First Investors Funds

Market Commentary

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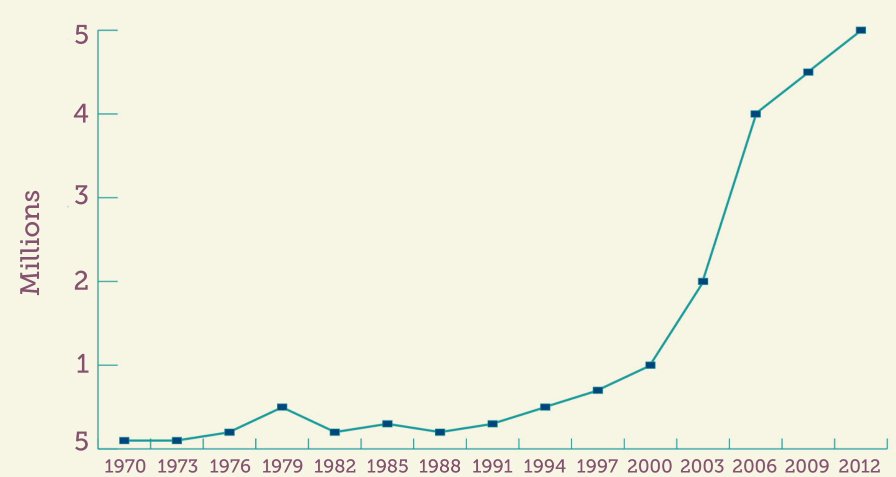
Brian Watts is Director of Research and Strategy for Foresters Investment Management Company, Inc. (FIMCO). Brian is responsible for several areas, including oversight of subadvisers, new manager search and selection, investment strategy development, asset allocation study and tools, development and management of new advisory portfolios and product development. Brian has more than 20 years of experience in the financial services industry, having worked at Fortune 500 financial services firms developing and overseeing investment platforms.

The Alternative Minimum Tax Effect on Municipal Bond Fund Investing

The Alternative Minimum Tax (AMT) was first introduced in 1969 to prevent very wealthy Americans from claiming large numbers of deductions and exemptions in order to avoid paying federal income tax. The AMT requires certain taxpayers who claim a number of exemptions and deductions or have large amounts of non-salary income to recalculate their federal tax under the AMT system and pay the higher of the two—essentially increasing their tax obligation.

Over the past decade, however, the number of Americans who face the AMT has grown significantly.

Taxpayers Subject to AMT



Source: Urban Brookings Tax Policy Center

The reason for AMT's expanded reach is that Congress did little to adjust it for inflation for many years, until 2013 when a permanent inflation adjustment was added. However, that move did not reduce the large increase over previous years in the number of U.S. taxpayers subject to the AMT.

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Today the AMT affects many people who wouldn't even be considered particularly wealthy. Among the Americans most likely to face the AMT today are those who generate income from sources other than earned income—such as retirees—and those who claim many deductions and exemptions, such as mortgage holders or couples with several children.

Implications of AMT for Muni Bond Fund Investors

Investors who pay the AMT need to be careful about how they invest in municipal bond funds. Investors in high tax brackets often turn to muni bonds because munis generally provide tax-exempt income. Certain types of municipal bonds, however, are considered federally taxable if the holder is subject to the AMT. These so-called "AMT bonds" are those issued to fund private (not public) projects, such as student loans. They often pay a higher interest rate than non-AMT bonds in order to compensate for the AMT risk.

When a taxpayer in the AMT bracket has an AMT bond in a muni fund, he or she must separate out that bond's income from the other muni bonds and pay federal tax on it. This not only costs extra time, it also reduces the true after-tax return of that bond fund. For example, two muni funds may say they provide a 4 percent yield after tax. But if one fund includes a large share of AMT bonds, that fund's yield would be much lower for a taxpayer subject to the AMT.

In other words: An AMT taxpayer should generally seek out municipal bond funds that don't include AMT bonds.

First Investors Muni Funds Protect Against AMT Risks

Unlike many of today's municipal bond funds, First Investors' municipal bond funds do not hold any AMT bonds. The funds typically attempt to invest all of their assets in municipal securities that pay interest that is exempt from the AMT. This means that our investors don't have to worry about their returns being reduced if they pay the AMT or computing how much extra tax they would owe on AMT bond income.

You may want to talk to your Foresters Financial Representative about the risks of the AMT and how our municipal bond funds can help protect you against those risks.

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