions (life insurance) and claims (insurance).

The objectives of internal control are general and apply to all public institutions, but insurances, in whatever form, realizes a risk transfer of risks that a natural person or a juridical person cannot support in part or in full in terms of finance.

Therefore, if there were no risk, there would be no insurance. But, do only policyholders need protection against risks? Definitely not! Every natural or legal person faces its own risks and thus the insurance companies are no exception.

To be detected and managed, peculiarities of internal control are manifested related to the risks related to different functions within an insurance company and which has a number of objectives, including:

A. Acceptance of risk (life insurance). Under a contract of life insurance is a guaranteed risk related to the length of human life, as the insured may die too early because (guaranteed death) or too late (annuity guaranteed). Because of this, the insurer must measure the risk:

- to decide whether to accept it or not;
- to determine the size of the corresponding insurance premium.

In this framework, internal control procedures applied for life insurance must answer a series of questions, such as:

- insurance proposal:
  - Is it designed to allow an adequate risk assessment?
  - Is it completed?

- investigation of cumulative risks:
  - Are there other contracts in force in society on the same subject of insurance?
- Medical Letter (guaranteed death):
  - Is it an effective protection against the risk of adverse selection?
- reinsurance capital guaranteed for the amount that exceeds the ability of the insurer:
  - Is it adapted to funds?
  - Is it applied?

For example, if in the case of a life insurance, the insured suffers from a chronic disease such as diabetes and did not declare this at the time of the contracted insurance policy, and death occurs due to this disease, then compensation will not be provided.

Monitoring issues of premiums and mathematical reserves raises various actions of internal control aimed at:

- dropped premiums (control procedures must allow the tariff applied by insurance risk to be measured according to the contract);
- collected premiums (procedures, to address the risk of diversion or loss of payment and risk of erroneously allocated payment of a contract, are organized and internal controls must ensure their correct application: of their revenue, segregation of duties between receiving funds, their allocation and monitoring of bank accounts);
- connection between each insurance premiums and the reserve determined under contract, aiming at two aspects:
  - Risk: a recorded premium has no counterpart in a reserve calculated on a contract basis;
  - The role of internal control: systematic analysis of remaining premiums, check the consistency of premiums and files.

The above description can be also applied for general insurance, except for medical letter and mathematical reserve. Two factors will be underlined: prices (how is the determined the applicable tariff? Is there a procedure for verification of charges? If so, which one? In case of tariff exemption, is there a particular hierarchical authorization procedure, if so, which one?) and reserves for disasters.

B. Provision for unpaid claims for damages (general insurance). We are facing technical reserves that should be sufficient to fully cover the commitments made by the insurance company.

In the general insurance company, the fund/reserve, for the payment of damages caused by disasters, is designed to allow full settlement of all claims (including costs and management costs) before the date of their inventory and which have definitively not been paid up to that date.

Reserves for damages (damages) hold a significant share in the liability side of insurance companies and any error can distort the financial image of the insurance company.

Internal control on claim-reserves is a priority to assess the incurred risks, particularly the risk of under-valuation, risks in determining insurance rates that may mask a misunderstanding of cost and inadequate damage management, fraud that can be registered by wrongful payment of real or fictional damages.

The internal control procedures should describe the quality of damage management and the appropriateness of the reserve amount. By the very nature of their position, people, involved in the control, examine in detail the created reserves, having two essential objectives in mind:

- verifying the amounts at a given time (balance sheet date);
- applied evaluation methods applied

answering a series of questions such as: are the reserves properly constituted?, are they sufficient? are they made according to the regulations? Are they logical? Are they well applied? Do they conceal fraud intentions?

Internal audit comes to reinforce the evaluation made by internal control as being proper, giving assurance that the accounting procedures were properly applied.

C. Protecting investments. Investments carried out by an insurance company represent the counterpart of the commitments as related to policyholders and they must provide security and performance.

Internal control should give the assurance that assets are managed in accordance with the general investment policy as well as the legal and accounting regulations, and the regulatory requirements.

