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Audit as a control mechanism used by insurance companies

Auditing is used by insurance companies in the form of external audits, internal audits, and audit committees. Their principal objectives are more efficient risk management processes and adequate generation of finance and accounting information. The significance of these control mechanisms will be enhanced by the introduction of Solvency II, though their operation is also provided for by balance sheet laws. Research indicates that insurance companies have integrated these mechanisms as part of their structures, yet the rules governing them need to be streamlined, as suggested not only by the regulations of the Solvency II directive, but also insurance companies themselves.

In view of the similarity between the objectives and scopes of audits carried out by insurers, it is reasonable to strive toward assuring principles of mutual cooperation in order to increase their effectiveness and improve the implementation of audit objectives.

This paper discusses the operation of audits in the practice of insurance companies, namely as internal audits and audit committees, as well as the principles of cooperation between internal audits and external audits in light of empirical research.

Key words: insurance, accounting in insurance companies, internal audit, external audit, audit committee.

Introduction

The key reason for applying control mechanisms is the presence of diverse irregularities – intended ones, defined as financial (book-keeping) frauds, or unintended errors, which are part of the operational risks experienced by every business. Thus, they comprise all kinds of irregularities caused by processes, humans, systems or accidents. Research shows that they are a major problem for all businesses. Therefore, appropriate control mechanisms may be a key step toward the improvement of the management system and a factor contributing to improved effectiveness of business undertakings.

The application of appropriate control mechanisms, including internal controls, internal audits and risk management, is not only a duty arising from regulations and good practices, but also a means of protecting shareholder interests against any abuses or improper disclosure of information presented in accounts. They are a part of corporate governance.

The functioning of adequate corporate governance, which is defined as a system according to which an enterprise is run and managed,[1] contributes to enhanced competitiveness, since a well-managed enterprise guided by the principles of sustainable development is better prepared to pursue a specific strategy and builds public confidence in the marketplace. Corporate governance is a method of restricting adverse practices, namely the adoption of short-term views and the acceptance of excessive risk[2].

Thus, adequate corporate governance,[3] inclusive of control mechanisms, is expected to provide for effective management and actions, chiefly in finance and accounting. Auditing is one of such mechanisms, applied as external audits, internal audits and audit committees.[4]

This paper is intended to discuss the reasoning behind auditing as a control mechanism in insurance companies and the various forms of audits, as well as to assess the principles of their operation in the practice of insurers.

Research conducted by the Polish Insurance Association, Polish Financial Supervision Authority, Polish Institute of Directors, Deloitte, and Ernst& Young has been used in this paper.

Descriptive and comparative analyses have been applied.

1. Scope and causes of applying control mechanisms

Article 41 of the *Solvency II* Directive stipulates that insurance and reinsurance companies are required to implement management systems that will assure correct and prudent management of the business in consideration of its nature, scale and complexity. This implies the need to introduce control mechanisms to provide for sufficient information flow and regularity of continuing business.

Insurance and reinsurance companies are required to maintain written rules of risk management, internal controls, internal audits and outsourcing, to be reviewed annually, mainly in the framework of new risks identified by insurers that may affect their adequate financial standing.[5]

1. The Committee on the Financial Aspects of Corporate Governance, "The Financial Aspects of Corporate Governance," The Cadbury Report. London: Gee, 1992, 15.
2. Directorate for Financial and Enterprise Affairs, OECD Steering Group on Corporate Governance, "Corporate Governance and the Financial Crisis. Conclusions and emerging good practices to enhance implementation of the Principles," OECD paper, 2010.
3. For more information about corporate governance, see the European Commission, "The UE corporate governance framework," Green Paper presented in Brussels, Belgium, on April 5, 2011; and European Commission, "Corporate governance in financial institutions and remuneration policies," Green Paper presented in Brussels, Belgium, on June 2, 2010.
4. For more information about audit, see: W. Gabrusewicz, ed., "Audyt sprawozdań finansowych," Warszawa: PWE, 2010; M. Kutera, "Rola audytu finansowego w wykrywaniu przestępstw gospodarczych," Warszawa: Difin, 2008; K. Winiarska, Audyt finansowy. Warszawa: PWE, 2009; B. Micherda, ed., "Kierunki ewolucji sprawozdawczości i rewizji finansowej," Warszawa: Difin, 2012; Mikołajczyk B. and M. Krawczyk, "Audyt wewnętrzny w teorii i praktyce ubezpieczeniowej," Warszawa: PWE, 2010.
5. Article 41 of Directive 2009/138/EC of The European Parliament and of The Council of 25 November 2009 (*Solvency II*), *Official Journal of the European Union*, L 335, 17/12/2009, and Directive COD 2011/0006 of The European Parliament and of The Council (Omnibus II) changing Directive 2003/71/EC and 2009/138/EC.

