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## **Memo Concerning Mutual Funds, Managed Accounts and Trusts**

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Attached are two separate charts concerning various mutual funds. The shorter of the two charts was done just about a year ago. This chart sources in a pension plan which offers mutual funds from multiple fund managers. For simplicity, I will refer to this one as the Pension Funds. The longer chart was done this month. For simplicity, I will refer to this one as the American Funds. It also sources in a pension plan but offers investment choices from a single fund manager. Both were done to assist in the analysis and selection of investments for individual USA pension plans offered by two different employers. Thus, the individual mutual funds merely reflect those offered by these two pension plans. They were selected for no other reason. However, the mutual funds listed in these charts are available to investors in general whether or not held in pension plans.

Information in these charts is calculated by the funds. We merely extracted the data from their prospectuses. These are presented as illustrative of a summary of some of the relevant data used by many to choose mutual funds in which to invest.

### **Definitions**

First, following are some terms and their definitions which are used in or inherent in the attached charts and this memo.

*Open end mutual fund* – An open end mutual fund is one which admits new fund owners by issuing additional shares. When an owner wishes to sell, the fund itself buys or redeems the shares. The purchase and redemption price per share are determined by calculating the fair market value of the mutual fund's investments at the end of each day and dividing it by the number of shares outstanding. As a result, the size of the fund is constantly changing typically without limit. Thus, a fund manager who is perceived as successful can attract an ever greater pool of money to invest. This has caused difficulty when a fund becomes too successful and the manager has more money than he or she is able to invest. Sometimes, open end funds suspend the ability of new comers to buy shares. This form of fund organization is the most common. All of the funds in the two attached charts are open end mutual funds.

*Closed end mutual fund* – A closed end fund has a fixed number of shares and a fixed amount of capital to invest. These typically trade on the world's exchanges. If one wishes to buy into the fund, one has to do so from a pre-existing shareholder. These funds sometimes trade at a premium or discount relative to the underlying fair market value of their investments. It is an odd circumstance which many debate as to its cause. This form of fund organization appears to be a bit more popular lately.

*Hedge funds* – Many would suggest these should not be included here. However, they really serve very similar purposes as mutual funds. Hedge funds are typically organized as partnerships or similar legal entities. In their origins, they were simply a vehicle used to pool a relatively small group of investors' funds often with the purpose of facilitating a specific investment manager's services. Typically, the investors were very wealthy folks who could invest relatively large sums of money. In today's world, hedge funds remain subject to less government regulation. They still retain greater flexibility and style of investing by the fund manager. Among other differences relative to mutual funds, hedge funds can borrow money from financial institutions. There have been many failures with these funds as well as some successes. Recently, the minimum investments, in some cases, have been greatly reduced. On the other hand, the mechanisms used to reduce the minimums nearly always increase the fees and sometimes increase risk. Because hedge funds can borrow money, the risks of loss are magnified. In some circumstances, investors in hedge funds can be called upon (required) to make up some of the funds losses. This is not the case with respect to mutual funds.

*Common trust funds* – These were established and used by the larger private banks and trust companies. Smaller individual trusts and accounts were invested in internal pooled funds. They worked very much like mutual funds. Typically, there were a relatively small number of funds within a financial institution focused on specific investment goals. An example would be a common trust fund limited to government bonds. These funds were available only to the clients of the private bank or trust company. Fee structures varied widely. However, there were seldom front or back loads and, in many cases, there were no management fees assessed on the common trust funds other than indirectly through the management fee from the individual accounts or trusts.

*Investment style* – This indicates the stated goal or style of investing espoused by the fund manager for the particular fund. For example, a "value" style of investing typically looks to some measure of underlying asset value relative to the price at which an investment can be purchased. An "income" fund typically focuses on dividends often investing some portion in bonds. A "growth" style typically focuses on some measure of how fast a business is growing such as sales, income, cash flow, etc.

*Commission to purchase* – This is sometimes called a "front load". It is exactly what one would expect – *i.e.*, a percentage charge for the privilege of buying the shares. It is often not charged on reinvested dividends. With respect to a purchase directly from a mutual fund, this commission goes to the fund manager. If one purchases the shares from a broker dealer rather than directly from the fund, the broker dealer may charge an additional commission. In other cases, the fund manager may essentially share their commission with the broker. The attached charts do not reflect a commission to a broker dealer. These commissions or loads are not charged by all mutual funds.

