
**OUTSOURCING AS A MODERN FORM OF MANAGING PROCESSES IN AN
ENTERPRISE ILLUSTRATED WITH AN EXAMPLE OF INSURANCE UNDERTAKINGS
IN POLAND**

Katarzyna Świetla, Krzysztof Jonas

Department of Financial Accounting, Cracow University of Economics, Poland

Abstract

Outsourcing is currently an inseparable element of the modern economy. Entities often take advantage of the services offered by other entities, outsourcing part of their activity. Insurance undertakings do the same, however in this case the decision about outsourcing certain activity is not made on the basis of the economic result but it is determined by the legal regulations which specify what and under what terms and conditions can be outsourced. The regulations also specify the principles for the supervision and control of the outsourced activities.

Key words: *outsourcing, insurance undertaking, outsourcing supervision*

1. INTRODUCTION

Every enterprise aims at the achievement of the best results of its activity, eliminating from it the processes or activities which are redundant or which can be outsourced. Insurance undertakings, as one of the modern economy elements, proceed in similar way. However, in order to outsource certain activity, it is necessary to meet the requirements set forth in the act that regulates the basic principles of functioning of these entities (the act, 2015). This act defines which activities can be outsourced and under what terms and conditions. It is characteristic that the said act regulates only the matters connected with insurance activities and those directed related thereto (namely the core of the insurer's activity), completely omitting the activity aspects which are not characteristic for insurance undertakings, such as promotion, advertising, administration, etc.

In the first part of this article, the authors discuss the conception of outsourcing and its role in the modern economy. The second part of the article focuses on the requirements set to insurance undertakings, which define in details the scope of the activities which they have to perform and which are not allowed to be outsourced, and those which can be outsourced. In addition, the authors mention in the article under what terms and conditions given activities can be outsourced, so that it would not disturb the continuity of insurer's activity. The last part of this article presents the issue of supervision of outsourcing activity in insurance undertakings.

This article's objective is to familiarise the user with the subject of outsourcing in insurance undertakings in the light of the new legal regulations. When preparing this articles, the authors applied the method of analysing the present domestic and foreign literature and the current legal acts.

**2. OUTSOURCING AS AN INSTRUMENT OF MODERN MANAGEMENT OF PROCESSES
IN AN ENTERPRISE**

The modern economy requires a thorough analysis of the level of the costs incurred and the avoidance of those which don't bring tangible benefits to entities. More and more often it is connected with delegating selected processes to specialised external companies. Thus, the economic entities employ them to perform the services which recently have been performed traditionally e.g. by headquarters such as accountancy and administration.

An advantage of such an approach is the possibility for the managers to focus on the key tasks of an economic entity and to purchase only such an amount of external services which are necessary for this entity to function properly, without the need to maintain its own developed resources in this respect.

Dissemination of the said practise has become a derivative of the development of specialised services on the global market and in consequence the development of outsourcing used, as commonly noticed, for the simplification of economic processes.

Table 1. Outsourcing, an attempt at a definition

Author	Definition
The Basel Committee on Banking Supervision.	A regulated entity's use of a third party (either an affiliated entity or within a corporate group or an entity that is external to the corporate group) to perform activities on a continuing basis that would normally be undertaken by the regulated entity,
M. F. Greaver	"The act of transferring some of a company's recurring internal activities and decision rights to outside providers, as set forth in a contract" in order to focus on the company's unique resources (key competencies) in order to lead its specialized activities,
Ch. L. Gay, J. Essinger	Outsourcing, considered from a strategic perspective, today is one of the most important business approaches that confers the greatest benefits, as it allows organizations of all types to make full use of their potential and achieve optimal efficiency and flexibility to respond to customer needs,
D. Lei, M. Hitt	Outsourcing is a business cooperation with external suppliers in the production of components and other activities of high quality
P. Doyle	Outsourcing generally allows companies to replace fixed costs with a variable spread over a longer period,
W. T. Bielecki	Ordering certain services and tasks from external companies specialized in the field
J. Penc	Outsourcing is the use of complex services, which are a combination of a variety of partial services sold and settled as a unit and they offered by external contractors (tenders)
M. Trocki	Outsourcing is a project that involves the separation of certain function of the parent organization and performance and transferring their implementation to other operators,
I. Sobańska	Outsourcing is a specific type of decision on the elimination of certain activities for the organization, or services that do not contribute to the growth of the company and its competitive position,
K. Perechuda	The ability to opt out of the development of specific areas within the parent company through the use of resources of external actors,
B. Liberska	Outsourcing involves the allocation, from a parent entity, of some of the previously performed services (processes) related to customer service and transferring them to an external entity that provides them at lower production costs.

