



The Corporate Governance
Association of Ireland

Code of Corporate Governance

**for
Independent
Directors of
Investment Funds**

**Guidance to CGAI members and to other parties
committed to high standards of corporate governance
in the Irish funds industry
January 2010**

A CODE OF CORPORATE GOVERNANCE FOR INDEPENDENT DIRECTORS OF INVESTMENT FUNDS

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Arthur Cox Building
Earlsfort Terrace
Dublin 2
Ireland

January 2010

www.cgai.ie

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ABOUT THE CGAI

The Corporate Governance Association of Ireland (the “CGAI” or the “Association”) is a professional association of members who are certified in corporate governance postgraduate studies. The Association encourages its members to pursue continuous professional development to keep abreast of this continually evolving subject.

The Association seeks to promote best practice in governance across the commercial, public and voluntary sectors.

Web: www.cgai.ie

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CGAI SPECIAL INTEREST GROUPS

Corporate Governance practices have evolved to govern the standards of board oversight in commercial organisations. The principles of good corporate governance propagated by codes and rules have been developed primarily for application to publicly quoted companies listed on stock exchanges.

The CGAI advocates that such definitions of best practice be adopted in private firms. However, it is recognized that the principles be intelligently adapted by the board of each company to suit their particular environment.

The CGAI also advocates that best practice in governance has application beyond the commercial sector and that best practice principles should also be adopted and adapted in the public and voluntary sectors.

To further this end and in recognition that 'one size does not fit all', the CGAI encourages the formation of Special Interest Groups (SIGs) among its members to study the adaptation of the principles of best practice in governance to different organisations and sectors.

The CGAI defines "Special Interest Groups" as

Special Interest Groups are groups of members of the Association which have been recognised by the CGAI's Board as actively pursuing the objectives of the Association within a defined subset of the areas of interest of the Association.

A Special Interest Group is formed to determine, propagate and continually update its definition of best practice in governance in its sector of interest.

INVESTMENT FUNDS SPECIAL INTEREST GROUP MEMBERSHIP

Adrian Waters Dip Corp Gov, C.Dir. (Chairman), David Casey Dip Corp Gov,
Jerry Kelly Dip Corp Gov, C.Dir., Werner Schwanberg Dip Corp Gov, C.Dir.,
Fergus Sheridan Dip Corp Gov, Paul Turpin Dip Corp Gov.

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FOREWORD

This Code has been developed as a response to the question frequently asked of CGAI members; namely, “what is best governance practice for Irish investment funds?” This is a difficult question to answer specifically as little direct legal, regulatory or other guidance exists for investment fund governance in Ireland.

In general, we believe that good governance is achieved through a principles-based approach that puts the investors’ interests above all others. In that regard, we have researched ‘best practice’ in operation for offshore funds as well as domestic funds registered in the United Kingdom and the United States of America. Drawing heavily from the excellent work of the UK’s Association of Investment Companies, this Code attempts to provide CGAI members with a framework through which good practice can be demonstrated.

We do not believe that this Code is all embracing nor do we believe that it is the only way for funds to achieve good governance. However, we do believe that by adhering to the principles of this Code, funds can demonstrate to all stakeholders a commitment to governance ideals.

History has shown that the introduction of governance codes in various jurisdictions has not been universally welcomed. Critics say such codes are unnecessary, cumbersome and/or bureaucratic. Some may view this Code in the same light. However, adherence to this Code will do at least one thing; it will demonstrate to all stakeholders of the fund that the INVESTOR COMES FIRST.

Note:

Throughout this document the terms ‘investment funds’ or ‘funds’ are used to refer to investment funds, investment companies, collective investment schemes, management companies (for the most part) or other relevant investment vehicles to which the Code could be reasonably applied. This Code is specific to Independent Directors but its provisions should be valued by every fund director.

