Individually Managed Accounts/ Separately Managed Accounts (SMAs)

An individually managed account is one in which your client signs a contract with a professional money manager who then invests your client's assets in a portfolio of equity or fixed-income securities or mutual funds. The money manager will generally have complete discretion over the activity in the portfolio, and purchases and sales of securities will occur without your client being consulted.

Like mutual funds, each managed account has a specific investment objective, such as those we discussed above and each manager must have some assurances that their style is appropriate for each client. For this reason, each managed account must have written investment objectives determined by you.

Unlike an investor in a mutual fund, however, clients with managed account directly own all the securities in the portfolio rather than owning fractional shares in a fund that in turn owns the securities. This gives you the ability to customize your managed account portfolios, which you don't have with a mutual fund. You can restrict certain securities from purchase, or you can request certain sales at tax time.

In addition, you receives a statement on a regular basis from the custodian (typically a brokerage firm), which reports all shares held, and any buys and sells during the period. Managed accounts issue quarterly, and sometimes monthly, reports to accountholders showing:

- Exactly which securities you hold
- The number of shares you own
- The current value of each security and of your total account
- The cost basis of each security
- Details of account activity (like purchases, sales, and dividends paid out or reinvested)
- Your portfolio's asset allocation
- Your portfolio's performance in comparison to a suitable
- Benchmark

Not all managed accounts are created equal. A typical managed account portfolio includes between 30 and 70 individual stocks or bonds. Portfolio turnover, or the rate at which holdings are bought and sold, varies from manager to manager and is reported regularly to you and other accountholders. Some investment advisers emphasize the benefits of transparency when they recommend managed accounts. They argue that, in contrast, mutual funds disclose their holdings just twice a year in their annual and semi-annual reports and provide much less detail about their underlying securities, showing only how many shares are held and their value as of the report date.

There are as many varieties styles and investment philosophies of individually managed accounts as there are investment styles, or mutual funds.

Once available only to the very wealthy, managed accounts are now available with account minimums as low as $25,000. Most major mutual fund companies also have a division, which manages individual (often called "separate") accounts, and there are more than 7000 managers registered with the SEC.

Managed accounts are offered by every major brokerage firm, and most independent financial advisory firm which uses an independent provider.

Managed accounts have attracted billions of dollars in new investments over the last few years.

The Appeal of Managed Accounts:

- They appeal to investors who have accumulated substantial assets and want to plan for long-term security.
- Investors of all ages are increasingly turning to professional advisers for help in managing their portfolios.
- Lower minimum investment requirements have put managed accounts within the reach of many more investors.
- Managed accounts offer opportunities for tax planning and customization.

Specific Advantages of Managed Accounts:

- Direct ownership of the securities offers a number of advantages, many of them tax-related.
- Short-term capital gains, which are taxed at your regular federal income tax rate, can be eliminated or reduced by asking the manager not to sell specific investments until a certain date.
- There are no phantom gains in a standard managed account. Customization is a potential benefit—allowing investors the flexibility to modify individual portfolios. Certain securities can be restricted, while others your client currently owns can be held for capital gain purposes.
- Diversification may be an advantage, as managed accounts typically hold 30 or more securities.
- Because money managers have large amounts of assets, there are trading efficiencies. Managers can take advantage of institutional rates typically not available to individual investors.

Risks of Managed Accounts:

- Market risk: Like any strategy we have been discussing, your client is subject to risks of their underlying investments.
- Style risk: Managers vary in the amount of investment risk they take; some are more aggressive, some more conservative. For this reason, setting your investment objectives is the most crucial factor in establishing a successful managed account strategy for your client.

  Managers can fail to meet their investment objectives, or worse, alter their style to suit market conditions. For this reason, due diligence (discussed in Session Six) is an essential responsibility of your financial helper.
- Fees: Fees vary by manager. Some managed account programs offer "Wrap fees" which bundle manager, custody and trading in one all-inclusive fee. The advantage is in its predictability, and the fact that your fee can also generally be combined, to price a single fee to clients. The disadvantage may be that wrap fees vary by program, and some may be more expensive than their "Unbundled" counterparts.

