CHAPTER 6

US Fund Expenses and Fees

Mutual funds provide investors with many investment-related services, and for those services, investors incur two primary types of expenses and fees: ongoing expenses and sales loads. Average expense ratios (i.e., ongoing expenses) paid by US mutual fund investors have fallen substantially over time. For example, on an asset-weighted basis, average expense ratios for equity mutual funds fell from 0.99 percent in 2000 to 0.40 percent in 2024, a 60 percent decline. Mutual fund share classes with sales loads are far less commonly sold today than they were a few decades ago. In 2024, the vast majority of gross sales to long-term mutual funds went to share classes that charge neither a sales load nor a 12b-1 fee.

IN THIS CHAPTER

Trends in Mutual Fund Expenses

Mutual fund investors incur two primary types of expenses and fees: ongoing expenses and sales loads. Ongoing expenses cover portfolio management, fund administration, daily fund accounting and pricing, shareholder services (such as call centers and websites), distribution charges (known as 12b-1 fees), and other operating costs. These expenses are included in a fund's expense ratio—the fund's annual expenses expressed as a percentage of its assets. Because expenses are paid from fund assets, investors pay these expenses indirectly. Sales loads are paid at the time of share purchase (front-end loads), when shares are redeemed (back-end loads), or over time (level loads). Mutual fund share classes with a sales load are far less commonly sold today than they were a few decades ago as investors have gravitated toward funds without them (see page 86).

On an asset-weighted basis, average expense ratios* incurred by mutual fund investors have fallen substantially (Figure 6.1). In 2000, equity mutual fund investors incurred expense ratios of 0.99 percent, on average, or 99 cents for every $100 invested. By 2024, that average had fallen to 0.40 percent, a 60 percent decline. Hybrid and bond mutual fund expense ratios have also declined over this period, by 35 percent and 50 percent, respectively.

Like the prices of most goods and services, the expense ratios of individual mutual funds differ considerably across the array of available products. The expense ratios of individual funds depend on many factors, including investment objective, fund assets, payments to financial intermediaries (see page 86), and whether the fund is actively managed or tracks an index (see page 87).

* In this chapter, unless otherwise noted, average expense ratios are calculated on an asset-weighted basis. ICI's fee research uses asset-weighted averages to summarize the expenses and fees that shareholders pay through funds. In this context, asset-weighted averages are preferable to simple averages, which would overstate the expenses and fees of funds in which investors hold few dollars. ICI weights the expense ratio of each fund's share class by its year-end assets.

The fund investment categories used in this chapter are broad and encompass diverse investment styles (e.g., active and index), a range of general investment types (e.g., equity, bond, and hybrid funds), and a variety of arrangements for shareholder services, recordkeeping, or distribution charges (known as 12b-1 fees). This material is intended to provide general information on fees incurred by investors through funds as well as insight into average fees across the marketplace. It is not intended for benchmarking fees and expenses incurred by a particular investor, or charged by a particular fund or other investment product.

