How blended funds can help you and your clients

A guide for consultants and advisers

Standard Life

There's a lot to look forward to

Contents

This information is intended for financial planning professionals, pension trustees, and individuals responsible for making decisions about corporate schemes. It shouldn't be relied on by anyone else.

In this guide, 'we' and 'Standard Life' mean Standard Life Assurance Limited.

Reasons to consider blended funds

Our blended funds proposition gives you and your clients the flexibility to design bespoke default investment options, such as lifestyle profiles, and fund ranges specifically for their members.

- You can provide your clients with bespoke investment options that allow you to influence the investment strategies used
- Reporting is simple – each blended fund has one annual management charge, one unit price and one fund factsheet
- It's a flexible structure. You can change the underlying fund mix without the agreement of individual members
- You can mix and match blended funds with our other investment solutions, such as our lifestyle profiles

We let you and your clients create bespoke investment solutions within our acceptance and governance criteria.

Who can use blended funds

Blended funds are available for the following products:

- Trust Based Pension Plan
- Master Trust
- Group Flexible Retirement Plan
- Group Self Invested Personal Pension

They're also available through the Fund Choices platform.

The roles and regulatory responsibilities in designing blended funds will vary between you and Standard Life depending on the product that they'll be available through.

You can find detailed information on our governance criteria in the 'The solid framework around blended funds' section on page 10.

They're suitable for some schemes, not for others

Blended funds are popular because of their flexible structure. But as they need commitment from you and your clients to monitor the performance and investment selection, we believe they're mainly suitable for larger schemes. We don't believe they're suitable for smaller schemes (usually schemes with less than £10 million of assets under management over three years) or for clients who can't take on an active role in making investment decisions.

And bear in mind that not all funds can be included in blended funds.

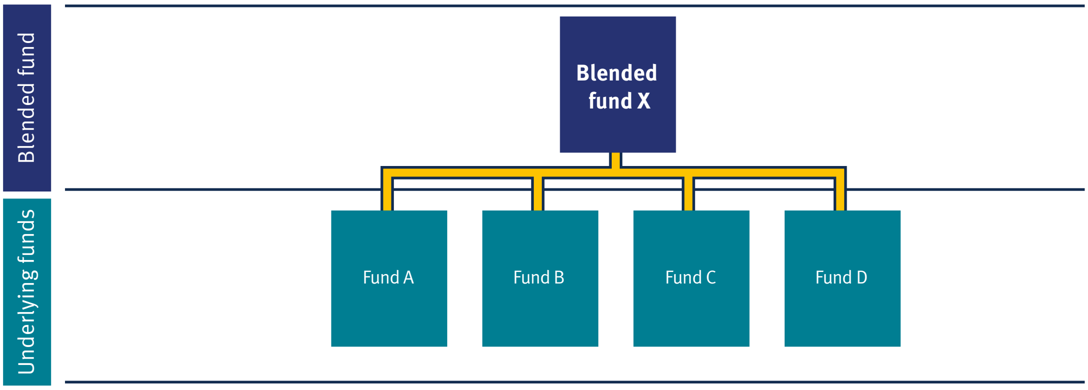
Your usual Standard Life contact can give you more information about suitability criteria.

How blended funds are structured

There are two blended fund structures – one tier and two tier.

One-tier structure

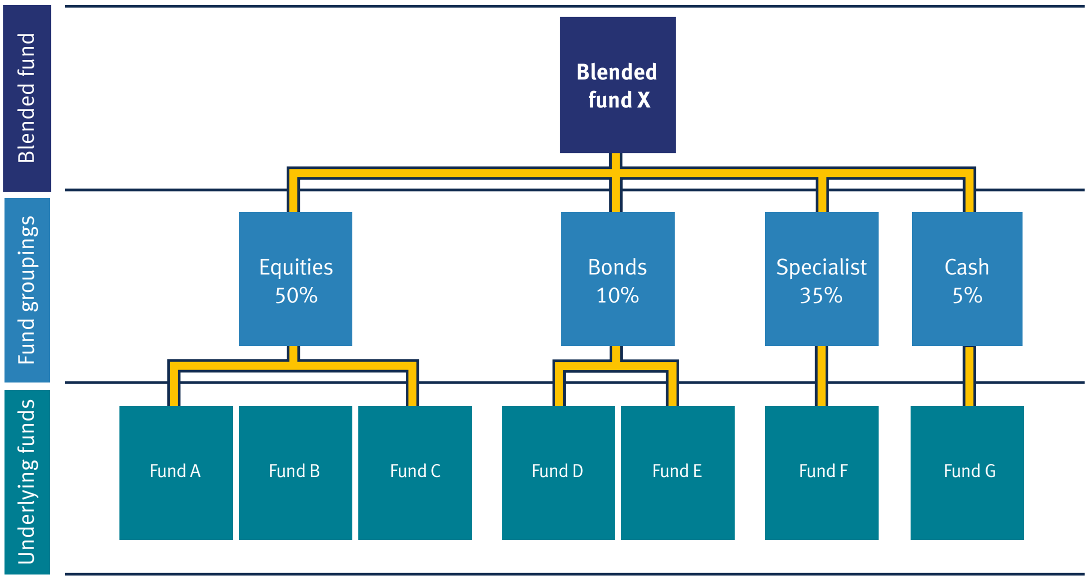
In this structure, there's a single layer of underlying funds. And the blended fund holds units in all the underlying funds. Here's an example:



