

10 Shops With the Biggest Spikes (and Dips) in 12b-1 Kitties

By Emily Laermer, Ignites, August 29, 2018 [subscription required]

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Investors paid \$12.3 billion in mutual fund distribution fees during 2017, or 3% more than in the year prior, according to an *Ignites* analysis of data from Morningstar Direct.

Yet the growth in assets within active funds was much greater: 15% between December 2016 and 2017, separate data from Morningstar Direct shows. That discrepancy suggests that market appreciation gets the credit for the increase in fees collected, says Dennis Bowden, head of U.S. mutual fund research at Strategic Insight.

“We continue to see the proportion of active fund assets held in 12b-1 share classes decline,” he says.

In fact, during the 12-month period ending July 31, the average active share class with a distribution fee bled by \$23.9 million. The typical share class without one, meanwhile, attracted \$17.4 million.

Nearly all of the distribution fees collected — \$12 billion of the total — came from active mutual funds.

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The SEC **sanctioned** so-called “clean shares” in a January 2017 **letter** to Capital Group, the parent company of American Funds. With that letter, the regulator green-lighted the practice of allowing brokers to set the sales charges on share classes that don’t have 12b-1 fees or sales loads. American Funds has since **rolled out** the F3 share class, which are no-load funds also stripped of 12b-1 fees and sub-transfer agency fees.

American Funds had \$828.4 billion in A shares and \$51.6 billion in C shares at the end of last year, separate data from Morningstar shows. Those share class types tend to have embedded distribution fees.

“We expect the industry to shift to this over time and we have share classes available today that support this [clean-share-like] model,” the company spokeswoman writes.

Some companies are getting rid of embedded distribution charges altogether.

“It’s a dinosaur business,” says John Rekenthaler, vice president of research at Morningstar. “You don’t see too many firms adding 12b-1 fees.”

For example, State Farm last April began waiving 12b-1 and distribution fees for all mutual fund share classes, according to a company spokeswoman.

And 30% of the 687 share classes that launched during the first seven months of 2018 are triple-zero clean shares that only charge management fees and operating expenses, according to a separate *Ignites* analysis. Another 40% have sub-TA fees, but no 12b-1 fees or other loads.

“Investors are waking up to fees,” says Niels Holch, executive director of the Coalition of Mutual Fund Investors.

Assets in 12b-1-fee-laden funds have been on the decline for years. In fact, at the end of 2017, a quarter of active mutual fund assets were in share classes with 12b-1 fees, down from 36% at the end of 2011, according to data from Strategic Insight’s Simfund service.

“I expect there to be little to no 12b-1 share classes used within fee-based platforms over the next few years,” says Strategic Insight’s Bowden.