*Deferred sales charge* – This is a technique where the sales charge or commission is reduced (including to zero) based upon the duration one holds the mutual fund. A common time frame is five years. The intent is to encourage investors to own their shares for a longer period of time. There is also an intent to discourage frequent trading in and out of a fund. Deferred sales charges are not charged by all mutual funds.

*Commission to sell* – This is sometimes called a “back load”. Like the commission to purchase, it is typically a percentage charge for the privilege of selling the shares. The same issues apply with respect to those purchases through a broker dealer. These commissions or loads are not charged by all mutual funds.

*Internal costs* – A fund manager charges a mutual fund a periodic management fee. This is typically calculated as a percentage of assets under management and may include certain fixed charges. Some, but not all, funds include a 12(b) charge. A 12(b) charge is an assessment on the fund owners for the costs of the fund manager to market the fund to others. The management fee is somewhat analogous in purpose and calculation to the typical fee charged by private money managers such as the private banking departments of the larger financial institutions.

*Internal commissions* – These are the amounts paid to a broke-dealer to execute the actual trades by the fund. These amounts are not disclosed by the funds. These commissions would be incurred by you the investor if you purchased and sold stocks and bonds outright without the use of a mutual fund. Allegedly, a mutual fund obtains a lower percentage commission because of the volume they inherently promise the executing broker dealer.

*Portfolio turnover* – This calculation indicates the average holding period of each investment or how frequently a fund trades its securities. For example, 100% indicates that, on average, a fund buys and sells each investment within one year. 200% indicates the fund buys and sells each investment twice each year. And, finally, 50% indicates an average holding period of two years. All other things being equal, less frequent trading results in lower transaction costs. For USA income tax purposes, the net realized gains, but not net losses, of an open end mutual fund are taxed to its owners. In order for there to be a taxable gain within an open end fund, the fund must actually sell an investment. Thus, a lower rate of turnover of the fund’s investments is typically more tax efficient for people subjected to the USA tax regime.

*Pretax rates of return* – This measures the average annual total return (interest, dividends and realized and unrealized gains within an open end mutual fund net of internal expenses and commissions charged by the fund manager but not by a broker dealer, if any). It does not consider any income taxes which the fund’s owners may have to pay by reason of the fund’s activity. Typically, where this statistic is not available, it indicates the fund did not exist for all or a portion of the indicated time period. As mutual funds are required to disclose, “past performance is no indication of future performance”. This is especially true where the fund manager today differs from the prior fund manager. However, theory and disclosure requirements aside, it is really one of the few available indicators of a mutual fund’s performance. *E.g.*, mutual funds are not required and, in fact, are loathe to disclose their current underlying investments. These disclosures are, in fact, done but with a sufficient lag in time that often the fund no longer holds the stocks and bonds shown in the currently available listing.

## Purpose of Mutual Funds

Mutual funds really serve two basic purposes, at least in theory:

- First, they are intended to provide professional and expert management of smaller investor's savings.
- Second, they allow efficiencies of scale especially with respect to diversification of smaller investors' holdings.

In other words, they act very much like the private banks for their customers. Mutual funds, however, are intended to provide this expertise "to the masses" which could not afford the greats like the old 1<sup>st</sup> National Bank of Boston trust department and more than a few others.

Many mutual funds were and remain faithful to this goal or structure.

With the advent of private pension schemes in the USA tax law, mutual funds blossomed. They have indeed become the foundation of the USA private pension schemes such as Individual Retirement Plans, 401(k) Plans, Keogh Plans, Simplified Employee Plans, and so on. More recently, USA tax policy has established similar schemes for education and health care costs. There are now literally thousands of mutual funds and fund managers.

As these funds have multiplied and their complexity expanded, there has evolved a group of financial advisors whose sole purpose is to assist people in selecting a mutual fund. I must conclude that, in theory, these advisors serve a much needed service. I think the attached spread sheets are ample evidence. *E.g.*, an investor has 144 choices if their universe is limited to 12 mutual funds within the American Fund Family.<sup>1</sup>

It also seems that as mutual funds became more prevalent, the private banks and trust companies ceded a larger share of their traditional market to the mutual funds. Indeed they became some of the financial advisors assisting their clients in selecting mutual funds.

Twenty-five to thirty years ago, there was an old "rule of thumb" as to how much principal it took to justify use of a trust as a solution to a particular problem. That amount was about \$225,000. If one inflates this over a 10 year period assuming 5% inflation, it becomes about \$365,000; over 20 years it becomes about \$600,000; and over 30 years it becomes about \$975,000. Today, I now hear minimums in the neighbourhood of \$3 million in order for the private bank or trust company to accept an account and manage the account without the use of mutual funds.

