

info sheet **Understanding separately managed accounts**

If you have a significant sum to invest — generally \$100,000 or more — you can now take advantage of an investment vehicle that was once available only to the very wealthy and to institutional investors. The investment is a separately managed account. It allows you to tap the expertise of a large, experienced money management firm while still investing through a portfolio that is tailored to your unique needs. Your investment professional may have already recommended that you consider a separately managed account. You may find it well worth your while to take a close look at the benefits these accounts can offer.

What is a separately managed account?

In a separately managed account, you obtain all of the benefits that mutual funds offer — professional management, diversification, and liquidity — but unlike a mutual fund, a separate account does not pool your money with other investors' money. All of the securities that the management team selects for the account are owned by you. That individual ownership affords you flexibility, control, and tax benefits that mutual funds and other pooled investment accounts cannot match.

Key benefits

A separately managed account is generally structured like a mutual fund in that it has a manager or team of managers who pursue a specific investment objective. A firm may offer a large-cap growth account, for example. In that case, the managers, on behalf of each individual investor, would invest in large companies that they believe have the potential to increase their profits significantly every year. Within that broad framework, the separately managed account offers individual investors unique benefits.

Customization: In a separately managed account, you have some say about what securities are owned in the portfolio. Your input into the buying and selling of securities for your portfolio can include

- excluding certain securities, which you may feel you already own enough of in other portfolios or in your personal investments
- excluding certain securities you have a moral objection to, such as tobacco industry stocks
- incorporating securities you already own into your professionally managed separate account

How much input you can provide will vary, as each firm that offers these accounts offers its own level of customization. While customization affords you greater freedom, it — like any other freedom — must be used judiciously. Trying to customize the portfolio too much can handcuff the professional managers and hinder their ability to pursue the investment objectives of the account. Your investment professional can help you choose the right separate account manager for you and also help you determine what level of customization will best serve your needs.

Control: In a pooled account, your investment experience can be affected by other investors. In a mutual fund, for example, if a number of investors request redemptions, the portfolio managers may be forced to sell a large stake in a security they like because they need to raise cash to fund the redemptions. In a separate account, other investors' decisions will not affect you because you independently own each of the securities in the portfolio.

Greater flexibility with taxes: Pooled accounts such as mutual funds can create some unwelcome tax consequences. For example, if you purchase a mutual fund just before a capital gain distribution, you could owe a tax on the distribution even though you've owned the fund for only a few days or weeks. That distribution — and your tax — can also be substantial if the fund sold shares of a highly appreciated stock it bought years ago at a low price.

You won't have to worry about this problem in a separately managed account. The account does not have to make annual capital gain distributions the way mutual funds do. When you first invest in a separate account, your cost basis in any of the shares the portfolio will own on your behalf are based on their value the day you made your investment. Your cost basis in securities subsequently purchased for the portfolio will be their value on the date those securities are purchased.

You will incur capital gains taxes only when individual securities are sold at a gain. You may also have some flexibility in determining how to incur those taxes. For example, if you expect a substantial capital gains tax, you may be able to ask the portfolio manager to incur some capital losses to offset your taxable gain. You may also be able to ask the manager to delay the sale of a security if the delay could potentially shift the gain into the following year or make the profit realized from the sale a long-term gain, which is taxed at a lower rate than short-term gains.

How much a separate account can be managed for tax-efficiency varies, again depending on the firm that offers the account. Some firms limit the flexibility account owners are granted with tax decisions because putting too much emphasis on tax issues can adversely affect the account's performance.

Key features

Asset-based fees: With separately managed accounts, investors pay an annual asset management fee, with the level of the fee determined by the amount of assets in the account. The fee covers the cost of the expertise delivered by your professional adviser and the investment team, and it also pays for the expenses associated with administering and servicing your account. Because the fee is a percentage of the assets of your account, all parties involved with your account have incentive to increase the value of the account as much possible. That can benefit you as the client. The rewards for continuing to serve your needs are not gone after the initial sale, as can be the case with products that levy an initial sales charge.

Extensive due diligence: All investment professionals must make diligent efforts to understand the products they recommend to clients. The firms that offer separately managed accounts make extensive efforts to meet these "due diligence" requirements. Firms that market this product — including brokerage firms, financial planning organizations, and financial institutions such as banks — do extensive research before admitting an investment management firm and its particular portfolio managers into their separately managed account programs. The extensive reviews do not end once a firm has been admitted. The sponsoring firms constantly monitor the performance of each investment management team.

Service: While mutual funds issue annual and semi-annual reports to update shareholders on holdings and performance, separate accounts typically provide quarterly updates to show all activity in the account and the performance of the account in relation to a benchmark. These updates often include additional information such as market outlooks, commentary from the portfolio manager, and a statement of the

tax liabilities the account owner incurred during the quarter. You and your investment professional can also schedule reviews of your account on a more frequent schedule, as you wish.

Personal performance: The performance of separate accounts is not published in newspapers, as mutual fund information is, because the performance of your account is strictly yours. You can track the current price and performance of the separate account you own through your investment professional and your customer statements.

Does a separately managed account suit your needs?

In the past, separate accounts were available only to very wealthy investors — generally those with \$5 million or more to invest. But advances in computer technology and account administration over the past decade have made it cost effective for firms to make this unique service available to more investors. Today, you generally need a minimum of \$100,000 to invest in a separately managed account.

As you consider whether this type of investment might be right for you, ask yourself the following questions:

- Do you have high balances in your personal and retirement accounts, such as Individual Retirement Accounts (IRAs)?
- Do you expect to receive a large sum in the near future — from an inheritance or a legal settlement, for example?
- Are you planning to retire or leave your current employer sometime soon and will you have a large rollover from your pension and retirement plans?
- Are your current investments creating large annual tax bills?
- Would being able to take advantage of separate account's customization and flexibility help you better manage your tax situation?

If you answered “Yes” to all or even most of these questions, you may want to speak in greater detail with your investment professional about separate accounts.

How your investment professional can help

While the features and benefits of separate accounts may appeal to you, your investment professional, if he or she has not done so already, will want to conduct a thorough analysis of your needs before recommending a particular product. To perform this needs analysis, your investment professional may ask you to complete a questionnaire about your goals, your risk tolerance, and your current financial circumstances. Armed with this information, your adviser will have a better understanding of what investment options are right for you. After a thorough evaluation of your needs, your investment professional can help you determine if separate accounts suit your needs.

You can also count on your adviser to deliver ongoing support. He or she can help you devise an asset allocation strategy to keep your assets diversified across a range of portfolios in different asset classes and with a variety of investment objectives. Working with an adviser also gives you an expert to turn to whenever you have questions about the financial markets or your investments.

Additional resources for more information

An MFS® white paper: “Is a Separately Managed Account for You?” This MFS piece provides an overview of the key differences between mutual funds and separately managed accounts.

A third-party Web site: www.moneyinstitute.com. On its Web site, the Money Management Institute, a national organization for the managed account industry, provides information to help investors learn more about separately managed accounts.

Investment return and principal value of both mutual funds and separately managed account investments will fluctuate, and sale proceeds may be more or less than the amount invested.

A prospectus containing more complete information, including charges and expenses, for any of the MFS products can be obtained from your investment professional. Please read it carefully before you invest or send money.



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