

Chartered  
Insurance  
Institute

# AF6 Senior management and supervision

## Coursework Exemplar and Guidance

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## Unit AF6 – Senior management and supervision

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## Introduction

This guide has been developed to provide candidates with practical guidance on how to approach assignments when completing coursework for the Advanced Diploma unit AF6.

### Important information:

We strongly recommend prior to writing your assignments, that you review this exemplar along with the following information:

- ❖ The additional information found within the 'Coursework Support Centre' in RevisionMate.
  - Here you will find a suite of guidance documentation and other resources to assist you with your coursework assignments.
  - This includes all the rules that you will need to follow throughout your enrolment.
- ❖ The assignment Walkthroughs, available through RevisionMate.
  - The walkthroughs are an interactive eLearning segment for the key points of the assignment question.

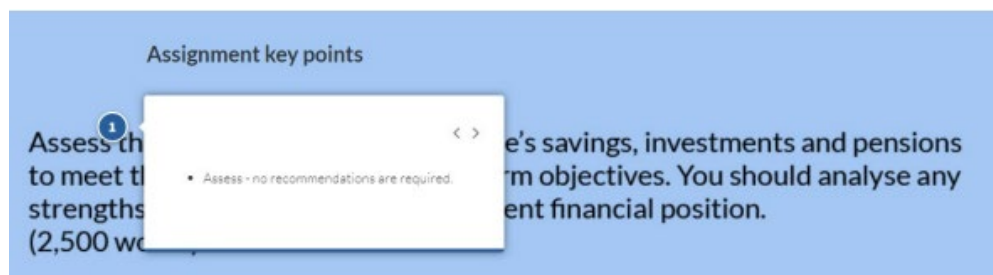
## Learning outcomes and assessment criteria

The syllabus for AF6 is found on the CII website. It sets out the learning outcomes for this unit; these define what you should know by the end of your course of study. The syllabus contains a set of assessment criteria which specify what you will need to demonstrate through your assignments in order to satisfy these learning outcomes.

## AF6 assignment walkthroughs

The AF6 walkthroughs are interactive eLearning segments of the assignments. The format is responsive, easily readable on mobile devices (unlike PDFs) and has allowed us to create a more interactive and engaging walkthrough by linking the guidance directly to the referred content.

Interactive hot spots have also been added (see example below) and learners can view guidance and advice directly linked to key words. The eLearning is split into multiple segments and students cannot continue past hotspot areas until all information has been accessed, ensuring all content is suitably accessed. The Walkthroughs are there to help you better understand the key requirements of each question.



## Original content and referencing

Please be sure to include your own analysis and recommendations for the best chance of being awarded higher marks.

Any content within your assignment that is not directly referenced or quoted is assumed to be your own. Referencing is how you make it clear to the marker where content that isn't your own original material appears within the assignment.

If you include any content that is not your own original material, then put it in *italics* so that it is obvious that you are not passing it off as your own and cite where it has come from at the end of the sentence (you can put citations in brackets).

Please see the 'Plagiarism & collusion' section of the Coursework Support Centre on RevisionMate for details on how to reference.

## Word count

The assignments have a recommended word count that should enable students to demonstrate the required application of knowledge and skills.

## Marking grid

You will be required to complete three assignments to the required standard within this course. The pass mark for each assignment is 50%.

The three assignments will be assessed on the basis of:

- 30% of marks on Knowledge and understanding of the topic;
- 50% of marks on Application and analysis of the topic;
- 15% of marks on Structure, in terms of logic and coherence;
- 5% of marks on Evidence, by use of relevant work and industry examples and/or examples gained from further reading.

The marking grid below contains a detailed breakdown of the assessment methodology used to mark assignments.

This marking grid reflects the coursework assessment method where students have access to learning material and are expected to take the time to demonstrate more research and analysis, and to reference appropriate sources in their answers.

Knowledge and understanding (includes accuracy and completeness of facts) Marks weighting 30% of the 100 available marks			
Your answer identified almost all of the points of content and clearly explained these	Your answer identified most of the points of content and described these in some depth	Your answer would have benefitted by identifying more points of content and explaining these more fully	Your answer would have benefitted by identifying sufficiently more points of content and explaining these more fully
23-30 marks	15-22 marks	8-14 marks	0-7 marks

