Governance and Independence: The crucial role of the Independent Fund Director

In today's dynamic financial landscape, strong governance and the role of the independent fund director has never been more critical.

Governance is a key pillar underpinning investor protection, and practices that may have been acceptable in the past may not be tolerated to the same extent today. Fund directors are now subject to higher expectations and increased investor scrutiny, as well as more explicit regulatory expectations in some jurisdictions.

The model of directorship has also evolved, with the rise of 'professional' independent fund directors and hosted regulatory platforms (including platform providers and offshore legal and secretarial compliance organisations). It is time to take stock and assess whether the different models of directorship deliver on desired outcomes or if there are areas that need improvement to prevent governance (or fund) failures.

While we collectively refer to all directors in an investment fund board as the Board, independent non-executive directors (INEDs) play a vital role in mitigating conflicts by giving objective oversight. This paper examines the sourcing and responsibilities of INEDs, different models of directorship, lessons from past failures and how to foster good governance, current and future challenges faced by INEDs, and how the industry can work together to improve.

Key Takeaways:

- Strong governance and investor protection go hand-in-hand: independent directors empower this by giving *objective oversight*.
- While sole proprietors traditionally dominated the industry, the model of directorship has become *commercialised* with the rise of Board Service Providers.
- Strengthening independence begins in the *board appointment process* – a more open process can help reduce conflicts.
- When sourcing directors, beyond experience and skill, there is a *need for courage, curiosity, and integrity.* Identifying these characteristics can help deliver adequate challenge but require more nuanced due diligence.
- Independent directors must remain *adaptive* to regulatory changes and industry developments, including responsible investment initiatives and artificial intelligence.
- Institutional investors have a vital role in *setting expectations* for board behaviour.
- The Standards Board for Alternative Investments (SBAI) Standards and Toolbox guidance can help independent directors, managers, and investors navigate these challenges as ultimately strong governance is a *shared responsibility*.

Responsibilities of the Independent Non-Executive Fund Director

Independent directors have a broad remit of responsibilities, including overseeing the fund's management, ensuring alignment with the fund's objectives and investors' interests, ensuring compliance with all relevant laws and regulations, and overseeing the fund's financial reporting and audit processes.

They play a crucial role in the fund's risk management, ensuring that risk levels align with regulatory, prospectus, and investor-mandated tolerances and restrictions. Independent directors may also be responsible for anti-money laundering oversight and approving valuation of the fund's assets – depending on jurisdiction.

The primary duty of independent directors is to protect investors' interests by ensuring fair and impartial treatment and acting in good faith with care, diligence, and skill.

This can involve making decisions that are not popular with the investment manager (or some investors) to ensure fair treatment. For instance, enacting liquidity management tools during market volatility to prevent a run on the fund and to protect remaining investors from being trapped with a pool of illiquid assets.

Non-executive, particularly independent non-executive, directors are essential for good governance – balancing the power of executive directors, ensuring due process and fair treatment of investors, and promoting transparent and accountable decision-making by the Board.[1]

Not all Independent Fund Directors are created equal!

Two distinct approaches to independent oversight dominate the fund board industry: sole proprietorships and board service providers (BSPs).

Sole proprietorships offer boutique, flexible arrangements on a part- or full-time basis, relying on the experience and knowledge of their individual directors to secure work.

In contrast, BSPs offer professional governance services, appointing knowledgeable individuals to boards with the backing and additional resources of the BSP to support these appointments. These BSPs may offer supplementary services such as legal, compliance, and regulatory advice to the fund in addition to providing independent directors – which can be a source of conflicts of interest.

This article does not intend to argue whether one approach is superior, as both their own merits and should be chosen based on a fund's specific needs and circumstances.