Source: K. Świetla, 2013, p.29-30; M. F. Greaver, 1998, p. 91; Ch. L. Gay, J. Essinger, 2002, p. 7; D. Lei, M. Hitt, 1995, s.835; D. P. Doyle, p. 57; W.T. Bielecki, p. 192; J. Penc, *Leksykon biznesu*, 1997, p. 302; M. Trocki, p.13; *Rachunek kosztów i rachunkowość zarządcza*, Ed. I. Sobańska, 2003, p. 415; K. Perechuda, 2000, s.116; B. Liberska, 2005,Nr 3.

As it results from the above, the implementation of outsourcing activity is based on limited resources and own skills, what makes it necessary to perform only the tasks in which an entity is specialised in accordance with the lean enterprise approach. Owing to such an approach, it is possible for an entity to acquire complementary benefits, which in combination with own benefits will allow offering a unique product to the buyer, being a derivative of the cooperation between several participants of the process in progress. (Nowak, 2012, p.467).

Therefore, the essence of outsourcing implementation is the possibility to replace fixed costs with variable spread over a longer period (e.g. the lack of the necessity to employ full-time workers, to maintain the equipment base which gets old together with the development of technology or to provide office equipment). Whereas variable costs are a derivative of the use of external services only when they are required and in the amount corresponding to the actual needs related to the management of separated process.

An undertaking can be successfully implemented only when the service provider guarantees that particular tasks will be performed by employees specialised specifically in the performance thereof. This results from the assumption that it is the knowledge that constitutes one of the most significant resources of an organisation and is considered mainly in respect of the input that can be provided for the purposes of the achievement of assumed goals. (Kowalczyk, Nogalski, 2007, p. 21). Certainly there is certain risk of outsourcing cooperation resulting from the level of mutual relationships between the cooperating entities and the failure to match or precisely define their expectations. Therefore, at each stage of the cooperation it is required to control the course of pursued processes and this requirement cannot be abandoned even in case of mutual satisfaction of the parties of its effects. (Kopczyński, 2010, p.133-138; Świetla, 2013a, pp. 995-1007; Świetla, 2014, pp. 100-101).

It should be noted as well that the issues presented in the article are indeed strictly connected with the development of the sector of modern services. It is a derivative of placing the entities indicated in the article in the group of innovative service providing organisations, which comprises both the insurance or reinsurance undertakings which are considered in the article as the key subject, and the outsourcing units which are used for the purposes of providing them with accounting services, and so being of ancillary nature.

3. OUTSOURCING IN INSURANCE UNDERTAKINGS AND REINSURANCE UNDERTAKINGS

Insurance undertakings or reinsurance undertakings are the entities which may perform their activity within the scope that is defined strictly in the act. The insurance activity (the act, 2015, Article 4 item 1) shall be construed as the performance of insurance activities related to offering and providing protection against the risk of occurrence of fortuitous event effects. The same article defines in item 2 the term of reinsurance activity as the performance of activities connected with assuming the risk ceded by the insurance undertaking or the reinsurance undertaking and further ceding of the assumed risk. Simultaneously, the same article contains a full catalogue of insurance and reinsurance activities. In addition, it was defined in the act that the insurance undertaking is not allowed to perform activity other than insurance activity and activity directly related to it, same as the reinsurance undertaking.

Insurance undertakings and reinsurance undertakings are entities which use the outsourcing services on an equal basis with other entities, however due to specific nature of its activity not each activity can be outsourced.

Pursuant to Article 3 item 1 (the act, 2015) outsourcing is an agreement between the insurance undertaking or the reinsurance undertaking and the service provider, on the basis of which the service provider performs a process, service or activity, which otherwise would be performed by the insurance undertaking or the reinsurance undertaking, and also an agreement, on the basis of which the service provider outsources the performance of such a process, service or activity to other entities by the agency of which he performs a given process, service or activity.

An insurance undertaking may outsource in writing the following insurance activities:

- making declarations of will regarding claims for damages or other benefits due under the insurance contracts, suretyship contracts or reinsurance contracts,
- risk assessment within personal and property insurance and suretyship contracts,
- payment of damages and other benefits due under the insurance contracts, suretyship contracts or reinsurance contracts,
- taking over and selling objects or rights acquired by an insurance undertaking in connection with the performance of insurance contract or suretyship contract,
- conducting the control of compliance, by the policy holders or the insured, with the obligations and safety rules indicated in the contract or general terms and conditions of insurance agreement with regard to the objects covered by insurance,
- conducting recourse proceedings and receivables collection proceedings with regard to the performance of insurance contract or suretyship contract, as well as reinsurance contracts in the scope of ceding the risk from the above contracts,
- investing assets of insurance undertakings,
- performing other activities attributed to insurance undertakings in separate acts.