Control mechanisms imposed on insurance companies in line with the *Solvency II* Directive:

- requirements relating to competences and reputations of individuals who actually manage an insurer or occupy other key positions – Article 42,
- risk management – Articles 44 and 45,
- internal control – Article 46,
- internal audit – Article 47.

According to Article 41 of the *Solvency II* Directive, the selection of control mechanisms should comply with the following principles:

- the system should have an appropriately transparent structure including clearly assigned and divided tasks that provides for the appropriate flow of information,
- they should be subject to regular internal reviews every year as a minimum,
- they should be approved by an administrative, management or supervisory authority,
- a control system should be verified by a supervisory authority with regard to risks identified by the insurer that may affect adequate financial standing,
- a supervisory authority should have the right to require improvement and strengthening of the management system,
- they should be adapted to the nature, scale and complexity of an insurer,
- they should reflect any changes in the insurer's operations,
- the control mechanisms applied should contribute to continuity and regularity of the insurer's operations,
- rules of risk management, internal audit, internal control and outsourcing should be executed in writing.

The implementation of the *Solvency II* Directive will oblige insurance companies to run effective management systems that will execute a substantial amount of their tasks via appropriate control mechanisms, both qualitative, as part of the corporate culture, and those based on corporate control mechanisms.

The system should be adapted to the needs, scale and complexity of an insurer's operations and should as a minimum comprise risk management, internal controls and internal auditing. Adjustment to needs, scale and complexity means that an insurer may outsource certain mechanisms, keeping in line with specific principles.

Such a management system including a full range of control mechanisms will undoubtedly improve information flow and thereby help to detect any irregularities faster, thus giving rise to a better system of diagnosing the financial standing of insurance companies.

Of course, having a variety of control mechanisms is not a guarantee of their effectiveness. A lot depends on proper selection, the instruments applied, and their assignment to particular areas of an insurance company's business. It must be noted, though, that it is true that the more control mechanisms are utilised, the more easily irregularities will be detected[6].

The control mechanisms introduced will enhance the quality of insurance businesses. This will result from on-going reviews, verification, evaluation and the adjustment of old principles and solutions to meet new needs and conditions. This is the only effective way of exploring new risk types and their effective management, or at least one that will not jeopardise an insurer as a going concern.

6. For more information about control mechanism and economic crime, see: PriceWaterhouseCoopers et al., "Economic crime: people, culture and controls. The 4th biennial Global Economic Crime Survey," London: PriceWaterhouseCoopers, 2008.

Unfortunately, the research demonstrates that these mechanisms are not well-known or understood. Costs and the absence of data to support their profitability are common barriers to their implementation, with the new legislation imposing the duty of introduction as the only incentive. Therefore, the solutions proposed by the *Solvency II* Directive must be appreciated in relation to businesses such as insurers where reliable and real service is required, since each instance of insolvency can undermine confidence in the entire insurance market for years to come.

It is worth noting that Article 2, part 4d and Article 86 of the Act on Expert Auditors and Their Self-Government, Entities Authorised to Examine Accounts, and Public Supervision of 7 May 2009 ("Act on Auditors and their Self-Regulatory Bodies", Journal of Laws No. 77, item 649, as amended) treat insurers as public interest organisations, subject to financial auditing that is compulsorily strengthened by the duty to establish audit commissions and introduce public supervision in order to provide for high professional standards of auditors and auditing companies, and thus to streamline supervision of financial reporting processes and ensure reliable internal control and risk management.

2. Public supervision of insurance companies – audit committee

Public supervision is carried out by audit committees appointed by supervisory boards or boards of auditors from among their members,[7] which companies were required to establish by 6 December, 2009, i.e. within six months of the effective date of the amended Expert Auditors Act.

Article 86 (2) of the Act contains a list of entities that are exempt from the obligation to establish an audit committee. These are:
- pension funds, investment funds,
- branches of credit institutions and branches of foreign banks,
- the main branches of insurance companies,
- co-operative banks,
- public interest entities, in which a supervisory board or an audit committee has not been established,
- co-operative savings and credit societies.

