AMG – Distributions & Tax Information FAQs

Why do mutual funds pay distributions?

In order to avoid the imposition of federal income and excise taxes, a mutual fund must distribute substantially all its net investment income and realized net capital gains to shareholders annually. Ordinary income and capital gain distributions are made in order to satisfy such requirements.

Generally, distributions from a fund are taxable to shareholders, unless the fund shares are held in a 401(k) plan, IRA, 403(b) account or other tax advantaged account. Investors in tax advantaged accounts generally will not have tax consequences as a result of these distributions. However, withdrawals from such accounts may be taxable.

What is the difference between ordinary income, short-term and long-term capital gains?

Ordinary income for federal income tax purposes is net investment income plus net short-term capital gains for a taxable year. Net investment income is the sum of a mutual fund's income (dividends, interest, etc.) less expenses. Short-term capital gains result from the sale of an investment held for one year or less. A distribution of short-term capital gains by a mutual fund is taxed as ordinary income for federal income tax purposes. The sum of net investment income and net short-term capital gains determines the total amount of ordinary income distributions to be paid by a fund to its investors. Ordinary income distributions received by shareholders are generally taxed at their ordinary income rates. A portion of a mutual fund's ordinary income distributions may be classified as qualified dividend income (QDI) which are generally taxed at lower rates.

Long-term capital gains result from the sale of an investment held for more than a year. A distribution of long-term capital gains by a mutual fund is taxed for federal income tax purposes at the investor's capital gains tax rate.

When are capital gain distributions taxable to a shareholder?

Generally, capital gain distributions are taxable the year in which they are received regardless if it's in the form of cash or reinvested shares. Investors are notified of the taxable amounts when they receive Form 1099-DIV.

What is the difference between Record Date, Ex-Date and Payable Date?

The Record Date is the date used to determine which shareholders are entitled to a given distribution; shareholders of record as of the close of business on that date receive the distribution.

The Ex-date is after the record date and is when the fund accounts for the distribution, which causes the net asset value (NAV) to drop by the amount of the distribution.

Payable Date is the date that cash payments are sent to shareholders who do not reinvest their distributions. Those shareholders who reinvest their distributions receive additional shares based on the NAV on the Ex-date.

Why does a mutual fund's NAV drop when a distribution is paid?

When profits from sales of securities exceed losses, they accumulate and contribute to the rise of the NAV of the fund. Since a portion of the NAV is being deducted and distributed to the shareholders, the NAV will drop by the distribution amount. For example, if a fund's shares sell at a NAV of $10 of which $3 a share relates to realized gains on the sale of fund securities, the fund may need to make a capital gain distribution. If so, the capital gain distribution of $3 will be deducted from the NAV on the Ex-date and the fund share price will decline to $7.

This drop in NAV does not reflect a loss since the portion deducted from NAV is passed through to shareholders. Distributions do not impact a mutual fund's total return as they are taken into account as part of fund performance.

Why would a mutual fund distribute a capital gain in a year it had negative performance?

Even if a mutual fund's NAV has fallen during the year, it is still possible that securities sold by the mutual fund during the year resulted in a capital gain. For example, a security bought three years ago at $100 that appreciated and was sold this year at $150 will realize a $50 capital gain. This realized capital gain is then distributed to the shareholders.

Is it true that mutual fund shareholders have to pay "someone else's taxes" if they buy fund shares at a certain time?

No—fund shareholders do not pay someone else's taxes. Every fund shareholder is taxed only on his or her own economic income over the life of the investment.

Shareholders purchase and sell a fund at the fund's NAV, which is calculated daily. A fund accumulates realized and unrealized capital gains, interest, and dividends until it makes distributions. These gains and income increase the fund's NAV until they are distributed. A fund distribution reduces a fund's NAV; thus, amounts that are distributed reduce the gain (or increase the loss) that a shareholder realizes later when fund shares are sold.

Assume an investor purchases fund shares on Monday for $10 per share. The fund distributes a $1 capital gain distribution (attributable to previously realized gains accrued in the fund's NAV) on Tuesday. The $1 distribution reduces the fund's NAV to $9. If the investor sells the fund shares on Wednesday for $9, the investor will have no economic gain or loss.

What is a cost basis?

The amount of gain or loss on the sale of fund shares is determined by the difference between the "cost basis" of the shares (generally, the original purchase price) and the sale price. To calculate the gain or loss on a sale of shares, it is essential to know the cost basis. Assuming no sales charges, the cost basis of a mutual fund share, including shares received from a reinvestment of a distribution, is simply the purchase price. If there were fees or commissions paid at the time of purchase, they are included in the basis.

For example, let's say a shareholder purchased 100 shares of a fund at $10 each for a total cost of $1,000. If the shareholder later sells the 100 shares for $1,500, the capital gain will be $500 ($1,500 minus $1,000).

Why is a Form 1099 sent to shareholders?

Various Form 1099's may be sent to shareholders as required by the IRS to report certain transactions that occur during a mutual fund's taxable year. For example, a Form 1099-DIV is sent to shareholders of mutual funds to provide a record of all dividends and distributions paid, including those that have been re-invested in a given tax year and a Form 1099-B is sent to shareholders to report information regarding shares redeemed from their mutual fund investment.

How are distributions recorded on forms 1099-DIV?

Mutual funds report ordinary dividends and long-term capital gain dividends separately on Form 1099-DIV. These amounts are reported to the IRS for tax purposes. Investors use Form 1099-DIV to help report income received from investments on their tax returns each year.

Where can I find more information on the AMG Funds?

For more information on AMG Funds, please contact AMG Funds shareholder services at 800-548-4539.

This is for informational purposes only and should not be considered tax advice. Please consult your tax advisor concerning your particular situation.