Comparing director types: Sole Proprietorships versus BSPs

Independence	Both sole proprietorships and BSPs face potential conflicts of interest **Sole Proprietorships:** • Individual directors are seen to have direct personal accountability, which can lead to a stronger sense of ownership and commitment • Close relationships and dependency risk may make it difficult for directors to critique managers for fear of loss of role and income

[1] See Appendix B for a comparison of various director types

	BSPs: • BSP-appointed directors may be less dependent on maintaining good relations for job security, by virtue of their employment with the BSP • Where BSPs offer additional services (e.g., legal, compliance, and regulatory advice), these additional revenue sources can create pressure to keep managers happy for fear of losing these lucrative engagements
Adaptability	**Sole Proprietorships:** • May offer more flexibility in service arrangements • Potentially more responsive to changing circumstances or specific fund needs **BSPs:** • May manage time commitments of their directors better as workloads can be split across a wider pool of employees • Standardisation can increase consistency, but may can instil false comfort in taking on a greater number of directorships • Can offer continuity and reduce key person risk, provided replacement directors have adequate skills and experience
Personalisation	**Sole Proprietorships:** • Provide more personalised attention and focus to a specific fund • May be better positioned to understand the fund's unique aspects and needs • One-on-one interaction can foster closer relationships with the fund's management and other board members, potentially leading to more effective governance and oversight **BSPs:** • Professionals are appointed in their individual capacity, maintaining personal responsibility despite broader organisational support
Institutionalisation	**BSPs:** • Often have institutionalised processes for governance and risk management which can offer a more systematic and standardised approach to oversight • Could increase potential for 'tick box' approaches or 'groupthink' in lieu of truly independent thought and action
Expertise	There is a need for directors in both models to continually educate themselves on the key industry trends and initiatives **Sole Proprietorships:** • May face intellectual isolation without the support of a large organisation **BSPs:** • Have access to a wider range of resources and expertise • Benefit from a diverse pool of professionals with various specialisations

Key lessons from governance failures

The collapse of Neil Woodford's Woodford Equity Income Fund (WEIF) in 2019 serves as a prominent example of professional independent director service providers failing to fulfil their primary responsibility of protecting investor interests and holding managers accountable.

Woodford, a high-profile UK investment manager, had become difficult to challenge due to a "cult of personality", a risk often heightened in owner-led firms.[2] Link Fund Solutions (LFS), the Authorised Corporate Director (ACD), failed to scrutinise Woodford's increasing investments in small-cap and illiquid equities which led to a significant deviation in the fund's marketed strategy.[3] LFS failed to act, and Woodford was only removed after the fund was suspended due to a lack of liquidity to pay redemption requests.

This failure underscores the danger of rubber-stamping investment manager decisions and highlights the need for effective challenge and oversight. It also raises the critical question: *Who do directors work for?* Is it the investment manager or the investor? Ultimately, the answer is the fund with the interests of the investor in mind, but practical realities are more complex.

All independent directors, whether from BSPs or sole proprietorship, face a common problem: they are chosen and appointed by the investment manager which creates an inherent conflict of interest that can never be fully mitigated. Being paid from fund proceeds, these directors must balance their basic duty to investors and the fund whilst maintaining a good relationship with their sponsor. This complex dynamic was highlighted after the Woodford failure, when the UK Financial Conduct Authority (FCA) criticised ACDs for referring to investment managers as 'clients'.[4]

While no fund is immune to failure – independent directors who fail to effectively challenge managers can create environments that may lead to, or increase the chances of, fund failures or risk events occurring.

Good governance: the need for courage, curiosity and challenge

Before launching a fund, managers should evaluate the relevant legal framework and ensure a governance structure that can manage conflicts of interest.[5] This structure should include members with relevant skills who can operate independently of the fund manager.

The SBAI's Alternative Investment Standards ('Standards') for fund governance emphasise the importance of establishing a robust and independent governance structure for investment funds.[6] Further guidance can be found in the SBAI Governance Toolbox, including a Standardised Board Agenda, which we encourage investment managers and independent directors to adopt.[7]

This guidance includes best practices such as ensuring board members have appropriate expertise, integrity, and independence, as well as regularly reviewing governance processes.

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[2] SBAI *Culture Matters* (June 2023) discusses issues around culture and the need to safeguard integrity and openness, access here: https://www.sbai.org/resource/culture-matters.html

[3] *FCA announces plan to deliver significant redress to Woodford investors* (April 2023): https://www.fca.org.uk/news/press-releases/fca-announces-plan-deliver-significant-redress-woodford-investors

[4] FCA *Review of host Authorised Fund Management firms* (June 2021): https://www.fca.org.uk/publications/multi-firm-reviews/host-authorised-fund-management-firms

