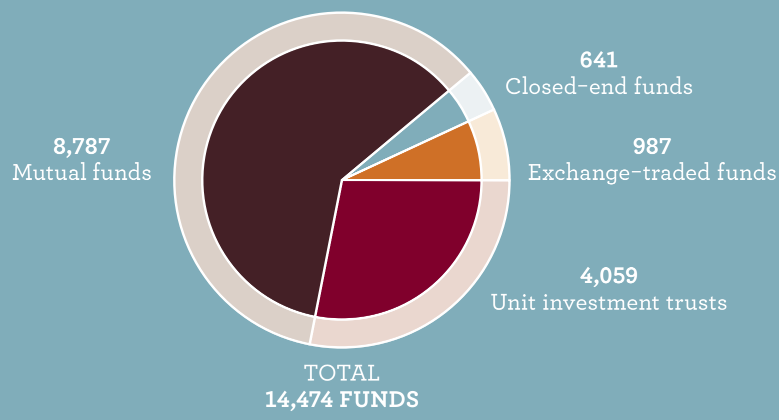
2012
Annual Report to Members

INVESTMENT COMPANY INSTITUTE®

Who Does ICI Represent?

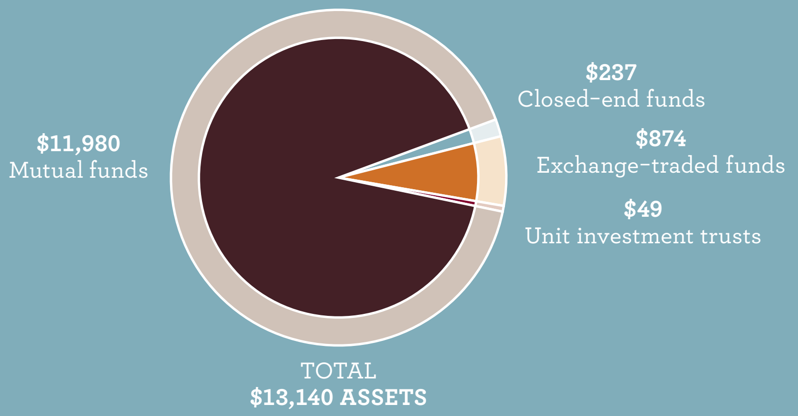
More than 14,000 funds*

Number of investment companies by type



With more than $13 trillion in assets*

Investment company assets, billions of dollars



Serving more than 90 million shareholders

Ownership of funds offered by investment companies, May 2012

45.1 percent
OF U.S. HOUSEHOLDS OWN FUNDS

54.6 million
U.S. HOUSEHOLDS OWN FUNDS

93.7 million
INDIVIDUALS OWN FUNDS

* *Data for mutual funds, closed-end funds, and exchange-traded funds are as of June 2012. Data for unit investment trusts are as of December 2011.*

SOURCE: *Investment Company Institute*

Contents

TO OUR MEMBERS

Gregory E. Johnson

CHAIRMAN, INVESTMENT COMPANY INSTITUTE
PRESIDENT AND CEO, FRANKLIN RESOURCES, INC.

Investment company shareholders enjoy many benefits—diversification, comprehensive regulation, solid governance, and the fiduciary standards that guide fund managers. Yet one of the advantages of our approach to investing is so central that it's often overlooked. This essential feature of fund investing is *mutuality*—the pooling of shared interests that allows millions of shareholders to obtain professional management, scale, and a level of service individual investors could never obtain on their own.

A similar concept serves our funds as members of the Investment Company Institute. By pooling our resources, we have built an organization that brings outstanding skills in economic analysis, legal insight, operational expertise, and advocacy to advance the shared interests of funds and their shareholders, directors, and advisers. And the strong involvement of ICI's members allows us to leverage our individual firms' knowledge and talents to attain far greater results than firms could achieve by acting independently.

We saw the benefits of this industry unity across the entire range of issues that we faced in 2012, but two in particular stand out: global regulatory challenges and the ongoing debate over reform of money market funds.

The launch of ICI Global at the start of fiscal 2012 took the Institute's advocacy for funds in non-U.S. jurisdictions—already one of ICI's strengths—to a new level. This member-driven initiative responds to a clear need that affects all fund sponsors: the growing tendency of policymakers to look across national boundaries in seeking transnational approaches to regulatory concerns. In response, investment funds need an organization that is able to speak with one voice on global issues—and ICI Global is filling that need.

One year after its launch, ICI Global has built strong relationships with fund sponsors, regulators, and other fund associations. It has developed a robust policy agenda on fund regulation, reform of market structure, and international tax issues, and has pursued this agenda vigorously in Europe, Asia, and Latin America. Like its parent organization, ICI Global combines deep member participation, through its Steering Committee and policy committees, with the expertise of staff in London and Washington to provide strong advocacy for global funds and their advisers and investors.

The benefits of this new organization will only grow in the years ahead. One area where it is already paying dividends is the discussion over the future regulation of money market funds. While Washington debates proposed changes to those funds, overseas regulators and multilateral bodies are moving on parallel courses to address similar concerns. Those global discussions, in turn, feed back into and fuel the U.S. debate. Working together, ICI and ICI Global can engage seamlessly with regulators wherever these issues arise, enhancing our advocacy on behalf of both domestic and global funds.

Gregory E. Johnson, Chairman, Investment Company Institute; President and CEO, Franklin Resources, Inc.

The shared interests of all ICI member funds and their shareholders also figure prominently in the effort to preserve the value of money market funds for investors, issuers, and the economy. Money market funds played a vital role in the growth of fund investing in the United States. Historically, they gave millions of Americans their first exposure to the unique advantages of mutual funds. Today, more than 60 million individuals and thousands of institutions rely upon the stability, convenience, and efficiency of money market funds to help manage cash.

Through research and advocacy, ICI has built a strong case against harmful changes to money market funds. The effectiveness of ICI's approach was evident when the Securities and Exchange Commission decided not to pursue its staff proposals. While that debate is not over, our progress to date demonstrates once again the benefit of speaking with a single voice on behalf of our funds and their investors. We are all fortunate to be part of an organization able to do so strongly and effectively.

PRESIDENT'S LETTER

Paul Schott Stevens

PRESIDENT AND CEO
INVESTMENT COMPANY INSTITUTE

One important strength of ICI is its versatility. Even when the energies of our staff, members, and volunteer leadership are dedicated to coping with some major challenges for the industry, the Institute continues its efforts across a broad range of other matters of consequence for funds and their advisers, directors, and shareholders. This capacity has been on full display in recent months.

Throughout fiscal year 2012, the headline coverage of the Institute's activities focused on two matters: reform of money market fund regulation and the legal challenge brought by ICI and the U.S. Chamber of Commerce to the Commodity Futures Trading Commission (CFTC) over its amendments to Rule 4.5. Those were major initiatives, and they drew notice accordingly. They also attracted attention because they were occasions when we took stances in fundamental opposition to the courses our regulators were pursuing, based on our sense of duty to fund shareholders. On these matters, we have worked especially hard to demonstrate how investor interests will best be served and to demonstrate how regulators might best fulfill their statutory mandates.

At same time, however, our staff and our members have remained deeply engaged across the entire spectrum of regulatory, legislative, and public debates affecting funds, retirement plans, and shareholders. We commented extensively on the ongoing implementation of the Dodd-Frank Wall Street Reform and Consumer Protection Act, participating in rulemakings by the Securities and Exchange Commission (SEC), the CFTC, and the new Financial Stability Oversight Council. To cite just one example, both ICI and ICI Global raised serious concerns about the harm to funds and shareholders from regulators' overly broad reading of the Volcker Rule.

Funds' use of swaps, options, and futures was another area of particular importance. In response to an SEC concept release, we hosted a roundtable on the legal framework for funds' use of derivatives and offered concrete suggestions designed to preserve investor protections while securing the benefits of derivative investment.

