

New Corporate Governance Code for Irish Funds

On 14 December 2011, the Irish Funds Industry Association issued a Corporate Governance Code (the “Code”) for Irish Investment Funds and their Management Companies. It simultaneously issued a Frequently Asked Questions document (“FAQ”), to complement the Code and support its introduction.

The introduction of the Code arises from an invitation from the Central Bank of Ireland (the “Central Bank”) to the funds industry in 2010 to develop such a code, as part of a process of introducing corporate governance codes for the many sectors of the financial services industry in Ireland. A steering group within the industry was established to lead the project, which involved significant consultation with the Central Bank.

1. Application

The Code will apply to Irish authorised investment funds and Irish authorised management companies. Although the Code is voluntary in nature, its adoption is strongly recommended by the industry and the Central Bank. The Code comes into effect on a “comply or explain” basis. This means that where a Board decides not to apply any provision of the Code, it should set out its reasons why in the Directors’ Report accompanying the annual audited financial statements or alternatively publish its reasons through a publicly available medium (e.g. a website) detailed in the annual report.

2. Timing

The Code will be effective from 1 January 2012, with a transitional period of 12 months until 1 January 2013. The FAQ states that for Funds or Management Companies with financial year-ends of 31 December, the first statement of compliance will be included in the financial statements of 31 December 2012. For financial year-ends of 30 June, the first statement of compliance will be included in the financial statements of 30 June 2013.

3. Main Implications of Adopting the Code

We are satisfied that the vast majority of the requirements set out in the Code are already being complied with by the Irish authorised funds and management companies we advise.

However, over the coming months, Boards will need to review the Code and consider whether to adopt it. Obviously, the practical implications of adopting the Code will need to be understood by each director. Accordingly, the following is a summary of the principal practical implications of adopting the Code in full, in terms of processes to be implemented and documented, which may or may not be in place at the moment:

- (i) the Board will need to specify on a periodic basis, as appropriate, the time commitment it expects of each director;
- (ii) directors will be required to disclose to the Board any concurrent directorships held on other authorised funds, management companies and/or related entities which supply services to such schemes;
- (iii) directors will also be required to disclose to the Board their other time commitments, including those devoted to any directorships of non-Irish funds;
- (iv) the Board will need to satisfy itself that directors have sufficient time to fully discharge their duties;
- (v) in considering director appointments, the Board will be required to assess, and document its consideration of, possible conflicts of interest;
- (vi) the Board will also be required to document its procedures for dealing with such conflicts and must review compliance with those procedures annually;
- (vii) the Board will be required to formally review Board membership at least once every three years;
- (viii) the Chairman of the Board will be required to be reviewed at least once every 3 years;
- (ix) the overall performance of the Board will be required to be reviewed annually, together with the performance of individual directors, with a formal documented review taking place once every three years;
- (x) a schedule of directors' attendance at Board meetings will be required to form part of the annual informal Board performance review process;
- (xi) the Board will be required to establish a documented "conflict of interest" policy for its members and where conflicts arise, the Board must ensure they are noted in the minutes;
- (xii) the Board will be required to establish a formal schedule of matters specifically reserved to it for decision, which schedule must be documented and updated in a timely manner;
- (xiii) the Board may establish committees, which will be required to have documented terms of reference evidencing all authorities delegated to them and detailing their functions, membership, reporting lines, meeting frequency, voting rights and quorums;
- (xiv) the company will be required to detail in its annual report its compliance with the Code and explain any deviation, or alternatively publish the information through a publicly available medium (e.g. a website) detailed in the annual report;
- (xv) the Board must ensure that internal control procedures of delegates are being monitored to ensure that they are effective;
- (xvi) the Board will be required to ensure that there are appropriate processes and systems in place to monitor and manage risks identified by it or its delegates at all times.

The above is a summary only of what we see as being the most likely practical implications of adopting the Code. We would recommend that the directors review the Code in detail and formally consider the Board's current practices to identify any deficiencies.

4. Other Key Provisions

The other key provisions contained in the Code can be summarised as follows:

(i) Composition of the Board

- three directors is recommended as the minimum size for the Board;
- the majority of the Board must consist of non-executive directors and there must be at least one independent director;
- an independent director will not be an employee, partner, significant shareholder or director of any service provider firm receiving professional fees from the fund;
- it is strongly recommended that at least one director be an employee, director or partner of the promoter or the investment manager;
- a minimum of two directors on the Board must have Irish residency;
- if any director has in excess of eight non-fund directorships it raises a rebuttable presumption that that director's time available is impacted – this must be explained in the “comply or explain” statement referred to above;
- before being appointed, a new director needs to demonstrate to the satisfaction of the Board that he or she meets the Central Bank's fit and proper standards; and
- appointments to the Board require the prior approval of the Central Bank and any departure from the office of director, along with the reason(s) for departure, should be made known to the Central Bank.

(ii) Chairman

- a non-executive Chairman, who will lead the Board, encourage critical discussions, challenge mindsets and promote effective communication, must be appointed to the Board.

(iii) Independent Directors

- independent directors must be identified clearly in the annual report;
- they must have a knowledge and understanding of the investment objectives, policies and outsourcing arrangements to enable them to contribute effectively.

(iv) The Role of the Board

- the Board is responsible for the effective and prudent oversight of the company;
- it is ultimately responsible for ensuring that risk and compliance is properly managed on behalf of the Fund/Management Company and the Code sets out how this responsibility might be discharged;
- it may delegate to committees or third parties, must have mechanisms in place for monitoring the exercise of delegated functions but cannot abrogate responsibility for those functions.

(v) Appointments

- the Board is responsible for appointing all directors and for ensuring they are adequately trained to discharge their duties.

(vi) Meetings

- the Board must meet as often as is appropriate to discharge its duties but should normally meet quarterly;
- detailed agendas must be circulated in advance and detailed minutes must be prepared afterwards;
- all directors should attend all meetings;
- ongoing conflicts of interest may necessitate a change in Board membership.

(vii) Committees

- the Code outlines some details governing the manner in which Committees of the Board conduct their business.

(viii) Delegates

- the Board may delegate all or part of the management of the Fund/Management Company to third parties and the Code makes specific reference to investment management, administration and distribution as examples of management functions that may be delegated;
- the Code outlines under what conditions the Board can delegate;
- the Board shall be responsible for monitoring the performance of such delegates and must have mechanisms in place to do so;
- specific reference is made to the fact that the delegates should provide reports to the Board on at least a quarterly basis.

(ix) Risk Management, Audit, Control & Compliance

- The Code also outlines in detail the specific responsibilities of the Board in the areas of:
 - External Audit
 - Compliance
 - Identification, Monitoring and Management of Risks
 - Internal Control

5. Conclusion

Rather than introducing a completely new corporate governance regime, the Code represents a re-statement of obligations that already apply to Irish domiciled Funds and Management Companies. It largely outlines a set of principles and guidance which codify existing practice and it combines this with what is seen as best international practice. The requirements outlined in the Code are stated to be the minimum recommended requirements that a Fund or Management Company should meet in the interest of promoting strong and effective governance. As stated above, albeit that it is a voluntary Code, the expectation from the industry and the Central Bank is that all Funds and Management Companies will adopt it. In doing so, the practical implications set out above will need to be considered.