Financial Conduct Authority

# UKLA Technical Note

## Master-feeder structures

Ref: UKLA / TN / 409.1 Guidance Consultation

LR 15.2.6R, LR 15.4.6R and LR 15.4.6AG

LR15 sets out specific requirements for master-feeder structures. LR 15.2.6R and LR 15.4.6R recognise that a feeder fund may achieve a spread of investment risk by ensuring:

- the investment policies of the underlying master fund are consistent with its own and provide for the spreading of investment risk, and
- the master fund acts in a way which is consistent with the feeder fund's investment policy and spreads investment risk

The effect of these rules is to enable feeder funds to comply with the LR 15 rules on spread of risk by taking into account diversification at the level of the master fund.

As set out in LR 15.4.6AG, a feeder fund should have the ability to withdraw its funds if the master fund does not in fact spread investment risk, although we recognise that in practice this withdrawal may be after some delay, for example because the underlying investments held by the master fund are illiquid or subject to restrictions on their realisation.

The effect of the additional rules which apply to feeder funds (LR 15.2.6R, LR 15.4.6R and LR 15.4.6AG) is to recognise that the board of the listed issuer will have less direct control over the underlying portfolio than it would if the funds were invested directly, as feeder funds are typically minority investors.

We have come across structures that differ from traditional master-feeder structures, either because the feeder fund also proposes to invest some funds directly (outside of the master fund), or because the feeder holds a percentage stake in the master fund that should allow it to exercise some control over the master fund (in extreme cases 100%).

Clearly, in such scenarios the implicit recognition that the issuer could not influence the direct investments, or the investment choices of a majority-owned master respectively, does not hold. As such, the investment policy of the issuer should reflect the issuer's control of these investments by clearly describing how investments will be made by the issuer in a way which is consistent with its objective of spreading risk, rather than just referring to the master's policy as would normally be the case for a feeder fund.

In addition, a feeder fund which proposes also to make direct investments will need to consider whether it continues to meet the criteria for a feeder fund, given that LR 15.2.6R applies where an issuer invests principally in a master fund.