



the basics

brokerages (i.e. Fidelity Investments, Ameritrade, E*Trade, Scottrade, etc.)

- Brokers are middlemen that mainly exist to execute your trades.
- There are full-service and discount brokerages.
- Full-service brokerages offer recommendations and handholding, and for that they typically charge you up to \$100 or even several hundred dollars *per trade*. (This is why stockbrokers make so much money)
- However, if you want to conduct your *own* research, you can open your account with a discount broker. They typically charge \$10 or \$15 or less per trade and offer an ever-increasing array of services—including published research reports featuring recommendations.

mutual fund companies (i.e. Vanguard Funds, Fidelity Funds, American Funds, Franklin-Templeton, TIAA CREF)

- A Mutual Fund Company is a company that pools money from shareholders and invests in a variety of securities such as stocks, bonds, and money market instruments. (from Google Dictionary)
- However, you don't have to open up an investment account at a mutual fund company if you want to invest in a *mutual fund*. Most mutual fund companies offer brokerage services, and their commissions are usually significantly higher than online discount brokerages.
- A mutual fund company is a good choice if your plan is to invest only in index funds, especially if you are inclined to add small amounts to your account on a regular basis.
- Many discount brokerages will let you invest in mutual funds for free, so it makes little sense to go with a mutual fund company if you have plans to invest in individual stocks as well. (At the very least, perhaps you could invest in your desired index/mutual funds through the company, but also open a separate brokerage account for stock investing.)

comparing brokerages

There are, broadly speaking, two factors to consider when choosing a discount broker: fees and services

fees

- **how much do they charge per trade for a market order?** (A market order is just an order at the price that the stock is at in the market... basically you saying "buy" or "sell," but not specifying any specific price.) The answer might range from \$7 or less up to \$30 or more. If you only plan to trade once or twice a year, the difference shouldn't matter too much. But if you trade twice a

month, the difference between \$10 and \$25 trades amounts to \$360 per year. (You may also worry about fees on “limit orders,” which you should be aware of if you want to be a bit more advanced in your investing)

- **is there an account minimum?** Is it lower for IRAs? Is it lower if you agree to an automatic deposit plan? If you're flush with funds, this factor might not be a deal-breaker for you. But if you've got just \$1,000 to invest, you can cross off any brokerages with minimums higher than that.
- **are there any account maintenance fees (especially IRA fees)? What about account closing or transfer fees?** Compare the fees that you're likely to be charged at any brokerages you're considering.

services

- **how you can trade:** All online brokers offer Web-based trading, but do they also allow you to make trades over the phone -- either by using a touch-tone keypad or by speaking to a human being (and how much more do they charge for these services)? Also, do they have local offices near you (if that's important to you)?
- **customer service:** Do they have a reasonably good reputation for customer service (i.e., if you need to speak to someone do you have to be put on hold for seven hours)? You can assess this for yourself just by calling or emailing each contender and asking any questions you have.
- **account statements:** Are their account statements easy to read? You may be able to view sample statements on their website. If not, perhaps some contenders will fax or mail you samples.

mutual funds/mutual fund companies

- Does the fund you're interested in have loads (i.e., commissions) or any other fees associated with it besides modest annual maintenance fees?
- What's the account minimum? Is it lower for IRAs or if you have an automatic deposit plan?
- Are there IRA account maintenance fees?
- What are the account closing or transfer fees?

SWS Editors' Note: many of these brokerage firms also offer banking solutions now as well, where you can open a savings and checking account along with your brokerage account, and vice versa (for example, Bank of America, a traditional commercial bank, has been trying to grow its brokerage business and now offers \$0 equity trades if you have over \$25,000 in assets held in BofA accounts).

