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Zac Leman
head of platforms investment product development, platforms and investments
BT Financial Group

Under changes that became law last month, financial advisers can no longer offer Managed Discretionary Account (MDA) services to their clients in the same way that they've done in the past.

While many licensees are ready for the new rules, others missed the October 1 deadline. The question is, "how can they still offer the same investment outcomes without falling foul of the new government rules?"

There are several ways to solve this problem including the use of separate managed accounts (SMAs) or varying the adviser's AFSL as the way forward.

To date, only 59 licensees have applied for AFSL variations and that there are 244 licensees authorised to offer MDAs.

If you're a financial adviser and you want to know whether MDAs make sense for your practice, watch our interview or read this explanatory article.

Michelle Baltazar
Director of Media & Publishing

Is it too late to board the MDA boat?

On 1 October 2018, the requirements for advisers wishing to offer managed discretionary account (MDA) services to their clients changed. Whilst two years' notice of this change was given, and many advisers and licensees took steps in preparation, what are your options if you missed the boat?

What has changed

Previously, many advisers offered MDA arrangements under a "no action" position from the Australian Securities and Investments Commission (ASIC) providing their arrangements met certain conditions noted by ASIC. For many advisers, the result was the ability to manage tailored investment portfolios for certain clients, without the need to seek specific permission from the client each time a change to the investment portfolio was required. Similarly, there was no need to issue an advice document each time a change to the investment portfolio was made. These were often referred to as "limited MDA arrangements".

However, from 1 October 2018, anyone who wants to offer MDA arrangements must have, or operate under, an Australian Financial Services Licence (AFSL) that contains the authorisations to provide such arrangements. According to ASIC, 59 licensees applied for AFSL variations to accommodate this change and there are now 244 licensees with the authorisation to provide MDA arrangements[1].

As mentioned above there are some clear benefits to the operation of MDAs– both at the adviser (and AFSL) level, as well as for the client. For advisers, the benefits come in the ability to transact quickly on a client's investment portfolio for changing conditions or opportunities, and the reduced level of documentation required – with the first of these also a potential benefit for clients.

However, for many clients, the added benefit of MDA arrangements is the increased transparency provided. This is not just the ability to have a greater level of understanding of the actual underlying investments (when compared to many managed fund alternatives), but also the physical transparency that exists by the client being the direct beneficial owner of the underlying investments. This may provide clients with certain tax benefits. Whilst not necessarily restricted to direct equities only, it's like the client owning a direct equity portfolio, but with a professional manager over the top.

What are the opportunities

The answer is there are options, although which one is right will differ for not only each adviser, but also for each client.

From an adviser perspective, if you want to provide MDA services to your clients (where essentially you are directly managing the portfolio), then you need to ensure that the AFSL under which you operate is authorised for MDA services. If it's not, then if you are the AFSL owner, you can look to have it varied, but you need to be conscious of the fact this can take some time. If you can't influence this outcome, but as an adviser you see value in MDA services for your clients, then you can explore the option of moving to a different AFS licensee where the appropriate authorisations exist.

However, moving licensees can be extremely time consuming and can cause considerable disruption, not only to your business, but also to your clients. And there are other options.

Consider SMAs

If you aren't licensed or authorised to provide MDA services directly, you could consider exploring the use of separately managed accounts (or SMAs). SMAs are a form of discretionary account, but generally are provided through a registered managed investment scheme (MIS). For the most part, they operate like a managed fund from a client's perspective, but provide the transparency benefits of an MDA structure. Like with a managed fund, as an adviser you aren't making the underlying investment decision, as that is left to the MIS operator and, as a result, there is generally little (or no) individual tailoring of underlying investments available. However, as you (the adviser) are not operating the MDA, your AFSL does not need to contain the authorisation to provide MDA arrangements. To obtain the more tailored approach, you would need to consider individual managed accounts (or IMAs), or the previous limited MDA approach, but this requires the specific AFSL condition.

SMAs can often have a more concentrated investment portfolio when compared to traditional managed funds, but this doesn't mean you need to introduce concentration risk for your clients. Over recent years there has been a significant increase in the suite of SMA offerings available, covering a range of asset classes, meaning you can mix and blend a range of SMAs to suit the needs of your clients. Some AFSLs have also used the increased awareness of MDAs to develop their own core SMA offerings, which largely reflect their in-house view for model portfolio construction.

The quote

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The fact that these different options are available, both in approach to use of MDAs as well as the investment mix available, is a significant benefit to advisers. For those who previously offered MDA services, they may be in a position to continue the same service to their clients. For those who haven't used them, they are worth considering as they can add value to not only your clients, but also to the operation of your business.

If you aren't able to advise on SMAs, it is still possible to follow templates or paper-based models for portfolio construction. Those models may reflect similar views to one or more SMA offerings. However, turnover of the underlying assets remains a concern with this approach given the need to engage with clients for each portfolio change and/or rebalance.

It is always important to come back to some of the basics. MDAs can be simple, or they can be complex. Before offering them to your clients, you need to ensure you are appropriately educated and trained about how they work and how they fit as part of a potential solution for your clients. You need to understand your clients' needs, and whether MDAs can solve that need. You should be comparing MDAs to managed funds and seeing what is in the best interests of your clients.

But the good news is the MDA boat hasn't set sail forever, and could be coming to a berth near you in the future. FS

Our BDM team would be more than happy to assist with your managed accounts needs, call us on 1300 784 207 or visit bt.com.au/managed-accounts

1. ASIC media release, 1 October 2018. https://asic.gov.au/about-asic/news-centre/find-a-media-release/2018-releases/18-292mr-all-managed-discretionary-account-providers-now-required-to-be-licensed/

Watch the video on www.fsitv.com