As always, we maintained our focus on data collection and economic analysis. ICI Research supplemented its regular studies of funds and shareholders with groundbreaking papers on such topics as funds' impact on commodity prices and the effects of disclosure of funds' proxy votes on corporate governance. ICI Research provides a strong foundation for our advocacy and our efforts to improve public understanding of funds and their investors, and such pioneering work helps anticipate and address policymakers' concerns with hard data and sound economic reasoning.

We brought the same approach to our outspoken support for 401(k) plans and the defined contribution retirement system throughout 2012. In two major speeches and numerous press interviews and commentaries, ICI marshaled the evidence to show that the 401(k) system is working to provide substantial retirement assets for Americans—and that participants and others have confidence in and support this system of voluntary, private-sector savings. Our research and advocacy are focusing now on demonstrating the workings and the

Paul Schott Stevens, President and CEO, Investment Company Institute

value of tax incentives for retirement savings—certain to be crucial questions in the coming debates on budget policy and tax reform.

Another indispensable element of ICI's service to its fund members is the Institute's expertise in industry operations. Our Operations Department, led by Kathleen C. Joaquin, once again demonstrated its unique value to ICI members by helping them address the myriad issues in pricing, fund accounting, clearance and settlement, and processing that arose when Hurricane Sandy forced the closure of U.S. financial markets. ICI's industry operations expertise benefits our shareholders in fair weather as well as foul.

As a new fiscal year begins, ICI and its members will find themselves facing all of these issues, and more. Concerns about the federal government's fiscal challenges—after four years of budget deficits topping $1 trillion annually—and the spending and tax choices needed to address those deficits will take center stage. Funds, retirement plans, and investors have much at stake in prompting Washington to adopt sound, long-term fiscal policies without damaging the incentives for saving, investment, and growth that our economy needs.

Throughout these and other debates, the Institute will continue to exercise its many strengths: outstanding legal and economic analysis, deep roots in our industry, clear communications and advocacy, and—perhaps most importantly—the strong involvement and support of our members. We welcome that support and pledge to continue working to our utmost for funds and their shareholders, directors, and advisers.

Standing Up for Money Market Funds and Their Investors

Money market fund investors contended with a difficult environment in 2012, marked by record low interest rates, ongoing financial turmoil in Europe, and a high-profile global debate over the merits of potentially disruptive regulatory changes for these funds.

Yet in this challenging setting, investors continued to demonstrate their reliance on money market funds—and to show strong support for preserving these funds' current features under a robust regulatory structure. Their support played a crucial role as ICI and others—political leaders, investors, and issuers in state and local governments, businesses, and nonprofit institutions—raised their voices in the regulatory debate.

That debate, of course, had been underway for several years. Since the financial crisis, ICI and its members have worked constructively with regulators from the Securities and Exchange Commission (SEC), Department of the Treasury, and the Federal Reserve System to pursue ideas that could strengthen the resiliency of money market funds without undermining their core features, their value to investors and the economy, or the competitive market that allows funds and sponsors to provide a wide range of choices to investors. The fruits of that work were evident in the substantial reforms to Rule 2a-7 governing money market fund regulation adopted in January 2010—reforms that were tested and proven in the European and U.S. debt crises during the summer of 2011.

Despite this success, regulators continued to press for another round of rulemaking. In November 2011, SEC Chairman Mary Schapiro announced that the Commission would pursue two alternative proposals

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>
> Paul Schott Stevens
> President and CEO
> Investment Company Institute

for "structural" change: money market funds would be required either to abandon stable net asset values, or to maintain capital buffers and to impose redemption "holdbacks" that would deny redeeming shareholders full access to their cash for as long as 30 days.

As they advanced these ideas, Chairman Schapiro and others—primarily current and former banking regulators—made speeches, gave media interviews, and published commentaries supporting the SEC's contemplated proposals. Federal Reserve officials were particularly active in promoting the notion that additional regulations for money market funds were necessary to address risks to the financial system.

ICI and its members responded with empirical analysis and vigorous outreach to investors. The Institute made the case that either of the SEC's contemplated alternatives would render money market funds useless as cash-management vehicles for many individual and institutional investors. The proposals would increase costs for funds, intermediaries, and investors sharply; fail to address issues of financial stability; and drive hundreds of billions of dollars out of well-regulated money market funds into less-regulated, less-transparent alternatives.

Such moments of tense and public confrontation between the fund industry and its primary regulator have been rare since ICI's founding. As ICI President and CEO Paul Schott Stevens told ICI's 54th General Membership Meeting (GMM) in May, "everything in our history and our culture as an industry and an association disposes us to work collaboratively." Indeed, Chairman Schapiro, a GMM speaker, received a standing ovation from attendees in recognition of her distinguished career and work on behalf of investors.

Nonetheless, Stevens noted, the best interests of investors required ICI and its members to advocate strenuously against the SEC proposals. "We cannot envision a future in which American mutual funds are foreclosed from providing our investors tools for effective cash management through which they can access current money market returns," he said.

As ICI made its case, it began where it always has: with the facts. Following clear and rigorous methodologies, ICI researchers shed light on the substantial flaws of the ideas under consideration at the SEC. In May, ICI published *The Implications of Capital Buffer Proposals for Money Market Funds*, which found that requiring fund sponsors to provide capital would change advisers' business models fundamentally and probably would drive advisers to offer less-regulated products or exit the cash-management business altogether. ICI followed in June with *Operational Impacts of Proposed Redemption Restrictions on Money Market Funds*, which concluded that redemption holdbacks would drive up costs for funds, intermediaries, and investors. With surveys of investors showing that these restrictions also would shrink the market for money market funds, many advisers or intermediaries likely would decide that the product was uneconomical, and cease to offer it.

ICI Research also heavily informed the Institute's congressional testimony. In June 2012, Stevens had the opportunity to appear before the Senate Banking Committee to discuss money market funds. His 62-page written statement provided lawmakers with a thorough airing of the issues surrounding money market funds and solid data vividly illustrating how the 2010 amendments, such as new minimum liquidity requirements, have had, in Stevens's words, "a transformative effect on money market funds."

Infusing the public discourse with solid facts was all the more important given the news media's troubling level of incorrect or incomplete reporting. All too often, news

Yet in this challenging setting, investors continued to demonstrate their reliance on money market funds—and to show strong support for preserving these funds' current features under a robust regulatory structure.

stories and commentary wrongly recast money market funds as a primary cause of the financial crisis; overstated the size of the government's temporary guarantee program for money market funds during the crisis; or failed even to mention the SEC's 2010 reforms.

To counter the misinformation, ICI made full use of its communications capability. The Institute's media relations team engaged continuously with journalists, providing facts and perspective. Upon publication of inaccurate reporting or commentary, ICI responded not only with conventional letters to the editor but also through social media, rapid-response comments to websites, and analyses posted to *ICI Viewpoints*. From September 2011 through September 2012, *ICI Viewpoints* published 46 items on money market funds.

Beyond communicating its own positions, ICI also endeavored to make sure that the public and policymakers were aware of the remarkable array of citizens, businesses, local chambers of commerce, nonprofit institutions, and government officials who have voiced consistent support for money market funds. ICI showcased the depth and breadth of these views at its dedicated website, www.PreserveMoneyMarketFunds.org.

All this material, in turn, aided ICI's Government Affairs Department as it engaged in its dialogue with members of Congress. Fortunately, many lawmakers proved willing to listen to the voices of the economy. More than 100 members of the House and Senate, hailing from across the country and from across the political spectrum, expressed their concerns that the SEC's contemplated changes could destroy the value of money market funds for their constituents.

