What You Should Know About Mutual Fund Share Classes and Breakpoints

Because you recently added a load mutual fund to your Vanguard Brokerage Services® account, we are required to describe the sales charges and potential discounts associated with load funds in general. Understanding these charges and discounts can help load mutual fund investors choose funds that best meet their needs and can save them money on future purchases.

Sales charges and share classes

Mutual funds that carry sales charges, known as load funds, generally offer investors a choice of share "classes." Each share class—the most common are Classes A, B, and C—represents a similar interest in a mutual fund's portfolio but differs in its sales charges. In addition, investors in Class A shares may be eligible for volume discounts if their purchases meet certain investment levels, or breakpoints.

That is why investors should consider not only whether a fund's investment strategy is compatible with their investment objective but also which of a fund's share classes best fits their investment plan. Sales charges and breakpoints vary from fund to fund. They are described in each fund's prospectus and statement of additional information.

A closer look at share classes

Generally, Class A shares carry a sales charge, or "front-end load," that is deducted from an investment when the fund shares are purchased. In addition, an investor may pay an ongoing sales charge—an "asset-based sales charge"—indirectly. Also known as a "12b-1 distribution fee," this sales charge is included in a fund's total operating expenses along with management expenses and other operating expenses, all of which are deducted from fund assets. A fund's total operating expenses expressed as a percentage of assets is called its expense ratio. The expense ratio, and the asset-based sales charge also expressed as a percentage of assets, is displayed prominently in a fund's prospectus.

In contrast to a fund's Class A shares, its Class B and C shares usually do not impose a front-end sales charge and offer no volume discounts. Class B and C shares may have higher asset-based sales charges (which are reflected in higher expense ratios) compared with Class A shares.

Also, unlike with most Class A shares, investors in Class B and C shares may have to pay a fee when they sell their shares. This fee is known as a "contingent deferred sales charge" (CDSC), or "back-end load." The CDSC for Class B shares generally declines over a period of five or six years. Once the CDSC is eliminated, Class B shares usually convert into Class A shares with their lower expense ratio. The CDSC for Class C shares often declines over a period of a year, but the shares do not convert into Class A shares and the higher expense ratio remains.

Potential discounts for investors in load funds

Most load funds that offer Class A shares allow investors to qualify for reduced sales charges in a variety of ways. Generally, as the amount of the purchase increases, the percentage used to determine the sales load decreases. The sales load may even be waived for very large purchases. Mutual fund prospectuses contain tables that show the discounts and the breakpoints at which these discounts apply.

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Investors who purchase Class A shares may be able to qualify for volume discounts through "rights of accumulation," based on the extent of holdings acquired in the past or through new purchases, or "letters of intent," based on a commitment to buy more shares in the future (and possibly counting recent purchases toward the commitment). In certain circumstances, a mutual fund company may decide to grant waivers from sales charges to investors who satisfy criteria established by the mutual fund company. Keep in mind that rules for load waivers, rights of accumulation, and letters of intent differ among load funds. The specific terms of each method are described in each fund's prospectus and statement of additional information.

Rights of accumulation

Many load funds allow investors to receive a breakpoint discount by offering rights of accumulation. These permit investors to qualify for a discount by adding the value of previous purchases of the same fund, or another fund within the same fund family, to the value of a purchase.

A load fund may allow investors to add holdings in multiple accounts—including mutual fund shares held in IRAs and accounts held at other brokerage firms—to the total. Many load funds allow investors to also add in the value of holdings in accounts of spouses, children, and other related parties. To make sure you qualify for any volume discounts when you purchase Class A shares through Vanguard Brokerage Services, inform a brokerage associate of your accounts at other firms or those held by relatives. Also be ready to provide documentation attesting to these holdings.

Another factor that influences whether you may qualify for a reduced sales charge is how a fund determines the value of current holdings. Some funds use the current net asset value (NAV) of existing investments. A small number of funds rely instead on the cost of the initial purchase. If so, you may need to provide account records, such as confirmation statements or monthly statements, to see if you qualify for a discount. You should review the mutual fund's prospectus to determine whether the fund uses the NAV or historical costs to determine breakpoint eligibility.

Letters of intent

Most load funds allow investors to qualify for breakpoint discounts by signing a letter of intent, which commits the investor to purchase a specified dollar amount of Class A shares within a defined period of time, usually 13 months.

For example, an investor plans to purchase $50,000 worth of Class A shares over the next 13 months, but each purchase would be below a fund's breakpoint for a $50,000 investment. To receive the discount, the investor signs a letter of intent at the time of the first purchase. (In many cases, purchases made in the 90 days prior to the letter of intent may also be included in the commitment.) The sales charge on each future purchase would then be reduced by the amount of the discount. If the investor fails to invest the amount he or she has committed to, the investor is required to pay the difference between the discounted sales charge and the full charge based on actual purchases.

We're here to help

Because each load fund has different rules that determine qualification for volume discounts, investors should be familiar with the fund's prospectus and statement of additional information, which describe these rules. Vanguard Brokerage associates can also explain the investment options available to investors. Note that our brokerage associates are salaried and receive no commissions from the sale of fund shares. They are rewarded on service standards, such as accuracy and client satisfaction, not sales output.

To learn more about mutual fund share classes or mutual fund breakpoints, visit www.finra.org, the website of the Financial Industry Regulatory Authority, which regulates securities firms doing business in the United States. Or visit the website of the mutual fund that is of interest to you.

For more information about breakpoints for non-Vanguard funds offered through Vanguard Brokerage Services, please contact Vanguard Brokerage at 800-992-8327. You can also research non-Vanguard funds on Vanguard's website at www.vanguard.com/research.

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