Audit committees must have a minimum of three members, including at least one independent member with accounting or financial auditing qualifications.[8]

Independence requirements are detailed in Article 86 (5) of the Act, which lists cases disqualifying one as being considered independent, including:
- holding of shares or other titles in the organisation or its associated organisation,
- involvement in the drafting of the organization's books or accounts within the past 3 years,
- marriage, relation or first or second-degree direct affinity, or relations of care, adoption or guardianship with a member of management or of the organisation's supervisory or administrative bodies.

In mutual insurance societies, the independence condition is also regarded as fulfilled when a committee member holds shares or other titles in the organisation or its associated entity due to the unique nature of mutual assurance societies.

7. Article 48 of the Act on Auditors and their Self-Regulatory Bodies of 7 May 2009 (Journal of Laws of 2009, No. 77, item 649).
8. Ibidem, article 86.

The requirements of accounting and financial auditing are not defined by statutes, and the relevant decisions are left to authorities appointing audit commission members. They are, thereby, not only capable of selecting appropriately qualified individuals, but also of considering experience corresponding to the profile of a given organisation.

Notably, in public interest organisations with supervisory boards of up to five members that fulfil the functions of an audit committee, the requirements concerning independence and accounting or financial auditing qualifications are not enforced, though failure to meet these requirements is treated by the Polish Financial Supervision Authority as a major risk factor to be included in share issue prospectuses and information memoranda.[9]

The operation of audit committees in Poland, and in particular, their goals, have been presented on the basis of the research conducted by Deloitte in association with the Polish Institute of Directors Foundation under sponsorship of the Polish Financial Supervision Authority.[10]

Twenty eight per cent of the organisations examined were active in the sector of financial services, which includes insurance companies.

Applicable legislation states that goals of audit committees may be carried out by:

- audit commissions consisting of a minimum of 3 members, including at least 1 member meeting the conditions of independence with accounting or financial auditing qualifications,[11]
- supervisory boards comprising not more than 5 members.[12]

Thus, the composition of a supervisory board determines the means in which public supervision objectives should be carried out.

Research by Deloitte shows that in 57 per cent of the organisations examined, supervisory boards consisted of more than 6 members (6–7 members in 42 per cent organisations, 8–10 members in 10 per cent of organisations, 11 and more members in 5 per cent of the entities examined), which means that audit commissions should function in these organisations.

Five-member supervisory boards operated in 33 per cent of organisations and 3–4-member boards in 5 per cent of entities, which signifies that public supervision objectives could, but did not have to be undertaken by supervisory boards of 38 per cent of these entities. Research shows audit committees were established in 66 per cent of the organisations queried, which indicates they have been created in some organisations where it was not necessary, pointing to increased awareness and perception of absence of a committee as a risk factor to business operations.

The objectives as part of public supervision, implemented by either audit committees or by supervisory boards, are tabulated below.

In summary, the tasks of audit committees relate to the process of risk management – its identification and restriction in the areas of financial reporting and auditing, as provided for by legislation defining the roles to be fulfilled by audit commissions. The analysis shows, however, that only some audit commissions take a complex approach to the risk management process, i.e.,

9. Urząd Komisji Nadzoru Finansowego (Polish Financial Supervision Authority), "Rekomendacje dotyczące funkcjonowania komitetu audytu," Warszawa: Urząd Komisji Nadzoru Finansowego, 2010, 6.
10. Deloitte and Urząd Komisji Nadzoru Finansowego, "Raport: Współczesna rada nadzorcza 2012. Praktyka ładu korporacyjnego w Polsce," Warszawa: Polski Instytut Dyrektorów, 2012.
11. Article 86 of the Act on Auditors and their Self-Regulatory Bodies of 7 May 2009 (Journal of Laws of 2009, No. 77, item 649).
12. Ibidem.

cyclical and considering key risks associated with business operations (36 per cent). Most entities under consideration take incidental (54 per cent) or no (9 per cent) interest in risk. Worryingly, most audit committees do not perceive the risk of abuses as their major task – only 24 per cent of the entities reviewed undertake regular analyses of business operations with regard to this risk.