<b>Application and analysis</b> <b>Mark weighting 50% of the 100 available marks</b>			
Your answer showed a deep understanding of the underlying concepts and their application	Your answer showed essential understanding of underlying concepts and their application	Your answer would have benefitted by exploring the concepts and their application in more depth	Your answer would have benefitted by exploring the concepts and their application in far greater depth
39-50 marks	26-38 marks	13-25 marks	0-12 marks
<b>Coherent structure</b> <b>Mark weighting 15% of the 100 available marks</b>			
Your answer showed a high level of coherent structure	Your answer showed an essential level of coherent structure	Your answer would have benefitted by structuring your content more logically and better grouping of the information	Your answer would have benefitted by structuring your answer logically and paying careful attention to the grouping of information
12-15 marks	8-11 marks	4-7 marks	0-3 marks
<b>Evidence of the use of relevant examples and/or further reading to support answers</b> <b>Mark weighting 5% of the 100 available marks</b>			
Your answer showed considerable evidence of relevant examples and/or further reading	Your answer showed evidence of relevant examples and/or further reading	Your answer would have benefitted by including more relevant examples and evidence of further reading	Your answer would have benefitted by including a lot more relevant examples and evidence of further reading
5 marks	4 marks	3 marks	0-2 marks

## Exemplar Assignment and Example Answers

### Exemplar Assignment

You work for a regulated firm that is considering outsourcing its Human Resources (HR) and Payroll functions to a third party, based in an overseas jurisdiction.

Produce a formal report for the risk committee of a regulated firm that:

- Discusses the benefits and risks of outsourcing.
- Makes **three** recommendations for effective oversight of the outsourcing partner.
- Explains the potential consequences for the regulated firm should the outsourcing partner not perform effectively, providing relevant examples.

Your answer must include an overview of the legal and regulatory environment.

(2,500 words)

Exemplar Answer

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[word count: 2,464 words]

This report aims to assess the benefits and risks of the proposal to outsource the HR and payroll functions, as well as to provide recommendations for effective oversight of any such outsourcing arrangement in line with legal and regulatory requirements.

## OVERVIEW OF LEGAL AND REGULATORY REQUIREMENTS

### Regulatory requirements

There are a range of rules in the Financial Conduct Authority (FCA) handbook which stipulate the minimum requirements that regulated firms must follow, supplemented by specific requirements regarding outsourcing arrangements.<sup>1</sup>

- PRIN 3 – a firm must ‘take reasonable care to organise and control its affairs responsibly and effectively, with adequate risk management systems’.
- SYSC 3.1.1R – ‘a firm must take reasonable care to establish and maintain such systems and controls as are appropriate to its business’.
- SYSC 4.1.1R – ‘a firm must have robust governance arrangements, which include a clear organisational structure with well defined, transparent and consistent lines of responsibility, effective processes to identify, manage, monitor and report the risks it is or might be exposed to, and internal control mechanisms, including sound administrative and accounting procedures and effective control and safeguard arrangements for information processing systems’.
- SYSC 3.2.4 G - a firm cannot contract out its regulatory obligations and should take reasonable care to supervise the discharge of outsourced functions. This section provides additional guidance on managing outsourcing arrangements (and will be relevant, to some extent, to other forms of third-party dependency) in relation to operational risk. Outsourcing may affect a firm's exposure to operational risk through significant changes to, and reduced control over, people, processes and systems used in outsourced activities.
- SYSC 13.9.2 says that ‘A firm should not assume that because a service provider is either a regulated firm or an intra-group entity an outsourcing arrangement with that provider will, in itself, necessarily imply a reduction in operational risk.’

The regulator also expects firms ‘to be operationally resilient by having a comprehensive understanding and mapping of the people, processes, technology, facilities and information necessary to deliver each of your important business services. This includes people and other dependencies such as third parties,’ and to ‘assess the risks and controls in place to ensure it is operationally resilient’.<sup>2</sup>

Senior managers have supplementary requirements, introduced by the Senior Managers and Certification Regime (SM&CR) – which was introduced to strengthen and embed individual accountability in the financial services sector. It aims to encourage staff to take personal responsibility for their actions, improve conduct at all levels, and to make sure firms and staff clearly understand and can show who does what.<sup>3</sup>

<sup>1</sup> Financial Conduct Authority, ‘SYSC 13.9 Outsourcing - FCA Handbook’: <https://www.handbook.fca.org.uk/handbook/SYSC/13/9.html>

<sup>2</sup> Financial Conduct Authority, ‘Outsourcing and operational resilience’, July 2022 <https://www.fca.org.uk/firms/outsourcing-and-operational-resilience>

<sup>3</sup> Financial Conduct Authority, ‘The Senior Managers and Certification Regime: Guide for Solo Regulated Firms’ July 2019, <https://www.fca.org.uk/publication/policy/guide-for-fca-solo-regulated-firms.pdf>



### Legal requirements

All organisations that hold or process individuals' personal data have an obligation under the sixth principle (Security) of the Data Protection Act (DPA) 2018<sup>4</sup>, which aligns to the 'Integrity & Confidentiality' principle of the General Data Protection Regulation (GDPR), to ensure that personal data is stored and processed securely.