Two-tier structure

Blended funds with a two-tier structure have an upper tier of chosen asset classes and their weightings. The second tier has the individual funds and their proportions.

As with the one-tier structure, the blended fund holds units in all the underlying funds. Here's an example:



This structure may be more suitable if a client has a specific focus on asset classes rather than on individual underlying funds.

How blended funds are rebalanced

We offer several rebalancing options.

One-tier blended funds

Rebalancing option	Description
Periodic with full rebalance	Rebalancing takes place at a set interval (such as monthly or quarterly) and moves all of the underlying funds back to their original weighting. All the funds are rebalanced even if only one of them has moved outside its tolerance level.
Periodic with partial rebalance	Rebalancing takes place at a set interval (such as monthly or quarterly) and moves all of the underlying funds partially back to their original weighting. All the funds are rebalanced even if only one of them has moved outside its tolerance level.
Auto with full rebalance	Rebalancing takes place on the day any underlying fund moves outside its tolerance level. All the underlying funds are moved back to their original weighting.
Auto with partial rebalance	Rebalancing takes place on the day any underlying fund moves outside its tolerance level. All the underlying funds are partially moved back to their original weighting.

Two-tier blended funds

The rebalancing options are the same but we also offer:

Rebalancing option	Description
Periodic directional rebalance	Depending on the set interval for periodic rebalancing, the system rebalances within each top tier asset class group, in the necessary direction, to bring each group back towards its weighting.
Auto directional rebalance	Rebalancing takes place on the day any of the top tier asset class groups move outside their tolerance levels. The groups are rebalanced in the necessary direction to bring each back towards its weighting.

The finer points

- Tolerance ranges for auto-rebalancing are larger than those for periodic rebalancing
- Tolerance levels don't have to be the same for all funds
- The auto with partial rebalance option may result in frequent rebalancing taking place. This is because the partial rebalance may mean that one or more of the underlying funds are regularly outside the tolerance range. **Your clients should be aware that this could cause frequent trading and so a higher level of implicit dealing costs**
- You and your clients can request ad-hoc rebalances at any time
- You and your clients can ask for an ad-hoc rebalance if a fund hasn't rebalanced for a period of time due to its underlying funds remaining within tolerance ranges

Rebalancing can be a complex area. We discuss the aims and objectives in detail with you before deciding on the most appropriate solution for each client.

Rebalancing examples

1. Periodic with full rebalance

- One-tier blended fund with four underlying funds
- Full rebalance
- Periodic – every quarter
- Fund's tolerance level +/- 3% of target

Fund	Target	Rebalance range	End of 1st quarter	End of 2nd quarter
1	40%	37-43%	42%	45%
2	25%	22-28%	23%	23%
3	15%	12-18%	13%	12%
4	20%	17-23%	22%	20%

In this example, the underlying fund proportions are within the +/- 3% tolerance level at the end of the first quarter. So we don't need to rebalance.

At the end of the second quarter, the fund proportions have moved outside the tolerance level. So we'd do a full rebalance back to the target.

If the client had decided to set the tolerance level to 0% then we'd rebalance at the end of both quarters as the underlying funds have moved away from target.