Trends in the Expenses and Fees of Funds, 2024
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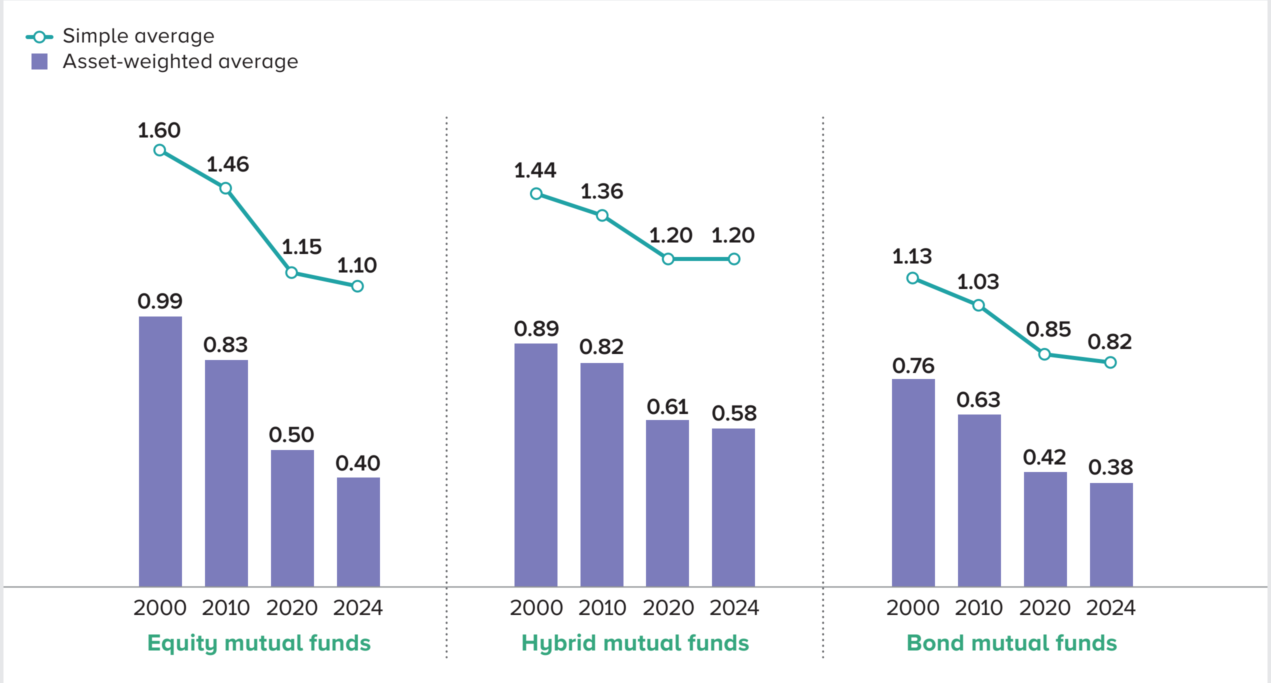
FIGURE 6.1

Expense Ratios Incurred by Mutual Fund Investors Have Declined Substantially Since 2000

Percent



Note: Data exclude mutual funds available as investment choices in variable annuities.

Sources: Investment Company Institute, Lipper, and Morningstar. See *ICI Research Perspective*, "Trends in the Expenses and Fees of Funds, 2024."

Mutual Fund Investment Objective

Mutual fund expense ratios vary by investment objective. For example, bond mutual funds and money market funds tend to have lower expense ratios than equity mutual funds. Among equity mutual funds, expense ratios tend to be higher for funds that specialize in a given sector (for example, healthcare or real estate) or those that invest in equities worldwide, because such funds tend to cost more to manage. Even within a particular investment objective, mutual fund expense ratios can vary considerably. For example, 10 percent of equity mutual funds that focus on growth stocks have expense ratios of 0.59 percent or less, while another 10 percent have expense ratios of 1.77 percent or more (Figure 6.2). Among other things, this variation reflects the fact that some growth funds focus more on small- or mid-cap stocks and others focus more on large-cap stocks. Portfolios of small- and mid-cap stocks tend to cost more to manage since information about these types of stocks is less readily available, which means that active portfolio managers must spend more time doing research.

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Five Important Points on Mutual Fund Fees and Expenses
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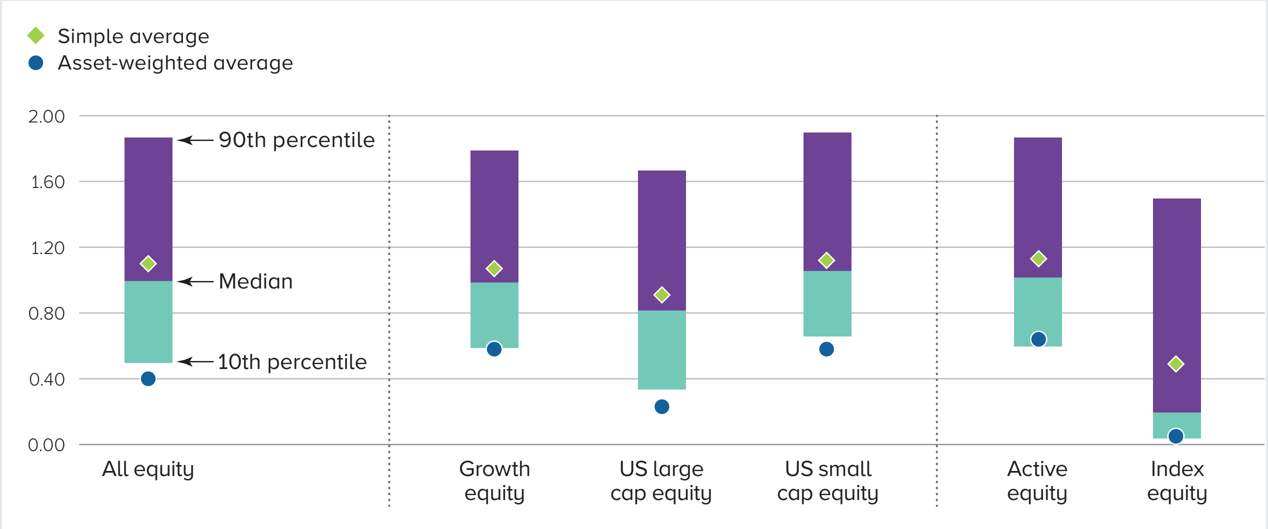
FIGURE 6.2