Table 1. Objectives as part of public supervision (% of entities examined)

Type of objective	All-round approach	Partial realisation	No realisation
Analysis of business and operational risk, rules of risk management	36	54	9
Assessment of effectiveness of internal control system (independent from management board)	2	71	27
Work with management board in the assessment process of internal control and risk management system	19	21	60
Prevention of abuse (risk management)	24	59	17
Assessment of entity's social responsibility regarding quality of the communication process and investor relations reporting	26	42	30
Assessment of internal auditor's performance	22	36	42
Meetings with internal audit director	34	30	36
Meetings with external audit (external auditor takes part in meetings of supervisory board or audit committee)	5	71	24
Supervisory board or audit commission meets the external auditor of the accounts	43	33	24
Assessment of cooperation quality between external audit and management board	38	–	62
Impact of supervisory board on responsibilities of internal audit function (planning of audit objectives)	15	28	57
Supervisory board or audit commission are informed about results of the internal auditor's efforts	22	36	42

Source: the author's own compilation on the basis of a report by Deloitte and Polish Financial Supervision Authority "Współczesna rada nadzorcza 2012. Praktyka ładu korporacyjnego w Polsce."

Collaboration of audit committees with internal and external auditors and other company authorities is successful, though in most cases it does not represent an all-around approach to the issue under analysis, thus it cannot be treated as programmatic or systematic.

In time, the flaws will be eliminated, which will contribute to a fuller implementation of objectives envisaged for audit committees. This still requires increased awareness of risk and the role of audit committees as mechanisms of public supervision, although businesses are obliged to set them up and supply them with relevant instruments and mechanisms of control. Their development will only be possible, though, once the absence of an audit committee is seen as a major risk factor interfering with business growth.

The figures tabulated below are proof of the continuingly scant application of tools essentially providing for the effectiveness of audit committees.

The analysis of these results shows that the bulk of entities do not take advantage of these instruments, largely for the reasons discussed before – audit committees are not seen as tools supporting the risk management process or as effective mechanisms of public supervision.

Surprisingly, such globally common mechanisms as codes of ethics, whistleblowing and compliance are employed by fewer than a half of the businesses examined: whistleblowing – by 29 per cent, compliance – by 44 per cent, codes of ethics – by 53 per cent.

It should be stressed, however, that as audit committees develop, control tools will increase in numbers and new ones will emerge, while some others will cease to be applied since the changing business environment will give rise to new risks, as well as new methods and instruments to evaluate and monitor them.

Table 2. Instruments exercised by audit committees (% of entities examined)

Control instrument	Complex approach	Partial realisation	No usage
Whistleblowing – procedure of anonymous notification of abuses to management or the supervisory board	29	11	60
Codes of ethics	53	–	47
Analysis of transactions between company and management board members and of transactions with associated entities, other than typical (operational) transactions	69	14	17
Analysis of links between commercial partners of a company and management board members or staff with regard to conflicts of interest	38	36	26
Compliance function of an entity	44	–	56
Analysis of corruption and abuse risks	29	26	45

Source: the author's own compilation on the basis of a report by Deloitte and Polish Financial Supervision Authority "Współczesna rada nadzorcza 2012. Praktyka ładu korporacyjnego w Polsce."

3. Internal audit in practice of insurance companies

The importance of internal audits for insurance companies is set to increase as the system of solvency assessment in compliance with assumptions of *Solvency II* is implemented. Pillar II will focus on the particular significance of control mechanisms, including internal audits, on the relationship between the internal auditing function and the effectiveness of insurance company management.

Ernst&Young evaluated the role of internal audits in insurance companies in a 2011 study, part of which analysed UK and Western European insurers in the following respects:

- scope of internal auditing,
- qualifications of internal auditors,
- audit planning,
- methodology of internal audits,
- impact of *Solvency II* on internal audits,
- challenges to internal audits.[13]

13. Ernst & Young, "Insurance internal audit survey. Current challenges and emerging trends," a report by Ernst & Young, September 2011.

The principal role of the internal auditing is to support business operations by evaluating processes of risk management and internal control. The research demonstrated that the expectations of internal auditing chiefly involve:
- risk management,
- responding to changing business factors,
- assessment of management systems and prevailing practices.

Insurers pointed to the following key areas to be monitored by internal audits:
- business goals – support for their implementation,
- business productivity,
- staff qualifications and skills – better utilisation,
- consultancy on programmes implementing changes,
- indication of change areas,
- reducing the risk of fraud,
- consultancy on launching new products and entering new markets,
- comparison with other insurers or other similar businesses,
- continuation of business monitoring.

