Unified Managed Accounts
Turbo-Charge Your Practice

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Most of us are familiar with the history of separate account investing, but the latest development—commonly referred to as the unified managed account, or UMA—perhaps is the biggest positive change in advisor practice management since the introduction of the original separately managed account program by E. F. Hutton in the 1980s.

We are also all familiar with the investor benefits of using separate accounts (as opposed to mutual funds), e.g., control of tax basis and timing of gain recognition, portfolio customization, cost efficiencies, etc. In this article, rather than focus on the benefits to the investor, we want to focus on the efficiencies the new UMA platforms can bring to an advisor’s practice.

Background

Before the introduction of separate account wrap programs, only the largest investors could afford true investment consulting services (i.e., customized manager search and due diligence, professional investment management in separate accounts, consolidated portfolio reporting, and analysis). We know separate account wrap programs made this type of investing available to smaller investors, but what effect did it have on a practice with larger clients that did not need a solution for smaller clientele?

A friend of ours ran an independent investment consulting practice back in the late ’80s and early ’90s. The travel to the investment managers, the documentation of the research, the manual inputting of account information every month, and the tedious process of creating quarterly performance and attribution reports in Microsoft Excel was very labor intensive. At one time, the practice employed two senior advisors, two senior technical employees, and four administrative employees. Once a separate account wrap program that was flexible enough in manager selection was available, they were able to shrink the staff to one senior technical and two administrative employees. Additionally, they were at client capacity under the old manual system, but even after shrinking the staff from six to three, they were able to add several hundred million more in client assets to their practice. That is a revolutionary change in practice management. The separate account wrap platform allowed the advisor-to-support ratio to shrink from three to one and one-half while still increasing client service capacity.

To understand the UMA, we have to understand a stepping-stone transition development called by various names, such as Smith Barney’s multidisciplinary account (MDA). In the traditional separate account wrap program, each manager still traded securities in individual accounts, and the program sponsor still would handle the consolidated performance reporting. As computer technology advanced, it became possible to combine two or more managed portfolios into one single brokerage account. The managers no longer traded the accounts directly but provided their security models to the trading firm, which would combine them, then use complex trading programs to replicate the effect of the separate accounts in the one brokerage account.

Initially, these models were fairly static, and advisors would choose pre-built multimanager portfolios that fit clients’ needs. Many managers were not willing to accept the lower fees that platform sponsors would pay on these accounts, and many did not want to publish their security models. These accounts became very popular, however, and many managers are realizing that although they are paid fewer basis points in this model, by eliminating much of the administrative cost associated with opening and trading separate accounts their margins actually widen. As more firms began to offer these types of programs, including service providers to independent advisory practices, more managers began to provide their security models in addition to trading in traditional separate accounts.

Flexible Model UMA

The “flexible model” unified managed account has redefined the advisor’s landscape. It is an extraordinary new tool that enables the advisor to maximize the value/efficiency ratio. With traditional separate account wrap programs, individual account minimums still were fairly high, typically $100,000 for equity accounts, higher for fixed-income accounts. While multiple manager programs were able to compress these minimums, there still was a lack of allocation flexibility. A vast amount of computing power is needed to prepare hypothetical illustrations and consolidated reports covering multiple managers in one brokerage account.

Now major wirehouse brokerage firms and even independent-advisor service providers are offering the next step in this evolutionary process, the UMA.

A UMA is a brokerage account that may contain securities traded in accordance with individual money managers’ model portfolios as well as individual securities selected by the investment advisor or the client. Individually selected mutual funds, exchange-traded funds (ETFs), and individual stocks can...
be commingled in the single “unified” brokerage account. Of course, different registrations still must be held separately, but all investments identically titled now may be combined.

UMA programs are in varying stages of maturity. Some still have somewhat limited investment choices or limitations on their ability to break out benchmarks for reporting on parts of the portfolio. For this reason, they have not yet replaced traditional separate account and mutual fund wrap programs, but for now are being offered as an alternative vehicle. However, most development efforts at larger brokerage firms and service providers are focusing on UMA programs. As technological hurdles continue to fall and firms add flexibility and gain experience with the UMA, the UMA will gain greater acceptance in the advisor community.

Before the UMA, the financial consultant’s advisory choices were very compartmentalized. An advisor could maximize efficiency at the expense of flexibility only by using a separate account solution, a mutual fund solution, or a broker-managed solution. Or, the advisor could maximize value-added by emphasizing flexibility at the expense of efficiency.

Using only a mutual fund wrap program solution, for example, maximizes advisor efficiency. In fixed-model programs, however, this feels product-centric, almost like selling an annuity or lifestyle fund. Using a separate account wrap program solution may be more flexible, but the high account minimums may limit diversification opportunities.

On the other end of the spectrum, imagine an advisor who trades domestic large-cap stocks for clients but uses separate account programs for small-cap and international managers and mutual funds for bonds and salt-and-pepper categories such as emerging markets equity, real estate investment trusts, or other specialty areas. This advisor may have had some client money in a brokerage account, some in a separate account wrap program, and some in a mutual fund wrap program, with no way to consolidate reporting for these accounts. This diversification may have a high value for the client, but it comes at a high cost in terms of advisor efficiency.

Now imagine one delivery platform an advisor can use for all these solutions, the flexible model UMA. UMA programs allow for varying degrees of flexibility depending on the firm, but all program sponsors are working toward more flexibility and greater reporting capability. The most common limiting factor is how the program sponsor allows for discretionary advisor activity or client-directed security holdings; in some programs these still must be segregated. A growing number of separate account money managers, however, are providing security models for program sponsors to trade, and the selection of mutual funds and ETFs available in UMA programs continues to grow.

The flexible UMA is an efficient tool for the advisor serving the lower-end of the market, yet it still provides adequate diversification opportunities for the higher end. Advisors can tap into the efficiency benefits of firm-directed models using mutual funds and ETFs for smaller clients while delivering customized solutions to larger clients. The program sponsor still provides a protective layer of due diligence in the selection of separate account managers, mutual funds, and ETFs for inclusion on the UMA platform. But the advisor now has a wide set of solutions to choose from and more flexibility in allocation amounts. Separate account manager models once available only at $100,000 may be available at $50,000 or less, and mutual funds or specialized exposures such as economic sector ETFs are available in small amounts. This enables advisors to take a more active role in shaping their clients’ portfolios—and highlight their value proposition as advisors. The ability to hold all of this in one brokerage account greatly simplifies administrative, paperwork, and tax-reporting burdens.

All this has the effect of maximizing the advisor’s efficiency ratio—the number of clients and amount of assets manageable within a given time and staffing level. Technological gains will continue to drive more efficiency into UMA program administration, freeing up advisor time for client problems and solutions. Advisors will be able to increase supervised assets with no increase in staff or time expended.

UMA programs are relatively new in their present form and still face obstacles. However, we believe the advent of the flexible UMA is every bit as revolutionary as the original separate account wrap programs were to firms that manually created consolidated portfolio reports in Microsoft Excel. While traditional separate accounts still may be useful for some very large institutional investors with specialized needs, we believe the industry will migrate toward the UMA as the primary—perhaps the only—service delivery model. As more money managers provide portfolio models for others to trade, and as sponsors solve technical problems and provide more flexibility, advisors can anticipate ever-greater administrative efficiencies and productivity gains in their practices.

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