

# FINANCE AND MONEY TURNOVER

UDC 368.024

DOI <https://doi.org/10.26661/2414-0287-2024-2-62-15>

## PROBLEMS OF FORMATION OF A CAPTIVE INSURANCE COMPANY AT THE PRESENT STAGE

**Kisilyova I.Yu., Gorbunova A.V.***Zaporizhzhya National University**Ukraine, 69600, Zaporizhzhia, Zhukovsky str., 66*

inna\_kisileva@ukr.net, gor\_an\_v@ukr.net

ORCID: 0000-0002-6486-6546, 0000-0001-6450-4740

**Key words:**captive insurance company,  
synergistic effect, advantages of  
captive insurance.

The article discusses the modern problems of introduction of captive insurance organizations. It is noted that the issue of the activities of captive insurance organizations is not reflected in the legislation, that is, there is no legislative framework, although the activities of captive companies differ significantly from the activities of commercial insurers. Another problem that hinders the development of captive insurance is the lack of qualified personnel. There is also a problem with the information and technical support of captive insurance. It is shown that the parent company can consider a captive insurer as a tool for insuring only its own risks (the most common option now), or as a tool for obtaining a synergy effect. The main synergistic effects of captive insurance have been determined.

The main problems that arise during the organization of a captive insurance company are defined: limited insurance field; additional costs for the establishment and operation of a captive insurance company; the need to use the services of the insurance market; deterioration of the financial stability of a captive insurance company; time spent by management structures during the period of organization of a captive company for its creation and formation.

The advantages of creating a captive insurance company for the parent organization are determined: saving the company's funds and shorter terms of compensation for losses than with insurance; making a profit from the activities of a captive insurance organization; risk minimization; diversification of risks; supplement to insurance in professional insurance companies; entering the reinsurance market, etc. It is determined that the introduction of captive insurance can have a positive impact on the economic security of the parent organization and revive the development of the insurance market.

The ways of introduction of captive insurance in Ukraine are proposed.

---

## ПРОБЛЕМИ ОРГАНІЗАЦІЇ КЕПТИВНОЇ СТРАХОВОЇ КОМПАНІЇ НА СУЧАСНОМУ ЕТАПІ

**Кисільова І.Ю., Горбунова А.В.***Запорізький національний університет**Україна, 69600, м. Запоріжжя, вул. Жуковського, 66***Ключові слова:**кептивна страхова компанія,  
синергійний ефект, переваги  
кептивного страхування.

В статті розглянуто сучасні проблеми впровадження кептивних страхових організацій. Зазначається, що питання діяльності кептивних страхових організацій в законодавстві не відображено, тобто відсутня законодавча база, хоча діяльність кептивних компаній суттєво відрізняється від діяльності комерційних страховиків. Іншою проблемою, яка перешкоджає розвитку кептивного страхування є відсутність кваліфікованого персонала. Також існує проблема із інформаційно-технічним забезпеченням кептивного страхування. Показано, що материнська компанія може розглядати кептивного страховика як інструмент для страхування виключно власних ризиків (найпоширеніший зараз варіант), або як інструмент отримання ефекту синергії. Визначено основні синергійні ефекти кептивного страхування.

Визначено основні проблеми, які виникають під час організації кептивної страхової компанії: обмеженість страхового поля; додаткові витрати на створення і функціонування кептивної страхової компанії; необхідність використання послуг страхового ринку; погіршення фінансової стійкості кептивної страхової компанії; витрати часу управлінських структур в період організації кептивної компанії для її створення і становлення.

Визначено переваги створення кептивної страхової компанії для материнської організації: економія грошових коштів підприємства і коротші, ніж при страхуванні, терміни відшкодування виниклих збитків; отримання прибутку від діяльності кептивної страхової організації; мінімізація ризиків; диверсифікація ризиків; доповнення до страхування у професійних страхових компаніях; вихід на ринок перестраховання тощо. Визначено, що впровадження кептивного страхування здатне позитивно вплинути на економічну безпеку материнської організації і поживати розвиток страхового ринку. Запропоновано шляхи впровадження кептивного страхування в Україні.

