Tax-aware Portfolio Transitions

Separately Managed Accounts (SMAs) have earned a reputation as the preferred investment vehicle for investors who need tax management, portfolio customization, or both. While pooled vehicles such as mutual funds and ETFs may offer diversification, they are structurally incapable of enabling personalized selection of individual holdings or tailoring the tax experience to the needs of the individual investor.

Yet SMAs have been less widely adopted by advisors than their pooled counterparts, perhaps because of lingering misperceptions about their accessibility and complexity. VAST aims to change this by placing SMA solutions at advisors' fingertips, with all the back-office, administration and custodial "wiring" already built in. And, in an industry first, VAST's Unified Managed Account (UMA) structure allows advisors to combine index-based SMAs, actively managed SMAs, mutual funds, ETFs and individual securities into cohesive multi-asset accounts offering broad personalization and tax-efficient overlay management.

These robust capabilities likely have their broadest application in the tax-aware transitioning of client assets into new target investment strategies. "Tax transition," as it is commonly known, can solve a wide range of advisor challenges in tax-efficient ways that respect each investor's needs and preferences. And VAST can offer these solutions across an advisor's (or even a firm's) entire practice, allowing for holistic client conversations and investment advice.

This paper explores several investment challenges that VAST tax transitions can solve.

Replacing a manager you're no longer using

Investment preferences or objectives change, a favorite portfolio manager retires, an independent money manager is acquired by a larger firm, an asset class no longer meets a client's needs, or a life event dictates a major strategy shift. With pooled investment vehicles like mutual funds and ETFs, replacing one strategy with another typically means selling for cash (perhaps with significant tax consequences) and allocating the remaining funds to the new investment.

Separately Managed Accounts offer another path that is typically more tax-efficient, and a VAST transition analysis can help to illustrate that. SMAs allow clients to enter and leave a strategy in kind because individual securities are held in the client's name. VAST can analyze a client's existing positions to determine which specific tax lots to contribute in kind to the new strategy and which to sell as tax-efficiently as possible. VAST's advanced optimization process can reduce transition tax costs by retaining existing appreciated positions that are similar to model positions, minimizing the number of holdings that need to be sold and potentially allowing clients to achieve desired performance characteristics without incurring unwanted tax costs.

This transition capability can also accommodate client preferences and restrictions by eliminating a company or industry from consideration for the new portfolio.

Transitioning an unmanaged collection of assets to a tax-efficient index portfolio

The passage of time can gradually make an account unrecognizable. What was once a deliberate portfolio can come to resemble a random collection of securities. Clients who doubt they can ever achieve benchmark performance with such an unmanaged collection may feel trapped by the tax bill that would result from selling appreciated positions to invest in a more structured way.

VAST offers a potential solution - a suite of index SMAs that enable personalization, tax management, and tax-efficient in-kind transition of existing assets. As the foundation of a broadly diversified portfolio, these index SMAs can accommodate customization of security selection, tax-efficient handling of life events, and on-going tax-loss harvesting to potentially improve the after-tax performance of a client's entire account. A VAST UMA portfolio can include index SMAs, actively-managed SMAs, ETFs, mutual funds and individual securities, all managed in harmony with one another.

Sharing a VAST transition analysis with a client can help you show how you plan to turn chaos into order in a tax-efficient way.

Find out more about VAST

See for yourself how VAST can change your practice. Contact us for a demonstration of the VAST Advisor Portal. We think you'll agree that VAST offers an effective and efficient approach to tax transitions.

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Vestmark does not provide tax or legal advice. Prospective investors should consult with a tax or legal advisor before making any investment decision.

There are several investment-related risks associated with tax loss harvesting. There is potential that the tax loss harvesting may:(i) negatively affect the overall performance of an investor's portfolio; and (ii) result in a temporary overweight and/or underweight of certain sectors, securities, and/or cash in an investor's portfolio that influences performance, and VAS will not consider any other account that the investor may have. Tax-loss harvesting involves the risks that the new investment could perform worse than the original investment and that transaction costs could offset the tax benefit. VAS may repurchase securities after the end of the tax loss "wash sale" period at a price higher than that for which they were sold. Securities sold for the purpose of tax loss may or may not be repurchased by VAS following the 30-day wash sale period. VAS cannot prevent wash sales that may occur in other accounts besides the account to which the tax loss harvesting was applied. Furthermore, VAS cannot prevent wash sales that may occur due to investor or financial advisor requests that impact trading in the account.

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