Mutual Fund Expense Ratios Vary Across Investment Objectives

Percent, 2024



Note: Each fund's share class is weighted equally for the simple average and the median, 10th, and 90th percentiles. Data exclude mutual funds available as investment choices in variable annuities.

Sources: Investment Company Institute and Morningstar

Understanding the Decline in Mutual Fund Expense Ratios

Several factors help account for the long-term downward trend in mutual fund expense ratios. First, expense ratios are often inversely related to fund assets. Some fund costs included in expense ratios—such as transfer agency fees, accounting and audit fees, and directors' fees—are more or less fixed in dollar terms. This means that when a fund's assets rise, these costs contribute less to a fund's expense ratio. Another factor contributing to the decline of the average expense ratios of long-term mutual funds is the shift toward no-load share classes, particularly institutional no-load share classes, which tend to have below-average expense ratios. In part, this shift reflects a change in how investors pay for services from brokers and other financial professionals (see page 86).

Mutual fund expense ratios also have fallen because of competition and economies of scale. Investor demand for mutual fund services has increased dramatically in the past few decades. From 1990 to 2024, the number of households owning mutual funds tripled—from 23.4 million to 71.0 million (see Figure 7.1). All else being equal, this sharp increase in demand would tend to boost mutual fund expense ratios. Any such tendency, however, was mitigated by downward pressure on expense ratios—from competition among existing mutual fund sponsors, new mutual fund sponsors entering the industry, competition from products such as exchange-traded funds (ETFs) (see chapter 4, Figure 3.9, and page 89 of this chapter), competition from collective investment trusts (CITs) in retirement plans (see Figure 3.11), and economies of scale resulting from the growth in fund assets.

Finally, analysis of where mutual fund shareholders have invested their money finds they tend to hold mutual funds with below-average expense ratios. The simple average expense ratio of equity mutual funds (the average for all equity mutual funds offered for sale) was 1.10 percent in 2024 (Figure 6.1). The asset-weighted average expense ratio for equity mutual funds (the average shareholders actually paid) was far lower, at 0.40 percent. Another way to illustrate the tendency for investors to gravitate to lower-cost funds is to examine how the allocation of their assets across funds varies by expense ratio. At year-end 2024, equity mutual funds with expense ratios in the lowest quartile held most (81 percent) of equity mutual funds' total net assets, and this pattern holds for both actively managed and index equity mutual funds. Furthermore, shareholders indicate that they typically review the fund's fees and expenses when selecting their mutual funds (see Figure 7.8).

The Shift to No-Load Funds

Many mutual fund investors engage an investment professional, such as a broker, an investment adviser, or a financial planner. Among households owning mutual fund shares outside employer-sponsored retirement plans, 67 percent owned mutual fund shares through investment professionals in 2024 (see Figure 7.7). These professionals can provide many benefits to investors, such as helping them identify financial goals, analyzing an existing financial portfolio, determining an appropriate asset allocation, and—depending on the type of financial professional—providing investment advice or recommendations to help investors achieve their financial goals. The investment professional also may provide ongoing services, such as responding to investors' inquiries or periodically reviewing and rebalancing their portfolios.

Over the past few decades, the way that fund shareholders compensate financial professionals has changed significantly, moving away from sales loads (e.g., front-end loads) and toward asset-based fees, which are assessed as a percentage of the investor's assets managed by a financial professional. Increasingly, these fees compensate brokers and other financial professionals who sell mutual funds. An investor may pay an asset-based fee either indirectly through a fund's 12b-1 fee, which is included in the fund's expense ratio, or directly (out of pocket) to the financial professional, in which case it is not included in the fund's expense ratio.