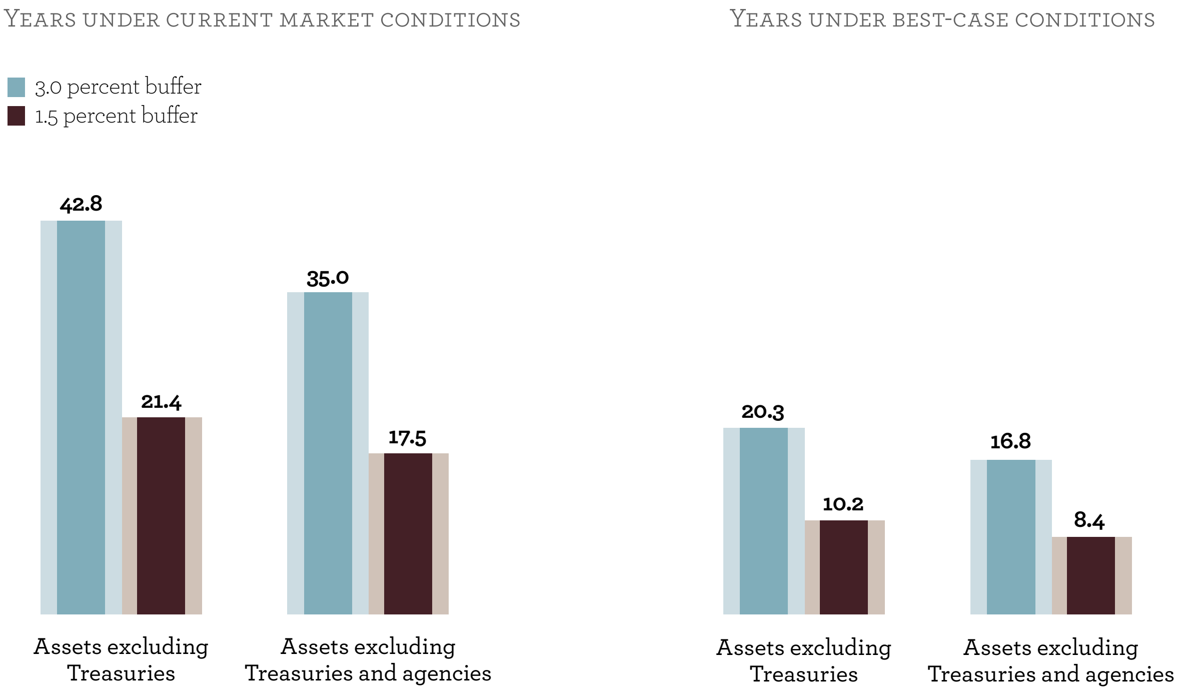
Though Chairman Schapiro persisted in pursuing structural changes, she could not persuade a majority of the five-member Commission to issue the proposals as a potential rulemaking. In late August, Schapiro called off an expected SEC meeting to consider the staff proposal. In statements explaining their views, the three dissenting Commissioners all cited the need to study the impact of the 2010 reforms carefully. They also expressed concern that Chairman Schapiro's ideas might harm money market funds severely, to the detriment of investors and issuers.

At the close of fiscal year 2012, however, the discussion around money market funds showed no sign of abating. In late September, Treasury Secretary Timothy F. Geithner wrote to members of the Financial Stability Oversight Council, which he chairs, urging it to use its authority to recommend that the SEC proceed with money market fund reform. Shortly thereafter, underscoring the global nature of this issue, the International Organization of Securities Commissions issued a number of recommendations, some of which mirrored those under consideration at the SEC.

With the help of members and allies, ICI will remain highly engaged on money market funds in the coming year. "As we have for more than four years, ICI will continue to present empirical analysis to inform this regulatory debate, in the hopes that regulators will take an objective, fact-based view of the issues," Stevens said in September. "The role that money market funds play in the U.S. economy is far too important to proceed on any other basis."

For more information on money market funds, please visit www.ici.org/mmfs.

Years of Advisers' Estimated Net Earnings That a Capital Buffer Would Absorb



In May 2012, ICI published research showing that capital buffers in the range of 1.5 percent to 3 percent for money market funds would likely make prime and tax-exempt funds uneconomical. Even under best-case conditions, ICI found, these buffer requirements could well absorb at least eight to 20 years of advisers' profits from operating money market funds.

SOURCE: Investment Company Institute

ROUNDTABLE

The Role of Industry and Financial Analysis

A CONVERSATION WITH ICI STAFF

ICI published a great deal of industry and financial analysis in the past year. What's behind that emphasis?

Sean S. Collins, Senior Director, Industry and Financial Analysis: Since the financial crisis, there's been a tremendous regulatory reform effort, with major legislation and rule proposals affecting our members. We've had to provide detailed analyses of the economic and financial effects of these reforms to help regulators understand the institutional details of how markets and our industry work.

The issues run the gamut from money market fund regulation to cost-benefit analyses for relevant rules. We've also been called upon to focus on new areas, such as commodity funds and the impact of exchange-traded fund (ETF) trading in the markets.

All of this work is based on ICI's data collection. Tell us about the role of data in the Research Department's work.

Judith A. Steenstra, Senior Director, Statistical Research: ICI has been collecting and publishing statistics on the mutual fund industry for 70 years. As the industry has grown, we've followed suit. Each year we release more than 150 statistical reports on all types of registered investment companies—mutual funds, ETFs, closed-end funds, and unit investment trusts (UITs).

We rely on our members to report their data to us, and we publish aggregated data so that members, regulators, policymakers, the media, and the public have access to complete and reliable statistics on the industry. In the past year, we began a new monthly collection on taxable money market funds using the data collected by the Securities and Exchange Commission (SEC) on Form N-MFP, which includes holdings data and mark-to-market prices.

How did your research on money market funds affect the debate around the SEC concepts for structural changes?

Collins: One of the SEC's ideas was to require money market funds or their sponsors to maintain capital buffers. There are three primary ways a capital buffer could, in theory, be structured. We looked at all three, and we found that they all create costs and problems for funds and investors. Requiring fund sponsors to put up large amounts of capital would eat up their revenues, especially with today's low interest rates. Building a buffer within a fund could take 10 years or even longer, and would amount to, at most, 50 basis points of the fund's assets. And a capital buffer raised in the market poses difficult legal and operational issues—for example, will the market continue to provide capital in a financial crisis, when it's needed most?

Rochelle L. Antoniewicz, Senior Economist: Our paper on redemption restrictions was primarily intended to educate a broader audience on the intricate systems that funds and their intermediaries rely upon to serve shareholders. Regulators and academics who proposed that money market funds "hold back" a percentage of every redemption seemed to believe that would be an

Sean S. Collins, Senior Director, Industry and Financial Analysis; L. Christopher Plantier, Senior Economist; Judith A. Steenstra, Senior Director, Statistical Research; Rochelle L. Antoniewicz, Senior Economist

> "For me, measuring the decline in expenses is a bit like watching Olympic swimmers: just when you think a world record can't be beat, people swim even faster."

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> “We believe feedback to regulators on the costs and benefits of proposed rules leads to more effective rulemaking.”

Rochelle L. Antoniewicz
Senior Economist
Investment Company Institute

easy way to reduce the risk of runs. Kathy [Kathleen C.] Joaquin and Marty [Martin A.] Burns of ICI's Operations Department outlined the complexities of transaction processing and the costs this proposal would impose. The critical economic point in the paper is that many intermediaries would not offer money market funds if they had to bear the large fixed costs of adopting this change.

What have you found out from the monthly data that the SEC now collects on money market funds' holdings?

L. Christopher Plantier, Senior Economist: Quite a bit. We have carefully tracked how prime money market funds responded to the evolving eurozone debt crisis in 2011 as they reduced their eurozone holdings and shortened the maturity of their remaining holdings. And we've used these data to document how stable money market funds' mark-to-market values are. These values have moved very little, even during the summer of 2011 when the eurozone debt crisis worsened and the debt ceiling debate raged. The monthly money market fund holdings data provide tremendous insights into how these funds prudently manage their portfolios, but unearthing these insights requires intensive data analysis.

Mutual fund fees and expenses are a perennial issue for the fund industry and ICI. Is there anything new to report on that front?

Collins: The data seem to be consistent year in, year out. Fund expenses continue to decline. That's a pretty remarkable thing, given continuing expansion in regulation, the capital investments advisers make to keep up with ever-changing technology, and the cost of the highly trained support staff that shareholders expect. For me, measuring the decline in expenses is a bit like watching Olympic swimmers: just when you think a world record can't be beat, people swim even faster.

Regulators are required to conduct meaningful economic analyses in rulemaking. When and how does ICI weigh in on the costs and benefits of rules that affect funds?