Therefore, internal control objectives are clear:

- ensuring that the asset management complies with the laws and regulations;
- ensuring that the investment strategy determined by the Board of Directors is properly applied regarding: distribution of investment is made among different licensed categories, there is a ceiling of investment by type of asset, delegated administration, market, currency, geographic regions, profitableness objectives adjusted according to the effectiveness of the liability types;
- assessment of risk protection devices likely to affect the technical reserves and solvency margin: market risk, interest rate, liquidity, material destruction, misappropriation or fraudulent use;
- verifying the integrity and reliability of information processed and revenue: held investments, acquisitions and divestments made and the corresponding income;
- ensuring segregation of duties in order to answer the following questions: are the acquisitions and disposals rightly carried out? Are they executed under the best conditions? Is the evaluation of investments in the balance sheet properly carried out?
- proposals to improve the quality of management.

Regarding the procedures used within this objective, internal control includes:

- verifying the concordance between placements appearing in the balance sheet and those existing, established through transaction monitoring and reviewing the information provided by accounting;
- operation justification acquisition and / or transfer through verification of ownership or sale of real estate;
- monitoring internal or external evaluation system;
- establishment of a separate records of participants;
- implementation of a management control aimed at monitoring the profitability, performance indicators, time simulations etc.

In our opinion, internal control in this area has rather a preventive role, otherwise it should allow early detection of accidents damaging the company's financial situation.

D. **Asset-liability management** or simply known by the acronym ALM (Asset and Liability Management), is a practice developed by Anglo-Saxon financial institutions since 1972 at the crossway between risk management and strategic management.

More generally, asset-liability management is a method that consists of reconciliation of uses and resources included in the balance sheet of an insurance company in terms of risks. The goal of this method is to optimize return on equity while maintaining an acceptable level of interest rate risk, liquidity and exchange.

The internal control procedures take into account, first, to comply with the instructions given to the administrator. Specification or instruction enforcement can be achieved based on the administrator's report or on a financial control specific to ways and places.

The verifier may make content-points on asset-liability policy, or to conduct a full audit of asset-liability risks.

To regularly check the level of risk trends, the verifier may use balance simulations, the design of future results and financial condition of the company based on predefined scenarios. These scenarios or sets of assumptions, including economic and financial environment, enterprise revenue, customer behavior will help build risk indicators, including alert thresholds.

E. On-term financial instruments (derivatives). Insurance companies operating on the derived products market are exposed to particular risks arising from:

- the abstract nature of derivatives, transactions are carried out through verbal commands quickly, sometimes in a considerable volume which gives a quasi imperceptible character;
- an important leverage role, gains and losses can be considerable relative to investments;
- complex use, derivatives managing staff should be trained, as well as the one who decides policy followed in this area;
- liquidity problems;
- counterparty risks. The use of derivatives calls for monitoring and a rigorous internal control. Their use must be in accordance with IFRS 4 "Insurance Contracts" and IAS 39 "Financial Instruments: Recognition and Measurement" that include restrictions on their trading.

Mastering the risks arising from financial instruments is a matter of internal control, which must take into account various aspects, among which:

- it should refer to a detailed description of the strategies;
- it should see if the enterprise is equipped with efficient enough electronic means of communication and management, so to allow operators to respond quickly and wisely. System-efficiency can be tested by some assessments, either relating to a given position, or envisaging a crisis scenario, the so-called "stress test";
- liquidity monitoring to determine whether, within the investment strategy, the insurance company to purchase securities under the future agreement contract. In this context, internal control must pursue both liquidity materialized in cash flows from existing current bank accounts, term deposits and immediate liquidity.

F. Information risk. Information technology has transformed the structures of insurance companies, enabling a fast processing of a number of important items of information on contracts, premiums, claims, technical reserves, commissions, investments. At the same time, IT has created new risks that fall within the scope of internal control.

There is no question of treating the specific risks related to technical particularities for each and every type of system because they pose similar risks inherent to their use, such as:

- the risk of error, which can be caused by abnormalities of the program, it means the use of a number of complex processing and significant repetitive transactions, each error being systematic;
- the risk of fraud or intentional, which is a consequence of the ease of software usage and it can lead to deliberately recording incorrect information;
- the risk of neglect, it is due to the fact that, although careful control is required the growing blind-confidence in operators' professionalism, who operate with increasingly sophisticated means, creates a favorable psychological atmosphere for mistake and fraud;
- the risk of technical failure, resulting in faulty running programs, file overcapacity etc.