In accordance with GDPR, firms must ensure that they have appropriate security measures in place to protect the personal data they hold and or process:

- Data shall be processed in a manner that ensures appropriate security of the personal data, including protection against unauthorised or unlawful processing and against accidental loss, destruction or damage, using appropriate technical or organisational measures. (Information Commissioner's Office, 2020)<sup>5</sup>

This is particularly relevant if the outsource provider is based overseas, in a jurisdiction that does not have an equivalent privacy environment.

HR and payroll have certain statutory and legal obligations. Staff are entitled to certain statutory rights, health and safety, employment law such as diversity and inclusion. The Employment Rights Act 1996 gives workers' rights regarding their pay and must not be discriminated against abiding by the Equality Act 2010.

### BENEFITS AND RISKS OF OUTSOURCING

An overview of the principal benefits is provided below:

- **Reduced costs** – As most outsourcers have multiple clients, they have the staff readily available or can increase or decrease the staffing requirements to handle the volume of work as required and thus charge accordingly. Smaller firms don't have the capability of adapting in this manner, with payroll staff costs being a fixed overhead that cannot be changed month on month depending on volumes.
- **Increased efficiency** – Outsourced providers are incentivised to improve efficiency for the functions, which will benefit the firm. In contrast by keeping the Human Resource (HR) and payroll functions in house the firm will continue with the same processes and resourcing levels.
- **Access to Improved expertise** – As the majority of providers involved in outsourced functions work with a number of clients and have been providing these services for years it is often found that they have a far more extensive knowledge on the functions along with superior knowledge and expertise. This would not only result in these functions being run at a cheaper cost but at a more effective level too. These providers are often found to have access to superior systems too and as a result can provide much improved management information (MI) than we currently receive in terms of Human Resources (HR).<sup>6</sup> This can include human capital metrics which helps to measure the value and effectiveness of (HR) initiatives which would then allow our management to plan for the future accordingly.<sup>7</sup>

<sup>4</sup> Gov.uk, 'Data Protection Act 2018, <https://www.gov.uk/government/collections/data-protection-act-2018>

<sup>5</sup> Information Commissioner Office, 'Guide to the UK General Data Protection Regulation, <https://ico.org.uk/for-organisations/guide-to-data-protection/guide-to-the-general-data-protection-regulation-gdpr/>

<sup>6</sup> Personnel Today, 'HR outsourcing (HRO): an in-depth guide', Jan 2008, <https://www.personneltoday.com/hr/hr-outsourcing-hro-an-in-depth-guide/>

<sup>7</sup> Paypro Workforce Management, 'Tracking Which Human Capital Metrics Can Save You Money', July 2019, <https://www.payprocorp.com/resources/blog/which-human-capital-metrics-can-save-you-money/>

- **Freeing up management time** – Whilst a level of supervision would still be required if an outsourcer was conducting Human Resource (HR) and Payroll functions, it would not consist of the same level of time currently required to deal with essentially non-core issues. Ultimately management will be freed up to focus more on their day to day work.

#### Risks

- **Data security** – Due to the nature of the functions proposed for outsourcing, a significant amount of personal information will be transferred to a third party. This presents the risk of a data breach.
- **Regulatory breach** - There is a high risk of regulatory breaches, either by the company or the outsource partner.
- **Failure Rate** – “an estimated 50% of arrangements do not deliver the expected results<sup>8</sup>” due to several reasons, including the partner going out of business. However, often the Service Level Agreement (SLA) does not meet the needs of both parties and is not specific enough in design. There is also risk that the outsourcing requirements will change over time, with the addition of staff or new regulations for example, and so our agreement with the partner may need to be amended and/or may not be able to.
- **Reputational Risk** – The company’s reputation could be affected by the choice to outsource if it is perceived that moving a function overseas is driven financially, to benefit from lower costs, regardless of the treatment or working conditions of the partner’s staff. This could impact the reputation of the company immediately, if the markets view this as an unwise, purely cost cutting measure.