### Problem statement

A captive company is an insurance company that is associated with a large structure, business group, or holding. Captive insurance companies provide risk mitigation services for the business of the dominant or parent structure and are united with them by common business processes.

Thus, captive insurance companies are an effective risk management tool. In Ukrainian realities, with high economic and political risks inherent in the country, and a rather low management culture, the work of captive insurers could be a serious help to business in maintaining safe and stable development. The introduction of captive insurance is fraught with certain problems, in addition, there is no definition of a captive company in the legislation.

### Analysis of recent researches and publications

A captive company is an insurance company that is associated with a large structure, business group, or holding. Captive insurance companies provide risk mitigation services for the business of the dominant or parent structure and are united with them by common business processes. However, the creation of a captive can both increase the efficiency of the company and reduce the results of current economic activity, worsen the management process of the company. Under certain circumstances (for example, without taking into account the costs of creating captives), it is possible not only not to achieve a synergistic effect, but also to reduce the competitiveness of the company.

In the foreign scientific literature, a sufficient number of works are devoted to the issue of captive insurance, in particular [1, 2].

It should be noted that captive companies are a common form of insurance business, but the issue of captive insurance is not sufficiently disclosed in the domestic scientific literature. Bidnyk N.B., Dzoba V.B. [3] analyze the peculiarities of the formation of captive insurance companies in Ukraine. Kravets A.V., Danylovykh T.B., Tymchyshyn I.E. [4] consider the issue of creating captive insurance companies as a method of self-insurance of industrial enterprises. However, recently there has been an increased attention to captive insurance from insurers. Thus, Chernyakhovsky V. [5], General Director of AIB,

analyzes the advantages of creating captive insurance organizations.

However, the literature does not sufficiently systematize the advantages and disadvantages of captive insurance companies, as well as the problems of their implementation.

### Formulating of objectives

The aim of the article is to analyze the possibilities and problems of the use of captive insurance organizations in Ukraine, to consider the measures necessary for the active introduction of captive insurance.

### Presentation of the main research material

The main purpose of a captive insurance company is not to make a profit, but to meet the needs of the owner. The owner may decide to liquidate the insurance company only if the use of the captive insurance company becomes unprofitable, i.e. the costs of maintaining the insurance company exceed (or in the near future will exceed) the total income from its use. Total income means the amount of money saved on insuring the risks of the holding's enterprises, the profit generated by the insurance company from the sale of insurance products through market channels, tax savings, income from the investment activities of the insurance company and income from the reinvestment of insurance reserves in its own investment projects. Thus, if the satisfaction from the benefits received by the holding company when using its own insurance company becomes less than expected, the financial and industrial group is forced to consider options for getting rid of the non-core asset.

Despite the fact that the institution of captive insurance companies is widely represented in the structure of the insurance market of Ukraine, it can be stated that the issues of captive insurance companies are not reflected in the legislation. In fact, there is no regulatory framework for them, although their activities differ significantly from those of commercial insurance companies. The requirements of the Central Bank of Ukraine in relation to insurance companies for captive insurance companies are unreasonably high. Since most of the insurance portfolio of a captive insurance company consists of contracts concluded within a financial and industrial group, when calculating the regulatory ratio

of own funds and assumed liabilities, it is necessary to take into account liabilities to affiliates, this is the group's obligation to itself, so the amount of these liabilities should not be applied to the calculation.

The interest of financial and industrial groups in the development of their own insurance companies has decreased against the backdrop of an unspoken ban on the use of funds accumulated by an insurance company in the interests of the owner. The NBU has established requirements for the placement of insurance reserves, in which it has excluded the possibility of using financial instruments of affiliates, and even more so lending to them. Thus, the funds accumulated by the insurance company actually fall out of the economic activities of the holding, but replenish the stock market, which, as a rule, the owners of the group have nothing to do.

The main problem in the development of captive insurance companies in Ukraine is the negative attitude of the regulator towards captive companies. Taking into account that a number of advantages that captive insurance companies give to the owner have a negative connotation for the state, the position taken by the Central Bank becomes clear. If the regulator follows the path of liberalization of the regulatory framework and makes the work of captive insurance companies effective, then we can expect a dynamic development of this cluster of the insurance market.