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THE AIM OF THIS CODE IS:

***To promote a set of principles that
makes a valuable contribution
towards the achievement and
maintenance of higher standards
of corporate governance in
investment funds in
Ireland***

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1. INTRODUCTION

This Code offers guidance for members of Boards of investment funds that are authorised by the Financial Regulator in Ireland.

The Code has been prepared to offer specific guidance to CGAI members in fulfilling the role as independent board members. It is based on the premise that the principles of corporate governance adopted by the Boards of investment funds should accord with international best practice.

This Code has been devised around the primary aim of meeting the specific expectations of investors in investment funds. Investors expect the following:

- A commitment to achieving an optimal total return whilst taking acceptable and appropriate risk. Such risk being consistent with the investment policies and objectives of the fund.
- Transparent fund objectives and investment policies that accurately portray the specific fund's risk parameters.
- A competitive expense ratio with appropriate incentivisation that leads to above average risk-adjusted returns and superior service.
- Appropriate risk management processes which are diligently monitored for effective implementation.
- Timely, accurate and appropriate communication from the Board and the Promoter.
- Professional service standards from all service providers.

The development of a Code at this time reflects the growing demands and responsibilities associated with Board membership of investment funds as a result of:

- The increasing scale and complexity of the funds industry in Ireland;
- The rising expectations of stakeholders with regard to the contribution of Board members;
- The key importance of consistently high standards of corporate governance to the reputation of the sector;

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- The emergence of codes of governance in the main jurisdictions in which many of the promoters of funds authorised in Ireland reside;
- The increasing legal and regulatory obligations emanating from both Ireland and the EU.

2. CONSIDERATION OF THE COMBINED CODE

An objective of this Code is to offer guidance based on the principles in the Combined Code of Corporate Governance¹. The Combined Code highlighted

- The special role and responsibilities of independent non-executive directors (“Independent Directors”)
- That appointments to the Board should be made on merit and against objective criteria
- The separation of Board leadership and control from the executive (promoters)
- The responsibility of directors in monitoring the integrity of financial reporting
- That Independent Directors should promote the highest standards of corporate governance and seek compliance with the provisions of the Combined Code wherever possible.

The report Good Practice Suggestions from the Higgs Report (Financial Reporting Council, 2006) gave guidance on the role of the Independent Director:

“Independent directors should constantly seek to establish and maintain confidence in the conduct of the company. They should be independent in judgement and have an enquiring mind. To be effective, Independent Directors need to build recognition by executives (promoters) of their contribution in order to promote openness and trust”

¹ The Combined Code on Corporate Governance (Financial Reporting Council, 2008) sets out standards of good practice in relation to issues such as board composition and development, remuneration, accountability and audit and relations with shareholders. All companies listed on the Main Markets of the London and the Irish Stock Exchanges are required under the Listing Rules to report on how they have applied the Combined Code in their annual report and accounts. The Code has achieved a much wider currency as it has become common for companies outside the designated group to adopt the code as a demonstration of their commitment to the principles of good governance. For the purposes of clarity, it should be noted that the Irish Stock Exchange exempts funds listed on it from the provisions of the Combined Code.

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3. INDEPENDENT DIRECTORS

The Combined Code highlights the value of independent board members. Whilst the size of boards of investment funds is typically smaller in number than the companies which are required to adopt the Combined Code, independence is nonetheless an important and valuable principle.

Independent directors could be deemed to be those directors who have no other business connection with the fund of whose board they are members. An independence requirement would place Ireland on a comparable basis with best international practice.²

Independent Directors bring:

- Freedom from real or perceived conflicts of interest;
- Freedom to put protection of investor interests to the fore;
- An objective and independent voice.

4. PRINCIPLES

4.1 Fundamentals

- 4.1.1 Directors shall put the interests of investors above all others.
- 4.1.2 Directors shall treat all investors fairly.
- 4.1.3 In the pursuit of investor interest, directors should be prepared to resign or take such steps that could lead to loss of office.
- 4.1.4 Directors shall communicate in a transparent manner with investors and the Financial Regulator.