[5] See Appendix F for Examples of Conflicts of Interest

[6] See Appendix D for SBAI Standards related to Fund Governance

[7] SBAI *Standardised Board Agenda* (Nov 2019): https://www.sbai.org/resource/standardised-board-agenda.html

Directors should disclose conflicts of interest, maintain tenure policies, and meet at least quarterly to discuss key issues such as investment performance, regulatory compliance, and risk management.[8] Service providers should be actively involved in board meetings and directors should be empowered to scrutinise their oversight. Contracts and performance of service providers should also be periodically reviewed to ensure they meet fund requirements.[9]

Many corporate governance codes set out principles for good governance, focusing on behaviours, processes, and procedures. However, when assessing the fitness and probity of an independent director for an investment fund, factors beyond industry experience and prestigious employers should also be considered.

While traditional attributes such as *relevant qualifications and experience, absence of conflicts of interest, and sufficient time to perform the role* are essential, qualitative attributes such as ***integrity, strong ethical sense, and behavioural skills such as courage, critical thinking, and independence of mind*** cannot be stressed enough – all of which are hard to evidence in the absence of enhanced due diligence and direct interactions with incumbent and prospective independent directors.[10]

When building a fund board, it is imperative to consider the collective personalities and skills of all directors and how this 'team' would interact. The dynamics of the group can significantly impact the level of challenge posed to a manager, with certain combinations potentially reinforcing groupthink or biases.

How can boards foster better governance?

Independent directors should not fear challenging the status quo. While highly choreographed board meetings may fulfil regulatory requirements, they can fall short in addressing changing market and risk environments. All board members should be aware of and understand emerging risks and seek to educate their peers.

Board self-assessments can be an effective tool for generating self-reflection to foster better governance. Directors should use this process as an opportunity to ask difficult, thought-provoking questions – not just treat it as a "tick box" exercise. A robust self-assessment process that values open and frank dialogue, avoids groupthink, and focuses on value creation and board performance will continually push directors to critically evaluate their practices to ensure they remain in the best interest of the fund and investors.[11]

Sourcing Independent Fund Directors

To strengthen the degree of independence of fund directors, managers should reassess the board appointment process. A more open process, e.g., through an open advertising campaign, can lead to a broader range of candidates and reduce opportunities for personal and commercial relationships to dominate the process.[12]

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[8] See Appendix E for Practical examples of good governance
[9] See Appendix G for Good governance practices in relation to service providers
[10] See IOB's 2023 *Fund Governance Survey Report* (page 15): https://iob.ie/news/fund-governance-survey-report
[11] See *Report of the Mutual Fund Directors Forum - Practical Guidance for Fund Directors on Board Self-Assessments* (July 2021): https://www.mfdf.org/docs/default-source/default-document-library/publications/white-papers/mfdf-self-assessments.pdf
[12] IOB's 2023 *Fund Governance Survey Report* found that an open advertising campaign was the most acceptable director appointment practice (page 19), see here: https://iob.ie/news/fund-governance-survey-report

Additionally, referrals from other independent directors or unaffiliated service providers could be useful. Regardless of the approach taken, it is pertinent to perform effective due diligence on the individual(s) being considered, with a view to build a board with diverse skills and experience that are relevant for the fund's structure and strategy.

While many jurisdictions lack formal education or experience requirements for independent directors, the Institute of Banking (IOB) in Ireland has developed the Certified Investment Fund Director (CIFD) qualification to bring a degree of formal training, which we view positively.

In APAC, the Singapore Fund Directors Association (SFDA) similarly provides training and guidance, while the Australian Institute of Company Directors (AICD) contributes broader governance insights.

Future developments and challenges for Independent Fund Directors

The role of the independent director has and will continue to evolve, requiring Boards to evaluate their skills against industry and regulatory developments, as well as investor expectations.

Industry developments:

- Investor **allocations to private market assets** have increased steadily. This move towards more illiquid and closed-ended investment vehicles raises concerns about whether independent directors, with backgrounds typically rooted in open-ended, liquid, long-only, and hedge-fund strategies, possess the necessary skill and experience.
- Growing **adoption of responsible investment strategies** presents new challenges given the rapidly evolving landscape of related regulation.[13] Independent directors must stay update-to-date with regulatory changes across different jurisdictions to ensure compliance.
- As **artificial intelligence (AI)** becomes more integrated into financial services, independent directors must navigate regulatory and ethical issues related to AI-driven decision-making. Staying informed of evolving best practices in AI governance is essential for fulfilling fiduciary duties and maintaining investor trust.