However, according to experts, an overabundance of captive insurance companies in the market can lead to the following consequences [3]:

- declining the volume of the open insurance market, and the weakening of a number of major players;
- a decrease in the dynamics of the increase in funds placed in the capital market;
- an increase in the number and amount of insurance contracts and a decrease in tax collection from financial and industrial groups.

As a result, there may be a positive dynamics of development and stabilization of the financial condition of large financial and industrial groups. The multiplier effect of large FIGs can lead to the growth of a number of related industries, which will undoubtedly have a positive impact on the overall economic condition of the state.

The unipolar approach to captive insurance companies used by the financial regulator cannot lead to the maximum economic effect. The institution of captive insurance companies, like other financial and economic institutions, requires a balanced approach that would help to use the best aspects of captive insurance companies and apply the best world practices.

Another problem that hinders the effective functioning of the captive insurance company is staff shortages or lack of qualified personnel.

The desire to win more customers and new markets has focused the attention of corporate training programs in the direction of sales. But the crisis has led to cost reductions, including the use of technologies to optimize the structure and personnel. As a result, there are significantly more candidates with experience and sales skills in the personnel market, but there are practically no candidates with experience in risk assessment, financial and accounting in

insurance companies. In addition to this, it can be said that the specifics of captive insurance companies, risk management in self-insurance, and management of the insurance portfolio of a financial and industrial group are not taught, it can only be acquired with experience.

It is impossible to ignore the problem of captive companies related to information and technical support. Since it is officially believed that there are no captive insurance companies in Ukraine, all of them are commercial, universal, software manufacturers are not interested in developing a specific software product that would meet the needs of captive insurance companies. There are no domestic developments in this area, and foreign analogues are not applicable due to the difference in legislation. Therefore, the activities of captive insurance companies are based on the use of standard information systems of insurance companies [5].

Thus, the lack of a systematic approach to the development of software for captive insurance companies will not allow the creation of a special structured software product.

Therefore, it can be stated that all this makes the efficiency of the captive insurance company extremely low, their work ceases to meet the needs of the owner. The saddest thing is that there are no positive changes in this direction either on the part of the legislator or on the part of the regulator.

As noted in the work of Bidnyk N.B., Dzyoba V.B. [4], the main condition for the existence of a captive insurer is the policy of the parent company, which depends on how the parent company considers the insurance company: to insure only its own risks (the most common option now), or as a tool for obtaining a synergy effect. The main types of synergistic effects are shown in Tab. 1.

However, the creation of a captive can both increase the efficiency of the company and reduce the results of current economic activity, worsen the management process of the company. Under certain circumstances (for example, without taking into account the costs of creating a captives), it is possible not only not to achieve a synergistic effect, but also to reduce the competitiveness of the company. The value of many insurance companies directly depends on such specific assets as human resources: on the professionalism of managers, the qualifications of employees. In addition, achieving a synergistic effect, as a rule, takes several years.

In Ukraine, insurers claim that many of the captive companies are striving to restructure their work in order to become full-fledged market participants capable of independently fighting for customers and increasing the volume of insurance premiums collected. Traditionally, the services of captive insurance companies in Ukraine were used by large business structures to serve their clients and implement tax optimization and capital redistribution schemes within financial and industrial groups. Banks also actively developed controlled insurance companies, thus receiving additional profits, and prevented the outflow of their customers' money to competitors' structures.

At the same time, insurers note that the creation of a captive company, despite everything, remains the most effective way to launch your own insurance business, since

Table 1 – Main types of synergistic effects

See the effects of synergy	The main possibilities of the company are within reach of synergy
Marketing	Development of new markets and distribution channels
	Introduction of complementary products to the market
	Reaping economic benefits from economies of scale
	Gaining Competitive Advantage
Management	Reducing the level of risk of doing business
	Obtaining the technological integrity of the association
	Optimal use of human resources
Financial	Increase in the market value of the integrated merger
	Opportunity to reduce costs and increase the amount of net profit
	Opportunity to save on tax payments
	Additional accumulation of monetary resources
	Financial diversification

