Fund Expenses

In addition to their regular expense ratio and trading costs, funds may assess sales charges as follows:

- **Front-end load (A-shares)**. You pay front-end loads at the time of purchase. Funds usually impose a fee in the neighborhood of 3% to 6% of the total investment. Sometimes they also charge when shareholders choose to have their capital gains and dividends reinvested in additional shares. You can receive discounts on the commissions of A-shares by using a few different techniques:
    - Breakpoints give you a volume discount on sales charges when making purchases of $25,000, $50,000, $100,000, or more.
    - Letters of intent allow you to tell the fund that you plan to invest enough additional money in the next year to reach a breakpoint. The fund then takes a lower fee for your current smaller purchase, since you agree to invest more in the near future. The fund will grant you the discount, but if you fail to fulfill your letter of intent ("LOI,") they will retroactively charge you the higher fee.
    - Rights of accumulation allow you and your family to effectively view all of your investments in one mutual fund family (not just one of their funds, but any of their funds) as one big investment with regard to breakpoint benefits. Thus, if you put $60,000 into a stock fund and your wife invests $40,000 in a bond fund, you can claim the $100,000 breakpoint in order to get a lower commission. Also, if you invested $20,000 in a fund last year (with a $50,000 breakpoint) and now add $30,000, you should get the discounted charge on the newly invested money, as you have now reached the required breakpoint.
    - Transfers, also known as "switching," allow you to move money between different funds in the same family of funds without having to pay a charge for the trade. Sometimes the company charges a small transaction fee.
- **Contingent deferred sales charge (B-shares)**. Sometimes referred to as a backend load or a redemption fee, mutual fund companies impose this charge on a gradually decreasing scale, and you pay no up-front charge. For example, if you buy shares and then sell them in the first year after the purchase, you would pay 5% of the value of the sale. Sell them in the second year and pay 4%, then 3%, until you get down to 0%. As with the A-shares, you can move between different funds within the family without incurring a sales charge, and without forfeiting accumulated time on the holding pattern. In general, if you liquidate shares and withdraw money, the fund assumes you are selling the oldest shares first, so you end up paying the lowest possible fee. Though many people like the "B-share" structure, it often ends up costing more in fees than A-shares and also does not allow for getting discounts by reaching breakpoints. You can quickly run a cost comparison by using the FINRA Fund Analyzer (look in the "resources" section of www.RichAsAking.com for a link).
- **Level-load (C-shares)**. This class of shares doesn't have a front-end load, but usually charges 1% if you sell within the first twelve months. After that, you would pay no surrender charge. While you hold the fund, you'll pay a "level-load" of 1% per year on top of the fund's other expenses.

Other fees associated with mutual fund investing include:

- **Investment advisory fees**. Covering the fund's overhead, this expense can often range from half a percent to well over 1%.

- **Administrative costs**. This pertains to general operating outlays and fees for related fund services.
- **12b-1 fees**. Named after an SEC rule, 12b-1 fees cover the marketing and distribution fees for the mutual funds.
- **Trading fees**. No mutual fund can tell you how much trading it will do in the future. As such, you cannot find that information in the prospectus. Nonetheless, when transacting on the exchanges, the funds must pay commissions. Though they may only pay pennies per share for their trades, they pass along these costs to the investors, and over time, the numbers become significant. More actively traded funds, for example, might run up 1% to 2% or more in extra costs over the course of a year.

Don't pay tax on someone else's gains

Sometimes, timing can save you money. Most funds make their capital gains and dividend distributions around the end of the calendar year. If you plan to buy into a fund, consider doing so after it has made these distributions. If you buy the fund right before it pays out, you will appear on record as the owner of the fund and have to pay tax on the profits (which may have come into the fund months before you bought your shares). For example, let's say you buy shares in January at $8 each and during the year earnings of $2 come in. At the end of the year, when the stock is selling for $10, you will receive a distribution of $2 and a statement indicating you owe taxes on the $2. After this distribution, the price of the share will be worth $2 less and so the share price will fall to $8 (to take into account the amount deducted from the fund and distributed to shareholders). Now let's consider what would happen if your neighbor bought the shares in December, just two days before the distribution date. He would pay $10 per share.

Two days later, he too would receive a distribution of $2 per share and a statement saying he owes taxes on this $2. In January, his shares would also be worth $8, just as yours are. Now, although he got back $2 on his $10 purchase (in effect he only paid $8) he had to pay taxes on the $2. Had he bought the shares a week later, in January, he would be out-of-pocket the same $8, but would not be liable for taxes on the $2 distribution.

In addition to paying taxes on distributions, you must also pay long- or short-term capital gains taxes when you sell shares at a profit. If the market didn't move in your favor, you can take a loss to offset other profits.

In order to ease your calculating gains and losses, keep statements showing your "cost basis," the price you paid for the shares you bought. If you acquired more shares through a reinvestment program, each new purchase will have its own cost basis. If you inherit shares from a U.S. citizen, the IRS allows you to "step up" the cost basis to the value of the shares on the date of death of the person who bequeathed the stock. So if your Uncle Bob left you shares of a fund that he had bought at $4 each, and if those shares were worth $50 apiece when he died, and if you sold them right away at $50, you wouldn't owe capital gains tax.

Not every shareholder worries about the cost basis of his shares. If you hold mutual funds in tax-deferred investing accounts (e.g., IRAs) you don't pay taxes on distributions or capital gains each year. Instead, you will only have to pay tax when you withdraw money from the account.