Antoniewicz: We believe feedback to regulators on the costs and benefits of proposed rules leads to more effective rulemaking. When a major rule proposal may affect our members, we generally ask members to complete an informational survey tailored to the proposal and use that data to conduct an in-depth cost-benefit analysis. Last spring, we found that a Commodity Futures Trading Commission (CFTC) proposal to harmonize CFTC and SEC disclosure rules for funds required to register as commodity pool operators would impose costs as high as $65 million initially and $34 million annually after that—with no corresponding benefits for mutual funds. That's a powerful argument against such rules.

Why did ICI do research on commodities pricing?

Plantier: Investing in commodities has become increasingly popular with mutual fund and ETF investors seeking diversification and a hedge against inflation. This trend has raised concerns among policymakers that commodity funds may increase prices or volatility. In response, we used empirical techniques and found that economic fundamentals—such as strong global growth and the value of the U.S. dollar—are the key drivers of commodity prices, not flows into commodity mutual funds and ETFs.

What analysis has ICI Research done recently on ETFs?

Antoniewicz: In the past year, some commentators have tried to link the growth of ETFs to an increase in stock market volatility. Our analysis of market data going back to the 1980s, as well as intraday price data during the volatile summer months of 2011, suggests that market volatility is driven primarily by macroeconomic events, not by trends in ETF assets. We've taken our findings to the readers of *ICI Viewpoints* and to interested regulators.

What do you see as the continuing challenges or areas of growth in your work in the coming year?

Steenstra: As the market grows, we're always adding new funds to our statistical database. There's been an expansion in ETFs and UITs in recent years. We've also revised our closed-end fund survey to gather additional information, including the use of leverage by these funds.

Collins: One of our biggest challenges, spurred by technology, will be to respond in real time to the growing use of data and requests for it. Largely because of technology, we'll have to deal with an incredible increase in the amount of data in the next five to 10 years. That will require a capital investment in technology and people for both funds and ICI. The reward for that will be the impact on policy that we gain from our data collection and research.

For more information on ICI's industry and financial analysis, please visit www.ici.org/research. ICI Viewpoints *is available at www.ici.org/viewpoints.*

"EACH YEAR…WE RELY ON OUR MEMBERS TO REPORT THEIR DATA TO US, AND WE PUBLISH AGGREGATED DATA SO THAT MEMBERS, REGULATORS, POLICYMAKERS, THE MEDIA, AND THE PUBLIC HAVE ACCESS TO COMPLETE AND RELIABLE STATISTICS ON THE INDUSTRY."

Judith A. Steenstra
Senior Director, Statistical Research
Investment Company Institute

OPERATIONS UPDATE

In a Changing Environment, a Steady Focus on Investors

BY KATHLEEN C. JOAQUIN

For funds, the operations challenge remains constant: how can our industry successfully deliver products and services to investors in the most efficient and effective way? Over the past 12 months, ICI's Operations Department has kept that question in the forefront, even as we've contended with a regulatory environment marked by unprecedented change.

Happily, ICI can face operational changes and challenges with a clear mission and an approach that has stood the test of time. The Operations Department helps the fund industry tackle business, policy, and compliance issues that significantly affect the services provided by funds to investors. We do this by convening industry operations leaders and applying their expertise to a wide range of operations priorities: improving the industry's best practices and standards, increasing operational efficiencies, and mitigating and managing the operational impacts of regulatory initiatives.

Through our committees, task forces, and working groups, we work closely with members and service providers in a variety of functional areas for fund complexes. These areas include fund accounting and financial reporting; the valuation and pricing process; mutual fund transfer agency and shareholder servicing operations; fund distribution; and the clearance and settlement of fund shares through our industry utility. We also focus on technology, business continuity planning, the unique challenges faced by our small funds members, and the global context of operations matters (through our International Operations Advisory Committee).

Our collaboration with industry operations professionals advances automation and standardization that reduce risks and costs, while maximizing the efficiency of conducting business through our various distribution channels. A vital component of these efforts is ICI's partnership with the Depository Trust & Clearing Corporation (DTCC). DTCC's suite of mutual fund services, developed over many years in close coordination with ICI, provides centralized, automated, and standardized clearance and settlement. These services enable funds and the vast network of industry participants—including broker-dealers, banks, trusts, and other financial services firms—to facilitate mutual fund investing through financial advisers working with millions of investors.

Through the ICI-DTCC partnership, we continue to make good progress in meeting the demands for industry solutions to nonstandard, manually intensive, and costly processes; to comply with legislative and regulatory initiatives; and to foster transparency. On the latter, consider the ongoing trend toward the use of intermediary omnibus account structures. Both the Operations and Broker/Dealer Advisory Committees are working to improve omnibus transparency through OmniSERV, a DTCC product suite that provides industry participants a standard, secure environment for omnibus processing, as well as promising potential for cost savings.

The industry also continues to improve and encourage the use of the DTCC's Mutual Fund Profile Security database. The Profile database houses prospectus and business

Kathleen C. Joaquin was named ICI's Chief Industry Operations Officer in March 2012. She has been a member of ICI's Operations Department since 1989.

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>
> Kathleen C. Joaquin

rules on thousands of funds—including breakpoint schedules and linkage rules—to support best pricing for investors and to assist intermediaries in accurately processing shareholder transactions.

On the regulatory front, ICI and its operations members worked with the DTCC to help funds, firms, and investors comply with the mandatory cost basis reporting regulations that became effective on January 1, 2012. Spearheaded by ICI's Broker/Dealer Advisory Committee, this work included improvements to DTCC's Fund/SERV, Networking, and Cost Basis Reporting services to automate the movement of cost basis information sent by funds and firms on transfer reporting statements when investors move assets to another firm. This automation was a major step in establishing an efficient and accurate process for reporting the cost basis information that shareholders need to prepare their tax returns.

ICI's Transfer Agent Advisory Committee also developed cost basis documentation to aid fund transfer agents in implementing policies and compliance procedures. The group has focused in particular on improving shareholder communications—including related customer options and fund policies—to make it easier for investors to understand and comply with the new rules.

The debate around money market funds led to another key regulatory initiative for ICI Operations. In June 2012, ICI published *Operational Impacts of Proposed Redemption Restrictions on Money Market Funds*, one of several ICI papers analyzing the implications of structural changes then under consideration by the Securities and Exchange Commission (SEC). Incorporating robust member input, this paper addressed the operational impacts of redemption restrictions that would deny investors full use of their cash by holding a portion of investors' money market fund accounts in escrow under all market conditions. The study found that these restrictions not only would have harmful consequences for the broader financial markets, but also would create serious and costly operational issues that would restrict or eliminate the usefulness of money market funds in many services that funds and financial providers extend to investors.

Naturally, accounting and financial reporting for investment companies is a high priority for Operations. Through our Accounting/Treasurers Committee, we coordinate with members on accounting, reporting, audit, and valuation issues. Generally, our work on financial reporting and auditing issues enables us to communicate the industry's position on proposals and other actions of standard setters and regulators. We also assist members with implementation of new or changed requirements and discuss ways to help members minimize divergent practices.

We are closely monitoring accounting standard setters' contemplated transition to international financial reporting standards, which could affect the industry-specific financial reporting model followed by investment companies under U.S. Generally Accepted Accounting Principles. Elimination of specialized industry accounting and reporting standards would harm our investors, who rely on specific information provided in investment company financial statements.