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<sup>1</sup> Admittedly, 36 are limited to certain USA education schemes and 36 are limited to employer sponsored pension plans but, nonetheless, one must at least sort through and eliminate 72 options which do not apply and then evaluate the 36 which remain.

## Disadvantages of Mutual Funds

Mutual funds are now actually trumpeted by the financial advisors as the means of buying the expertise of the best money managers.

So what are the disadvantages of using mutual funds?

### *Personalized Management*

In theory, there should be only one disadvantage to mutual funds. That is, mutual funds, by the very nature of pooling many investors' funds for common investment, lack the ability to serve the individual investor's unique circumstance. For example, mutual funds do not permit the timing of the realization of gains and losses to mesh with an individual's other circumstances. Indeed, with their now current focus on USA retirement and other plans, this tax efficiency has receded even further.<sup>2</sup>

### *Fees and Management or Advisory Structures*

Another real "difference" with mutual funds relative to the past is the pyramiding of fees and duplication of efforts. Privately managed funds like the old trust departments typically involved the following costs:

- There were commissions associated with the purchase and sale of the underlying investments – brokerage commissions. While not always but often these commissions were not charged directly or indirectly by the trustee or an affiliate of the trustee. Thus, there generally was no conflict of interest or self dealing between the manager and the broker which would encourage frequent trading of stocks and bonds.
- There was a management fee charged by the trustee. This was typically a small percentage of assets under management and income collected.

This generally remains the case with respect to the private banks and trust companies. Although, many of the private banks are now a part of groups which include broker-dealers.

When one invests in mutual funds, there are also certain fees and commissions involved:

- There are commissions associated with the purchase and sale of the underlying investments within the mutual fund – again, brokerage commissions. It is not uncommon to find direct or indirect relationships between the broker and the mutual fund managers. Hence, there is more frequently a conflict of interest and

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<sup>2</sup> USA pension and other tax driven savings schemes have distorted much of the result – tax and economic – over the years. *E.g.*, the USA taxes certain capital gains and dividends at much lower rates of tax when owned by an individual than other sources of income. However, these same dividends and capital gains realized within the confines of a USA pension ultimately generate personal income tax at the highest rates when the funds are withdrawn from the plan.

self dealing between the fund manager and the broker executing the actual trading.

- With respect to some, but not all, mutual funds, there is a commission to either buy the fund's shares or sell them or both. In some cases, there is a broker-dealer commission to buy and sell the mutual fund shares.
- There is a management fee charged by the fund manager. This is also typically a small percentage of assets under management.

The problem for the investor arises when the traditional private bank or trust department structure is piled on top of the mutual fund structure. Assuming there are no loads in the mutual fund, it doubles the fees. If the mutual fund has loads, the fee structure is more than doubled.

The question is whether there is double the service or value brought to the investor. I think the answer has to be no. Assuming everyone is performing their job, the mutual fund manager is the "brains and talent" that is applied on a daily basis. They are the ones who do the large amount of necessary research and monitoring of the individual companies or other investments. As such, one would expect them to receive the bulk of the fees in the traditional form of a small percentage of assets under management.

Those who assist the investor in selecting the appropriate mutual fund for their purposes do provide a valuable service. However, it is a "one time" or "infrequent" service. Once the mutual fund is selected there really is little more that **should** be needed. Perhaps, once a year or every couple of years, the overall selection should be reviewed but this does not warrant a duplication of the fee structure intended to compensate for daily investment management in the form of a percentage of assets under management. If this is necessary, there is something seriously wrong with the mutual fund managers.

#### *A New Group of Financial Advisors*

There is a developing group of financial advisors who do not charge commissions or a percentage of assets under management. Rather, they charge an hourly rate for their services when needed. It strikes me, at least in theory, that this structure is the one which is appropriate when the underlying investments consist of mutual funds.

#### *The Trust Function*

What is getting lost in this process with the rise of mutual funds over the prior traditional private bank trust function is the availability of true "trust" services. These services go beyond the mere management of wealth. They include such things as administering the restrictions on generational transfers of wealth to younger people or even heirs with some limiting factor such as a minor child or a child with limited abilities. This circumstance also limits the ability to implement certain estate and gift tax reduction strategies and asset protection strategies. In other cases, trust are used to provide for personal financial management in the case of temporary or longer-term incapacity due to age or illness. Mutual funds simply cannot provide these services.