The shift toward no-load share classes has been an important force in driving down the average expense ratio of mutual funds. Some movement toward no-load funds can be attributed to "do-it-yourself" investors who invest through discount brokers or directly with fund companies. Another factor is an ongoing shift to compensate financial professionals with asset-based fees outside of mutual funds (for example, through fee-based professionals and full-service brokerage platforms). Additionally, 401(k) plans and other retirement accounts have bolstered assets and flows into no-load share classes. Since 2000, gross sales to no-load mutual funds without 12b-1 fees have grown substantially, accounting for 92 percent of total gross sales to long-term mutual funds in 2024 (Figure 6.3).

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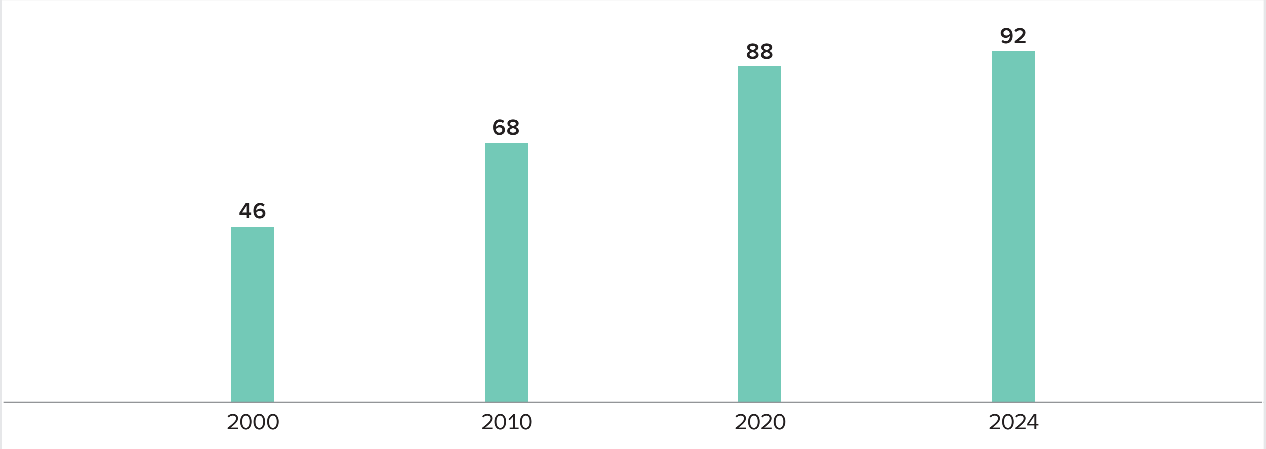
FIGURE
6.3

Long-Term Mutual Fund Investors Have Increasingly Purchased No-Load Mutual Funds Without 12b-1 Fees

Percentage of long-term mutual fund gross sales, annual



Note: Data exclude mutual funds available as investment choices in variable annuities and “R” share classes.

Sources: Investment Company Institute, Lipper, and Morningstar. See *ICI Research Perspective*, “Trends in the Expenses and Fees of Funds, 2024.”

Expense Ratios of Index Mutual Funds and Index ETFs

An index fund generally seeks to replicate the return on a specified index. Under this approach, often referred to as passive management, portfolio managers buy and hold all—or a representative sample of—the securities in their target indexes. This approach to portfolio management is a primary reason that both index mutual funds and index ETFs tend to have below-average expense ratios. By contrast, under an active management approach, managers have more discretion to increase or reduce exposure to sectors or securities within their funds’ investment mandates. Active managers may also undertake significant research about stocks or bonds, market sectors, or geographic regions. This approach offers investors the chance to earn superior returns or to meet other investment objectives such as limiting downside risk, managing volatility, underweighting or overweighting various sectors, and altering asset allocations in response to market conditions. These characteristics tend to make active management more costly than management of an index fund.

The rising popularity of index funds over the past two decades has contributed to the decline in long-term mutual fund expense ratios. For example, the growth in index mutual fund assets has placed downward pressure on asset-weighted average expense ratios of all long-term mutual funds. Total net assets of index mutual funds grew to $6.9 trillion at year-end 2024 and represented 32 percent of all long-term mutual fund net assets. Additionally, the growth of ETFs (in particular, index ETFs) has also contributed to the decrease in long-term mutual fund expense ratios as both mutual funds and ETFs compete for market share. Overall, the share of all long-term mutual fund and ETF net assets held in index funds has increased from 19 percent at year-end 2010 to 51 percent at year-end 2024 (see Figure 2.5).