In addition, the act provides the possibility to outsource the activities considered to be insurance activities on condition that they are performed by insurance undertakings. Outsourcing them means that they can no longer be considered as insurance activities. They include:

- determining the causes and circumstances of fortuitous events,
- calculation of the amount of damages and the volume of compensations and other benefits due to entities entitled under insurance contracts or suretyship contracts,
- determining the value of an insured object,
- preventing the occurrence of or reducing the effects of fortuitous events and financing these activities from the prevention fund.

The insurer performing, next to insurance contracts, also reinsurance contracts, may additionally (apart from the activities mentioned above) outsource the performance of the following activities:

- making declarations of will regarding claims for damages or other benefits due under the accepted reinsurance contracts and retrocession contracts,
- conducting the control of the ceding undertaking's compliance with the conditions of the accepted reinsurance contracts and retrocession contracts,
- activities directly related to reinsurance activity, in particular activities within the scope of statistical advisory, actuarial advisory, risk analysis, studies conducted for clients, investing the resources, as well as activities aimed at preventing the occurrence of or reducing the effects of insurance accidents or financing these activities from the prevention fund.

The above regulations also refer to companies engaged in reinsurance only.

Analysing the activities which can be outsourced, one may notice that the legislator left for the discretion of insurance undertakings only the activities which are strictly related to the activity subject. Namely, it is not allowed to outsource:

- concluding insurance contracts, suretyship contracts or commissioning the conclusion thereof to authorised insurance intermediaries, as well as performing these contracts,
- concluding reinsurance contracts or commissioning the conclusion thereof to reinsurance brokers, and also performing these contracts in the scope of ceding the risk from the insurance contracts or suretyship contracts (ceded reinsurance),
- calculation of premiums and commissions due under the above contracts, and

- establishing, by way of civil law activities, proprietary or personal collaterals, if it is directly connected with the conclusion of the above contracts.

In case of reinsurance undertakings, it is not allowed to outsource:

- the conclusion and execution of accepted reinsurance contracts and retrocession contracts, and
- the calculation of premiums and commissions due under the above contracts.

Insurance undertakings and reinsurance undertakings may also outsource, in writing, the performance of the functions included in the system of governance.

They are also obliged to draw up, in writing, the outsourcing principles in the situation when the entity takes advantage of it or intends to do so. The principles shall comprise in particular:

- a) the list of functions included in the system of governance and the insurance or reinsurance activities which the undertaking intends to outsource with the indication which of those activities the undertaking considers as critical or important,
- b) the criteria for choosing the entity to which the undertaking intends to outsource the performance of insurance or reinsurance activities and the functions included in the system of governance,
- c) the manner of fulfilling the conditions that enable to outsource a given activity or management function, as well as the border conditions which have to be prevented
- d) the principles of managing the risk related to outsourcing the performance of the activities and functions included in the system of governance.

Insurance undertakings and reinsurance undertakings are obliged to review at least once per year the above principles in respect of the necessity to adjust them to the changes in the areas they refer to. They are also obliged to inform the supervisory authority about the intentions to implement the principles regarding the outsourcing and about a substantial change to these principles by providing the authority with the content of the principles.

The insurance and reinsurance activities or the functions included in the system of governance may be outsourced on condition that the service provider will cooperate with the supervisory authority within the scope of the outsourced activities or functions. Additionally, all interested parties, including the authority authorised to examine the financial statements and the solvency and financial condition report, must have access to the data related to the outsourced activities or functions. In addition, the supervisory authority needs to have an opportunity to examine the activity and assets of the service provider within the scope of the outsourced activities or functions.

Outsourcing of the functions included in the system of governance and of the critical or important activities cannot lead to:

- delegating the management of the insurance undertaking or the reinsurance undertaking pursuant to Article 368 § 1 Commercial Companies Code
- delegating the performance of insurance or reinsurance activity in such a way as to result in the lack of factual performance of activity by the insurance undertaking or the reinsurance undertaking,
- impairing the quality of the system of governance of insurance undertaking or reinsurance undertaking,
- increasing the operational risk of insurance undertaking or reinsurance undertaking,
- impairing the ability of the supervisory authorities to monitor if the insurance undertaking or the reinsurance undertaking complies with its obligations,
- undermining the quality of service to policy holders, the insured or entitled on the basis of insurance contracts and the ceding undertakings.