Our rules supporting periodic with full rebalance are that:

- **we'll rebalance if any of the underlying funds are out of the periodic rebalance range**
- **rebalancing will move all funds back to the target**

2. Auto with partial rebalance

- One-tier blended fund with four underlying funds
- Partial rebalance – 75%
- Automatic
- Fund's tolerance level +/- 8% of target

Fund	Target	Rebalance range	End of day 6	End of day 12	Partial rebalance by 75%
1	60%	52-68%	55%	68%	62%
2	15%	7-23%	23%	10%	14%
3	10%	2-18%	15%	12%	10%
4	15%	7-23%	7%	10%	14%

In this example, the underlying fund proportions are within the +/- 8% tolerance level at the end of day 6. So we don't need to rebalance.

At the end of day 12, the fund proportions have moved outside the tolerance level. So we'd partially rebalance back to the target.

If the client had decided to set the tolerance level to 0% then we'd rebalance at the end of both quarters as the underlying funds have moved away from target.

Our rules supporting auto with partial rebalance are:

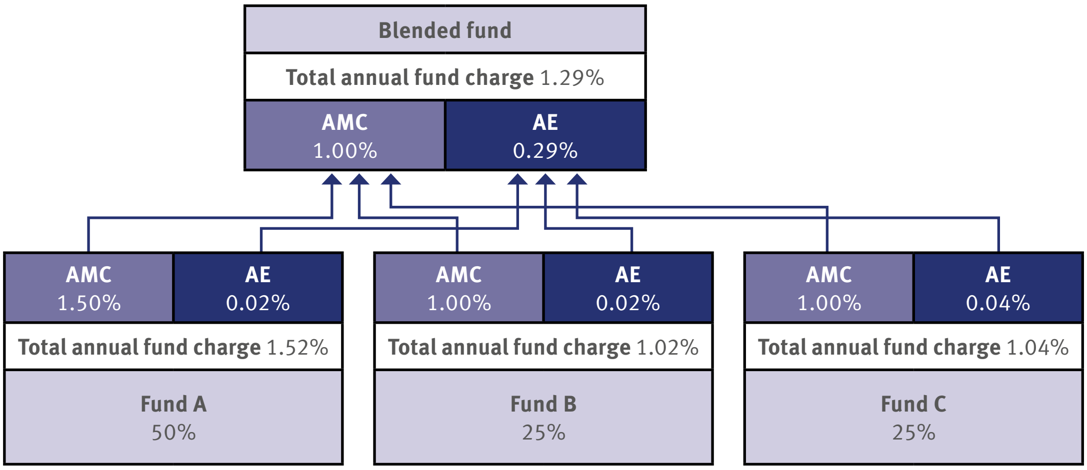
- **we'll rebalance once any of the underlying funds are out of the rebalance range**
- **rebalancing will move all funds partially back to the target**

Blended fund costs

Most blended funds have a fixed annual management charge (AMC) of 1%, but additional expenses (AE) vary in line with the underlying funds. There's likely to be a change in the level of additional expenses if there are any changes to underlying funds within the blended funds or their proportions change.

We calculate additional expenses based on the weighted average of the underlying funds' additional expenses, plus the weighted average of any underlying funds which have an AMC of more than 1%.

The following diagram helps explain this:



The blended fund's total annual fund charge is shown before we apply any scheme-specific discount.

The total annual fund charge includes one change each year to the underlying structure. We may charge for any additional changes requested.

The solid framework around blended funds

All of the blended funds we offer are run within a comprehensive governance framework to give you and your clients reassurance that they're set up, managed and reviewed by the right people and are supported by robust processes.

We can support blended funds within trust-based and contract-based schemes, as well as through investment management agreements (IMAs).

Governance for blended funds within trust-based schemes

Under trust-based arrangements, the trustees are responsible for all investment decisions, including the governance of any blended funds. They may choose to delegate these decisions to you, but we'll still view the instructions as coming from the trustees.

Here's a summary of how it works, and your/your client's involvement and responsibilities

	Process flow	Involvement	Responsibility
1	Set the blended fund's investment objectives	Trustees and Investment Adviser	Trustees
2	Select underlying investments to include in the blended fund	Trustees and Investment Adviser	Trustees
3	Iterative process between Trustees and Investment Adviser to ensure we have a clear understanding of the blended fund operational requirements	Standard Life, Trustees and Investment Adviser	Standard Life
4	Ensure the blended fund complies with relevant FCA rules	Standard Life and Investment Adviser	Standard Life and Investment Adviser
5	Launch the blended fund	Standard Life	Standard Life
6	Annual performance review of blended fund and suitability for scheme members	Standard Life, Trustee and Investment Adviser	Trustee

