



Independence

Flexibility

Commitment

Trinity Fund Administration Limited

The Board of Directors

Series 1.3

Dublin



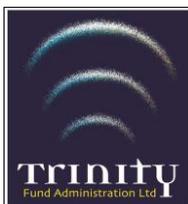
Cayman



New York



Cyprus



The Board of Directors in Alternative Investment

Corporate governance of alternative investment funds has undergone increased scrutiny since the 2008 financial crisis. The roles and responsibilities of the board of directors and how an effective board addresses shareholder interests within a fund have made major headlines and become of increasing interest to investors. The recent examples of the Weaving court cases in the United Kingdom and the Cayman Islands are a useful source to explore some of the ways in which an ineffective board of directors generates poor corporate governance, and produces adverse effects for an investment fund and its shareholders.

In April 2012, in his outgoing speech as CEO of the Financial Services Association (UK), Hector Sants discussed the need for improved corporate governance and the symptoms which contributed to the failure of financial firms over the last five years. He identified the indicators of financial failure as follows:

- A dysfunctional board
- A domineering CEO
- Key posts held by individuals without the correct technical expertise
- Inadequate oversight of risk
- Inadequate understanding of the aggregation of risk

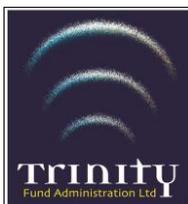
Although Hector Sants' speech referred to financial firms in general, his views on corporate governance are also relevant to the corporate governance of alternative investment vehicles.

Board Composition

One of the symptoms listed of a fund heading for failure is a dysfunctional board. A fund ensures that its corporate governance is well executed by laying out a suitable structure, corporate attitude and monitoring follow through. An effective board is composed of members who understand how an investment vehicle could fail and therefore must possess the correct technical competence and experience to comprehend and anticipate these potential circumstances. In addition to the relevant knowledge and experience, board members who possess the desired values and character are also an asset to a firm.

To achieve the desired variety of board members, the presence of independent non-executive individuals is an extremely effective way of bringing an outside perspective to a company. Independent board members allow for greater emphasis on investor needs. Executive directors are usually affiliated with the investment managers, or advisors and are thus highly involved with the fund's day to day running. Therefore, the managers and advisors benefit from having an outside perspective when making important decisions for the fund. As the title suggests, independent directors must not have any financial interests within the fund, in order to provide a truly independent viewpoint. Independent directors do not take part in the daily discretionary investment management of a fund and to ensure their neutrality, should not be involved in these decisions.

Independent directors can be sourced from independent director firms, or there are many established independent directors from the investment industry offering their services. Board members do not need to all possess the same level of expertise; in fact it is more desirable to include a diverse range of expertise and experience which encourages a superior level of debate and less 'group think' among board members.



Decision Making

Meaningful debate among members is essential to a competent board of directors. A board needs to regularly challenge the decisions that they are asked to make and ratify at board meetings. As has been covered in the media, the Weaving hedge fund case, (to be discussed further in detail), demonstrated how failure by board members to challenge decisions resulted in a major lack of oversight of the fund's activity. As such, it is recommended that each decision be subject to the correct amount of debate, where all potential risks are covered before a final decision is taken.

Directors of an investment vehicle are required to take a broad range of decisions. For an investment fund, directors should review the Offering Memorandum ("OM"). The OM relates to the fund's strategy, and overall operational activities of the fund. Some of the important points to cover within the OM are trading instruments, information on counterparty exposure risk, and redemption and subscription procedures. On establishment, cases can occur whereby a board is overloaded with management information, obscuring the relevant information and constraining debate on the key issues. It is therefore recommended that meeting briefs are carefully prepared, and in good time, to ensure the correct content is present in the necessary level of detail.

Content to be covered during meetings

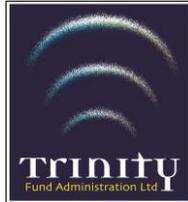
In order to ensure that the agreed strategy for the fund is properly executed, it is recommended that a board ensures a flow of information in order to monitor the implementation. This increases the effectiveness of subsequent meetings and allows for the correct preparation of meeting briefs. Directors must be familiar with and understand the investment vehicle's official documentation, including the Articles of Association and the OM. The Articles of Association set out the duties of the board and guidelines for meetings proceedings.

Directors may also be required from time to time to review and approve written resolutions, which are legally binding. Resolutions can be signed outside of meetings, and are generally considered approved after all directors have signed. Directors should ensure that any such changes referred to in the resolutions are legal under the corporate documents and discern the reasoning for such changes to the functioning of the fund. It should be established that any decisions taken which concern a certain group of shareholders do not adversely affect another group of shareholders. Typical share dealing matters contained in written resolutions include waiving or reducing notice periods, application of gates, redemptions proceeds or any variances to the dealing procedures set out in the OM.

The overall financial performance of the fund is an important topic for directors to cover as well. At the end of an accounting year, the board are required to review and approve the audited financial statements of a fund.

Investor communications are another possible item on a board meeting agenda. These are sent to investors on a regular basis in order to inform them of the overall performance of the fund and to explain how the investment strategy has played out since the last investor update. These are very important during lower performance times for a fund, in order to reassure investors. The investment manager composes the investor letter, and it is useful for independent directors to use their expertise to review communications and ensure a suitable investor letter is issued.

If conflict were to occur between an investment vehicle and service providers to the fund, such as administrators or prime brokers, this can be mediated by independent directors.