When asked about the expected time frame over which internal audits should improve business functions, 50 per cent of the queried insurers selected the forthcoming 12 months, 25 per cent – within 1–2 years (between 12 and 24 months), while 25 per cent perceived no such need.

These results can be interpreted as follows:
- insurance companies see no reasons for change since, in their beliefs, internal audits properly fulfil their purposes, and their scope covers all key areas,
- insurance companies perceive limitations on the verification of internal audit schedules in place, therefore 50 per cent of surveyed insurers see no potential for changing internal audits within 12 months. These are limitations arising from the planning process of internal audits.

Actuarial, risk and finance management skills are internal auditor qualifications most commonly highlighted by insurance companies. Actuarial knowledge deserves particular attention as it is unique to insurers, and without it the examination of any insurance business is basically futile and incapable of generating any reliable knowledge of an insurer's current position.

In the short term, internal auditing in insurance companies should comprise the following areas:
- *Solvency II* – contribution to the sustainable development of processes to be carried out, as well as monitoring of the extent and manner of their implementation,
- changes – monitoring implemented projects and business programmes, with more focus on the actual effects of changes rather than conforming project assumptions to reflect the implementation of these changes,
- risk management – concentration on effective management, as well as the development of new risk management rules and practices.

Solvency II and the management of change processes were the key areas to be included in audit schedules as indicated by insurers – 78 per cent each.

The methodology of an audit is based on the specific characteristics of the on-going changes – 58 per cent of the analysed insurance companies had varied their strategies of internal audits in the previous three years. The most common changes included:
- staffing changes,

- the need to adapt internal auditing to the objective and strategy of the insurance company (this cause seems to be a result of the implementation of *Solvency II*),
- software changes.

When asked to assess the extent of changes made to their internal auditing methodology, 41 per cent of insurers said they were moderate, with only 17 per cent not having undertaken any changes at all.

The major challenges to internal auditing include continuing improvement of risk management processes and standardisation of control. This was corroborated by the results – 84 per cent of examined insurance companies found that risk management and compliance should improve in the future, chiefly thanks to *Solvency II*.

The function of internal auditing in insurance companies is tabulated below.

Table 3. Principles of internal audit operation in insurance companies

Area of evaluation	% of insurers queried
Key qualifications of internal auditors in insurance companies:	
• Actuarial	83
• risk management	33
• IT, finance	25
Cooperation of internal audit with the environment of insurance company:	Mark[14]:
• external audit	3.00
• professional institutions	2.92
• public information	2.58
• other audit companies	2.50
• other	1.58
Areas most commonly included in internal audit scheduled of insurers:	
• *Solvency II*	78
• management of changes processes	78
• risk	44
• finance	33
• assessment of insurance risk	33
• other	44
Scope of changes to internal audit methodology:	
• significant	17
• moderate	41
• minor	25
• no change	17
Assessment of risk management processes and compliance in insurance companies:	
• optimized	0
• advanced	8
• established	84
• evolving	8
• basic	0
Areas of *Solvency II* included in annual internal audit schedules (pillar I):	
• standard models	100
• internal models	83
• independent model validation	58
• quantitative indicators	92

14. The highest mark is 3.50 – it represents very effective cooperation; the lowest mark is 0.50 – it represents an absence of effective cooperation.

Areas of *Solvency II* included in annual internal audit schedules (pillar II):	
• management	100
• effectiveness of risk management	92
• ORSA (Own Risk&Assessment)	92
Areas of *Solvency II* included in annual internal audit schedules (pillar III):	
• external monitoring	75
• publication readiness	67
• compliance with internal solutions and financial reporting	67

Source: the author's own compilation on the basis of a report by Ernst & Young, "Insurance internal audit survey. Current challenges and emerging trends".

It can be concluded that the area of internal auditing for insurance companies will continue to develop, largely due to the implementation of *Solvency II* and to the very nature of internal auditing, which by definition must consistently undergo changes to be capable of effectively supporting risk management. This will be reflected in modifications to current audit methodologies and in the development of the actuarial function, which is unique to insurance companies.