Insurance companies, in case of taking advantage of outsourcing, are subject to full responsibility principle, i.e. their liability for damages caused to clients in consequence of non-performance or improper performance of the outsourced activities can never be excluded or limited. The same refers to reinsurance undertakings, whose liability towards ceding undertakings for damages resulted from non-performance or improper performance of the outsourced activities cannot be excluded or limited either.

The insurance undertakings and reinsurance undertakings which take advantage of outsourcing are obliged to register the outsourcing agreements and such a register should include:

- 1) the identification data of the entrepreneurs to whom the activities and functions included in the system of governance were entrusted under outsourcing agreements,
- 2) the scope of the outsourced activities and functions included in the system of governance, and the place where they were performed,
- 3) the terms of agreements.

The insurance undertaking's areas of activity which are most frequently outsourced include:

- IT support, (by developing dedicated IT systems used for the operation of insurance activity and general functioning of the entity¹ and later managing it),
- actuarial support,
- human resources (handling personnel matters, recruitment and training of employees),
- archiving documents (storage and preservation of accounting documentation, both in the form of hard copies and electronic files, creating and recording data copies from IT system,
- call centre (establishment and ongoing operation),
- settlement of claims,
- marketing and advertising insurance services,
- administering the undertaking's assets (management of real properties, administration services),
- risk assessment and calculation of the value of insured object,
- determining the causes and circumstances of insurance accidents and damage values,
- managing the insurance undertaking's investments (Czublin, 2010).

4. THE SUPERVISORY AUTHORITY VS. OUTSOURCING IN THE INSURANCE INDUSTRY

Insurance undertakings or reinsurance undertakings are obliged to notify the supervisory authority minimum 30 days before outsourcing the functions included in the system of governance and the critical or important activities, as well as of any substantial change to the outsourcing agreement. The supervisory authority has the right (the act, 2015, Article 342 item 2) to examine the activity and assets of the provider of insurance services within the scope of the outsourced insurance and reinsurance activities, and the functions included in the system of governance. In particular, this refers to the insurer's contacts with the clients, the works using confidential data and information, as well as the capital outsourcing (Witkowska, 2016).

¹An example is SAP for Insurance (Witkowska, 2016)

When examining the cases of outsourcing in the insurance industry, the supervisory authority should analyse the following:

- 1) the knowledge of the insurance undertaking about the service provider, his past and experience,
- 2) the level of security of the insurance undertaking's interests, the interests of the insured persons and the beneficiaries under the insurance contracts, also in case of omitting to perform the ordered activities or contract termination
- 3) the level of increasing the risk by taking advantage of outsourcing and making the insurance undertaking's activity dependent on the service provider
- 4) the reasonableness to outsource services due to the quality of the execution thereof
- 5) the level of controlling the outsourced services and activities
- 6) possible „empoisoning” of employees and the executive staff of the insurance undertaking or “lulling” their vigilance towards the incorrectness and the threat to the interests of the undertaking and its clients (Ścisłowski, 2002).

When supervising the insurance undertaking in the aspect of outsourcing, the supervisory authority has:

- the possibility to order the insurance undertaking to terminate the outsourcing agreement, prohibit the planned outsourcing of critical or important insurance activities and functions included in the system of governance and make a substantial change to it,
- the right to examine the service provider at his premises, whilst in case of the service provider from other EU member state – the examination by the supervisory authority of that member state,
- the possibility to examine the activity and assets of the service provider within the scope of the outsourced insurance and reinsurance activities and the functions included in the system of governance,
- the possibility to examine the service providers located on the territory of Poland within the scope of the activities outsourced by the foreign insurance undertaking (Domański, Zakrzewski, Palinka, 2016).

In case of failing to comply by the insurance undertaking with the supervisory authority's guidance, it may impose pecuniary penalties (the act, 2015, Article 363 item 4):

- on the member of the management board or a proxy – up to the amount corresponding to triple average remuneration from the last 12 months, and if this cannot be determined – up to the amount of 100,000 PLN,
- on the insurance undertaking or reinsurance undertaking – up to the amount equal to 0.5% of the gross written premium reported in the financial statement for the previous financial year, and if the activity was not performed or the gross written premium was less than 20 ml PLN – up to the amount of 100,000 PLN.

5. SUMMARY

The objective of outsourcing activity in insurance undertakings and reinsurance undertakings is to supplement, to support the critical insurance activities facilitating an undisturbed course of activity. Nevertheless, not every insurance activity can be outsourced. The scope of the insurance activities that can be outsourced is provided for in the legal regulations which determine not only what but also on what terms and conditions can be outsourced.

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