



association of the
luxembourg fund industry

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**GUIDANCE ON THE PROCESS
FOR THE IMPLEMENTATION
AND ONGOING ADHERENCE
TO THE ALFI CODE OF
CONDUCT FOR LUXEMBOURG
INVESTMENT FUNDS AND
MANAGEMENT COMPANIES
[“THE CODE”]**

Introduction

As set out in the Introduction to the last revision of the Code, the purpose of the Code 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 management companies. The Code is “principles” rather than “rules” based in that it relies upon good judgement 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.

The adoption of the Code, although recommended by ALFI, remains entirely voluntary. Even in the absence of obligation, the Code has nonetheless been adopted on a widespread basis by both funds and management companies as shown by recent surveys of fund governance in Luxembourg. The Code is seen as a badge of good fund governance and as evidence of commitment by the board of directors to best practice. During the initial set-up of the fund or management company the sponsor and its advisors should carefully consider the contents of the Code and the manner in which it is to be applied.

Initial adoption of the Code

The decision to adopt the Code should be taken by the boards of directors of the fund and of the management company. This decision should only be taken after careful consideration has been given to each principle and underlying recommendation of the Code. This process should be documented by comparing actual practice with each of the Code's principles and recommendations. Such a comparison is often referred to as a "mapping exercise". If this process reveals any significant gaps between the requirements of the Code and actual practice,

remedial action should be taken. In exceptional circumstances there may be valid reasons for one or more recommendations of the Code not being implemented. Such instances should be documented in the mapping exercise and be subject to the board's specific consideration. Boards are, however, expected to adhere without reserve to the ten principles of the Code.

Process for ongoing adherence to the Code

After the initial adoption of the Code, the mapping of actual practice against the Code's requirements should be updated and reviewed by the board on an annual basis. In particular, careful consideration should again be given by the board to any gaps between the Code's requirements and actual practice and as to whether such gaps, if any, could be considered to prevent full adherence to all ten principles of the Code.

It is recommended that the annual review of adherence to the Code is done at the same time as the board's approval of the annual financial statements.

Disclosure of adherence to the Code

Adherence to the Code should be disclosed in the Annual Report. It is recommended that such disclosure be made in the Directors' Report to shareholders. Alternatively, the disclosure can be made in the notes to the annual financial statements of the entity. The Directors' Report to shareholders is a communication that is not directly subject to external audit whereas the notes to the financial statements form part of the information that is directly subject to external audit review.

In addition to disclosure in the Annual Report, consideration should also be given to disclosure of adherence to the Code on the website of the fund, management company or fund sponsor. An increasing number of fund sponsors have developed a governance section on their website and, where this is the case, this medium can be used to explain the governance policies and practices that have been adopted.

Guidance material on topics covered by the Code

A substantial body of guidance material has been developed by ALFI on topics covered by the Code (please refer to the ALFI web-site under the tab "Setting up in Luxembourg - Fund Governance"). This web page provides links to guidance on specific topics included in the Code as well as links to the numerous ALFI guidelines and recommendations on a wider range of topics.

Additionally there is a link to the web-site of ILA which has developed guidance material on several topics that are of relevance to the Code.

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