Investor expectations:

- Investors look for strong governance structures that promote independence, accountability, and effective oversight. They expect directors to actively monitor fund management practices, ensure compliance with regulatory requirements, and address conflicts of interest promptly and transparently.
- **Institutional investors play a crucial role in maintaining high standards.** Investors may need to invest more time getting to know the independent directors on their funds as part of initial due diligence and on an ongoing basis. This requires buy-in from both independent directors and managers and raises questions about how investor scrutiny and access to directors can be structured in a workable and efficient manner.

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[13] The SBAI Responsible Investment Toolbox can help directors and stakeholders navigate these challenges, access here: https://www.sbai.org/toolbox/responsible-investment.html

Regulatory expectations:

- Boards in some jurisdictions face heightened regulatory oversight and increased personal liability exposure, for example:
  - The Central Bank of Ireland's (CBI) Individual Accountability Framework (IAF) seeks to hold senior management of investment firms and management companies, including directors, accountable for the decisions they make.[14]
  - The UK FCA's Senior Managers Regime (SMR) requires senior managers, certified persons, and non-executive directors to comply with fit and proper (FIT) requirements, as well as regulatory reference rules.[15]

A survey of directors cautioned that the CBI's IAF could result in more risk-averse decision-making, higher director fees, and blur lines between executive and non-executive directors. However, it also highlighted potential benefits, such as greater accountability for misconduct, strengthened internal controls, and a greater emphasis on cultural leadership.[16]

While many jurisdictions set minimum expectations for director behaviour, regulating behavioural quality and working practices in areas as complex, diverse, and innovative as governance of (alternative) investment funds is difficult and will likely result in voluminous rule books to cater for various scenarios and circumstances.[17]

This could backfire and lead to "tick box" approaches to governance and compliance which meet the letter of the law, but not the spirit.

At the SBAI, we believe that principles and standards that apply across jurisdictions are better suited for establishing good practices and behavioural outcomes in such areas – without the rigid complexity, level of prescription, and cost of detailed blackline rules.

Conclusion: strong governance is a shared responsibility

Strong governance, facilitated by independent director oversight, is not just a necessity – it is the backbone of trust in the investment industry. So, how can stakeholders safeguard this?

Independent directors must demand quality engagement and reporting from managers (and their service providers) to enhance their oversight and reduce the risk of failures. In extreme circumstances, if faced with irreconcilably poor engagement and transparency, directors should be prepared to resign.

Managers must provide disclosure and transparency, recognising that strong governance drives accountability, robust risk management, and investor alignment and trust. It is essential for managers to be considerate of investor expectations, understanding that a partnership approach is key to building and sustaining healthy investor relationships – which is ultimately in the manager's best interest.

Alongside this, institutional investors play a pivotal role in establishing and upholding governance standards. Their influence empowers them to demand transparency, integrity, and

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[14] CBI's *Individual Accountability Framework* (IAF): https://www.centralbank.ie/regulation/how-we-regulate/individual-accountability-framework
[15] FCA's *Senior Managers Regime* (SMR): https://www.fca.org.uk/firms/senior-managers-and-certification-regime/senior-managers-regime
[16] IOB's 2023 *Fund Governance Survey Report* explored likely effects of CBI's IAF (page 24), see here: https://iob.ie/news/fund-governance-survey-report
[17] See Appendix C for Regulatory Influences on INED Responsibilities

rigorous oversight to protect their interests. This includes conducting thorough due diligence on independent directors and managers before allocation, seeking direct access to directors to assess the quality of oversight, and ensuring that directors have the necessary skills and integrity to provide effective oversight.

While strong governance is a shared responsibility, all stakeholders in this process stand to benefit from demanding high standards of one another, fostering transparency, and advocating for continuous improvement.

Appendix A: Key questions investors should ask managers and INEDs

Board Composition and Independence

1. Can you confirm that independent directors represent a majority of the voting rights on the board?
2. Are there any employees of the investment manager holding voting rights on the board? If so, how is their influence managed to maintain board independence?

