



Investment Fees Study

Investors need to pay close attention to the fees charged to them when making any investment. According to the Securities and Exchange Commission, even small differences in fees can translate into large differences in returns over time. Since virtually every investment you make will have fees and costs associated with it, you should fully understand what those fees and costs are before deciding to invest. This report will focus on both the transactional fees, and the ongoing fees, built into various general types of investments. These include a long list of fees that range from the obvious, like a sales commission, to the obtuse 12b-1 fee.

Most investors are familiar with the commissions charged when buying or selling shares of stock. These sales commissions can range from as low as about \$10 per trade at a no-frills discount broker up to about 3% of the principal invested at a full service brokerage firm. Similarly, sales charges on bonds or Certificates of Deposit can range from about 0.5% to 3% of the principal invested in a fixed income security per transaction. Investors often are not aware of these charges on bonds or CDs as they are factored into the net yield of the security, and therefore the security's price paid by the investor. Transactions in options also incur commission charges that range from about 1% to 5% of the principal invested. In all these products, brokerage firms often charge minimum commissions on smaller transactions that can far exceed the percentages described above for normal sized trades. These fees are all one time transaction fees that are charged at the time of purchase or sale of the security. The number of transactions that occur in a portfolio during a period of time can quickly add up to have a very meaningful impact on the performance of that portfolio.

As you move beyond the basic investment vehicles described above, the fees tend to grow with the complexity of the investment vehicle, and the amount of individual attention you receive when making that investment. Investment products like Unit Investment Trusts, that contain fixed portfolios of either stocks or bonds, or other structured fixed portfolios of securities, usually contain total fees and expenses in the area of 5% to 7% of the investment if it is held for at least 2 years. In these cases the bulk of the fee is a one-time placement fee, while the balance is usually on going management and service fees that get deducted from the regular distributions made to investors from the portfolio's earnings. These fees reduce the amount of the investor's principal actually being put to work when the investment is first made, and the ongoing fees reduce the distributions earned from the securities in the portfolio over the life of the investment. The ongoing fees add to the total expenses paid by investors each additional year the investment is held. Most products of this nature are listed on a securities exchange, and their price reflects both the underlying value of the securities held in their portfolio and investor sentiment.

Mutual Funds are the actively managed version of the fixed portfolio products mentioned in the previous paragraph. Since they are actively managed by portfolio managers, the cost of those managers, and the infrastructure they require, is paid for in the form of a variety of fees charged to mutual fund investors. Not only do investors pay similar placement fees and service fees as those contained in fixed portfolio products, mutual funds also charge some or all of the following on going fees paid from the fund's assets; account fees, purchase fees, management fees, distribution/service (12b-1) fees, and the broad category listed as "Other Expenses" by most mutual funds. "Other Expenses" commonly contain items such as; custodial expenses, legal expenses, and other administrative expenses. All these expenses are added up to calculate the fund's Total Annual

Operating Expenses, which is listed as a percentage of the fund's average net assets. This percentage is commonly referred to as a fund's Total Expense Ratio. Obviously, the lower the Total Expense Ratio, the better for investors. Keep in mind that the placement fee (also known as a sales load), and other transaction based fees such as redemption fees or exchange fees must be added to the fund's Total Operating Expense in order to get an accurate picture of the total cost of investing in a particular fund. With average placement fees of about 5%, and an average annual Total Expense Ratio of just under 1%, you can see that mutual funds can be quite expensive. Therefore their performance has to be quite good to overcome the costs they pass on to investors. Generally speaking, these high fees have caused mutual funds to rarely outperform the broad market indices they use as benchmarks. Of course there are occasional exceptions, but investors should carefully examine a fund's past performance before investing. However, as the saying goes, past performance does not guarantee future performance.

In light of most mutual funds' general underperformance, and investor demand for lower fees, the securities industry created No Load Mutual Funds. There now are quite a number of "No Load" mutual funds, although that name is not truly accurate. No Load, really means that the sales load has been eliminated, and some of the other various expenses charged by regular mutual funds have been reduced. The average No Load fund still has a Total Expense Ratio of around 25 basis points (1/4 %), which is significantly lower than the mutual fund average of about 1%. While No Load funds do offer significantly lower fees, once again many of these funds do not outperform their benchmark market index. Therefore individual fund selection is very important to your overall success. As with most mutual funds, No Load funds are generally priced at the end of the day based on the underlying value of the securities in their portfolio.