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Index Mutual Funds

Index mutual funds tend to have below-average expense ratios for several reasons. First, their approach to portfolio management lends itself to being less costly. This is because index funds' portfolios tend not to change frequently and therefore have low turnover rates.

Second, index mutual funds tend to have below-average expense ratios because of their investment focus. Net assets of index equity mutual funds are concentrated more heavily in large-cap blend funds that target US large-cap indexes, such as the S&P 500. Net assets of actively managed equity mutual funds, on the other hand, are more widely distributed across stocks of varying capitalizations, international regions, or specialized business sectors, which are generally acknowledged to cost more to manage (see page 84).

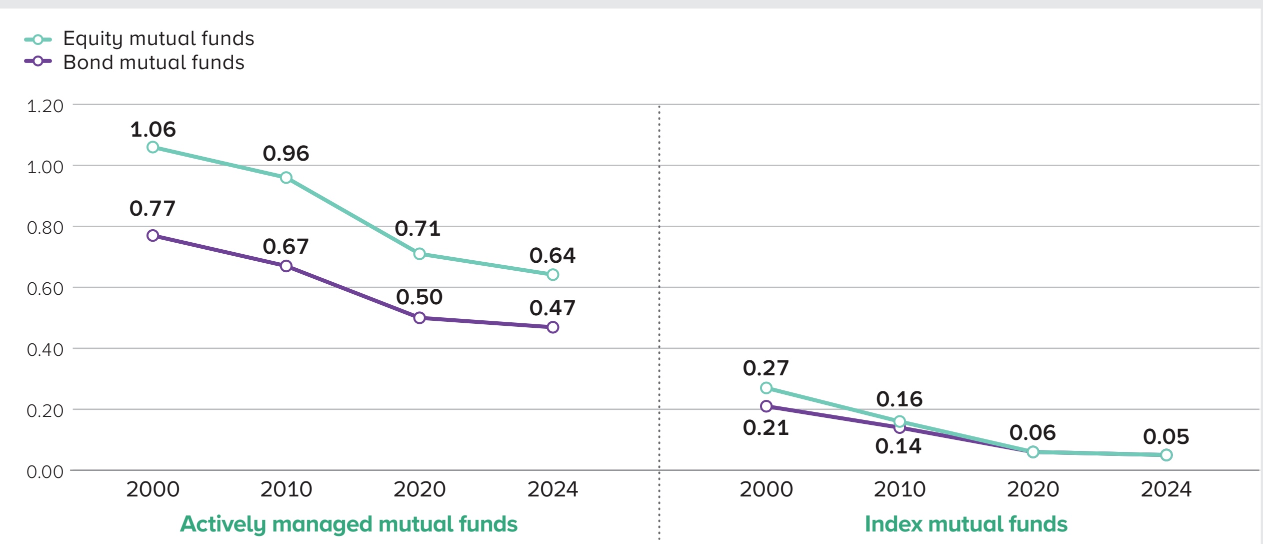
Finally, index mutual funds are larger on average than actively managed mutual funds, which helps reduce fund expense ratios through economies of scale. At year-end 2024, the average index equity mutual fund ($13.6 billion) was significantly larger than the average actively managed equity mutual fund ($2.5 billion). These reasons, among others, help explain why index mutual funds generally have lower expense ratios than actively managed mutual funds. However, both index and actively managed mutual funds have contributed to the overall decline in the average expense ratios of mutual funds (Figure 6.4).

The downward trend in the average expense ratios of both index and actively managed mutual funds reflects, in part, investors' increasing tendency to buy lower-cost funds. Investor demand for index mutual funds is disproportionately concentrated in funds with the lowest costs. Index equity mutual funds with expense ratios in the lowest quartile held 87 percent of index equity mutual funds' net assets at year-end 2024. This phenomenon is not unique to index mutual funds, however; the proportion of assets in the lowest-cost actively managed mutual funds is also high (73 percent).

FIGURE 6.4

Average Expense Ratios of Actively Managed and Index Mutual Funds Have Fallen

Percent



Note: Expense ratios are measured as asset-weighted averages. Data exclude mutual funds available as investment choices in variable annuities.