Conflicts of Interest

1. How do independent directors and investment managers identify potential conflicts of interest that may impact the fund's operations?
2. What processes are in place to manage and monitor conflicts of interest? How often are these conflicts reviewed?
3. How and when are conflicts of interest disclosed to investors?
4. Is there a formal Conflict of Interest Policy adopted by the board? Can you provide details on this policy?
5. How are conflicts of interest recorded and updated? Can you provide an example of a recent update?

Independence and Links to Investment Manager

1. Are there any personal, economic, or commercial links between independent directors and the personnel working for the investment manager or service providers? How are these disclosed and monitored?
2. Do any of the independent directors have a history of working for the investment manager or being sponsored by influential investors? How is their independence assessed?

Director Duties and Time Commitment

1. How do directors ensure they have sufficient time to fulfil their duties and responsibilities? Are there any directors with commitments exceeding 2,000 hours a year?
2. How regularly do directors evaluate their commercial relationships and commitments?

Service Providers and Legal Advisors

1. Are the fund and investment manager serviced by the same third-party legal advisor on regulatory compliance and conflicts of interest? How is independence ensured in such cases?
2. How actively do service providers participate in board meetings? Are they given opportunities to be questioned and challenged by the board?

Board Meeting Dynamics

1. Can you provide examples of how board meetings go beyond formality and show evidence of challenge and substantive discussion?
2. How have virtual meetings impacted the dynamics of challenge and oversight?

Service Provider Oversight

1. How often are material service provider contracts reviewed to ensure roles and responsibilities are clearly defined and adhered to?

2. What is the process for the ongoing review of a service provider's suitability and capabilities?

Due Diligence and Rotation

1. What due diligence is undertaken for the selection and monitoring of service providers? Can you provide examples of recent due diligence materials reviewed by the board?
2. How often are independent directors and service providers rotated? What criteria are used to determine the appropriate duration of service?

Reporting and Communication

1. How do independent directors assess the quality of reporting from the investment manager? What steps are taken if reporting is found inadequate?
2. What mechanisms are in place to maintain communication between the manager and the board in the interim periods between board meetings?

Fees, Expenses, and Distribution Model

1. How do directors assess whether the fees and expenses paid out of the fund are justified and represent value for money for investors? How is alignment of interests ensured with the investors?
2. How do directors engage with the investment manager to understand the fund's distribution model and strategy?

Appendix B: Differentiating between the various types of directorships

An investment fund board ensures the fund is managed in the best interests of its investors, adhering to legal, regulatory, and ethical standards. It typically includes independent and executive directors who monitor the fund's performance, approve key decisions and assess risks. Provided below is a comparison of the key differences between executive and non-executive directors:

	Executive Directors	Non-Executive Directors	Independent Non-Executive Directors
Degree of daily involvement	Actively involved in daily operations and management	Not involved in daily operations	Not involved in daily operations
Employment Status	Senior employees of the investment manager (e.g., CEO, CFO, COO/Head of Operations) Not independent	Typically, senior employees of the investment manager or a related party such as a parent entity could not be considered independent Often have other primary employment or commitments	Fully independent from the company and external
Responsibilities	- Develop and implement operational policies - Strategic planning - Make significant business decisions	- Contribute to strategy development - Oversee executive directors	- Provide independent oversight - Oversee executive directors
Compensation	May include bonuses, stock options, performance-based incentives	Not typically linked to performance-based incentives	Not linked to performance-based incentives

Appendix C: Regulatory influences on INED responsibilities

The fiduciary duties and responsibilities of independent fund directors have expanded over time and now require a more active role in overseeing fund management and operations. Independent directors, as result, have had to adapt and evolve with the changing regulatory landscape to ensure compliance.

The role and concept of independent directors has evolved significantly since inception under the US *Investment Company Act of 1940*, which sought to prevent conflicts of interest in the mutual fund industry by requiring at least 40% of fund directors to be independent. Subsequent amendments broadened their role significantly:

- *Investment Advisers Act Amendments of 1960 (Public Law 86-750)*: Addressed structuring of performance-based fees and required independent directors to oversee compliance to ensure fees were fair and aligned with investor interests.
- *Investment Company Amendments Act of 1970 (Public Law 91-547)*: Explicitly defined the fiduciary duty of mutual fund managers regarding the redemption of securities and required directors to monitor fulfilment of these duties including accurate disclosure of information to investors.