The success of No Load funds inspired the creation of Exchange Traded Funds or ETFs. This variation allows investors to purchase shares of a portfolio designed to mimic the performance of a certain sector or index. For example, ETFs were created to provide the same performance of market indices like the S&P 500, or the Russell 2000. This allowed investors to simply make one purchase that would provide them with the performance of all the stocks that make up the S&P 500, or the Russell 2000. In addition, the ETF's shares are traded just as any share of stock is traded on major exchanges. The ETF market blossomed rapidly to mimic almost any imaginable market index or sector. In addition, inverse ETFs were created to allow investors to bet against the underlying index or sector. Finally, leveraged versions of many ETFs are now available that allow investors to magnify the results of the underlying portfolio by 2 or 3 times. ETFs also have costs associated with them that do cause their performance to be lower than the underlying index or sector, and leveraged ETFs suffer even more due to the cost of the leverage being added. In general purchasing ETF shares incur commission charges similar to those charged by your broker to purchase common shares on an exchange. In addition to the commission, ETFs have fees that are deducted from the value of the portfolio that cover the operating costs of the ETF. According to the Wall Street Journal, the average expense ratio for an ETF is .44%, which equates to \$4.40 for each \$1000 invested in the ETF annually. These fees vary depending on the nature of the ETF and the issuer of the ETF.

As the pressures to reduce commissions have grown over the years, investors and advisors have moved towards managed accounts that charge a fee based on the assets under management. Management fees tend to vary based on the size of the account being managed, and the types of securities contained in the account. Generally speaking most individual investors will pay from about 50 basis points (1/2 %) to 300 basis points (3%) annually for a managed account.

Very high net worth investors, and many organizations now invest in what are generally known as hedge funds. These are private funds with very limited liquidity that invest in various securities or other assets, and are managed by independent managers. Fees in general on hedge funds range for 1.5% to 3% of the asset value, plus 20% of the profits generated. While it is impossible to generalize

the performance of hedge funds, the investors' expectations are that paying such high fees will result in the manager producing annual returns of 10% to 25%. Of course there is usually a higher degree of risk that accompanies returns of that nature.

Finally, accredited investors have increasingly turned to private placement investments in search of alternative asset classes to diversify their investment holdings. While private placements of equity and debt for small risky early stage companies, and oil and gas drilling partnerships, have been around for many years, private placements are now being offered for large portfolios of real estate, mortgage loans, business development loans, and other alternative assets. Some of the larger private offerings are publicly reporting, but not traded on an exchange. Private placements generally have limited liquidity provisions, and can range from very risky equity to fully secured debt. Placement fees on these types of investments usually range from 5% to 15% of the principal invested, and often times the placement agent earns a percentage of the equity offered, which can dilute the investor's positions. In addition, investors are often charged fees such as; management fees, acquisition fees, divestiture fees, organizational fees, legal fees, administrative fees, etc.

Below is a table that summarizes the information discussed above. As you can see from this data, investors need to be fully aware of the fees they are paying for the entire life of the investment.

Investment	Avg. Transactional Fees	Avg. Ongoing fees	Fee Description
Common Stocks	\$10 to 3% of \$ invested	N/A	Commissions, exchange fees, handling fees
Bonds and CDs	1/2% to 3% of \$ invested	N/A	Commissions, exchange fees, handling fees
Options	1% to 5% of \$ invested	N/A	Commissions, exchange fees, handling fees
Unit Investment Trusts	2% to 4% of \$ invested	1/4% to 1/2% annually	Sales charge, management fees, service fees, creation fee, legal fees, handling fees, admin fees
Mutual Funds	3% to 6% of \$ invested	1/2% to 1% annually	Sales charge, management fees, service fees, record keeping, custody fees, legal fees, admin fees
No Load Mutual Funds	N/A	1/10% to 1/4% annually	Management fees, service fees, record keeping, custody fees, legal fees, admin fees
Exchange Traded Funds	\$10 to 3% of \$ invested	about 4/10%	Commissions, exchange fees, handling fees, custody fees, legal fees, admin fees
Individual Managed Account	\$0 to \$20 per transaction	1/2% to 3% of asset value	Execution fees, management fees
Hedge Funds	N/A	1.5% to 3% of asset value, plus 20% of profits	Management fee plus performance incentive
Private Placements	5% to 15% of \$ invested	unknown, but can be meaningful	Placement fees, management fees, acquisition fees, divestiture fees, organizational fees, legal fees, administrative fees