Unified Managed Accounts (UMAs)

UMAs are managed account programs which combine a number of investment managers, each with a different area of expertise, under a single umbrella to provide greater diversification than a single-focus account. The advantage is that they can combine every single investment in investor accounts into a single account for reporting purposes. In addition, they can be rebalanced daily, across the multiple accounts. A variant of the UMA is the UMH or Unified Managed Household which applies across an even broader range of client-related accounts.managed investments offer investors actively managed core portfolios, which combine investments in different styles, either from a single manager or from multiple managers. Historically, these sort of products have been usually offered by a large sponsor and were restricted to institutional clients and in-house managers. However the UMA market is in the process of expanding to include smaller firms and clients, and independent consultants and managers. While UMAs are often packaged like a product, they are more of a process. UMAs allow access to many of the benefits associated with managed accounts in an affordable way.

With an UMA, one or more investment firms may be chosen to manage the assets, spread across styles. In some cases, the individual managers may have limited discretion over the client's total investment, and to minimize investment overlap, asset allocation is monitored by an Overlay Portfolio Manager or OPM. The benefits of IMAs include the professional management, diversification, tax efficient management capabilities, and, sponsor-driven Due Diligence of Individually Managed Accounts with lower investment minimums and at a lower cost. However, all of the risks inherent in using separately managed accounts apply to them.

UMH is a slightly expanded version of the UMA which includes other non-traditional assets, such as savings and unmanaged assets.

Evaluation Tools

Rating Systems

There is a lot of data to analyze to evaluate a money manager or a mutual fund (we will discuss there in more depth in the Session on Due Diligence). Past performance measures the manager or fund's historical returns and compares it against a peer universe or index. The key criterion to look for is consistence in results. Remember that past performance is no guarantee of future results. It may be one factor in the decision-making process, however.

Risk measures the volatility of the results. The more volatile a manager may perform, the greater the possibility that your client may suffer some losses along the way. Your client's tolerance for risk is a crucial element in the decision-making process.

Cost measures how much the client pays in sales charges, commissions, fees, and annual expenses. The cost of management in a fund or a separate account effectively diminishes the return on the investment. Therefore, in selecting investments for your client, the most important part of the process is called due diligence (more on this ongoing long-term process, which is of vital importance to the Consulting profession, later).

Fortunately, a number of research firms rate or rank mutual funds and individual account managers and provide reports to the financial press or directly to consumers. Ratings and rankings compare funds and managers to mutual funds or managers with similar investment philosophies.

In addition, many firms have a proprietary system of ranking and rating money managers and mutual funds, generally resulting in an "Approved list".

Public or governmental web sites, such as EDGAR and the SEC provide compliance, financial and regulatory information on funds and managers, and FINRA has resources on mutual funds.

Conclusion

Managed Accounts Prosper Because It's Difficult to do it Alone

Clients are bombarded daily with advertisements and promotional material about the success or merits on one investment, one company or one product over others. Consider these actual advertisement lines from publications:

- From Wall Street Journal "Straight talk about Biotech investing. Year to date our model portfolio is up 155%."
- Local newspaper advertisement "Looking for Money? Free Conference tells where free Government money is, and how to get some."
- "Houses for $1. Lots of success stories."
- "1500 surveyed (45+) can't answer basics about investments."
- AARP study: "Does diversifying investments decrease risk?"
- "45% get advice from family or friends."

The first thing to understand is this: **THERE IS NO ONE INVESTMENT VEHICLE RIGHT FOR ALL INVESTORS**. Investors are individuals, and must be treated as such. You need someone who is unbiased to help them maneuver through the often-confusing world of investing. We will discuss helpers and ways to invest in another session.