In 2004, the SEC sought to strengthen the role of independent directors by requiring funds to have an independent chair and at least 75% independent directors. However, this rule was challenged in court and ultimately overturned in 2006.

Globally, other regulators have sought to improve governance in their own jurisdictions:

- The **Central Bank of Ireland (CBI)** has been active in providing guidance to independent directors and fund management companies regarding their roles and responsibilities, often going into specific detail about the expectations for independent directors.[18]
- In 2018, the **UK's Financial Conduct Authority (FCA)** mandated that Authorised Fund Managers (AFM) (or Authorised Corporate Directors (ACD)) must have at least 25% independent board directors, or a minimum of two independent directors if the board has fewer than eight members.[19] While ACDs can effectively 'fire' an investment manager for unsatisfactory performance, the concept of independence is complicated if the ACD is also an affiliate.
- The **Association of the Luxembourg Fund Industry (ALFI)** has published a Code of Conduct on fund governance which has been regularly updated.[20]
  The **Cayman Islands Monetary Authority (CIMA)** has implemented rules and guidance requiring Boards to establish a corporate governance framework that includes, at a minimum a Code of Conduct amongst other elements. These requirements apply to all CIMA-regulated entities, with an emphasis on 'proportional application' based on the entity's specific circumstances.[21]

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[18] CBI *Fund Management Companies - Guidance* (Dec 2016): https://www.centralbank.ie/docs/default-source/regulation/industry-market-sectors/funds/ucits/guidance/fund-mancos-guidance.pdf
[19] IoD *Funds Governance in the UK: Strengthening the Role of Independent Directors* (Dec 2021): https://www.iod.com/news/finance-and-tax/iod-policy-paper-strengthening-the-role-of-independent-directors-in-the-asset-management-industry/
[20] ALFI Code of Conduct, access here: https://www.alfi.lu/en-gb/pages/setting-up-in-luxembourg/fund-governance
[21] CIMA *Rule on Corporate Governance for Regulated Entities* (April 2023): https://www.cima.ky/upimages/regulatorymeasures/RuleonCGforREs_1684531675.pdf

Appendix D: SBAI's Standards related to fund governance

Standard 21.1: Prior to the establishment of a fund, a fund manager should assess the appropriate legal structure for fund. In light of that assessment, the manager should be proactive in seeking to ensure that a fund governance structure which is suitable and robust to oversee and handle potential conflicts of interest is put in place at the outset.

Standard 21.2: Where a majority of the individual members of the fund governing body are not independent of the manager or where there is no fund governing body, certain key actions such as (a) material adverse changes to: the fees and expenses payable by the fund to the manager or the redemption rights available to investors, or (b) material changes to the fund's stated investment strategy or legal structure should (unless required by law or regulation) only be taken with investor consent (obtained in accordance with the provisions relating to investor voting/consent/approval contained in the fund's constitution or offering documents) or if advance notice is provided sufficient for investors to redeem before such actions take effect.

Standard 21.3: Members of the fund governing body should have suitable experience and integrity in order to discharge effectively their role with the appropriate level of independence.[63]

Standard 21.4: The composition of the fund governing body and the governance processes in place should be monitored and, if necessary, adjusted throughout the life of the fund to ensure that they remain

Standard 21.7: Regular reports on compliance with laws and regulations (in particular those relating to anti-money laundering) applicable to activities which are performed by the administrator on behalf of the fund should be obtained by the fund governing body from the fund's administrator.

Further guidance in relation to these Standards here: https://www.sbai.org/standards.html

