

# **ALFI Code of Conduct for Luxembourg Investment Funds**

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The initial version of the ALFI Code of Conduct was published in September 2009. In the past four years there have been many developments in fund regulations and governance and these have led to the need to review and update the ALFI Code of Conduct. However, the overall approach of the Code has not been changed insofar as it remains based on principles rather than detailed rules. As in its initial version, each of the principles of the Code is supported and explained by a number of recommendations which in most cases will represent the practice to be followed by industry participants in order to implement the Code's principles. It is strongly recommended by ALFI that all funds and management companies adopt the Code of Conduct.

Indeed it is encouraging to note the wide extent to which the Code in its initial version has already been adopted. According to the most recent survey on fund governance in Luxembourg, 85% of the UCITS surveyed reported that they had adopted the ALFI Code of Conduct. Furthermore all respondents in the survey declared that the principles-based approach of the Code was appropriate and welcome. In an era marked by the ever increasing number and complexity of rules and regulations, there is nonetheless a widespread acceptance by industry participants of the need to adopt sound principles of governance underpinned by recommendations for best practice. This is the approach that has been adopted by ALFI in both the initial Code of Conduct and its revision.

As explained in more detail in the Introduction to the revised ALFI Code of Conduct two additional principles have been added to the eight principles included in the initial version of the Code. These two new principles (respectively on external governance and remuneration of board members of funds) incorporate the significant regulatory and governance developments in these areas that have taken place since the initial version of the Code was published in 2009.

The recommendations underpinning the ten principles of the Code have been reviewed and updated to take account, in particular, of the increased focus on the management of conflicts of interest, risk management and internal controls which have been major features of new regulations and development in practice over the last four years. Additionally, greater focus on the role and the composition of fund boards is reflected in new and revised recommendations covering the role of the Chairperson, diversity in board membership, the role of independent directors and the recommendation for fund boards to perform periodic reviews of their performance.

We would like to express our thanks to all those who have contributed to the extensive work involved in the revision of the ALFI Code of Conduct. On behalf of ALFI, we urge all participants in the Luxembourg fund industry to carefully consider the contents of the revised Code of Conduct and to adopt its principles on a timely basis with a formal annual review of its application thereafter.

Board of Directors of ALFI  
June 2013

## Introduction

The purpose of the ALFI Code of Conduct is to provide boards of directors with a framework of high-level principles and best practice recommendations for the governance of Luxembourg investment funds and of management companies where appropriate. The Code is “principles” rather than “rules” based in that it relies upon good judgment rather than prescription. As such, the recommendations recognise that the “right approach” for many issues depends on the circumstances.

The Code is not designed to supersede applicable law and regulations.

In addition to the principles and best practice recommendations, this Code will be accompanied in due course by guidelines on specific issues which require more practical guidance.

References in the Code to the “Board” are to the body responsible by law for managing, administering and supervising the relevant fund or the supervisory function responsible for the management company. Unless otherwise specified or the context otherwise requires, all references to the Board in the Code shall therefore include, as appropriate, the boards of both Luxembourg funds and management companies.

References to “fund” in the Code cover all types of Luxembourg undertakings for collective investment, whether UCITS or non-UCITS (including SIFs) and other investment vehicles as appropriate.

Whereas the Code was initially introduced in September 2009 to formalise and encapsulate existing best corporate governance practice (including a corporate governance statement in annual financial reports making clear that the fund applies various provisions on corporate governance), the Code has been updated and re-issued in 2013 to reflect *inter alia*:

- a new principle on external governance (i.e. the exercise of shareholder rights);
- a new principle on the remuneration of Board members;
- a recommendation that consideration should be given to the appointment of one or more independent directors;
- a focus on the role of the chairperson;
- a recommendation that the Board conduct a periodic review of its performance and activities;
- an update of the description of the Board’s responsibilities with respect to risk management, internal controls and conflicts of interest.

ALFI believes it is appropriate to apply the Code to all funds – listed or unlisted – and management companies in order to have a uniform and consistent approach in the marketplace.

To improve transparency and demonstrate commitment to high standards of corporate governance, ALFI recommends that Boards of Luxembourg funds, and of management companies where appropriate, confirm adherence to the principles of the Code in their annual financial statements. Such confirmation demonstrates to investors a Board’s explicit commitment to good corporate governance.

## Principles

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- I. The Board should ensure that high standards of corporate governance are applied at all times
- II. The Board should have good professional standing and appropriate experience and ensure that it is collectively competent to fulfill its responsibilities
- III. The Board should act fairly and independently in the best interests of the investors
- IV. The Board should act with due care and diligence in the performance of its duties
- V. The Board should ensure compliance with all applicable laws, regulations and with the fund's constitutional documents
- VI. The Board should ensure that investors are properly informed, are fairly and equitably treated, and receive the benefits and services to which they are entitled
- VII. The Board should ensure that an effective risk management process and appropriate internal controls are in place
- VIII. The Board should identify and manage fairly and effectively, to the best of its ability, any actual, potential or apparent conflict of interest and ensure appropriate disclosure
- IX. The Board should ensure that shareholder rights are exercised in a considered way and in the best interests of the fund
- X. The Board should ensure that the remuneration of Board members is reasonable and fair and adequately disclosed.