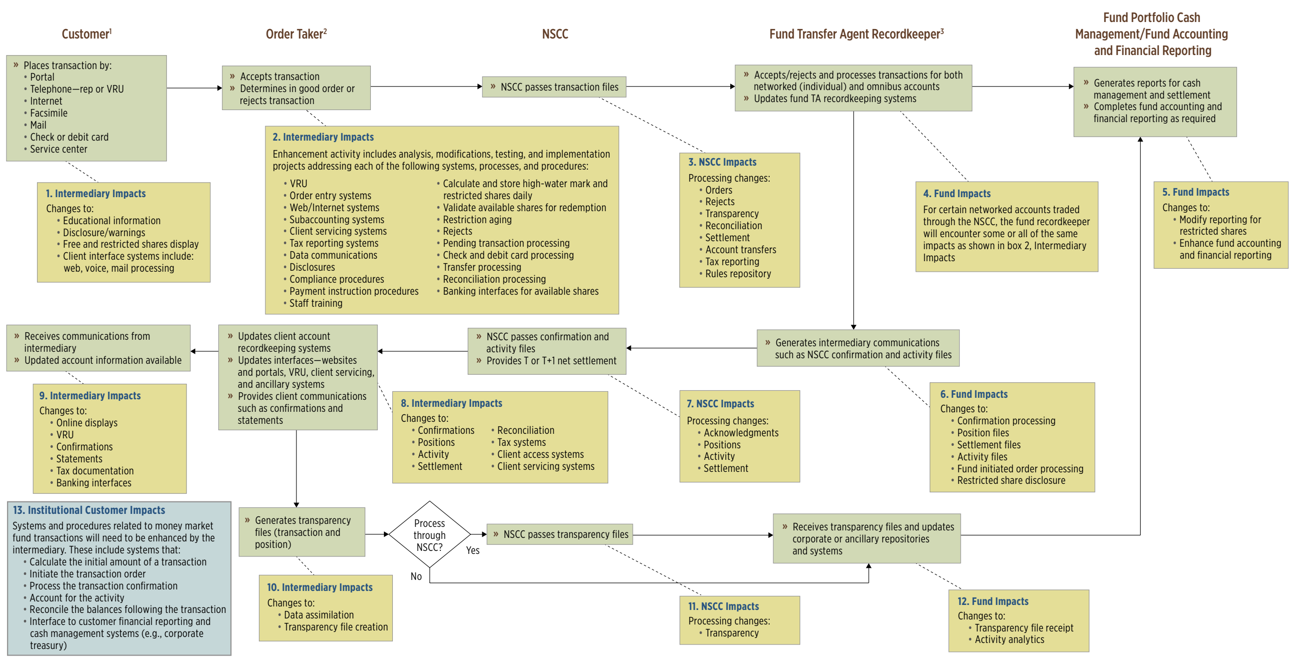
Last, but by no means least, ICI Operations interacts with fund technology leaders through our Technology Committee. This group monitors developments and practices of utmost importance to members and investors: business continuity planning, information security, collaboration technologies, desktop virtualization, cloud computing, monitoring social networking, and use of handheld devices, to name a few.

The Technology Committee's Social Media Task Force, formed in 2011, has been particularly active in addressing concerns regarding existing SEC recordkeeping rules. Over the long term, the industry cannot afford to meet the extensive recordkeeping requirements designed for paper-and-typewriter communications in a world of tweets, blogs, and instant messages. Collaborating with members of the industry's legal and compliance community, the task force is working toward developing recommendations for the SEC regarding an effective, risk-based recordkeeping approach that can accommodate rapidly evolving communications technologies.

Looking ahead, ICI Operations has a full agenda of initiatives to carry out that will benefit funds and their investors. Our work on this agenda would be impossible without the support and leadership of industry operations professionals. Their spirit of cooperation will continue to lead us to solutions that mitigate risks, reduce costs, and, above all, improve services for shareholders.

For more information on ICI's work on operations and technology issues, please visit www.ici.org/operations.

Impacts of Redemption Restrictions on Transaction Processing Through NSCC



This figure illustrates the interaction of mutual fund customers and industry groups in processing fund transactions and displays the role that industry groups play in processing the customer's instructions and delivering critical information in processing fund transactions (*Operational Impacts of Proposed Redemption Restrictions on Money Market Funds*, June 2012).

SOURCE: Investment Company Institute

ICI Global: Giving Funds a Voice on the International Stage

In recent years, investment funds around the world have been subject to two powerful trends in the international financial system. One is the worldwide rise of regulated funds as major financial intermediaries. The second: regulators and other policymakers have begun to focus on funds and fund management more intently than ever before. Regulation, too, has gone global.

As funds and their advisers increasingly responded to a formidable array of international regulatory and policy challenges, ICI's members and leadership recognized the fund industry's need for a global voice. To meet that need, in October 2011 the Institute's Board of Governors launched ICI Global—the first industry body exclusively focused on the global investment fund industry.

A year later, ICI Global has grown to represent a diverse group of members in North America, Europe, and Asia, who manage more than $1 trillion in registered fund assets. Leveraging ICI's traditional strengths in law, research, communications, and industry operations, and building upon its longtime involvement with international issues of consequence to U.S. funds, ICI Global gives a strong voice to the concerns and interests of regulated funds, their managers, and investors worldwide. It also provides a forum for managers from around the world to interact on policy issues and an ongoing mechanism for outreach and dialogue with the global regulatory community. Already, ICI Global has built solid relationships with important international regulatory bodies, such as the Financial Stability Board (FSB), the Organization for Economic Cooperation and Development (OECD), the International Organization of Securities Commissions (IOSCO), and others, to facilitate discussion about issues important to ICI Global's members.

Those issues fall into four main categories:

The Role of Funds in Financial Stability: ICI Global has worked hard this year to interact with international regulators about the role of funds and fund managers in financial stability. The FSB has been focused on nonbank financial intermediation conducted through the capital markets—activities sometimes pejoratively labeled as shadow banking, including securities lending and the operation of money market funds. Together with IOSCO and European regulators, the FSB is considering some of the same problematic money market fund regulatory proposals contemplated by the U.S. Securities and Exchange Commission (SEC).

In response, ICI Global has endeavored—in its commentary and active dialogue with policymakers—to ensure that they appreciate how money market funds work, the important role that these funds play in the international economy, the reforms already implemented in different jurisdictions after the financial crisis, and the lack of justification for further bank-like regulations. To this end, in October 2012 ICI Global joined ICI, the European Fund and Asset Management Association,

Dan Waters, Managing Director, ICI Global; Eva M. Mykolenko, Associate Counsel, International Affairs, ICI; Susan M. Olson, Senior Counsel, International Affairs, ICI; Ari Burstein, Senior Counsel, Capital Markets, ICI

Keith Lawson, Senior Counsel, Tax Law, ICI and ICI Global, is not pictured because he was chairing the FATCA Business Advisory Group at an OECD meeting in Paris, France.

ICI Global is working to highlight the effectiveness of defined contribution schemes and the contributions that funds make to retirement provision in many countries.

ICI Global gives a strong voice to the concerns and interests of regulated funds, their managers, and investors worldwide.

the Institutional Money Market Funds Association, and the Investment Funds Institute of Canada in convening an international summit on money market funds in Brussels to help policymakers and market participants better understand the global money market fund industry.

Transnational Regulatory Developments: Regulatory "spillover" has become an acute problem for global funds. It arises when one governmental authority, wittingly or unwittingly, crafts policies heavily implicating either some activity that spans national boundaries or an organization that operates in more than one jurisdiction. Examples of U.S. legislation with such an effect are the Volcker Rule and the Foreign Account Tax Compliance Act (FATCA). The European Union (EU) also deploys an increasingly extraterritorial approach to regulation, as is evident in the reform of the Markets in Financial Instruments Directive (MiFID II) and the Alternative Investment Fund Managers Directive (AIFMD).

ICI Global has been extremely active on behalf of global funds with respect to the Volcker Rule. Through extensive discussions with regulators and members around the world, ICI Global has worked hard to ensure that U.S. regulators and the international community understand the potential detrimental impact that the Volcker Rule, if adopted as proposed, will have on regulated funds outside the United States and on global securities markets.

FATCA, too, raises difficult issues for other countries and their respective financial institutions, particularly investment funds. Since FATCA might serve as a model for tax compliance laws of other countries, ICI Global has submitted comment letters, testified, and met extensively with responsible U.S. government officials to urge regulators to create workable rules. To help the international community understand FATCA and the model intergovernmental agreements (IGAs) that the U.S. Treasury developed to facilitate FATCA, ICI Global staff—led by Senior Counsel for Tax Law Keith Lawson—met with members, policymakers, and media in 10 leading fund jurisdictions in Europe, Africa, South America, and Asia. In addition, ICI Global recruited U.S. Treasury and OECD representatives to participate in a FATCA webinar.