Other important points

- We action the trustees' instructions, but we reserve the right to veto unsuitable fund names and descriptions
- The trustees must sign a legal agreement documenting their roles and responsibilities in relation to the fund
- An investment operational specification (IOS), which confirms the fund's objective, description, underlying funds, rebalancing arrangements and annual management charge, forms part of the legal agreement. So any changes to the fund mean that a new IOS is needed
- While scheme leavers remain invested in the fund, the trustees have responsibility for them. We consider arrangements for buyout plans individually

Governance for blended funds within contract-based schemes

Under contract-based arrangements, we have full regulatory responsibility for all the investment decisions relating to blended funds, as well as for their management. But you and your clients also have important roles to play.

Here's a summary of how it works, and your/your client's involvement and responsibilities

	Process flow	Involvement	Responsibility
1	Propose blended fund's key objectives and risk profile of target investor	Employer and Investment Adviser	Employer
2	Suggest underlying investments to include in the blended fund	Employer and Investment Adviser	Investment Adviser
3	Set the blended fund mandate based on key objectives and risk profile from step 1	Standard Life	Standard Life
4	Iterative process with Employer and Investment Adviser to ensure blended fund mandate meets their aims	Standard Life, Employer and Investment Adviser	Standard Life
5	Assess suggested underlying investments (from step 2), using in-house research capability, to ensure they're appropriate given the mandate terms and approve for inclusion within the blended fund	Standard Life and Investment Adviser	Standard Life
6	Launch the blended fund	Standard Life	Standard Life
7	Annual performance review of blended fund and suitability for scheme members	Standard Life, Employer and Investment Adviser	Standard Life and Employer

Other important points

- We assess the appropriateness of the employer's suggested underlying funds and the percentage allocations. We also assess future fund switch suggestions
- We set the blended fund's specification (or mandate). This states the fund's description, objective and risk profile, and how the fund will operate, including rebalancing frequency
- The blended fund description highlights that the fund has been designed in conjunction with the employer and their adviser specifically for the scheme members. We'll continue to consult you and your clients on the future composition of blended funds
- We carry out periodic reviews of blended funds and discuss ongoing suitability with you and your clients
- We take into account your and your clients' views when deciding whether to make any changes to underlying funds
- We're responsible for letting scheme members know about any notifiable events that come about because of a change to a blended fund mandate
- We assess each blended fund and its underlying funds to make sure it meets FCA guidance about distributor-influenced funds

Governance for blended funds through IMAs

If you have the necessary resources, operational controls and FCA permissions to make fund management decisions, we may be able to put in place an IMA. You'd then take full regulatory responsibility for investment decisions as detailed within the IMA.

For more information about using an IMA, get in touch with your usual Standard Life contact.

Here's a summary of how it works, and your involvement and responsibilities

	Process flow	Involvement	Responsibility
1	Propose blended fund's key objectives and risk profile of target investor	Authorised Investment Manager	Authorised Investment Manager
2	Suggest underlying investments to include in the blended fund	Authorised Investment Manager	Authorised Investment Manager
3	Set the blended fund mandate based on key objectives and risk profile from step 1	Standard Life	Standard Life
4	Iterative process with Employer and Investment Adviser to ensure blended fund mandate meets their aims	Standard Life and Authorised Investment Manager	Standard Life
5	Assess suggested underlying investments (from step 2), using in-house research capability, to ensure they're appropriate given the mandate terms and approve for inclusion within the blended fund	Standard Life and Authorised Investment Manager	Standard Life
6	Launch the blended fund	Standard Life	Standard Life
7	Annual performance review of blended fund	Standard Life and Authorised Investment Adviser	Authorised Investment Adviser

Other important points

- The IMA defines the investment universe that you can build blended funds from, as well as the roles and responsibilities of you (the investment manager) and us (Standard Life)
- We take full responsibility for making sure blended funds comply with the mandate at all times
- The blended fund description highlights that investment decisions are outsourced to you
- We carry out periodic reviews of all blended funds and discuss ongoing suitability with you
- We're responsible for letting scheme members know about any notifiable events that come about because of a change to a blended fund mandate
- We assess each blended fund and its underlying funds to make sure it meets FCA guidance about distributor-influenced funds

Find out more

If you'd like to find out more about how blended funds can help you and your clients, speak to your usual Standard Life contact.