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More Fund Shops Rethinking Redemption Fees

Article published on Apr 22, 2008

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First Eagle Funds has joined a rapidly growing list of fund providers that are eliminating redemption fees.

The \$33.3 billion firm will drop the 2% redemption fees on its U.S. Value and Fund of America products, according to a recent regulatory filing. It also is cutting the requisite holding period on its Global Fund, the Global Overseas Fund and the Gold Fund from 90 to 60 days.

First Eagle Funds' move, which comes six months after the final phase of the SEC's so-called redemption fee rule took effect, may signify a broader trend. In fact, since Rule 22c-2 first passed and last July, the number of U.S. mutual funds that impose redemption fees dropped from 70% to 62%, according to research from the **Coalition of Mutual Fund Investors**, a shareholder advocacy group in Washington D.C.

"In general, people feel like it's overkill," says Maureen Quill, executive vice president of investor services at **UMB Fund Services**. First adopted by the SEC in March 2005, Rule 22c-2 aims to thwart market timers, whose frequent trading harms long-term shareholders by diluting share prices and increasing trading costs.

To comply, fund companies and their intermediaries and recordkeepers underwent a legally arduous — and costly — process of negotiating information-sharing agreements by which funds could request trading data about individual shareholders. That data was meant to help funds determine whether shareholders were adhering to the funds' policies.

At the same time, fund boards were required to vote on whether to hit investors who move in and out of a fund quickly with a so-called redemption fee as high as 2%.

"People are probably more comfortable saying I don't know if we need these fees if we have 22c-2 [to identify market timers] and get at it that way," Quill says.

First Eagle Funds declined to comment on the decision to change its funds' policies, but it is not the first to alter its redemption fee stance in recent months. In November, **Forward Funds** eliminated the fees on its 14-fund lineup, while in October, **Oakmark Funds** removed the 2% redemption fee on its Equity and Income Fund.

Larger shops, too, have altered their policies. Like First Eagle Funds, **Pimco** last July reduced holding periods or eliminated these fees family-wide. In 2007, **State Street Global Advisors** did away with the fees on international and high-yield funds — those most prone to market timers.

In 2006, **Fidelity** eliminated redemption fees on the Hastings Street series, which included six large-cap domestic equity funds. About one-third of Fidelity's 430-plus funds use redemption fees, says spokeswoman Sophie Launay. Since 1989, Fidelity fund boards typically apply fees to those funds most likely to experience "shareholder churn," or those with higher-than-average trading costs, she says.

While 22c-2 has been on the books for several years, fund companies have had only six months to test how effective a tool it might be in nabbing market timers. "What we understand is that the majority of fund families that have redemption fees are questioning the need," says John Gray, a spokesman with **Envision Financial Services**. "Folks are saying market timing is not as big a problem as it was three or four years ago, and part of that is that 22c-2 is showing that short-term trading is not as rampant as perceived," he says.

Not everyone is as convinced, though. Niels Holch, executive director of the Coalition of Mutual Fund Investors, says that the rule really doesn't allow companies to effectively act, because when and if companies request data, it's usually long after market timing has taken place. Daily reporting would provide a more meaningful protection to long-term investors, he says.

Whatever way funds choose to monitor market timing, they must first consider the distribution channel, says Nick Prokos, managing director with **ACA Compliance**. Funds need to understand first how their intermediaries track their data and in what form reports will be delivered, he says. Fund boards may decide to scrap fees if getting reliable and timely information from third party administrators becomes too onerous, making it difficult to ensure the rules are equitably enforced, he says.

Alternately, funds may decide that the portfolio-turnover rate and liquidity of the assets mean that frequent redemptions have little effect on the overall expenses of the fund.

Still, even in rocky markets and in uncertain times when skittish shareholders may want to know they can access their funds at any time, most funds have a vested interest in keeping investors invested, he says.

"Most mutual funds are meant for long-term investing," Prokos says. "An investor who subscribes into a fund and later pulls out within 90 days of investing is not an investor that most fund companies want."

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