In a similar vein, ICI Global continues to engage officials at the European Commission (EC), the European Parliament (EP), and with national regulators in the EU on a range of transnational issues in directives that have been brought forward since the financial crisis.

Market Structure: Jurisdictions around the world face thorny questions about the rapidly evolving structure of their markets—most significantly, the proliferation of algorithmic and high-frequency trading. These and other questions demand continuing close attention from the buyside. ICI Global has undertaken to fill that role on behalf of the global funds. A consistent approach in major jurisdictions is an important objective, because the trading operations of global managers typically are closely linked. ICI Global commented on numerous proposals emanating from IOSCO and policymakers in Europe and Asia, including key aspects of MiFID II and Hong Kong's Securities and Futures Commission proposals concerning electronic trading. Led by Senior Counsel for Capital Markets Ari Burstein, ICI Global staff also have participated in numerous industry events and met with regulators, exchanges, and brokers in London, Brussels, Madrid, Hong Kong, and Singapore. Through its activities, ICI Global has signaled its determination to be a strong, constructive voice on trading and market structure issues.

Role of Funds in Pensions and Long-Term Savings: As fiscal and demographic pressures increase, nations around the globe are studying ways to enhance retirement security. Regulated funds are well positioned to be a key component in their efforts to increase retirement savings.

Much as ICI has done in the United States, ICI Global is working to highlight the effectiveness of defined contribution schemes and the contributions that funds make to retirement provision in many countries. In its first year, ICI Global has been analyzing the features of pensions and retirement systems from multiple jurisdictions to further its advocacy for funds as a component of retirement savings and to prepare for a major international conference on this subject scheduled for 2013 in Hong Kong.

To advance this ambitious agenda, ICI Global commenced operations in London under the direction of an experienced leadership team with deep understanding of the issues facing global funds and the ability to connect with policymakers around the world.

Dan Waters serves as Managing Director and Giles S. Swan as Director of Global Funds Policy. Both came from the UK Financial Services Authority, where they worked closely with IOSCO, the European Securities and Markets Authority, and the EP on important asset management issues, including AIFMD and the Undertakings for Collective Investment in Transferable Securities directive.

ICI Global's policy agenda and activities are directed by a Steering Committee, composed of representatives from each member firm. Jamie Broderick—Vice Chairman of J.P. Morgan Asset Management for Europe, Middle East, and Africa—has served with distinction as the founding Chairman of the ICI Global Steering Committee. Member committees and task forces help inform the direction for each of ICI Global's main policy areas.

Thanks to the active involvement of members and support of leaders in the global fund community, ICI Global already has become a respected voice for funds on the international stage. In years to come, ICI Global will play a role of growing importance as it advocates to advance the interests of global funds, their investors, and sponsors.

For more information on ICI Global, please visit www.iciglobal.org. For more information on ICI's work on international issues, please visit www.ici.org/policy/regulation/international.

Building on the Strengths of the 401(k) System

The defined contribution (DC) retirement system continues to grow and evolve to help millions of Americans meet their primary financial goal—achieving a secure retirement. By mid-2012, Americans had amassed $9.8 trillion within DC plans and individual retirement accounts (IRAs), more than half of all assets dedicated to retirement saving. Employers who sponsor DC plans and workers who participate in them continue to reap the benefits of innovation and growth in these plans, including the introduction in 2012 of significantly enhanced disclosure for plan fees and growing use of plan features that help increase participation, savings, and sound investment practices. The strength of DC plans, including 401(k) plans, is reflected in the widespread public confidence in these plans and support for their key features.

Despite these measures of growth and success, the DC retirement system has faced challenges from some policymakers and commentators who are skeptical of the 401(k) system's ability to help Americans achieve a secure retirement. Broader national issues—in particular, the need to right the nation's budgetary course and demands for fundamental tax reform—also promise to complicate the task of expanding and improving self-directed contributory retirement plans (page 26). In response, ICI has marshaled a strong, research-based effort in public commentary and legislative outreach to rebut criticism, set the record straight, and offer an affirmative agenda to defend and improve the 401(k) system.

The fund industry's decades-long efforts to ensure that DC plan sponsors and participants are provided with more complete and consistent disclosure achieved significant results in 2012. Employers and workers received, for the first time, a new, standardized set of disclosures on all investment options in their plans. These new disclosures highlight any plan-level fees and ensure greater uniformity of disclosures from investment

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type to investment type. In this respect, information that has long been available from mutual funds—for example, the identification of investment objectives, principal strategies and risks, historical performance, and fees—now will be required to be provided directly to participants for both mutual fund and non–mutual fund investments.

With such uniformity, participants should find it easier to make the comparisons needed for better-informed investment choices. The standards reflect hard work by ICI—through years of active engagement and collaborative work with government officials, members, policymakers, and trade organizations—to give employers and workers the tools to make informed choices in saving and investing for retirement.

The new disclosures on fees drew considerable attention from the press and critics of 401(k) plans. A report alleging that 401(k) investment and plan fees could claim as much as $155,000 over a participant's career garnered widespread coverage. The report's claims were refuted decisively by ICI's long-running research on mutual fund fees. In addition, research conducted by Deloitte Consulting for ICI found that the "all-in fee" for a typical 401(k) plan participant in 2011 was 0.78 percent, or approximately $248, per year. ICI mounted a spirited response through media interviews, articles posted to *ICI Viewpoints*, and letters and online comments to news organizations.

The Institute's advocacy for clear and useful disclosure also animated efforts to enhance understanding of target date funds (TDFs). ICI proactively commented on Department of Labor (DOL) and Securities and Exchange Commission proposals to make it easier for participants to understand these funds, which use a mix of asset classes (or asset allocation) that the fund provider adjusts to become less focused on growth and more focused on income over time. ICI advocates the use of a "glide path" illustration to help investors understand how a TDF's asset allocation will change before and after the fund's target date.

Reflecting ICI's belief that the Internet can help investors achieve a better understanding of fund and plan disclosures, the Institute advanced the priority of making electronic delivery the default communication

> The Institute's affirmative agenda for the retirement system includes a call to put Social Security on a sound financial footing; defense of the tax incentives that encourage employers to sponsor and workers to participate in retirement savings plans; efforts to advance innovation in employer plans; and measures to improve access to retirement savings.

for retirement plan information, with paper delivery remaining an option. The DOL issued interim guidance on e-delivery of the new participant disclosures in the fall of 2011, but the guidelines did not make it easier for employee benefit plan sponsors and their service providers to use electronic media instead of paper. ICI, working with many other trade groups, filed a comprehensive letter citing concerns about the guidance and encouraging the issuance of new guidelines to make e-delivery the default communication for plan information. ICI also carried its advocacy to Capitol Hill, supporting the introduction of legislation to modernize electronic media rules for retirement plans.

Congress also continues to discuss legislation to help plan participants project the income they can expect in retirement from their current and anticipated savings. While the fund industry supports these objectives, ICI expressed concerns that the proposed legislation—the Lifetime Income Disclosure Act—would stifle innovation of new educational and planning tools. The bill also could impose annuity-based estimates that would not provide meaningful information to participants, most of whom may be interested in a broader array of distribution options beyond annuitization. Through engagement with key lawmakers and staff, the Institute consistently has worked toward a broader, more-flexible approach for informing and educating plan participants.

Despite these ongoing efforts to improve and enhance the DC retirement system, some policymakers and commentators stepped up criticisms of 401(k) plans and expressed support for alternatives to the current retirement system. U.S. Senator Tom Harkin (D-IA) garnered headlines by claiming that 401(k)s aren't providing enough income to finance retirement needs, and with a wholly new model for the private retirement system. Legislation enacted in California proposes to create a new cash-balance retirement system run by the state on behalf of private employers.