## RECOMMENDATIONS

### 1. Service Level Agreement

It is important to ensure that a Service Level Agreement (SLA) is drafted, as an integral part of the contract with the third-party provider (outsource partner). This Service Level Agreement must be focused on the services received by the third-party provider and measures to determine the performance. It would be crucial that this contract was properly scoped by both the firm and the outsource partner so that everyone is clear what was and wasn't included as part of the contract.

The key areas to be included are:

- Services to be delivered;
- Metrics evidencing how performance is managed. As part of these, key areas to be called out specifically are:
  - Consumer outcomes
  - Data management and safeguards that may be required if data is transmitted and/or processed in a different jurisdiction
- Documentation explaining how potential problems are managed, including escalation, mediation and 'step-in' rights; there should be an agreement of a facility to escalate issues immediately when certain service level underperformance triggers are reached.
- Business continuity and disaster recovery provisions
- Exit provisions, in the event of the agreement being terminated (either at term expiry or due to 'force majeure')

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<sup>8</sup> Chartered Insurance Institute, 'Senior Management and Supervision (AF6), 2022

A robust agreement ensures clarity from the outset regarding the firm's expectations of the outsource partners and what actions may be required in the event of issues arising.

The contract must include a jurisdiction clause to ensure that in the event of a dispute, the case between the firm and the outsource partner are determined by a particular national court, in this case the UK courts.<sup>9</sup> This clause would help avoid uncertainty and delays on where disputes are to be resolved.

It should be agreed that updates must be provided regularly from the outsourcer to management within our firm on how they are performing against the agreed Service Level Agreement.

## **2. Appropriate oversight, through an open and honest dialogue**

The regulated firm will be relying on the outsourcing partner however the onus remains on the regulated firm. Care must be taken in relation to the performance of operational functions, regulated activities and other services to ensure that these are on a continuous and satisfactory basis whilst avoiding undue business risk.

This could be achieved by having regular reviews between the firm and the outsource partner, attended by relevant managers that can provide effective reporting on the key areas.

As well as receiving regular updates on how they are performing against the service level agreement as previously stated, it is crucial that regular formal reviews between the two parties are conducted.

These meetings would allow the following: either party to raise any ad hoc issues that may be outside the service level agreement and potentially allow for quick resolutions of such issues.

It is also important to have open discussions about any upcoming changes to law or regulations and to highlight potential items where efficiencies can be achieved by working together.

This would ensure transparency between our firm and the outsourcer and give comfort that we are regularly monitoring performance.

Management Information of both 'hard' and 'soft' data must be provided in line with the SLA to include areas such as:

- errors & delays in payroll services
- employee turnover and retention rates
- unfilled positions
- complaints (with focus on upheld complaints, and areas where consumer harm had been identified)
- data protection and record keeping breaches
- client and staff satisfaction surveys.

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<sup>9</sup> Ashurst, 'Jurisdictional clauses, January 2021, <https://www.ashurst.com/en/news-and-insights/legal-updates/quickguide---jurisdiction-clauses/>

Key Performance Indicators (KPIs), Key Risk Indicators (KRIs) and Key Control Indicators (KCIs) can enable an analysis of the data and an assessment of any risk that we are being exposed to.

By using agreed tolerances to indicate their severity, for example the 'RAG' reporting (red, amber, green) ratings to show which are within an acceptable tolerance will provide early warning signals.

Remedies and penalties should be included in the SLA if the expected standards aren't properly met and conditions for termination of the agreement.

### **3. Programme of thematic assurance**

The decision to use a third party provider should not impair the quality of the regulated firm's internal systems and controls and also the ability of the FCA to monitor this. The firm should assess the risks and controls in place to ensure that it is operationally resilient.

This could be achieved through having regular internal audits and supplemented by receiving assurance reviews from the outsource provider.<sup>10</sup>

Any issues identified must be reported promptly, and depending on their severity, any require escalation to the relevant governance forum. Business owners must be identified for all actions, and progress of the actions must be monitored, with regular reporting provided.

For example, the assurance reviews should review the operation of the key business processes and may lead to recommendations to map additional processes and document the key controls. Both companies will benefit from enhanced transparency, so they are aware of exactly what is expected from them.

As highlighted, the outsourcer would hold a high volume of employee data. Thus, monitoring that this is stored securely via regular audits or via assurance reviews would give peace of mind to both management and employees that the outsourcer is storing data securely.

In the event that the outsourcer didn't store data securely it would immediately be highlighted as a result of the internal audit or via receiving an assurance review. This would allow management within the firm to take appropriate action as per the agreed Service Level Agreement.

The staff should be afforded the opportunity to liaise with management in relation to any concerns about the outsourced services which will assist with the ongoing review of using the third party company.