² The *Report on Governance for Collective Investment Schemes* (IOSCO, 2007) states the principle of independent oversight should apply to ensure that such schemes are organised exclusively in the interests of their investors.

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4.2 Board Structure

- 4.2.1 Board members should receive a formal letter of appointment.
- 4.2.2 The term of office of Board members should be fixed.
- 4.2.3 Board members may be reappointed subject to an appropriate evaluation of their contribution to the work of the Board and the ongoing mix of experience and skills likely to be available to the Board.
- 4.2.4 A majority of directors should be independent of the promoter and regular service providers.
- 4.2.5 A Chairman should be formally appointed.
- 4.2.6 The performance of the Chairman should be discussed on an annual basis by the Independent Directors.
- 4.2.7 Board committees should be established where they would enhance the effectiveness of the Board. Specific consideration should be given to the establishment of an Audit Committee.
- 4.2.8 Separate independent director meetings should, on a needs basis, be formally convened to consider such areas as:
 - i. Performance of the Board and of individual directors,
 - ii. The governance processes and procedures of the Board,
 - iii. New director appointments,
 - iv. Training/induction needs, and
 - v. Requirements for independent legal/expert advice.

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- 4.2.9 To avoid undue reliance on the Promoter/Investment Manager, the fund should seek adequate and separate D&O cover for the independent directors.

4.3 Powers of the Board

- 4.3.1 There should be a formal schedule of matters reserved for Board consideration and decision.
- 4.3.2 The Board should agree policies with the Promoter and service providers defining the scope of their responsibilities and covering key operational issues.
- 4.3.3 The directors should be empowered, when they consider it necessary, to seek professional advice independent from the Fund, its Promoter/Investment Manager or its service providers.

4.4 Functions of the Board

The directors have a duty to implement procedures that enable a company to meet its legal and regulatory requirements. This includes meeting the requirements of the Fund Prospectus in addition to the requirements of Company Law such as the keeping of proper books of account and meeting reporting requirements. There is also the requirement to comply with requirements specific to funds supervised by the Financial Regulator (particular attention should be paid to the Financial Regulator's Guidance Note 4/07, which although specific to UCITS has broader resonance).

In addition to implementing procedures to enable compliance with regulatory requirements, it is proposed that the following areas should receive specific attention

- 4.4.1 Generally the Board should have as a primary focus of its meetings, review of the investment performance of the fund.

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- 4.4.2 The Board should regularly review the adequacy and effectiveness of the Fund's risk management processes.
- 4.4.3 The Board should regularly review the operational performance of, and contractual arrangements with, the investment manager.
- 4.4.4 The Board should monitor all service providers and formally evaluate their performance at least once every three years.

4.5 Duties of Board Members

It is the duty of directors to be aware of their responsibilities under company law³. They must have sufficient time capacity to adequately discharge their Board duties. They must also be informed on and familiar with the regulatory requirements applicable to investment funds. The Board should strive to be in a position to give assurance that the organisation operates in compliance with its obligations.

It is a responsibility of all directors to be well prepared, attend Board meetings, contribute to decision making, share responsibility for Board decisions, and keep up to date with subjects relevant to the Board's work.

The Chairperson has a particular responsibility to ensure that the Board operates effectively. This includes ensuring members understand their roles and responsibilities and maintaining a strong working relationship with the Promoter.

5. Implementation

CGAI members should actively promote these guidelines both within the investment funds in which they are involved and also within the investment community generally.

³ The Report on General Schemes of Companies Consolidation and Reform Bill (The Company Law Review Group, 2007) proposed the following obligations of directors - loyalty to the interests of the organisation; compliance with the company constitution; avoidance of secret profits; independence of judgement; avoidance of conflicts of interest; care, skill and due diligence; and to consider the interests of third parties.

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