Another key service provided through the old private trust function was the ability of a trust to hold and administer “special assets”. Special assets might include a home, art work or interests in closely held businesses. Mutual funds cannot do this.

As a result, people of modest means are simply foreclosed from using these tools. People of middle income or even upper-middle income categories end up paying the duplicate fees.

### **Other Problems, Issues and Abuses**

#### *Fees and Commissions Relative to Tasks and Responsibility*

I believe in fair and just compensation. However, there appears to be an evolving sense of greed and excessive view of personal worth on the part of managers and advisors. To illustrate, I will pick on one – my selection is somewhat arbitrary. The second item in the Pension Analysis is PIMCO Long Term Government Fund. This fund invests in USA government bonds with maturities of at least 8 years. In order to invest in this fund one must pay the fund manager a 3.75% commission to buy shares in the fund. Annually, there is a management fee of .91% of assets under management. To sell the fund shares there is a 2% commission. I have ignored for this purpose the deferred sales charge. The sum of these is 6.66%. Currently, USA government bonds with a 10 year maturity yield just over 5%. One also has to wonder why the portfolio turns over 3 to 10 times each year. Indeed, the one year total return was a negative 1.35%. I am not clear as to just how they were able to achieve the reported 6.17% average 5 year rate of return and 7.79% average over 10 years. In any event, regardless of performance, fees and commissions of 4.66% in year one, 2.91% in the year of sale and .91% annually to invest in USA government bonds is excessive.

Should one wish to purchase a USA government bond portfolio, there is no commission from a traditional brokerage<sup>3</sup> or one can buy them for nothing from the USA Federal Reserve Bank in a notional account. There are minimum amounts but they are not large.

With respect to PIMCO in particular, there has to be a reason for the outsized total return in the 5 and 10 year reporting periods. One simply does not make a consistently out sized gain or loss relative to the averages in government bonds without some “fancy foot work”. I confess I did not dig deep enough in this case to find it. However, what becomes clear in a circumstance like this is the manager is doing something outside of the typical which, of necessity, increases the risk of loss. When one buys a USA government bond, one is specifically intending to lower their risk of loss to near zero.

#### *Turnover*

Turnover is critical with respect to costs. The more one buys and sells, the greater the commissions. It also takes more effort as one must re-invest the proceeds. And, it costs

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<sup>3</sup> USA government bonds can be purchased from a traditional broker-dealer for a flat nominal fee plus nominal transfer taxes in the USA.

tax money to the investor in countries that tax such gains – the USA, of course, being one which does.

The tax cost can be significant. For example, let's assume the fund buys ABC Inc. for \$80. Six months later it sells it for \$100 resulting in a \$20 gain. Let's further assume that gain goes to USA investors. They will pay up to \$7 in USA Federal income taxes. In order for the investor to recover the \$7 of income taxes, the fund will need to make another 7% on the reinvestment of the \$100 of sales proceeds.<sup>4</sup>

### *Reported rates of return*

This brings us to the reported rates of return. These are calculated according to complex rules (assumptions) dictated by the various regulatory authorities. Of necessity:

- They do not account for the precise time which one buys into the fund or sells one's interest.
- They do not account for relative risk.
- They do not always account for all commissions or the impact of front and back loads based upon an investor's actual period or duration of ownership.
- They do not account for an investor's actual global income tax burden which can differ greatly.<sup>5</sup>

In my personal experience, I have come close to matching the reported rates of return only after holding a specific mutual fund for many years.<sup>6</sup>

One must also "bench mark" the reported rates of return. For example, if the overall averages are up by 30% and a fund manager is up by 20%, one might not be too satisfied. On the other hand, if the overall markets have declined by 10% and the fund manager is down 2%, one probably should be most satisfied. In other words, viewing a fund manager's rate of return in a vacuum does not get to the right answer.

### *Risk*

This brings us to risk of loss and risk of gain. Most people think of losses when they think of risk. However, risk is a double edged sword.

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<sup>4</sup> This example does not include the impact of commissions on the purchases and sales. Also, in reality from the investor's point of view, the investor will need to make about 7.5% to fully recover the income taxes paid. As will be seen below, using long historic statistically average rates of return, this could take a year to recover.

<sup>5</sup> Mutual funds sold in the USA are now required to show hypothetical after tax rates of return assuming USA rules and residency of the hypothetical investor.