ICI opposed these efforts with solid empirical research and informed advocacy. The Institute also carried its support for the 401(k) system into the arena of public debate. ICI President and CEO Paul Schott Stevens spoke on the success of 401(k)s at Town Hall Los Angeles and joined ICI Governor Mellody Hobson, President of Ariel Investments, in an appearance at the Commonwealth Club of California in San Francisco to discuss ways to improve Americans' retirement prospects. The Institute's affirmative agenda for the retirement system includes a call to put Social Security on a sound financial footing; defense of the tax incentives that encourage employers to sponsor and workers to participate in retirement savings plans; efforts to advance innovation in employer plans; and measures to improve access to retirement savings, including simplification of IRAs and creation of a new, simpler retirement plan to aid smaller workplaces.

Through this agenda, ICI will continue to advocate for ways to improve Americans' retirement preparedness, building on the proven strengths of the 401(k) system.

For more information about ICI's work on retirement research and policy, please visit www.ici.org/policy/retirement, www.ici.org/research/retirement, and www.ici.org/401k.

ICI Governor Mellody Hobson, President of Ariel Investments, and ICI President and CEO Paul Schott Stevens discuss "The Future of Retirement" at the Commonwealth Club of California on September 27, 2012.

Illuminating the Tax Incentives for Retirement Savings

In the next year, the tax incentives that successfully encourage millions of Americans to defer income for retirement—a cornerstone of America's employment-based retirement system—are likely to come under increasing pressure. Policymakers may well propose limiting the benefits of tax deferral for retirement savings in order to raise revenue to meet two demands: the need to resolve the federal government's severe fiscal crisis and growing calls for comprehensive tax reform.

Taken together, tax deferral for defined benefit pensions, defined contribution (DC) plans, and individual retirement accounts constitute the third-largest set of "tax expenditures" in the federal budget, trailing only tax exemptions for employer-provided health benefits and housing. As a result, these incentives form tempting targets for lawmakers seeking revenue.

As these tax incentives have come under the microscope, ICI has moved aggressively to rebut criticisms and show the economic and social value of preserving one of the crucial components of the success of private-sector pension plans. As ICI President and CEO Paul Schott Stevens told the Commonwealth Club of California: "We need to point our federal government in the direction of greater thrift—without sacrificing the incentives that help millions of Americans save for their own financial futures."

To that end, the Institute is marshaling research to explain how tax deferral works, to dispel myths about deferral's impact, and to demonstrate widespread public support for the tax incentives that encourage employers to sponsor retirement plans and enable workers to save for retirement.

In early September, the Institute published a study by ICI Senior Economist Peter J. Brady to enhance policymaker and public understanding of the tax benefits of tax deferral. The study, *The Tax Benefits and Revenue Costs of Tax Deferral,* demonstrates that the tax treatment of retirement savings—deferral of tax on

ICI HAS MOVED AGGRESSIVELY TO REBUT CRITICISMS AND SHOW THE ECONOMIC AND SOCIAL VALUE OF PRESERVING ONE OF THE CRUCIAL COMPONENTS OF THE SUCCESS OF PRIVATE-SECTOR PENSION PLANS.

> “We need to point our federal government in the direction of greater thrift—without sacrificing the incentives that help millions of Americans save for their own financial futures.”
>
> Paul Schott Stevens
> President and CEO
> Investment Company Institute

contributions and earnings—differs fundamentally from other tax breaks, such as the exclusion from income of employer-paid health insurance benefits or deductions for mortgage interest. The reason: unlike income that is excluded or deducted, deferred income eventually is subjected to tax—for example, when it is withdrawn from a retirement account. Thus, the benefits of tax deferral cannot be calculated simply by multiplying a taxpayer's contributions by his or her marginal tax rate (the standard calculation for exclusions or deductions).

Instead, the tax benefit of deferral depends on many factors—primarily the saver's age and time until withdrawal, but also the return on the plan's investments and whether that return is paid as interest, dividends, or capital gains. Indeed, under realistic assumptions, the tax benefits from a one-time $1.00 contribution to a retirement account are greater for a 45-year-old with a 15 percent marginal tax rate than for a 60-year-old in the 35 percent tax bracket.

ICI Research also has established that the vast majority of U.S. households overwhelmingly support preserving the nation's current tax incentives for retirement savings. In *America's Commitment to Retirement Security: Investor Attitudes and Actions*, ICI reported survey results showing that 85 percent of all U.S. households don't want the tax advantages of DC accounts to be eliminated, and 83 percent oppose any reduction in employee contribution limits.

"It is clear that the current tax incentives to encourage Americans to build a nest egg in retirement accounts are effective and command the overwhelming support of the American public," Stevens said when the study was released. Evaluating and documenting that effectiveness and support will remain a prime objective for ICI Research.

For more information on ICI's research on tax incentives for retirement savings, please visit www.ici.org/research.

Exchange-Traded Funds: Empowering Investors with Information

The extraordinary growth of exchange-traded funds (ETFs) over the past decade reflects the value of this product to investors. More and more, both retail and institutional investors recognize that ETFs share many of the same strengths as mutual funds—including low cost, liquidity, and a robust regulatory framework—while offering new options for executing portfolio strategy and achieving financial goals.

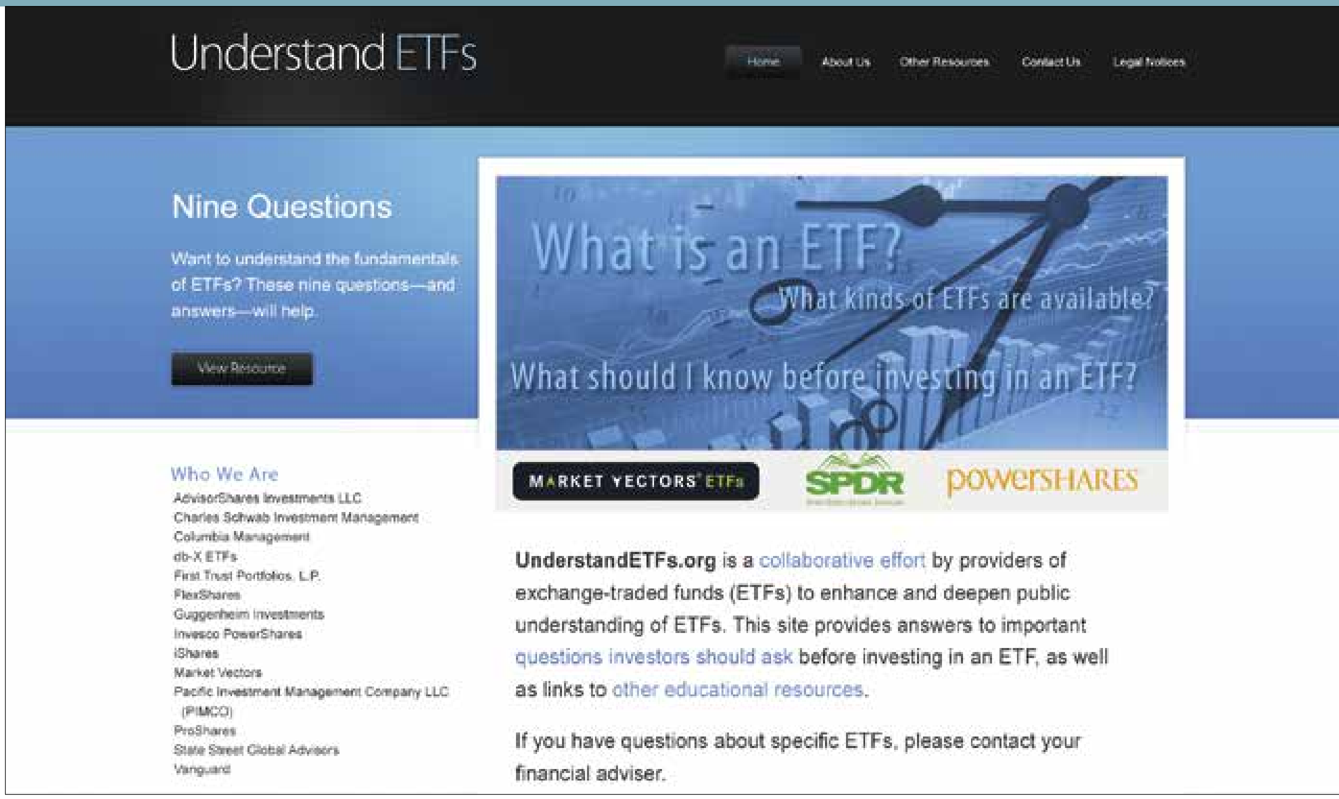
Along with the growth of the product, the importance of educating the public about ETFs has risen. In 2011 and 2012, ICI and its members advanced that mission.

