

equilibrium

# IFSL Equilibrium Portfolio Funds

Our Reasons



# The Plan

- 1 We have appointed IFSL\* to establish three new investment funds to replace our Cautious, Balanced and Adventurous model portfolios.
- 2 We will transfer investments for clients who currently hold our model portfolios into the new IFSL Equilibrium Portfolio Funds.
- 3 Following this we will review clients with bespoke portfolios to see if these funds can enhance their existing investment strategies.

This is a highly complex and time-consuming exercise at a significant resource and monetary cost to Equilibrium... so why are we doing this?

# Adding Value

We are confident that managing portfolios via a fund will deliver better investment outcomes for our clients.

The benefits are clear and compelling. It is difficult to quantify the exact value the new IFSL funds will add compared to our existing model portfolios, however, ultimately we feel the advantages will comfortably offset the marginal extra cost incurred for clients. This booklet outlines the reasons why we have made this decision and explains the benefits in detail.

If you have any questions about this document or what we are proposing in general, please contact your client manager in the first instance who will be able to direct your query to the most appropriate person.

# Our Service

The financial planning service that you receive from Equilibrium will not change. We are simply managing your investments in a more effective way and this booklet outlines the benefits that the new IFSL funds will provide to our clients.

Equilibrium will not receive any extra revenue or benefit of any kind from IFSL or any other party to the funds.

Equilibrium will meet the legal and regulatory costs of the initial set-up and also pay the trading costs within the funds on an ongoing basis.

\* Investment Fund Services Limited (IFSL) are part of the Marlborough group of companies which includes Marlborough Investment Management (MIM): This is the company we have selected to run the Equilibrium Portfolio funds.

# The Benefits

We have identified the potential benefits that the new funds will provide:



	Flexibility	Cost	Efficiency	Security
Improved market timing	✓		✓	
Access to discounts on the funds we use		✓		
Identical performance for every client in the same fund			✓	
Tax efficiency improvements			✓	
Fund charges are collected from within the fund		✓	✓	
Access to more specialist investment options	✓	✓		
Reduced out of market period on fund switches			✓	
Improved risk control when placing trades				✓
Simpler reporting			✓	
Oversight of our investment process				✓
More efficient management of contributions and withdrawals	✓		✓	

The following pages contain a detailed explanation of each benefit.

We have used the badges below to give an at-a-glance indication of how each benefit improves on our existing model portfolio investment processes.



**Flexibility**

Investment strategies & options that we cannot currently use



**Cost**

Factors that will lead to a cost benefit



**Efficiency**

Taxation enhancements & potential performance improvements



**Security**

Strengthening the oversight or control of our processes

## Improved market timing

- ✓ We cannot trade in real time within our current model portfolios.
- ✓ Trades are generally placed once a day using midday prices.
- ✓ To place a bulk transaction, we have to place the trade before close of business the previous day. The market could move substantially between us placing the trade and that trade being priced.
- ✓ We will have the ability to instruct real time trades within the IFSL funds, significantly improving timescales.
- ✓ This will be useful for *volatility trading* and also for asset allocation changes where speed is a priority, such as selling property funds if we believe those funds could become locked.



### Did you know?

We have over 2,300 model accounts for clients and may sometimes need to trade manually in periods of high market volatility. This trading will be outsourced to Marlborough Investment Management (MIM) resulting in significant time savings for our team.

**Volatility trading:** *this is where we buy equity on a short-term market dip with the aim of selling at a higher market level.*

## Access to discounts on the funds we use

- ✓ Some of the fund groups we use have multiple versions of the same fund at different costs.
- ✓ Fund managers do not generally make their lowest cost funds available to wrap platforms as this would allow anyone using the platform to buy that fund. However, some of the fund managers we use have already agreed to make their lower charge class of funds available to us should we hold them via the IFSL funds.



## Identical performance for every client in the same fund

- ✓ At present, each model client will have a slightly different version of our model portfolio, based on when cash is invested and if withdrawals have been made.
- ✓ Funds can close to new investors meaning longer standing clients may have a different portfolio to newer clients. Defined returns plans can also become fully subscribed and unavailable for new investments.
- ✓ In addition, defined returns cannot be held in investments bonds, meaning that a balanced model will perform differently in an investment bond compared to in a pension, general account or ISA.
- ✓ Investing via the IFSL funds will eliminate these differences.



### Did you know?

We currently run three models for each model portfolio to cope with the above factors; that's nine model portfolios in total.

## Tax efficiency improvements

- ✓ The IFSL funds will act as a tax wrapper around the underlying assets.
- ✓ Gains made from the sale of these holdings are within the IFSL funds and not immediately subject to capital gains tax (CGT).
- ✓ This means that we have more control over when gains are crystallised, rather than gains simply resulting from investment activity.
- ✓ CGT can also be deferred until death, when it would then not apply.
  
- ✓ A further benefit is that fixed interest income within a fund is treated as dividend income, not interest.
- ✓ As such, this income is not taxable as dividends are not taxable if held in a fund.
- ✓ In comparison, the interest received from fixed interest funds held directly would be taxable.