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## Recommendations

- I. The Board should ensure that high standards of corporate governance are applied at all times

### Recommendations

1. The Board is accountable to the investors for good governance.
2. The Board should ensure that sound management is in place.
3. The Board should discharge its functions soundly, honestly and professionally.
4. The Board should place emphasis on promoting transparency, good practices and conduct of business rules and efficiently manage conflicts of interest.
5. The Board should provide independent review and oversight, including effective oversight of delegated functions.
6. The Board should demonstrate leadership, integrity, ethical behavior and expertise.

- II. The Board should have good professional standing and appropriate experience and use best efforts to ensure that it is collectively competent to fulfill its responsibilities

### Recommendations

1. The composition of the Board should be balanced and diverse so it can make well-informed decisions.  
Members of the Board should therefore have appropriate experience, with complementary knowledge and skills, relative to the size, complexity and activities of the fund.
2. Consideration should be given to the inclusion in the Board of one or more members that are, in the opinion of the Board, independent.
3. The Chairperson, whether appointed on a permanent, ad hoc or rotating basis, should demonstrate leadership during as well as outside meetings. The Chairperson's duties should include setting the agenda, managing the meeting, steering the discussions and ensuring that effective and fair conclusions are reached.
4. The Board should ensure that it keeps abreast of relevant laws and regulations and that it remains vigilant about evolving risks and market developments.
5. The Board may call upon expert assistance and/or create Board committees for the proper fulfillment of its duties. The establishment of Board committees should not affect the collective responsibility of the Board.
6. The members of the Board are expected to understand the activities of the fund and devote sufficient time to their role.
7. The Board should conduct a periodic review of its performance and activities.

- III. The Board should act fairly and independently in the best interests of the investors

### Recommendations

1. The Board should at all times put the interests of the investors first.
2. The Board is expected to act fairly and independently irrespective of any Board member's affiliation.
3. The Board should arrive at decisions taking into consideration, where possible, any broader potential impact of such decisions on market integrity and on the wider community.
4. Fund expenses and their impact on fund returns should be subject to scrutiny by the Board. The Board should ensure that the expenses charged to the fund are reasonable, fair and appropriate.

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#### IV. The Board should act with due care and diligence in the performance of its duties

##### Recommendations

1. Board members should regularly attend and participate actively at Board meetings.
2. The Board should meet as often as required in order to oversee effectively the fund's activities and all Board meetings should be formally minuted.
3. The Board is responsible for approving the fund's strategy and for ensuring that the fund consistently follows its stated investment objectives.
4. The Board is responsible for the appointment of delegated parties and should oversee their activities and performance.
5. The Board should ensure it acts on a fully informed basis.
6. Where required, the Board should seek external professional advice or information to assist it in its duties.

#### V. The Board should ensure compliance with all applicable laws and regulations and with the fund's constitutional documents

##### Recommendations

1. The Board should verify that adequate organisation, procedures and safeguards are established to ensure compliance with all relevant laws and regulations and with the fund's constitutional documents.
2. The Board should verify that regular monitoring of such compliance is in place and that it receives regular reports to that effect.

#### VI. The Board should ensure that investors are properly informed, are fairly and equitably treated, and receive the benefits and services to which they are entitled

##### Recommendations

1. The Board should ensure that the information provided to investors about the fund particularly with regard to the fund's investment objectives, risks and costs, is true, fair, timely and not misleading.
2. The Board should ensure that investors are kept informed of matters relevant to their investment in a form and language that is clear and easy to understand.
3. The Board should ensure that information relating to the fund's financial situation and performance be prepared and disclosed in accordance with relevant accounting standards (e.g. Lux GAAP, IFRS) and applicable legal and regulatory requirements.
4. The Board should take into account the interest of all investors, in particular where Board decisions may affect investor groups differently.
5. The Board should ensure each investor complaint is reviewed and, if it is upheld, that redress is provided within a reasonable time.
6. The Board should ensure that investors receive the benefits and level of services to which they are entitled as defined by law, contractual arrangements and the fund's constitutional documents.
7. The Board should ensure that there is adequate disclosure to investors of the fund's policies on complaint handling, proxy voting, best execution and conflicts of interest.



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**VII. The Board should ensure that an effective risk management process and appropriate internal controls are in place**

**Recommendations**

**Risk management**

1. The Board should ensure that an adequate and documented risk management policy is established, implemented and maintained which identifies the risks to which the fund is exposed and how such risks are managed.
2. The Board should ensure that the permanent risk management function is adequately staffed, or properly managed when provided on any outsourced basis, and that it is independent of the investment and operational processes.
3. The Board should ensure that the risk management policy enables the proper identification, measurement and assessment of the fund's exposure to market, liquidity and counterparty risks, and exposure to all other risks including operational risks.
4. The Board should ensure that it receives regular risk management reporting and that it regularly assesses the adequacy and effectiveness of the risk management policy and processes.
5. The Board should ensure that it understands the impact of any complex financial products or strategies on the risk profile of the portfolio and the aggregate exposure of the fund to these products.

