

CP86- The 3 Year Journey

Fund Management Companies Guidance

Article 2 – Organisational Effectiveness

ISSUED: 27 MARCH 2017

CP86 – Overview

The scope of the new guidance as set out by the Central Bank of Ireland on 19 December impacts Investment Companies, UCITS Management Companies, Alternative Investment Fund Managers (AIFMs) and Alternative Investment Fund Management Companies incorporated and authorised in Ireland. As outlined in our introductory article it focuses on 6 key areas that are linked to effective Governance, Compliance and Central Bank of Ireland supervision. A timetable for transition has been provided in our introductory article. This article addresses “Organisational Effectiveness”.

Organisational Effectiveness – “Part II” of the December 2016 Guidance

When the Central Bank started the consultation process in 2014 Organisational Effectiveness was initially drafted as one of the 6 newly consolidated Designated Management Functions, to be completed by a Designated Person. This was clarified further in 2015 wherein the Central Bank redrafted the Designated Management Functions and Organisational Effectiveness became a separate role, one required to be carried out by an Independent Director.

An Overview of the Role:

The role requires the independent director (“OE Director”) to carry out an ongoing review of the effectiveness of the fund management company and its delegates. The Director responsible is required to escalate organisational effectiveness matters to the Board and propose improvements where identified. By having a person focused on organisational effectiveness, it means that fund management companies can effect change when and where required e.g. if the nature of the business has grown or developed significantly, some historical operational processes may have become obsolete and no longer apply. In such cases the OE Director is expected to act as a “change leader” and champion proposed change with the board. Other reasons for change may include unanticipated conflicts of interest that can emerge, developments in market practices or the impact of new legislation. Where change is agreed the OE Director should also ensure such change is fully implemented.

Areas of Focus:

- Board composition and effectiveness: This currently links to the Annual Fitness & Probity Review / Corporate Governance Code and the Companies Act 2014. Director’s Time commitments are also a factor for consideration.
- Conflicts of Interest: Ongoing monitoring is a requirement and this links to the funds Conflicts of Interest Policy.
- Availability of Resources: what resources are currently available / what additional resources are required to assist the OE Director in undertaking the role.
- Supervision of Delegates: Normally undertaken by the Designated Person resulting in a report provided to the Board. In some cases the OE Director may also attend e.g. an on site meeting with the Investment Manager.

The approach should reflect the level of complexity:

Whilst the Guidance does provide a general high level overview, it is notable that the Central Bank has not provided very specific requirements on key areas such as OE reporting and reporting frequency to the Board. It is clearly recognised that funds structures vary greatly and as a result so will the requirements of the OE role. The inference one may take from this is that each fund Board needs to consider it’s own requirements and there is no “one size fits all” approach that can be applied. Reporting, similar to the Risk Management framework needs to be customised to cater for the complexity of the business.

Impact Assessment

The end result of the OE role will be a formalisation of best practice in fund governance. Whilst a lot of the work may be in situ today, the requirements place emphasis on the need to record activity levels and to ensure a proactive approach is taken to the ongoing monitoring of the Fund Management Company, the Designated Persons and the funds delegates (the Investment Manager, Depository, Administrator and the Distributor).

- **Deadline:** This is a current requirement for all new funds or for funds that launched after 1 November 2015. For funds authorised prior to 1 November 2015 the implementation deadline is 1 July 2018.
- **Appointment of the OE Director:** Boards need to decide who is to take on the role. This needs to be carried out by an independent director. If the Chairperson is independent the likelihood is that this role will most likely be aligned to them, but this may not always be the case.
- **Impact to the OE Director:** As the role is new and there are still a number of outstanding questions, it is anticipated that additional clarity will come with time and experience e.g. new funds and funds where the OE role is already effective.
- **Impact to the investor:** The benefits to the end investor may not be overly visible. As additional time may be required from the OE Director, it is thought likely that there will be proportionate increase in the OE Director's fee.
- **Business Plans (UCITS) and Programmes of Activity (AIFs):** Documentation needs to be updated to incorporate the role of the OE Director, the Designated Persons and the fund's delegates and the communication and reporting required to support the OE Director and allow them fulfil their role. Such updates will form part of CP86 planning over the coming months and building towards the 2018 transition date.
- **Internal Audit:** The Central Bank is allowing each Board to decide where this function sits. This was previously allocated to the OE role but greater flexibility has now been provided.

Bridge Consulting in conjunction with Governance Ireland is currently hosting a series of industry workshops on Organisational Effectiveness and will publish feedback on it's findings over the coming weeks.

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