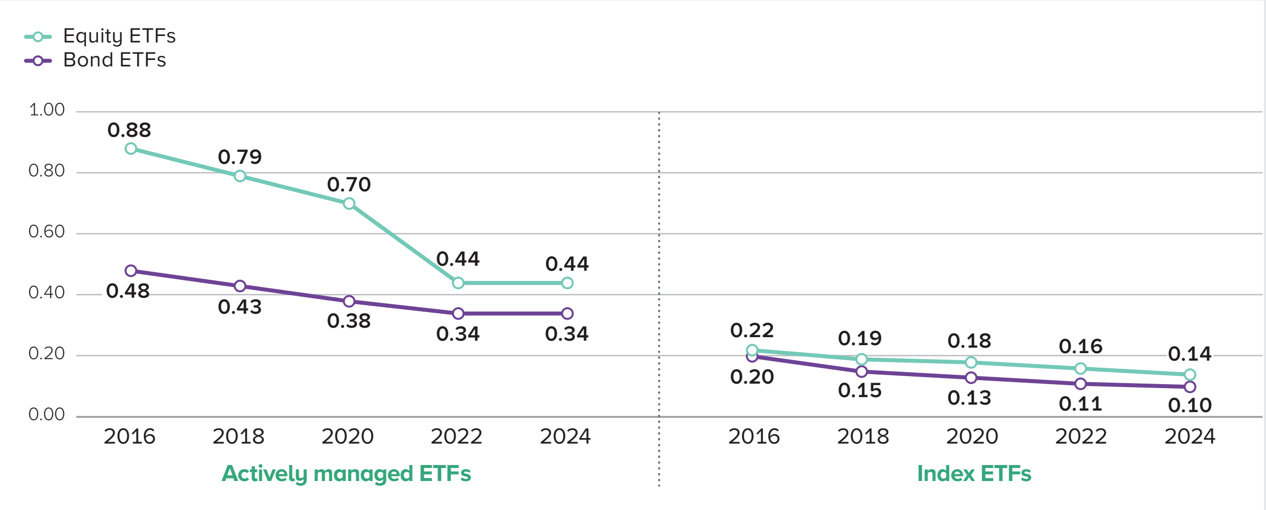
Sources: Investment Company Institute, Lipper, and Morningstar. See *ICI Research Perspective*, "Trends in the Expenses and Fees of Funds, 2024."

Index ETFs

ETF total net assets have grown rapidly in recent years, from $992 billion at year-end 2010 to $10.3 trillion at year-end 2024 (see Figure 4.1). ETFs are largely index-based and generally registered with the Securities and Exchange Commission (SEC) under the Investment Company Act of 1940. Actively managed ETFs registered under the 1940 Act represented 8.3 percent of ETF total net assets at year-end 2024, and ETFs not registered under the 1940 Act represented 2.6 percent. Part of the strong growth in ETFs is attributable to their distribution structure, in which the ETF generally charges an expense ratio that provides no compensation to financial professionals. Compensation to financial professionals for distribution or account servicing and maintenance is typically paid directly by the investor.* And because ETFs are generally index funds, they typically have lower expense ratios.

Like mutual fund investors, ETF shareholders also indicate that fund costs are important to their ETF selection. In 2024, 98 percent of ETF-owning households indicated that ETF fees and expenses are important to their investment decision, and 98 percent placed importance on ETFs' cost effectiveness. ETF owners also tend to invest in funds with below-average expense ratios. For example, the simple average expense ratio of index equity ETFs (the average for all index equity ETFs offered for sale) was 0.45 percent in 2024. The asset-weighted average expense ratio for index equity ETFs (the average shareholders actually paid) was much less than that, 0.14 percent (Figure 6.5). As with mutual funds, both index and actively managed ETFs have contributed to the overall decline in the average expense ratios of ETFs.

FIGURE 6.5
Average Expense Ratios of Actively Managed and Index ETFs Have Fallen
Percent



Note: Expense ratios are measured as asset-weighted averages. Data exclude ETFs not registered under the Investment Company Act of 1940.

Sources: Investment Company Institute and Morningstar. See *ICI Research Perspective*, "Trends in the Expenses and Fees of Funds, 2024."

* Some ETFs bundle distribution fees in the expense ratio to cover marketing and distribution expenses. These fees are usually small, typically no more than 0.05 percent.

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