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<sup>10</sup> KPMG, 'Third-party risk management: outsourcing', <https://assets.kpmg/content/dam/kpmg/ie/pdf/2019/04/ie-third-party-risk-management.pdf>

## CONSEQUENCES FOR THE FIRM

- **Loss of control** of the function could be of detriment when considering the accountability regime within the SM&CR where more personal accountability is placed on individuals for their actions and on senior managers for their respective business areas. This may be more difficult to manage with a remote service provider particularly one offshore which may be in a different time zone.
- **Loss of local knowledge and processes** – this would be particularly prevalent in an offshore structure and could impact compliance under COND 2.4. It also means the outsourced functions are not able to take advantage of local relationships such as with employment lawyers given the HR function does often require legal input on matters and also with internal teams on employment matters which require collaboration.
- **Employee Engagement** - Employees are key stakeholders in the business and as such could be impacted by the decision to outsource HR and payroll functions if for example errors were made and proved difficult to remedy quickly. This can very quickly lead to de-motivation and loss of trust. HR functions often provide career guidance, an important component of career management, the quality of which could be diluted if not disappear altogether given that any external partner would have less of an understanding of the business or industry than an internal resource. These two things alone could lead to disengagement and potentially higher attrition amongst staff and costs that might outweigh any potential savings.
- **Regulatory censure and fines**
  - a. GDPR - The maximum fine for GDPR data breaches and penalties is the higher of 4% of the total annual worldwide turnover in the preceding financial year or €20m. For example, in July 2019, British Airways incurred a hefty fine for a data breach in 2018 when British Airways website users were diverted to a fraudulent site<sup>11</sup>.
  - b. SM&CR – Censure, fines, and disqualification of directors from holding a senior management function could occur, depending on the infringement. For example, both FCA and PRA fined Raphaels Bank £1.89m in 2019, commenting that: 'Raphaels' systems and controls supporting the oversight and governance of its outsourcing arrangements were inadequate and exposed customers to unnecessary and avoidable harm and inconvenience. There is no lower standard for outsourced systems and controls and firms are accountable for failures by outsourcing providers.'<sup>12</sup>

## CONCLUSION

Outsourcing the HR/Payroll functions remains the company's responsibility. Adherence to the SLA, robust ongoing oversight with clear performance indicators and regular assurance will mitigate the risks and contribute towards benefit realisation, in a successful relationship.

<sup>11</sup> Information Commissioner Office, 'Information Commissioner's Annual Report and Financial Statements 2020-21, July 2021, <https://ico.org.uk/media/about-the-ico/documents/2620166/hc-354-information-commissioners-ara-2020-21.pdf>

<sup>12</sup> Financial Conduct Authority, 'FCA and PRA jointly fine Raphaels Bank £1.89 million for outsourcing failing, May 2019, <https://www.fca.org.uk/news/press-releases/fca-and-pra-jointly-fine-raphaels-bank-1-89-million-outsourcing-failings>

## Examiner comments

The mark given to this assignment is **67**.

Areas where the candidates displayed good knowledge and understanding included:

- demonstrated a clear understanding of the regulatory landscape, referencing specific regulatory provisions
- provided a balanced discussion of the benefits and risks associated with outsourcing HR and Payroll functions
- provided practical recommendations for effective oversight, such as robust SLAs and regular reviews
- explained the potential consequences, providing relevant examples to highlight the impact on a regulated firm

Areas for further improvement included the following:

- elaborate on regulatory breaches and reputational damage.
- develop implementation plans and set out support required from the board of directors.
- consider how success could be measured and reported to the firm's governance body.

## Feedback comments and Turnitin

Once you have submitted your assignment, you will be able to see your Turnitin score and your Turnitin originality report through your RevisionMate account.

Assignments are marked independently by at least two markers.

If the assignment is not marked unanimously as a pass, then the assignment is discussed through a moderation process to determine the final grade.

If that grade is then confirmed as not reaching the pass standard, feedback comments will be left on the assignment and will relate directly to the reasons the markers could not award a pass. The feedback comments will not provide the answer to the question but instead direct you to the areas that you need to improve upon. These feedback comments are provided through a Turnitin feedback report, available to view in the assignment submission area on RevisionMate.

This feedback is in addition to the overall mark and the feedback codes for each marking criteria (Knowledge and understanding, Application and analysis, Coherent structure, and Evidence of the use of relevant examples/further reading to support answers) provided in your MyCII account.

You can still purchase a post-results review of marking for a report on areas for improvement, if required.