Popular Online Discount Brokers:

Fidelity

www.fidelity.com

E*Trade

www.etrade.com

TD Ameritrade

www.ameritrade.com

Charles Schwab

www.schwab.com

Bank of America

www.bankofamerica.com/investing

Scottrade

www.scottrade.com

Sharebuilder

www.sharebuilder.com

Mutual Funds:

“Money 70:” best mutual
funds Money Magazine
money.cnn.com > rankings

making a choice

Check out a bunch of brokerages, make sure you understand the fee structures, look over the various services and features of interest, and then pick one. If you're getting butterflies in your stomach, pick one with no transfer or account-closing fees, and remind yourself that you can always switch if a better deal comes along.

opening the account

Although IRAs require some additional paperwork, opening a brokerage or mutual fund account is just like opening a bank account. Fill out a form and send them your money. Remember, you don't have to invest right away. You can put your money in a money market fund and let it rest a while before it's put to work in an index fund or stocks, and you'll probably be earning more in the money market account than you got in your savings account.

To set up an account with a mutual fund company, simply call the company (many phone numbers are listed online) to ask for an account application or go to its website where, in most cases, you'll be able to download an application. Remember to ask for an IRA application if that's the type of account you want to open.

Once you get to the site, you can print out the application forms, sign them, enclose them in an envelope with a check to initially fund your account, and you'll receive confirmation of your ability to start trading in pretty short order.

kinds of brokerage accounts

A brokerage account application will want you to choose among different types of accounts. So let's review the options here.

cash account: This type of account asks you to deposit cash (doing so with a check is fine), and then you can use that cash to buy stocks, bonds, mutual funds, etc. It's not much more complicated than that. Cash accounts are ideal for beginning investors.

margin account: In a margin account, the cash and securities in your account act as collateral for a line of credit available to you from the brokerage. In other words, with a margin account, you can borrow from your broker in order to invest in additional stock (or even just for your personal use). The interest rates that brokers charge, while below typical credit card rates, make the return that you need to earn on your investments much higher than if you're investing with your own cash. For example, if you're being charged 9% margin interest, then you'd better earn a good bit more than 9% on your investments in order to make the borrowing worthwhile. If your holdings head south for a while, you may find yourself making hefty interest payments while waiting for your investments to recover. (Alternatively, you might sell some of your holdings at deflated prices in order to cover your loan, or you might have to scrape together additional cash to deposit into the account.)

Margin accounts are generally for advanced investors. Still, even for seasoned investors, borrowing more than, say, 20% of the value of your holdings is pretty risky.

option account: This type of account allows you to trade options, which is a much riskier business than trading stocks. In general, options are also for advanced investors. They have relatively high fees associated with them, a short timeline, and can result in you losing *all* the money you put into them. (Very few stocks ever get to zero value like options can -- and often do.) Even options on good stocks can be bad investments. Most brokers won't let new investors open option accounts, so you don't need to worry about this one for a while.

IRA account: The popular Roth IRA is the best option for anyone who qualifies. Most of the tax-related work is done for you by the brokerage. (Note: Check to see if the broker charges an IRA account fee. Some do, and the service they provide is worth paying for, but some don't, and why pay if you don't have to?)

Be sure to specify whether you want to open a Roth IRA or a traditional IRA. The application form for each will be a bit different. Mainly you will have to specify beneficiaries who will get the account in the case of your death. Both mutual fund and brokerage accounts can be IRAs.

which account is right for you?

If you qualify for a Roth IRA, that should probably be your first choice. The tax advantages are so great that there just isn't any reason not to. After you've maxed out your Roth account and any company retirement plans, a plain cash account (or margin account if your broker requires it) is your next choice.

once the account is open

You generally go to the broker's website and log on with your account number and password. You can then check quotes, view your portfolio and account balance, and, if you like, make a trade. You can also view a history of prior trades over a given time period.

If you've never placed a trade over the Internet before, you might want to choose a brokerage that offers phone trading -- just in case. A phone trade will cost more, but you also get to pick the brain of the broker. After that, the next time you trade, the online form probably won't seem so intimidating.

Source: Unless otherwise cited, all the information above was edited from Motley Fool's "How to Start Investing" guide, which is a great resource for those who want to learn more. The link is here: <http://www.fool.com/seminars/sharebuilder/index.htm?sid=0008&lid=600&pid=0000>.

other links:

MSN Money: <http://articles.moneycentral.msn.com/Investing/StartInvesting/HowToChooseTheRightBrokerageForYou.aspx>

- A good site to determine what kind of investor you are and which types of brokers might be best suited for your needs.