Therefore**, internal control** should monitor: equipment reliability, the data entered the computer, data processing, data retention, describing treatments.

To prevent data damage, internal control must ensure that there are a number of basic rules concerning:

- security mechanisms (doors, passwords, etc.);
- files and programs protection;
- protection against natural phenomena (voltage drops, dust);

G. The role of intermediaries is an issue related to agents and brokers, to whom tasks are delegated, tasks such as issuing insurance policies, cashing of premiums, damage claims, tasks that pose specific risks, including:

- underwriting risk (the intermediary/ agent is likely to accept a bad deal and even to hire the insurer beyond the limits he has set);
- risk of fraud due to the sale of fictitious policy and the payment of unjustified service;
- the risk of contract-underwriter's diverting the paid funds;
- financial risk related to tarrying repayment of funds.

To protect against the above mentioned risks, internal control must have and implement procedures, such as:

- intermediaries/ agents' reputation control;
- separation of powers between intermediaries and the authorities responsible for underwriting, premium issuance etc.;
- regular monitoring of intermediate balances based on the indicators;
- spot checks, including cash checks made to ensure that intermediaries have not got undue advantages, the company pays regularly the premiums collected and does not involve the company above the permissible thresholds.

H. Outsourcing (outsourcing). Outsourcing is increasingly used by insurance companies that delegate certain functions to third parties under the direct supervision Regulatory Authority and internal control standards.

The range of outsourced functions is quite broad and includes:

- settlement of claims;
- calculation of technical provisions;
- fixing of rates;

- actuary work;
- IT management;
- active portfolio management;
- prudential reporting;
- internal audit etc.

Unlike other branches of activity, in insurance, outsourcing has the advantage of reducing costs through economies of scale, achieved by the service provider and subcontractor. On the other hand, it can exhibit a number of risks including:

- legal risks derived from non-compliance with legal provisions by providers, especially when they themselves are not insurers;
- operational risks materialized in: the risk of loss of control over outsourced activities, risk of loss of competence of the insurance company to manage outsourced activities itself, the risk of dependence on the supplier;
- general risks related to supplier's incompetence and thus deteriorating the quality of the provided service, entailing higher costs, that trigger higher expenses for the insured.

Internal control has as its objective to prevent risks and / or limit their possible effects by applying the following procedures that verify if:

- outsourcing does not jeopardize the interests of policyholders;
- the Board of Directors remains in charge of all outsourced activities and therefore envisages the setting up and monitoring the activities in question;
- the lines defined by the Board of Directors are described in detail in the outsourcing contract and is respected by the service provider;
- there are effective means in the enterprise to analyze the risks associated with outsourced activities;
- there are alternatives when activities do not work because of the service providers;
- the insurance company may terminate the outsourcing contract at any time if difficulties that damage its reputation, trade policy, financial position arise.

I. Money laundering. In many countries, legislation requires that financial organizations identify contractors and the real beneficiaries when there is a suspicion that the holder of the contract does not act on its own behalf. This is also prescribed by the laws of our country which states: "Data on the customer's identity is verified and updated or supplemented, if necessary for any transaction involving an amount equivalent in RON of at least 15,000 euro, whether the transaction is carried out in a single operation or in several linked operations."

A team of experts from the ONPCSB has developed a manual, which exemplifies a series of indicators for insurers, reinsurers and brokers, which, in our opinion, are nothing but targets that support the procedures for implementing internal control, including:

- "customers uninterested in the investment component of a product, but showing an increased interest in the redemption value of the policy;
- clients seeking or accepting contractual conditions that are clearly unfavorable to them;

- choosing insurance products that do not cover the risks which are related to the activity or customer profile;
- the client has no credibility, since there is information on his involvement in fraud, payment incidents or suspect transactions;
- payment of sums greater than the value of insurance premiums, followed by a request that the overpaid amount to be transferred to another account or to another beneficiary;
- payment of premiums in bank accounts from other jurisdictions than the one where the policy owner is domiciled or resident;
- the client unduly calls as compensation to be paid to a third party;
- the client requests that the compensation to be paid in cash or to be transferred to an offshore account in a currency other than the one used for the payment of insurance premiums "and examples can continue.