Efficiency

## Fund charges are collected from within the fund

- ✓ At present, the charges you pay are generally funded by cash held in your portfolio. This cash is topped up from income received from the underlying investments, which is taxable.
- ✓ The charges for fund expenses and fund management will be collected within the IFSL funds, thereby reducing the income receivable and consequently the amount which is taxable.
- ✓ As the fund manager, Equilibrium Investment Management will receive an annual management charge (AMC) of 0.25% from within each of the IFSL funds.
- ✓ AMCs are not subject to VAT, which is favourable when compared to paying investment management fees for portfolio management, which are subject to VAT.

Cost

Efficiency

### Did you know?

After the planned dividend tax allowance reduction from £5,000 to £2,000 per annum, more of our clients will need to complete tax returns on the income generated by their investments.

## Access to more specialist investment options

- ✓ In the IFSL funds we could opt to buy assets that are not practical holdings for our model portfolios.
- ✓ This includes investment trusts and exchange traded funds (ETFs) which are often lower cost.

Cost

Flexibility

### Did you know?

Assets such as investment trusts and ETFs can sometimes have limited liquidity which makes trading via platforms difficult. There is also often a cost for buying and selling such holdings through platforms. Platforms must carry out their own due diligence on assets, which can sometimes delay our plans to invest.

## Reduced out-of-market period on fund switches

- ✓ There is currently a small delay on fund switches (typically 2-3 days between a fund being sold and another being bought). This means it is possible that the price we get for the new fund is higher than anticipated.
- ✓ In the IFSL funds we will be able to eliminate the out-of-market period as there is no delay between a buy and a sell.
- ✓ This will also remove the requirement to hold *tactical cash* in portfolios.



### Did you know?

We typically make 15 to 20 switches in a year, resulting in 45 to 60 days where part of a model portfolio is not invested.

**Tactical cash:** this is cash held for the sole purpose of investing quickly into the stock market.

## Improved risk control when placing trades

- ✓ When we make changes to our model portfolios, we implement these changes in every client account where that model portfolio is held. This could result in thousands of transactions, which may sometimes be partially automated through the platforms or placed manually.
- ✓ There is the chance of an error occurring each time we do this, which then needs to be identified and corrected.
- ✓ Equilibrium will not be placing trades within the IFSL funds. These will instead be placed by MIM.
- ✓ There will also be far less trades required, one for each fund, compared to the thousands currently required.
- ✓ These factors will serve to vastly reduce the likelihood of trading errors occurring.



### Did you know?

Our defined returns products are always purchased via manual trading.

## Simpler reporting

- ✓ Currently you will see around 25 holdings on your statement or online account. On a transaction statement you will also see scores of entries for dividends, interest, rebates from fund managers and charges.
- ✓ An investor in one of the IFSL funds will own one fund. That fund will still contain the same 25 holdings within it and we will provide as much detail on those as you like but your statements and any associated tax returns will be much less complicated.



## Oversight of our investment process

- ✓ At present, the Equilibrium Investment Management Committee makes investment decisions and then instructs the changes.
- ✓ These changes are implemented by our investment team and client managers as appropriate.
- ✓ There are no third party checks to ensure that these changes are in line with the objectives of each model portfolio.
- ✓ Once the IFSL funds are established, Equilibrium will be appointed as the fund manager; we will continue to make investment decisions and instruct the changes as before, however Equilibrium will not be responsible for implementing the changes.
- ✓ The instructions will be verified as appropriate by IFSL and then placed by MIM. This will be a significant enhancement to our control processes.



### Did you know?

IFSL oversee funds for a number of our competitors, including: BNP Paribas, Brooks MacDonald and Tilney. Marlborough Fund Managers have been running funds for over 30 years, including the Marlborough Special Situations fund which is currently held within our model portfolios.

## More efficient management of contributions and withdrawals

- ✓ Via the IFSL funds it will be possible to net withdrawals off against contributions and undertake less transactions. This means that assets will remain invested more of the time and less charges will be incurred.
- ✓ As money comes into the funds we can choose where to invest it. For example, if equity markets are falling and money is invested into the fund, we might invest it in equity to top back up to our preferred weighting. If markets look expensive we can hold back the cash to invest on a dip.
- ✓ This process is effectively the same as regular *rebalancing* of the portfolio, but without the inefficiencies of a true rebalance where we are selling one asset class to fund another.



### Did you know?

If one of our clients is buying a fund via the platform and another is selling, these transactions are not currently netted off. This means the client buying could pay an initial charge or bid/offer spread (if there is one). Within the IFSL funds these will be netted off, producing a cost saving. For example, a 1% spread on a £1m defined returns deal would equate to £10,000.

**Rebalancing:** *this is where a portfolio is reset back to the ideal asset allocation. Regular rebalancing has been proven to enhance investment performance over time.*

Please be aware that any investment made into a fund can fall as well as rise and cannot be guaranteed; you may not get back the amount originally invested.

**Head Office**

Brooke Court, Lower Meadow Rd,  
Handforth Dean, Wilmslow,  
Cheshire SK9 3ND

**Chester Office**

19a Telford Court,  
Chester Gates Business Park,  
Chester CH1 6LT

**t** : 0161 486 2250  
**t** : 0808 168 0748  
**e** : [askus@eqllp.co.uk](mailto:askus@eqllp.co.uk)  
**w**: [www.eqllp.co.uk](http://www.eqllp.co.uk)

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