**Internal controls**

6. The Board should seek assurance that delegated parties comply with relevant and adequate Compliance and Internal Audit obligations.
7. The Board should ensure that Compliance and Internal Audit functions are independent of the investment and operational processes.
8. The Board should require direct and timely reporting of any material internal control and compliance issues, and ensure that they are appropriately addressed.
9. The Board should ensure that appropriate business continuity plans are in place, including for delegated parties.

**VIII. The Board should identify and manage fairly and effectively, to the best of its ability, any actual, potential or apparent conflict of interest and ensure appropriate disclosure**

**Recommendations**

1. The Board should identify the circumstances which constitute or may give rise to a conflict of interest which may entail a material risk of damage to the interests of investors.
2. The Board should establish, implement and maintain an effective conflict of interests policy (i) to identify such conflicts of interest and (ii) to provide for procedures to be followed and measures to be adopted in order to prevent them where possible and to manage such conflicts in an independent manner.
3. The Board should make all reasonable efforts to resolve conflicts of interest but in cases where a conflict of interest is unavoidable, the Board should seek to address it on an arm's length basis and to disclose it adequately to interested parties.
4. The Board should keep an updated record of the situations where conflicts of interest entailing a material risk of damage to investors may arise, have arisen and how they have been addressed.

**IX. The Board should ensure that shareholder rights are exercised in a considered way and in the best interests of the fund**

**Recommendations**

1. The Board should ensure that a policy on proxy voting is in place and adequately disclosed.
2. The Board should ensure that clear guidelines for monitoring investee companies are in place to determine if it is necessary to intervene with an investee company's board or management.
3. The Board should exercise the fund's voting rights in a considered and transparent way.

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4. Summary information on the exercise of voting rights should be made available to investors with detailed disclosure upon request.

**X. The Board should ensure that the remuneration of Board members is reasonable and fair and adequately disclosed.**

**Recommendations**

1. The Board should ensure that where appropriate a policy on remuneration of Board Members, is in place and is adequately disclosed.
2. The remuneration of Board members should reflect the responsibilities of the Board, the experience of the Board as a whole and be fair and appropriate given the size, complexity and investment objectives of the fund.
3. The remuneration of Board members charged to the fund should be separately disclosed in the annual financial statements either individually or collectively.

## About ALFI

The Association of the Luxembourg Fund Industry (ALFI), the representative body for the Luxembourg investment fund community, was founded in 1988. Today it represents more than 1 300 Luxembourg-domiciled investment funds, asset management companies and a wide variety of service providers including depositary banks, fund administrators, transfer agents, distributors, law firms, consultants, tax advisers, auditors and accountants, specialist IT providers and communications agencies.

Luxembourg is the largest fund domicile in Europe and its investment fund industry is a worldwide leader in cross-border fund distribution. Luxembourg-domiciled investment structures are distributed in more than 50 countries around the globe, with a particular focus on Europe, Asia, Latin America and the Middle East.

ALFI defines its mission as to “Lead industry efforts to make Luxembourg the most attractive international centre”.

Its main objectives are to:

### Help members capitalise on industry trends

ALFI’s many technical committees and working groups constantly review and analyse developments worldwide, as well as legal and regulatory changes in Luxembourg, the EU and beyond, to identify threats and opportunities for the Luxembourg fund industry.

### Shape regulation

An up-to-date, innovative legal and fiscal environment is critical to defend and improve Luxembourg’s competitive position as a centre for the domiciliation, administration and distribution of investment funds. Strong relationships with regulatory authorities, the government and the legislative body enable ALFI to make an effective contribution to decision-making through relevant input for changes to the regulatory framework, implementation of European directives and regulation of new products or services.

### Foster dedication to professional standards, integrity and quality

Investor trust is essential for success in collective investment services and ALFI thus does all it can to promote high professional standards, quality products and services, and integrity. Action in this area includes organising training at all levels, defining codes of conduct, transparency and good corporate governance, and supporting initiatives to combat money laundering.

### Promote the Luxembourg investment fund industry

ALFI actively promotes the Luxembourg investment fund industry, its products and its services. It represents the sector in financial and in economic missions organised by the Luxembourg government around the world and takes an active part in meetings of the global fund industry.

ALFI is an active member of the European Fund and Asset Management Association, of the European Federation for Retirement and of the International Investment Funds Association.

To keep up to date with all the news from the association and the fund industry in Luxembourg, join us on [LinkedIn](#) (The Luxembourg Fund Industry Group by ALFI), [Twitter](#) (@ALFI-funds), [Youtube](#), or visit our website at [www.alfi.lu](http://www.alfi.lu).



*June 2013*  
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