There are no requirements regarding who prepares the agenda for a board meeting, however it is generally the corporate secretary who drafts the agenda and prepares the minutes arising from a meeting. It is recommended that a service provider who is experienced in this capacity takes this role, in order to convene board meetings and circulate the relevant documentation in accordance with the statutory documents of the fund. Service providers such as administrators and directors can perform this duty. Notice requirements can be found in the funds articles which should be adhered to when drafting the notice and incorporating the agenda. The preparation of the minutes is highly important in order to ensure that there is accurate recording of the relevant issues that were discussed and debated in order to come to the most appropriate decision, as well as allowing the corporate secretary to note and document concerns and responsibility for appropriate follow up measures.

Delegation of Duties: Weaving

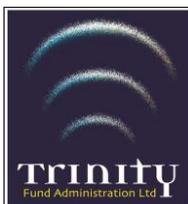
The case of the Weaving fund was a seminal case for hedge funds all over the world, after its \$600 million collapse in 2009. The Cayman Islands' civil case found two non-executive directors guilty of wilful default in the discharge of their duties. In a 37 page judgement by Justice Andrew J. Jones, he explained the requirements and expectations to which directors of alternative investments funds are subject to. It was emphasised that non-executive directors should be competent and knowledgeable, and should not allow for the dominance of one individual over the board, which is what is deemed to have occurred in the Weaving case.

In addition to the Cayman Islands' investment court case relating to the independent directors, the High Court in the UK found Weaving's manager Magnus Peterson guilty of fraud, two executive directors of the fund directors guilty of negligence which allowed fraud to happen, and a highly paid employee of the fund guilty of negligence. Following this judgement, the UK's Serious Fraud Office ("SFO") decided to reopen the case against Magnus Peterson which had been dropped in 2011.

In both the UK and Cayman Islands rulings, the poor corporate governance at one Weaving fund was highlighted, where non-executive directors were not considered suitably independent, or fit for their role. Of the non-executive directors convicted in the Cayman case, one was Magnus Peterson's younger brother, and one was his step father. The judge in this case found that although Magnus Peterson's company Weaving Capital UK was designated to be the fund's 'advisor' in the OM, Weaving Capital UK was in reality acting as the investment manager. Thus, the decisions made regarding the assets of the fund were controlled by Magnus Peterson and it was found that the necessary level of debate required to reach reasonable, investor driven decisions did not occur.

In the UK case, a similar line was taken in relation to the fund's corporate governance, where Mrs. Justice Proudman found that Magnus Peterson managed the fund however he saw fit, without being held accountable by the board of directors. It was also found that Mr. Peterson did not comply with the investment restrictions outlined in the fund's OM, whereby the Weaving Macro Fixed Income Fund Ltd. engaged in fictitious interest rate swaps, incorrectly inflating the fund's NAV for its investors.

The Weaving case also highlighted the issue of delegation of the various functions of an investment fund including investment management, administration and accounting to professional service providers. This practice does not reduce the level of responsibility of directors. In fact it increases the requirements for enquiry and supervision of the roles that service providers play in the fund's operations. Directors should be able to regularly verify that a third party service provider is performing its duties in accordance with the relevant service provider agreement.



Furthermore, heavy influence of an investment manager should not prevent directors from raising concerns. In the Weaving case, it was found that directors had signed documents without close inspection of their contents.

Corporate Governance after Weaving

Weaving, although a detrimental case for its investors and various creditors, also serves as an important source of education and potential improvement for the alternative investment community as a whole. The problems highlighted during the Cayman Islands ruling and the UK ruling show strong parallels with the issues articulated by Hector Sants in his outgoing speech as FSA CEO. The presence of a domineering CEO, who has more influence than his or her whole board of directors is a major barrier to effective monitoring of the various decisions to be made.

The ineffective board, lack of expertise of board members, proximity of independent directors to the investment manager (brother, stepfather) and lack of risk oversight all contributed to a poorly performing board of directors. As a consequence, it was deemed that decisions were not made based on the best interests of the shareholders. This is a highly influential case for all members of the investment management industry, as there has been a shift towards greater demands for transparency from financial regulators on a global scale, as well as from investors who are becoming more sophisticated and learning from these types of examples.

As such, it is understandable that the provision of documents which prove that board members met, discussed and debated relevant issues, is increasingly essential. An experienced corporate secretary who provides the relevant documentation pre-meeting, during a meeting, and takes appropriate measures post-meeting is invaluable in this respect.

The applicable domicile of choice will often provide guidance on how good corporate governance can be achieved. For example Ireland, the biggest hedge fund domicile in Europe, introduced the Corporate Governance Code for Collective Investment Schemes and Management Companies at the beginning of 2012. It is understood that Guernsey is developing a similar code and the Cayman Islands Monetary Authority's Statement of Guidance on Corporate Governance is under policy review. Companies can conduct 'gap analyses' in order to determine where their board needs to increase effort to comply with the recommendations and govern the investment vehicle to the highest standard possible.

Globally, corporate governance for investment funds is undergoing close examination, in an effort to prevent failure of financial firms in the future. This can only be achieved if a proactive approach is taken in order to ensure that boards of directors possess the right amount of expertise and that this expertise is utilised efficiently via the correct procedures and information flows.

For further information on any of the topics covered please call +1 345 743 6622 or email trinity@trinityfundadmin.com or visit our website at www.trinityadmin.com