Therefore, insurance companies must implement internal control procedures enabling;

1. raising the awareness of the personnel involved in underwriting and collecting, as well as of the intermediaries;
2. identification of the contract subscribers;
3. keeping the details of each and every transaction as long as the law requires it.

In case of suspicion, the insurance company must draw up a "declaration of suspicion" and pass it to the qualified authorities in combating money laundering, as well as to the Insurance Supervisory Authority.

4. CONCLUSION

Currently, the economic environment requires numerous changes in the management and structuring of business entities. This is because organizations act in an unstable environment characterized by fast, numerous, dispersed, unpredictable developments in time and space, which make the information uncertain. A real challenge for managers is to identify the avalanche of leading indicators in order to stay afloat.

In the set context, it can be said that the appreciation of the extent to which predetermined objectives match routes is performed through surveillance that use various mechanisms reunited generically under the name of control.

At first, the control of an organization was understood a "control-sanction", i.e. a form of control which aims to check the suitability of a predetermined the outcome of an action (H. Fayol 1918). Later, with the expansion of standardization of production and labor, control has evolved in "a budgetary control", moving from overseeing production to a policy of forecasting.

Mutations in the contemporary business environment (increased complexity of organizations, the emergence of new forms of competition, globalization and growing deregulation of markets, rapidly changing technologies, etc.) led to redefine the concept of control of the organization in the sense that it is an action seeking dominance or at least influencing a system.

So the role of controlling the use of resources allocated to various departments and activities within an organization, internal control has now become a function of management performance.

Bringing into attention the of concept of corporate governance and its development, from literature review we draw the conclusion that the problem is related to delegating part of responsibility related to control to whom receives this delegation.

Paradoxically, the term internal control is not as old as the concept which defines it, as in reality, it is a literal translation of contemporary English term "internal control".

Reviewing the definition of the term control and noting that it is at the same level as seen by COSO, Turnbull guidance and MFA, being substantially equivalent, we asked ourselves whether the internal control system is applicable to the insurance sector, a sector with multiple features.

Insurance is above all a business based on trust. Essentially an insurance contract is neither more nor less than a promise to pay, in the event of a disaster or another commitment, as a result of the payment of a premium. The promise or guarantee materializes only in the future, at the occurrence of the disaster or event that triggers payment commitments. The mechanism by which the policyholder pays first and subsequently receives is called reverse production cycle.

Therefore, any insurance company should be able to meet its commitments to the insured in a future period, i.e. it should be solvent and not go bankrupt in the meantime. This notion of commitment in the future is specific to the insurance sector and requires care and management rules that are more important than in a traditional activity because failures cannot be accepted unless all commitments are honored.

Thus, to protect insurance, public power appeared and it controls solvency of insurance companies in that it verifies the extent to which they maintain their commitments. Therefore, insurance companies are subject to specific legal obligations and prudential supervision.

For the insurance companies, it is noted that although almost all internal control systems are regulated by legislation and internal regulations of insurance companies, some of them, such as financial control; financial control management; damage investigation and verifying, and controlling the internal audit are often confused with each other, considering that they are too numerous and have the same duties and tasks.

In general, the approach to internal control objectives, principles, certain procedures in the insurance companies do not differ from those found in other companies in the financial sector, but the application of the specific procedures must take into account specificities of the insurance operations on one hand and on the other hand, the need to protect policy-holders.

In order to be detected and managed, the peculiarities of internal control manifest themselves in relationship with the risks related to different functions within an insurance company and have a number of objectives, including: acceptance of risk (life insurance); reserves for damage claims (insurance); protecting investments (investments); asset-liability management; on-term financial instruments (derivatives); information risk; the role of intermediaries; outsourcing; money laundering.

Reviewing each and every objective above mentioned, we find that risk management is a priority objective, and insurance companies, constantly confronted with new challenges, must remain reactive when it comes to managing emerging risks.

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