4. Cooperation between internal audit and external audits

Internal and external audits are control mechanisms tasked with the evaluation of certain processes of an insurance company in order to eliminate potential errors and threats. It must be emphasised, though, that the scopes of internal and external audits are essentially different:

– internal audits cover the entire business of an insurer, thus they are able to identify and assess any risks to operations,
– external audits involve, in particular, the verification of accounts and their compliance with applied accounting principles (policies), together with the reliability and clarity of the standing and financial performance of the entity under examination.[15]

Thus, the scope of internal audits is significantly broader than that of external audits. It cannot be said, however, that the scope of external audits is within the scope of internal audits – in theory, accounting and finance issues, as well as financial audits are parts of internal audits, however in this case they are usually not subject to, for example, a thorough annual review since they are treated as lower-risk and can be excluded from internal audit schedules as a result. Therefore, the role of external auditing does not diminish when internal audit is introduced. Verification of an insurer's accounts and accounting policies is the sole responsibility of expert auditors, that is, external audits.

Mutual cooperation between both types of auditing is highly recommended, not only because the scopes of both overlap, but also due to the fact that it can be of advantage to both internal auditors and expert auditors.

Collaboration between internal and external audits is rooted in standards governing both control mechanisms.

15. B. Mikołajczyk, M. Krawczyk, "Audyt wewnętrzny w teorii i praktyce ubezpieczeniowej," Warszawa: PWE, 2010, 27; T. Kiziukiewicz, ed., "Audyt wewnętrzny w jednostkach sektora finansów publicznych," Warszawa: Difin, 2007, 14–15; W. Gabrusewicz, ed., "Audyt sprawozdań finansowych," Warszawa: PWE, 2010, 14–16.

In line with the National Standard of Financial Auditing, No. 1, *General Principles of Accounts Auditing*, an expert auditor examining accounts can take advantage of the findings of an internal audit and internal control with regard to the reliability and conformity of information contained in accounts with applicable accounting principles (policies), provided they have previously verified that these findings could be relied on. The need to verify the reliability of an internal audit methodology is an added incentive to develop principles of cooperation between internal and external audits, as it would facilitate the preparation of some joint solutions. The compulsory change of expert auditors and the consequent need to re-establish rules of cooperation appears to pose some problems. The problem is only theoretical, though, and should be treated as an additional control mechanism helping to verify the existing cooperation and eliminate potential risks, e.g. flawed or missing procedures.

According to *International Standards for Professional Practice of Internal Auditing*, an internal audit is intended to coordinate the actions of both external and internal providers of assurance and consultancy services in order to ensure an appropriate scope of auditing and to avoid duplication of activities. Therefore, actions carried out by external auditing should be considered when planning tasks of internal auditing, in particular:

- scope of accounts audited,
- risk assessment,
- techniques and methods of examination.

These considerations imply that the standards concerning both internal and external auditing envisage mutual collaboration of these control mechanisms. The following elements are required to this end:

- an appropriate way of communication, involving the transfer of certain information and regular meetings,
- evaluation of generated information, involving the access to auditor programmes, working materials and notes,
- application of similar work techniques and methods,
- assessment of the effectiveness of cooperation between internal auditing and expert auditors by an internal audit administrator.

It should be mentioned that the management or supervisory board is the authority assuring cooperation between internal and external auditing, as well as monitoring the effectiveness of their cooperation. In line with the recommendations of the Polish Financial Supervision Authority,[16] audit commissions should act as coordinators of collaboration between expert auditors and internal auditors. However, these coordination efforts should include in particular:[17]

- joint discussions about draft annual schedules of internal auditing and the scope of accounts examination, including risk methodology and perception to apply,
- assessment of coordination of the cooperation between internal auditing and expert auditors, including determination of whether efforts by internal auditing and expert auditors are being doubled and, possibly, the determination of reasons for such duplication,
- verification of accounts prior to their approval, a discussion with internal auditing and expert auditors of the possible weaknesses in the internal control system identified as part of auditing,

16. Urząd Komisji Nadzoru Finansowego, "Rekomendacje dotyczące funkcjonowania komitetu audytu," Warszawa: Urząd Komisji Nadzoru Finansowego, 2010.
17. Polska Izba Ubezpieczeń (Polish Insurance Association), "Dobre praktyki w zakresie współpracy między audytem wewnętrznym a biegłym rewidentem w zakładach ubezpieczeń," Warszawa: Polska Izba Ubezpieczeń, 2011, 16.