<sup>6</sup> The circumstance where I owned mutual funds for many years was in my former employer's pension plan and then of necessity as the plan provided no other choice. Today, I own one closed end fund which is not a material part of my net worth.



Many argue that the interest rate on USA government bonds is close to the “risk free rate of return”. What they really mean is there is near zero risk of loss and near zero risk of gain. One is not going to get more or less back than the principal committed to the investment in a USA government bond. Thus, the interest paid on USA government bonds compensates the investor for only the market’s view of expected future inflation and the time value of the use of money. While one might rationally query these assumptions today, this is often the “bench mark” for evaluating through comparison the relative required rates of return necessary to assume greater risk of both gain and loss.

In evaluating any investment including mutual funds, one must evaluate these risks of gain and loss. They must be balanced and balanced differently for different circumstances.

The 80 year old retired person can afford little risk of loss. Should something adverse happen in the economy or their particular investment, they have no realistic amount of time to make up that loss. This is the primary reason that our portfolios should become more conservative as we get older.

On the other hand, a 25 year old person could be rendered a pauper by retirement if they invested only in USA government bonds just because of inflation. A 25 year old person also has the time to make up or recuperate from a loss.

Likewise, an 80 year old very wealthy person might be well advised to adopt some of the risk profile of their grandchildren if their goal is to leave a substantial bequest. They would be well advised in this regard only after they had established a sufficient conservative portfolio to provide for their life time needs.

Mutual funds provide both opportunities and pitfalls with respect to risk management.

One cannot see the current portfolio of a mutual fund. Indeed, the very purpose is to delegate some of this responsibility to the fund manager. Where one can subjectively evaluate this with respect to a mutual fund is in the “investment style” (column 2 on the charts) and “investments” (column 3 on the charts).

In the past, the fund’s very name often alluded to this issue. Mutual funds must also define their style and the investments they are “allowed” to hold. These definitions are self described by the fund. One of my criticisms of mutual funds today is these very disclosures. They have become obtuse sometimes bordering on the bizarre. I site the American Funds as classic. The very name suggests they are focused on investments located in the USA. Of the 12 funds in the attached charts, the word “American” is incorporated in 7 of the funds’ names and “Washington” in 1 of the funds’ names. At least 10 of these 12 funds can, however, invest in securities located outside of the USA. In fact, several invest in government bonds issued by countries other than the USA. While I personally advocate a global view of investing for the very purpose of risk management, there are others with differing views or needs. Regardless, the very names on these funds are misleading.

On a broader scale and certainly not limited to the American Funds, the descriptions of and actual fund investment strategies or goals have become far too many, too vague,

too confining and not confining enough – and that is not a contradiction on my part in my description. In short, they are difficult to fairly evaluate.

To overcome this, one must read very carefully. In addition to the verbal descriptions, mutual funds are required with considerable time lag to list their actual underlying investments. These also should be read to get a sense of whether the words in the investment style appear to fairly describe historic reality. Having written this, however, I wonder just how many investors actively seeking expert investment advice and management would be able and willing to spend the time to draw fair conclusions.

### *Diversification*

Diversification is one of the key tools to managing risk both of gain and loss. Simply put, if one places their entire investable money in the stock of one company, one will lose everything should that company fail. On the other side, if that one company is wildly successful, the investor will also succeed to the same degree. The classic fault of many individual investors is to put a disproportionate amount of their investable money in a single company or industry or category of asset. For example, during the “dot com” (or now “dot bomb”) era, fortunes were made literally overnight. Those same fortunes were also lost overnight. Few, in the end, were smart enough or clairvoyant enough to sell and hold cash. Those who were diversified over several industries never made as much wealth but did not lose it either.

Mutual funds by their nature provide the investor with diversification. Each fund invests in many individual companies. Oddly enough, a common error by investors in mutual funds is to be too diversified. This occurs when they own interests in too many mutual funds.

Excess diversification statistically removes the ability to succeed beyond the norm. *I.e.*, one essentially holds an index or average portfolio that will do no better or worse than the market averages. It carries a “perfect” market risk. Again, I return to the 80 year old example. Had that hypothetical investor had 100% invested in stock based mutual funds (as well as directly in stocks) during 2001, plus or minus, they probably would have been seriously and permanently harmed when the global equities markets, not just the dot bombs, declined significantly and for an extended period of time. The error would have been two fold – too much diversification in equities and none with respect to bonds.