Appendix E: Practical examples of good governance

- **Voting:** Independent directors should represent a majority of board voting rights.
- **Skills and Experience:** Independent directors should be able to carry out their duties without relying on the fund's manager or other directors – i.e., have sufficient skills and experience to administer independent, effective governance and oversight.
- **Time Commitment:** Independent directors should have sufficient time to fulfil their duties and regularly evaluate their commercial relationships to ensure capacity. This could include considering regulatory guidance, e.g., the CBI considers individual directors with aggregate professional time commitments of more than 2,000 hours per year, including service on at least 20 fund boards, to be "high risk", which can attract additional supervisory attention in line with the CBI's risk-based approach.[22] Some BSP directors may significantly exceed these thresholds. Conflict of interest logs and engagement records can give insight on how capacity and commitments evolve.
- **Conflicts of Interest:** Independent directors and investment managers should identify and seek to prevent conflicts of interest which may affect the operation of the fund and investor interests. The Board should adopt a Conflict of Interest Policy for guidance on reporting and monitoring conflicts. Where prevention is not possible, this should be disclosed to investors. Perceived and actual conflicts should be recorded, monitored, and reviewed annually (at minimum) in a Conflict of Interest Log.
- **No 'tick-box' Governance:** Board meetings should be more than choreographed formalities and Boards should be able to show evidence of challenge and maintain appropriate records. Where unresolved issues remain, there should be a follow-up process. This should consider how growing prevalence of virtual meetings impact the dynamics of challenge and oversight.
- **Communication:** Independent directors should not accept poor levels of reporting from the investment manager or fail to maintain communication in between board meetings. Inadequate information and poor reporting to the board is one of the most significant impediments to board effectiveness.[23]
- **Understanding the Investor:** Directors should understand how a product is being marketed, and to whom. This should improve alignment of interests by ensuring the investors in a fund are sufficiently aware of the risks involved and sophisticated enough to endure any volatility and liquidity constraints that may arise.
- **Rotation:** Rotating independent directors and service providers, especially auditors, can bring fresh insights and lines of questioning and challenge. Longevity of directors (and service providers) should be reviewed periodically. While changes may happen naturally through attrition, retirement, or voluntary departures, longevity of directors (and service providers) should be considered and reviewed periodically. A survey of directors suggests 7-9 years as the point where independence becomes undermined.[24]

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[22] CBI *Review of the Number of Directorships held by Individuals within the Investment Fund Industry* (June 2015): https://www.centralbank.ie/docs/default-source/regulation/industry-market-sectors/funds-service-providers/fund-administrators/gns-4-4-9-3-thematic-review-of-directorships.pdf?sfvrsn=231bd71d_8
[23] IOB's 2023 *Fund Governance Survey Report* found that inadequate information or poor reporting was the most cited impediment to board effectiveness (page 21): https://iob.ie/news/fund-governance-survey-report
[24] See IOB's 2023 *Fund Governance Survey Report* (page 20): https://iob.ie/news/fund-governance-survey-report

Appendix F: Examples of conflicts of interest

- Independent directors should not have personal, economic, or other commercial links with the investment manager or its related parties, or the service providers serving the fund.
- Independent directors who have previously worked for the investment manager may not be considered sufficiently independent by many investors. This includes independent directors sponsored or promoted by influential investors, or those with past connections to service providers that either currently support the fund (or have done so in the past).
- The fund and investment manager should avoid being serviced by the same third-party legal advisor on points of regulatory compliance and conflicts of interest. As an example, professional independent directors who work for offshore legal and company secretarial firms may not adequately scrutinise or challenge the advice provided by related party entities.
- The potential for conflicts of interest can be heightened in large Fund Management Companies where many sub-funds of umbrella structures could be serviced by only one board and may include representatives of the Fund Management Company as directors.

Appendix G: Good governance practices related to service providers

- **Reviewing contracts:** Directors should review all material service provider contracts to ensure roles and responsibilities are clearly defined, and that service providers are performing their defined function(s) in accordance with the terms of their contracts. Ongoing review of suitability and capability of service providers should be part of this, including requiring service providers to verify that they are acting in accordance with the regulated fund's constitutional documents, offering documents, and marketing materials as applicable.

- **Ongoing monitoring:** Independent directors should request appropriate due diligence be undertaken for the selection and monitoring of service providers. Initial and ongoing due diligence materials should be presented to the board for review.

- **Opportunity for challenge:** Key service providers should be present at board meetings. Independent directors should be given opportunity to question and challenge service providers at board meetings. Service providers submitting reports without opportunity for challenge should be avoided.

- **Communication:** Service provider representatives should report any material incidents to the Board in a timely manner. There is a risk that service provider representatives present a sanitised and generic report that does not provide sufficient detail of the day-to-day operations of the fund and service provider itself (cyber events, staff attrition, operational events affecting the fund, etc.)

- **Cost:** Independent directors should assess whether the fees and expenses paid out of the fund are justified and represent value for money for investors.