- joint consideration of monitoring results of an insurer's implementation of recommendations issued as part of account auditing,
- taking advantage of the results arrived at by internal auditing and expert auditors for the purposes of an annual assessment of the internal control and risk management systems,
- taking advantage of internal audit analysis as part of forming opinions about expert auditor's independence.

The cooperation of internal and external auditing is also based on the *Solvency II* Directive, according to which internal audit is a key function in the management system, in parallel with risk management, actuarial, and regulatory compliance functions.

For the internal audit function to be carried out, it should add value and improve organisation, which in turn requires a disciplined approach to assessment, and improved effectiveness of risk management, control and insurer management processes. Therefore, the management of an insurance company should employ a variety of sources in its assessment of risk management effectiveness.

Collaboration of internal and external auditing may undoubtedly contribute added value to an insurance company and thus bring a number of benefits to both sides, including[18]:

- more effective auditing (both internal and external),
- less effort on the implementation of audit tasks,
- better and more complete risk identification,
- better planning of an auditor's work,
- better understanding of the results that can affect future internal and external auditing actions,
- sharing knowledge and experience,
- cost reductions.

The cooperation of internal and external auditing is indubitably an element contributing to the improved effectiveness of internal and external audits, it helps to prevent doubling of certain actions as part of audit efforts and enhances the reliability of an insurance company – obviously, everything depends on the model of mutual collaboration used.

The state of cooperation between internal and external auditing has been appraised on the basis of surveys conducted by the Polish Insurance Association in 2011.

It was undertaken in respect of the following areas:

- form of communication, where the ways and frequency of communicating are evaluated,
- planning of internal audits, where consulting of internal audit schedules with expert auditors – scope and areas of the consultation – are assessed,
- utilisation of internal audit analyses (testing) by expert auditors – an area appraising reliability and effectiveness of internal auditing to a substantial extent. Based on internal audit tests denotes high appreciation by the expert auditor and a possibility of predicting results and analyses, whereas the failure of the internal auditor to take advantage of the analyses is proof of the expert auditor's low opinion about the internal auditor efforts, respectively,
- transfer of expert auditor's knowledge to internal audit, where the utilisation of internal auditing results by expert auditors and vice versa is analysed,
- assessment of quality of cooperation between expert auditors and internal auditing.

The results concerning cooperation between internal and external audit are tabulated below.

18. Polska Izba Ubezpieczeń, "Dobre praktyki w zakresie współpracy między audytem wewnętrznym a biegłym rewidentem w zakładach ubezpieczeń," Warszawa: Polska Izba Ubezpieczeń, 2011, 18.

Table 4. Cooperation of internal and external audits in insurance companies

Area of cooperation	% insurance companies examined
Form of communication between internal audit and expert auditor:	
• supply of internal audit documentation at the time of an expert auditor's visit	21
• 2–5 meetings a year – supply of internal audit documentation	64
• on-going supply of materials during the year	28
• tripartite meetings – internal auditor, expert auditor and audit commission	14
Planning of internal audits:	
• development of internal audit schedules by expert auditors	0
• consultation about scheduled audits at meetings between the expert and internal auditors	14
• expert auditor reports observations on areas subject to audit schedule	14
• expert auditor presents their own evaluation of major risks	14
Utilisation of tests by internal auditor:	
• expert auditor does not rely on testing carried out in the internal audit	35
• no information on expert auditor's reliance on testing by internal audit	35
Transfer of expert auditor's knowledge to internal audit:	
• expert auditors fail to share their knowledge or experience about the internal audit methodology	100
Assessment of cooperation between expert auditor and internal audit:	
• internal audit has no opinion on cooperation with expert auditor	64
• cooperation between expert auditor and internal audit must be more efficient	57
• opinion on cooperation of expert auditor and internal audit is submitted to management board	21
• opinion on cooperation of expert auditor and internal audit is submitted to audit commission	28

Source: author's compilation on the basis of: Polska Izba Ubezpieczeń, *Dobre praktyki w zakresie współpracy między audytem wewnętrznym a biegłym rewidentem w zakładach ubezpieczeń,* (Warszawa: Polska Izba Ubezpieczeń, 2011), 10 et. seq.