As with most things in life, the primary key with management of the risks of gains and losses is proper balance.

### *History as a Guide to Future Performance*

Mutual funds sold in the USA are required to repeatedly state in their information that “history is no guide to future performance” or variations on that theme. Factually, this statement is correct. If one compares the top performing mutual funds from year to year, it is unusual to see the same funds repeatedly in that top listing year after year.

As a pragmatic matter, however, there is little else to review to evaluate whether any given fund is actually likely to meet its stated goals in the future. The same is true with respect to individual companies. One starts with history and then attempts to

extrapolate into the future giving credence to current events and known or anticipated differences.

There is a key historical factor to check with respect to each and every mutual fund. Is the current fund manager the same individual or team who generated the prior track record reported in the mutual fund's prospectus?

### *Expectations*

Expectations are critical. Many people have outsized expectations. In relatively recent times, we have experienced a period of unusually large financial gains. Americans in particular have come to expect 15% to 30% gains as a norm in the appreciation of real estate and equities.

Some of these expectations are founded in factual experience. One can see it in the reported historical gains on the attached charts. Certainly, many American's homes have appreciated greatly over the past 10 years.<sup>7</sup>

Historically, stocks or equity based investments experience a total return of 7.5% annually; some say up to 10%. Total return includes dividends and capital appreciation. Bonds tend to return 2% to 3% above expected inflation rates within the issuing currency.

The studies which generated these "norms" are of the USA markets over a period of at least 100 years. There are some studies being done over longer periods oddly enough focused in Holland.<sup>8</sup> These studies generally support the studies based in the USA.

Thus, the key is not to get "greedy" in our expectations. Greedy expectations lead to taking outsized risks of loss at any age. More importantly, they lead to taking risks which have not been acknowledged or evaluated.

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<sup>7</sup> Many fail to recognize that our homes are not Investments. *E.g.*, my house can appreciate 100% but when I sell it, I have to replace the function of a "roof over my head". The replacement is not likely to be less costly than the one I sold especially if I intend to remain in the same general location with the same general size and shape of accommodation. My house also does not generate income in the form of interest or dividends. On the contrary, it costs me money to maintain it, heat it and pay taxes.

<sup>8</sup> Holland apparently is one of the few places with sufficient records to actually do the research.

This holds true with respect to mutual fund managers or the selection of individual investments where we choose to manage our own investing. We need to make a thoughtful selection of a manager and then give them the time and space to do their job. This is best illustrated by a little mathematics. Following is the result of a USA person's purchase and sale of a specific security:

Initial investment	\$ 1,000
Less: Commissions and costs assumed to be 1.5% to buy the investment and again to sell the investment	<u>30</u>
Net amount invested	<u>\$ 970</u>

In order to break even, the investor must make 3.1% (not 3.0%) on the investment (\$30 divided by \$970). If one assumes that an average annual rate of return is 7.5%, it will be at least five months before an investor's total rate of return is **zero**.

Where this is a mutual fund with a front and back load and an average turnover of 1 year or 100%, the following occurs:

Initial investment	\$ 1,000
Less: Commissions and costs assumed to be 1.5% to buy the underlying investment and again to sell the underlying investment plus a 3.75% front load, a 2% back load and a .91% internal management fee, all totalling 9.66%	<u>97</u>
Net amount invested	<u>\$ 903</u>

In order to break even, the investor must make about 10.7% on the investment to have a total return of **zero**. Using historical rates of return on equities, it would take about 1 year and 5 months to break even.

Income tax, if any, has not been considered in either of the above examples.

This is not to suggest that mutual funds are inherently evil. Rather, there is a cost to acquire the expertise of the fund manager.

This is an interesting concept to consider with the turnover in mutual funds. But the point is criticizing a money manager for not making me "a ton of money" within even a year is really quite unfair to the manager.

### *The Recent Scandals*

Recently, there have been a litany of scandals in the financial services industry including, but not limited to, mutual funds. Some include inappropriate kick backs from broker-dealers, mammoth conflicts of interest with respect to research and recommendations, after hours trading, commissions and so on.

There is always risk of this type of activity. However, the advent of mutual funds and the demise of the traditional trust department function have created layers of management. This seems to have fractured responsibility as well as eliminated services which require a special sense of responsibility to the client. Thus, common sense suggests there is greater opportunity for failure. There is also the loss of the person who has to made a mistake to actually personally face the person harmed.

For most, the only solution to this is some special personal vigilance.

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