Table 2 – Problems of creating a captive insurance organization

Problem	Detailed description of the problem
Limited insurance field	First of all, it means that the activities of a captive insurance organization are limited to the framework of the parent company at the first stage of its development, this increases the risk of occurrence and accumulation of losses. This situation requires a significant volume of reinsurance operations to ensure the financial stability of a captive insurance organization, as a result of which reinsurance costs may be too high.
Additional costs for the establishment and operation of a captive insurance organization	Obtaining an insurance license requires the availability of an authorized capital in the amount determined by law. In addition, the company must have sufficient own funds to ensure its solvency. In the course of the activities of a captive insurance organization, current expenses such as taxes, management costs, etc., also arise.
The need to use the services of the insurance market	The problem with the creation of a captive insurance organization is manifested in such services as inviting experts and specialists of insurance companies to perform work on risk analysis, loss assessment, etc. These services can prove to be expensive for a captive insurance company.
Deterioration of the financial stability of a captive insurance organization	Due to the desire of the parent company's management to reduce insurance costs. Since a captive insurance organization is actually a subdivision of the parent organization, its administration can influence the management structures of the captive insurance organization, forcing them to make certain decisions, which is impossible if the organization deals with an independent insurer.
Time spent by management structures during the period of organization of a captive company for its creation and formation	A large investment of time and money on the part of the parent company is required, which may not be adequate to the expected benefit from the creation of a captive insurance company.

it allows you to build a really working company with good potential in a short time, which, on the one hand, will be able to provide professional insurance risk management of the interests of financial and industrial groups, and on the other hand, gradually begin to increase income from work in a competitive market.

During the organization of a captive insurance company, various problems arise, which are presented and described in Tab. 2 [4].

From the creation of a captive insurance organization, enterprises can also receive many benefits, the implementation of which can have a positive impact on the financial and economic security of enterprises.

Setting up a captive insurance organization can help reduce the insurance rate by reducing certain cost items that are predominantly included in the cost of insurance (e.g., administrative costs). Insurance costs are also reduced because the parent company can gain access to a cheaper reinsurance market with the help of a captive insurance organization.

The successful operation of a captive insurance organization increases the profits of the parent company, as it makes it possible to reduce insurance costs by reducing the amount of insurance premiums and expand insurance coverage. In addition, a captive insurance organization can start working in the open insurance market. At the beginning of the development of the insurance market in Ukraine, almost all the largest insurance companies were sectoral or departmental to one degree or another, serving primarily the corporate insurance interests of their founders, as well as independent business entities that were part of the structure of multidisciplinary concerns or large financial and industrial groups. The transformation of a captive insurance organization into universal insurance companies is a common phenomenon of a natural process for the Ukrainian market. There are many former captive insurance companies in Ukraine, which then entered the all-Ukrainian insurance market and are successfully operating.

The creation of a captive insurance organization makes it possible to avoid many other potential risks that may

arise for the enterprise when interacting with an insurance company, primarily the risk of bankruptcy of the insurer. Depending on the class and type of possible losses, the risks can be transferred either to the captive insurance organization or to the external insurance market. Obviously, it is more profitable to keep more foreseeable and stable risks on your own maintenance.

One of the advantages for the development of a captive insurance organization is the lack of insurance coverage offers for some risks in the usual insurance market. A captive insurance organization is able to create insurance funds to cover any type of loss, including those for which the usual insurance market cannot offer insurance protection. The reinsurance market is essentially a wholesale insurance market in which reinsurance companies act as wholesalers (or buyers). The costs of establishing and managing a reinsurance company are much lower, and the average amount of insurance during reinsurance is much higher. The benefit for the insured is lower insurance rates. In addition, unlike insurance, the reinsurance market allows you to keep more predictable risks on the insured's care.

A captive insurance organization can serve as a lever to centralize the risk management of large corporations, taking over the implementation of insurance programs for regional branches, subsidiaries and affiliated companies, as well as the interests of corporations abroad. Insurance of branches and divisions can be carried out within the framework of the global policy of risk management by establishing a higher level of deductible, as well as providing higher limits of insurance coverage and coverage of wider classes of risks than could be achieved for individual enterprises. A captive insurance organization can also provide additional flexibility when insuring the interests of the parent company in other countries, since the primary insurance contract can now be concluded with a local insurance company and then reinsured with a captive insurance organization. This method allows you to circumvent possible legislative and tax restrictions and promises a considerable benefit.

