A DECADE OF INDEPENDENT GOVERNANCE

The Cayman Islands has successfully navigated a raft of almost constant regulatory change in the past decade. Geoff Ruddick at International Management Services spoke to *Cayman Funds* about the biggest changes in the environment and some of the challenges that remain.

You mentioned in last year's article that 'governance is not a game'—can you expand on what you meant by that?

In the past few years fundamental governance-related issues such as capacity (numbers), substance over form (form over substance), and board composition (split boards), have been used as marketing pitches. These are fundamental governance issues yet the sales side of the issue is increasingly the focus of attention.

Could you provide us with your perspective on each of these—shall we start with capacity?

There certainly has been an extraordinary focus on capacity since the credit crisis and rightfully so, as capacity is a critical governance issue.

Unfortunately though, for some time, an arbitrary number or cap had become analogous (and, arguably, in some cases the sole identifying factor) with determining the capacity of a director. Numbers are unquestionably relevant and therefore it is an important question to ask, but if it is the only query raised in assessing a director's capacity it will be of limited value. Questions are fortunately far more thoughtful and thorough now and people realise that numbers in isolation, without context or completeness, can be incredibly misleading.

What are people asking now that is different from before?

Queries now go beyond numbers to determine what a director does day in and day out and how their time is spent, as well as to assess the individual's ability. Simply put, capacity is a function of time and ability. People also now consider the composition of the clients the director serves; their role within the company; what other responsibilities they have beyond serving in a personal capacity on fund boards; their model, support infrastructure; their individual and firm capacity constraints; whether the director has any excess capacity for times of stress; and perhaps most important, how they personally view their role as a fiduciary.

Another debated issue is whether it is about the individual or the institution. What are your thoughts on this?

Most consideration should be given to the capabilities of the prospective director, but I don't think it is necessarily as simple as one or the other. There is a component of both, although with that said it is a 'personal' appointment and there is 'personal' liability that comes along with that. So the personal nature of the relationship certainly is paramount, as ultimately the individual, not the institution, has the fiduciary duties to the fund. Therefore it cannot be completely 'institutionalised' away. As for most things in life, the right balance is important.

You mentioned 'form over substance', can you give an example?

There are numerous examples from templated reports and agendas, to written resolutions versus meetings, etc. With respect to board meetings, if they are held just to tick a box where the constitutional documents, regulatory guidance notes, or institutional policies and procedures dictate, meetings being held for the sake of having meetings (ie, form over substance) are of limited benefit.

It seems to me as though many have lost perspective that the underpinning of fundamental good governance is about substance, not solely form. Well thought out, planned and attended, discretionary versus mandated, meetings that are timely and properly minuted (ie, substance over form) are incredibly important. Meetings certainly have their place and should be encouraged as appropriate, provided there is a thoughtful, measured, and balanced approach in the decision-making process.

It could, however, be argued, and perhaps at times be justifiable, that matters can be documented in more detail by emails and written resolutions than they would by verbal phone conversations, meetings, and corresponding minutes. Regardless of the form of governance, it is important that there is always sufficient evidence documented to support the decisions taken by a board.

The latest trend of having split boards has also received a lot of attention in relation to governance. What is your take on split boards?

Split boards have been the trend for the last couple of years, with investors in particular becoming increasingly interested in board composition and appointing directors with complementary skillsets from different service providers. My take is that an effective and diverse board requires competent individuals with complementary skillsets who can work collectively irrespective of whether they come from the same shop. The collaborative aspect is as important as the individual expertise. There should ultimately be synergies gained so that the board's collective value equates to more than the sum of its individual members. Good governance and the right board composition is really what it is all about.

What should people be focusing on when constructing a board and how do investors, funds, etc, go about this process?

Constructing an effective and diverse board does not have to be an arduous, time-consuming process, but the decision should not be taken lightly. The directors are accountable for leading and directing the fund's affairs, so effective corporate governance is essential and the appointment of experienced and qualified independent directors who collectively provide a diverse and complementary board composition is essential.

The industry needs to ensure the focus remains on the underlying fundamentals of good governance and the right board composition and not simply on retaining directors from different fiduciary firms. Where the main consideration or key focus is only to engage independent directors from different fiduciary firms, this narrow focus, for the most part, misses the fundamental objective of establishing an effective and diverse board.

They should go beyond the 'split board' sales pitch and have a thoughtful, measured, balanced approach and give all aspects due consideration.

Are there enough directors available with the requisite experience?

There has been an influx of individuals with varying skillsets into the fiduciary space which is a positive development, and there is certainly a greater depth of high quality directors in the space to choose from than there was a few years ago. Most are senior people who have excellent experience, qualifications, pedigree, etc, and are able seamlessly to make the transition from being an administrator, lawyer, auditor, regulator, risk or investment professional, etc, to being a director.

Others, however, have difficulty making the transition, as although they have impressive technical skills, they are unable to transition into a leadership and oversight role that goes beyond their area of expertise. Individual personalities can come into play as well.

Why have we seen an influx of new directors, and what do you mean by that comment about individual personalities?

The credit crisis was really the inflection point where governance started to be taken more seriously. As a result, there has been a flood of new entrants into the fiduciary space, which can be partially attributed to a supply shortage as long-standing individuals are reaching capacity. Other newcomers are simply being opportunistic as they are looking for a career transition.

With regard to individual personalities coming into play, for example, some people are too passive, or lack the intellectual curiosity or gravitas to effectively and appropriately challenge management or their fellow directors, while others have domineering and controlling personalities or simply lack the aptitude to participate in a collective approach.

The right balance of individualism and collectivity is paramount to an effectively functioning board.

In your opinion then, what are the key characteristics and considerations of a good fund director?

There is a wide range of attributes and characteristics to consider, such as background (accountant, lawyer, ex-regulator, investment or risk expert), independence, qualifications, stage of career/life, level of engagement, technical abilities, personality and interpersonal skills, jurisdictional residence/familiarity/knowledge of and experience within the industry, capacity, support infrastructure, etc. The list goes on but

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I would emphasise again, that perhaps most important is how the individual personally views his or her role as a fiduciary.

What skillsets should a director ideally have—what constitutes the right skillset?

One important skillset that is often overlooked is corporate governance in itself. Possessing one or more of the aforementioned attributes in isolation does not necessarily make someone a good director. Perhaps even more important than having a director with a specific skillset, expertise, or being from a different fiduciary firm is to select directors who have a broad range of experience, have the innate ability to ask intelligent and probing questions, and know when and where to find expert advice when needed.

It is often more effective to engage someone with specialised expertise when needed rather than recruit it on to the board. The ability to put issues into the appropriate context is also very important—sometimes the board has to provide high level oversight and other times a more detailed approach is required. Effective and experienced directors will be able to maintain perspective and context in such situations, regardless of their specific skillsets. ■

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