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FUND TRACK**New Managed Accounts Tout Tax Benefits**

**Offerings' Predecessor
 Also Advertises Savings,
 But Complexity Interferes**

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You may soon be hearing about how "model portfolios" and "unified managed accounts" can save investors on taxes.

These investment account structures are the successors to separately managed accounts, or SMAs. But there is a catch. The older SMAs were supposed to save investors on taxes, too. In fact, while traditional SMAs have long been marketed on their tax benefits, many believe these accounts' complexity has made it difficult for them to live up to their promise.

More Tax-Related Trades

It turns out that financial advisers request tax-related trades in less than a fifth of traditional SMAs. The new model portfolios appear to encourage more tax-related trades, reaching slightly more than a third of the accounts.

Traditional SMAs are individual investor accounts of, say, 20 to 40 stocks, managed by a professional money manager. Unlike with mutual funds, which pool investment dollars, an SMA money manager makes an investment decision and then buys and sells for each investor separately.

In terms of taxes, these accounts have two advantages over mutual funds. Because investors own their own shares, they don't have to worry about distributions of capital gains that have accrued to other investors, as mutual-fund holders sometimes do.


Also, SMAs are designed to be customized. That means financial advisers or other account overseers can buy or sell shares in ways that help minimize their clients' tax bills.

Complicated Process

Perhaps one reason SMAs aren't used very often for tax-related trades is that the process is complicated. A financial adviser, or someone else at a brokerage or third-party firm, must keep track of and coordinate the tax liability of each part of a client's investment portfolio. Often these investments sit in several different accounts.

Enter model portfolios. These resemble separately managed accounts in many ways, but instead of allowing several money managers to trade for each client, those managers hand a "model," essentially their trading instructions, to the brokerage or a third-party "overlay manager" who makes all the trades.

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One benefit of the new system is supposed to be making tax-related selling tailored to individual clients easier. All trading is centralized in a single account, often called a "unified managed account."

A recent study commissioned by the Money Management Institute, an industry association, found that model accounts do appear to make tax-selling easier, though the results might not knock investors' socks off. The study found tax-management tools were used in about 37% of taxable model-based managed accounts. The report didn't study traditional separately managed accounts but noted the figure should be much "much lower" for those.

"It's a problem with traditional SMAs that no one uses the tax-management features," says the report's author, Jean Sullivan, managing principal of Dover Financial Research LLC.

A spokesman for the MMI says the association is pleased with the level of tax management in model-based accounts and traditional SMAs. He adds that tax-loss selling in the older separately managed accounts should be somewhat less frequent than in model portfolios.

Individual investors typically have several SMAs, each representing a different investment strategy. If a financial adviser orders a tax-related trade on behalf of a client, he might do so in only one of the client's SMA accounts and not in the others. Model-based accounts, in contrast, combine different strategies into a single, unified managed account. So any tax-related trades are likely to be made in the single overarching account.

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