5 ways to avoid excessive investment fees

by Liz Wolgemuth
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Investment professionals often have different perspectives on how to keep costs low. One thing most will agree on – low-cost investments with poor performance are no bargain.

We asked some local planners to weigh in with their advice.

1. Look at no-load funds.

No-load funds essentially are commission-free mutual funds. Front-end load funds charge an upfront commission that can range between 3 percent and 6.25 percent of the investment. Back-end, or redemption funds, charge a commission at the time the investment is sold.

“I’m an advocate of no-load or low-load funds, because that comes right off the top of your investment,” said Mary Alice Fellers, a fee-only planner and owner of White Oak Financial Planning in Crystal Lake.

If an individual has $10,000 to invest and chooses a front-end load fund that charges a 5 percent commission, the initial investment is really just $9,500.

Liane Warcup, founder of Geneva-based Clarus Financial Planning, a fee-only financial planning firm, said she likes The Vanguard Group’s no-load funds, which number more than 70 and can be bought directly through www.vanguard.com.

John Georgy, a financial adviser with Financial Network Investment Corp. in Crystal Lake, said that higher annual operating expenses can make a no-load fund less profitable than a load-fund over the life of the investment.

“My rule of thumb that I use with my clients is, if you’re planning to be in an investment for less than five years, buy a no-load fund,” Georgy said.

2. Watch out for annual fund operating expenses.

Mutual funds, including no-load funds, may charge fees to cover their annual operating costs, according to the U.S. Securities and Exchange Commission.

Annual management fees are pulled out of the fund’s assets to pay its investment adviser or affiliates, and many funds also carry distribution fees – named “12b-1 fees” after the SEC rule authorizing their function – which cover the cost of marketing the fund, according to the SEC.

A category of annual expenses known as “other expenses” might include fees paid to cover legal expenses, accounting expenses, or general administrative expenses, according the SEC.

Fellers said that an investor simply needs to educate themselves on the details of their fund’s charges.

3. Try a discount brokerage.

“Some of the discount brokerages have just come a long way in reducing some of the fees that drive people crazy,” Warcup said.

FirstTrade, a December 2005 startup, ranked No. 1 in Smart Money magazine’s July 2006 list of discount brokerages.

The brokerage charges a flat $4.95 fee on stock trades, with an extra 65 cents tacked on for option trades, and $14.95 to buy or sell no-load funds. Load funds are charged $14.95 at redemption.

Other discount brokers include Scottrade, OptionsXpress, and TD Ameritrade.

A downside can be that you're pretty much on your own when it comes to investment decisions.

Because brokerages charge per transaction, "it's not cost effective" to be making a high number of trades, Fellers said.

Brokerages also may charge account transfer fees if assets are moved to another firm.

4. Get educated on your 401(k) plan fees.

It can be difficult to get the details on company 401(k) retirement plans, but employees have the right to know, Warcup said.

"There are some very well-managed 401(k)s," Warcup said. "There are also some that are very, very expensive."

It's an important investment product for many people, particularly because more employers are agreeing to match employee contributions in part or in whole, Fellers said.

401(k) plans can charge plan administration fees, investment fees, or individual service fees for employees using additional services, according to the U.S. Department of Labor. Some of the charges are covered by an employer and others are charged either against fund assets or deducted from returns, according to the U.S. Department of Labor.

Employees don't have much control over their plan administrator, but if plans have high expenses, "they should certainly note it to an employer," Warcup said.

5. Beware of 529 fees.

State-sponsored 529 college-savings plans allow investors to save for college through pre-paid tuition plans or general college savings plans.

529 plans vary, with some carrying higher administrative costs, Warcup said.

She recommends using the online comparison tool at www.savingforcollege.com to examine costs.

Annual fees should be around $10 or $20, Warcup said, noting that she has seen some as high as $75.