The research demonstrates that the scope and the principles of cooperation between internal and external audits in insurance companies need to be more efficient, as indicated by 57 per cent of the insurers examined. It applies to virtually every area of cooperation. The key reservations concern:

- communication – expert auditors take advantage of the internal audit documentation at the time of accounts auditing in only 21 per cent of entities queried, whereas tripartite meetings of internal auditor, expert auditor and audit commission are held only in 14 per cent of the organisations;
- schedule of internal auditing – consultation of audit schedules with expert auditors and expert auditor's observations on areas subject to audit schedule are arranged by merely 14 per cent of the insurers tested;
- utilisation of tests by the internal auditor – in principle, expert auditors do not rely on testing by internal audits in 70 per cent entities;
- transfer of the expert auditor's knowledge to the internal audit: One hundred per cent of the insurance companies analysed pointed to the absence of this transfer.

It can be concluded that the principles and the scope of cooperation between internal and external audits require the development of certain good practices, bound to emerge in time – internal auditing is a relatively recent control mechanism in insurance entities and both its work methodologies, significance and status are still evolving. It should be stressed that the objectives of internal auditing differ from those of external auditing, defined as financial auditing. Beyond any doubt, such cooperation is useful in the perspective of both internal and external auditing since it may facilitate auditing goals and contribute to the increased effectiveness of the control mechanisms in question.

Conclusions

Auditing is undoubtedly a very important control mechanism for insurance companies as it supports management processes, in particular, in the areas of finance, accounting and risk management.

Applicable legislation binds insurers not only to have their accounting policies and accounts verified by expert auditors (external – financial auditing), but also to implement internal auditing and audit committees, the elements of public supervision.

The introduction of these control mechanisms in pursuit of similar objectives – supporting risk management processes in insurance companies – enforces the development of principles and areas of cooperation in order to enhance their effectiveness, reduce labour expenditures on auditing efforts, and improve the management of risk associated with the operations of insurance companies.

The research indicates that insurers have pointed to such areas and overall principles of collaboration, yet this is a process to be detailed and modified many times in the future. This applies in particular to the cooperation between internal and external auditing, but also between internal audits and audit committees – more than 50 per cent of the insurance companies queried perceive the need for such improvements and for more detailed rules of collaboration, chiefly in the field of mutual communication and sharing of experience, as well as audit scheduling.

The implementation of *Solvency II* will become a major driver of changes in audit operations by insurers and particularly their scope, a key object of analysis by internal audit, audit committee, and external audit. In time, forms of cooperation between these control mechanisms and the range of control tools will expand. It is difficult to precisely envisage the directions of these changes, as they will depend on shifting realities and new types of risk threatening the operations of insurance businesses. This is coherent with the idea and purpose of internal auditing, which must be subject to an on-going process of change in order to effectively support the risk management process in an insurance company.

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Audyt jako mechanizm kontrolny wykorzystywany w zakładzie ubezpieczeń

Audyt występuje w zakładach ubezpieczeń w formie audytu zewnętrznego, wewnętrznego oraz komitetów audytu. Zasadniczym celem ich funkcjonowania jest usprawnianie procesów zarządzania ryzykiem w zakładzie ubezpieczeń, a także zapewnienie prawidłowego generowania informacji w obszarze finansów i rachunkowości. Znaczenie wymienionych mechanizmów kontrolnych wzrośnie wraz z wdrożeniem Solvency II, choć ich funkcjonowanie wynika także z prawa bilansowego. Jak pokazują badania zakłady ubezpieczeń posiadają w swoich strukturach wymienione mechanizmy kontrolne, jednak zasady ich funkcjonowania wymagają usprawnienia, na co wskazują nie tylko regulacje Dyrektywy Solvency II, ale także same zakłady ubezpieczeń.

Ze względu na podobieństwo celów realizowanych w zakładzie ubezpieczeń audytów, a także w znacznym stopniu ich zakresu celowe jest także zapewnienie odpowiednich zasad ich wzajemnej współpracy w celu zwiększenia efektywności oraz usprawnienia procesu realizacji zadań audytowych.

W artykule zaprezentowano funkcjonowanie audytu w praktyce zakładów ubezpieczeń, występującego w formie audytu wewnętrznego oraz komitetów audytu, a także zasady współpracy audytu wewnętrznego z audytem zewnętrznym w świetle badań empirycznych.

Słowa kluczowe: ubezpieczenie, rachunkowość zakładów ubezpieczeń, audyt wewnętrzny, audyt zewnętrzny, komitet audytu.

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