Insurance premiums shall be recovered by the insurance organization up to the insurance reserve and for the period of the contract shall be covered on a qualifying basis. In addition, insurance or reinsurance of risks in the offshore captive insurance organization will ensure the payment of taxes at the rates of the region of the city, as well as the lower rates for existing tax rates. The activity of the captive insurance organization is more active of the mother's organization, the ability to change the cost of saving or transferring a wide range of insurance premiums to the insurance company. In addition, it is possible to

regulate the development of the system and the accumulation of financial reserves.

According to V. Chernyakhovsky [5], an important task is to choose the right model for the transformation of the Ukrainian insurance market for its development in the coming decades. This applies both to the transformation of the legislative framework and regulatory policy, and to changes in business models and the work of insurers. Possible transformation options include closing or selling a business, turning an insurance company into an intermediary, expanding, and turning into a captive insurance company.

Therefore, experts see the introduction of captive insurance companies promising for the development of the insurance market. It should be noted that this can be implemented in the following ways:

1. Definition of the concept of a captive insurance company in the new version of the Law «On Insurance».
2. Determination of the range of counterparties (insureds) with whom the captive insurer has the right to work.
3. Reduction/restriction of prudential supervision requirements, similar to what is currently happening in Europe.
4. Regulation of the activities of captive companies should be carried out according to the requirements of Solvency I, implemented in the current version of the Law «On Insurance», and not according to the extremely complex mechanism of Solvency II.
5. Introduction of softer requirements for capital, reserves, and solvency margin of a captive insurer.
6. Simplification of the requirements for corporate governance of a captive insurance company, since all complex mechanisms are required for structures without a controlling owner and in the presence of a large number of third-party individual clients.

### Conclusions

The purpose of creating a captive insurance company can be expressed in the achievement of specific indicators for the insurance of enterprises of the parent financial and industrial group. The objectives of the development strategy of a captive insurance company are defined as areas that contribute to the achievement of the set goal. Currently, there are certain obstacles to the widespread introduction of captive insurance, which are primarily related to the lack of a legislative framework, the absence. However, the introduction of captive insurance can have a positive impact on the economic security of the parent organization and revive the development of the insurance market.

### References

1. Captive Insurance Companies – What They Are & Potential Benefits Thoughtware. URL : <https://www.bkd.com/article/2020/08/captive-insurance-companies-what-they-are-potential-benefits>.
2. Recent Developments in the Captive Insurance Industry. URL : [https://www.naic.org/cipr\\_newsletter\\_archive/vol2\\_captive.htm](https://www.naic.org/cipr_newsletter_archive/vol2_captive.htm).
3. Kravets, A. V. & Danylovykh, T. B. & Tymchyshyn, I. E. (2011) Osoblyvosti stanovlennia keptyvnykh strakhovykh kompanii v Ukraini [Peculiarities of the formation of captive insurance companies in Ukraine]. Effective Economy – Efektyvna ekonomika. № 4. URL : <https://ena.lpnu.ua:8443/server/api/core/bitstreams/68c2e609-d6fa-4ee8-a80b-588ea52f545e/content>. [in Ukrainian].

4. Bidnyk N.B.& Dzoba V.B. Stvorennia keptyvnykh strakhovykh kompanii yak metod samostrakhuvannia promyslovykh pidpriemstv [Creation of captive insurance companies as a method of self-insurance of industrial enterprises] URL : <https://ena.lpnu.ua:8443/server/api/core/bitstreams/68c2e609-d6fa-4ee8-a80b-588ea52f545e/content>. [in Ukrainian].
5. ASB CEO: Three Ways to Transform Insurance Companies [Heneralnyi dyrektor ASB: Try shliakhy dlia transformatsii strakhovykh kompanii] URL : <https://insurancebiz.org/discuss/interview/detail.php?ID=7944>. [in Ukrainian].