Given the vibrant and multifaceted nature of the ETF market, these educational efforts are aimed at a number of different audiences, including those who are just beginning to learn about ETFs and their benefits. ICI has developed dedicated resources for ETFs, launching an online resource center featuring information on ETFs, material on recent ETF developments, ICI research and statistics, and links to third-party sites of interest. The Institute also published documents answering frequently asked questions (FAQs) on several topics: ETF basics and structure, comparisons of ETFs to other investments, important considerations for retail investors, and the U.S. ETF market.

In addition, ICI's ETF Committee, working together and under the leadership of James E. Ross, ICI Governor and Senior Managing Director and Global Head of ETFs at State Street Global Advisors, collaborated with ICI staff to develop educational materials on those key aspects of ETFs that everyone should understand before investing in ETFs. The committee endorsed plans for promoting this material at a new, dedicated website, unveiled in the fourth quarter of calendar 2012.

ICI also continued its outreach to policymakers, as regulators and legislators examined ETFs and their expanding presence in the marketplace. "Changes in technology, regulation, and trading practices are transforming today's financial markets," ICI said in response to an October 2011 Senate hearing on market structure and ETFs. "Any analysis of those market changes that singles out ETFs—without looking at all of these forces in the light of hard data—is premature and simplistic."

ICI conveyed that message in the past year to another key audience, the news media. Reporting and commentary around ETFs have given critics the occasional opportunity to level inaccurate charges at ETFs, particularly the suggestion that ETFs are responsible for driving stock market volatility to unprecedented extremes. In *ICI Viewpoints*, ICI Senior Economist Rochelle L. Antoniewicz countered such charges with posts that presented a careful examination of the data. Among other things, Antoniewicz's analysis put recent equity market volatility into historical context and showed that macroeconomic events—not particular market instruments—offer far more plausible explanations for episodes of volatility.



UnderstandETFs.org addresses questions investors should ask before investing in exchange-traded funds.

Finally, given growing research interest in ETFs, ICI engaged with the academic community. At the fall 2011 Investment Company Institute/AIM Investment Center Academic and Practitioner Conference at the University of Texas at Austin, finance professors and industry professionals exchanged views on ETFs at a session titled "Pros and Cons of Exchange-Traded Funds."

With their benefits to investors, ETFs undoubtedly will continue to gain prominence in the investing landscape. ICI will further its efforts to ensure that investors have the information they need to make the most of those benefits.

For more information on ETFs, please visit ICI's Exchange-Traded Funds Resource Center at www.ici.org/etf_resources and the new ETF educational website at UnderstandETFs.org. ICI Viewpoints *posts covering ETF issues are available at www.ici.org/viewpoints?tag=Exchange-Traded+Funds.*

Along with the growth of the product, the importance of educating the public about ETFs has risen.

QUESTION & ANSWER

With the Chair of the Independent Directors Council

DOROTHY A. BERRY

At the beginning of your tenure in 2010, you said it was not just a busy time for directors, but an uncertain time as well. Do you think some of the uncertainty has dissipated?

Directors were wondering what would come out of all of the rulemakings and studies required under Dodd-Frank [the Dodd-Frank Wall Street Reform and Consumer Protection Act] and where our work would be affected. Although the Securities and Exchange Commission (SEC) has completed many of its requirements, there is still unfinished business. There is also new leadership at the SEC Division of Investment Management, and money market fund reform continues to be a subject of high interest. All in all, I'd say some uncertainty still remains for directors, albeit much less than there was two years ago.

Can you talk a bit about how the Independent Directors Council (IDC) contributed to the recent debate on changes to money market funds?

IDC was active in providing the voice of fund directors on this significant issue. Directors—as well as the entire industry—were supportive of the SEC's 2010 amendments, particularly directors' ability to suspend redemptions to protect investors when a fund was under pressure. Since 2010, the financial system has absorbed a considerable amount of stress—the U.S. debt ceiling crisis, the historic downgrade of the U.S. credit rating, and the ongoing European debt crisis—and we've all seen how well money market funds responded. The amendments did what they were intended to do: make these funds more resilient.

We were deeply concerned about additional changes to the structure of money market funds reportedly being considered by the SEC—for example, floating the net asset value or redemption restrictions and capital requirements. For the first time, IDC issued a joint statement with the Mutual Fund Directors Forum to underscore our grave concerns about the potential collateral consequences and negative impacts that these changes could have on investors, on capital markets, and on the economy in general.

What does IDC do to help directors understand the implications of other policy issues?

Amy [B. R. Lancellotta, Managing Director of IDC] and her team do a great job of keeping directors informed about industry and policy developments in a number of ways: discussions at chapter meetings, memoranda through *ICI Daily*, summaries in *Board Update,* panels at conferences, and IDC staff presentations to fund boards.

In addition, IDC acts as the voice of the fund director community to policymakers on issues affecting boards. Through comment letters, testimony, and commentary on *ICI Viewpoints*, IDC weighed in on derivatives, mandatory audit firm rotation, and Commodity Futures Trading Commission regulations, among other issues.

How does IDC work to inform the media about the role of fund directors?

Unfortunately, from time to time there are articles about the fund industry that mischaracterize the role and

Dorothy A. Berry, Chair, Independent Directors Council; Independent Trustee, PNC Funds; Independent Chair, Professionally Managed Portfolios

"IDC acts as the voice of the fund director community to policymakers on issues affecting boards. Through comment letters, testimony, and commentary...IDC weighed in on derivatives, mandatory audit firm rotation, and Commodity Futures Trading Commission regulations."

> It’s a critical mission of IDC to promote public understanding of the role of fund directors, and we will continue to be vigilant on this front.
>
> Dorothy A. Berry

practices of fund directors. We saw it a couple of times this past year, and it’s certainly frustrating. IDC issued prompt and vigorous responses. We pointed out that the duties of independent directors are highly regulated, and that independent directors are robustly independent—they provide strong oversight of fund performance and fees—that their compensation is transparent, and that board oversight of multiple funds in a complex is a benefit to shareholders. It’s a critical mission of IDC to promote public understanding of the role of fund directors, and we will continue to be vigilant on this front.

The fund independent director community is highly diverse on many levels. How has IDC responded to the challenge it faces serving such a diverse group?

I’m glad you asked that because this is a really important area. There are nearly 2,000 independent directors of ICI member funds, and there is great diversity among them in terms of directors’ professional backgrounds, size of the funds they represent, nature of their funds’ sponsors, and distribution channels their funds rely on. All directors have access to IDC’s services, and to IDC staff.

IDC is led by a Governing Council of independent directors, and they are all high-caliber professionals who reflect the diversity of our community. Governing Council members make a concerted effort to ensure that our positions on policy matters express the views of the overall director community, and that communications and educational resources serve all fund directors.

What are some of the educational offerings IDC provided during your tenure?

I am very proud of the exceptional educational programs IDC has offered. IDC’s premier event is the fall conference for fund directors. We have continued to offer stellar programs with outstanding speakers at these big gatherings—but we set aside time for directors to engage in small group discussions. IDC also has enhanced its webinar program, which has proven very successful. Directors can dial in from anywhere at no cost to learn about topics like target date funds, audit committee practices, litigation and insurance, and legislative developments.

We also continued to publish papers offering practical guidance for directors. *Fundamentals for Newer Directors*, which is targeted to directors with up to five years of experience, is a dynamic resource that helps newer directors understand their role and responsibilities. Other published papers include *Fund Board Oversight of Risk Management, Board Oversight of Exchange-Traded Funds,* and *Overview of Fund Governance Practices, 1994–2010*. We’ve also made successful upgrades to IDC’s website and *Board Update*, our monthly e-newsletter.

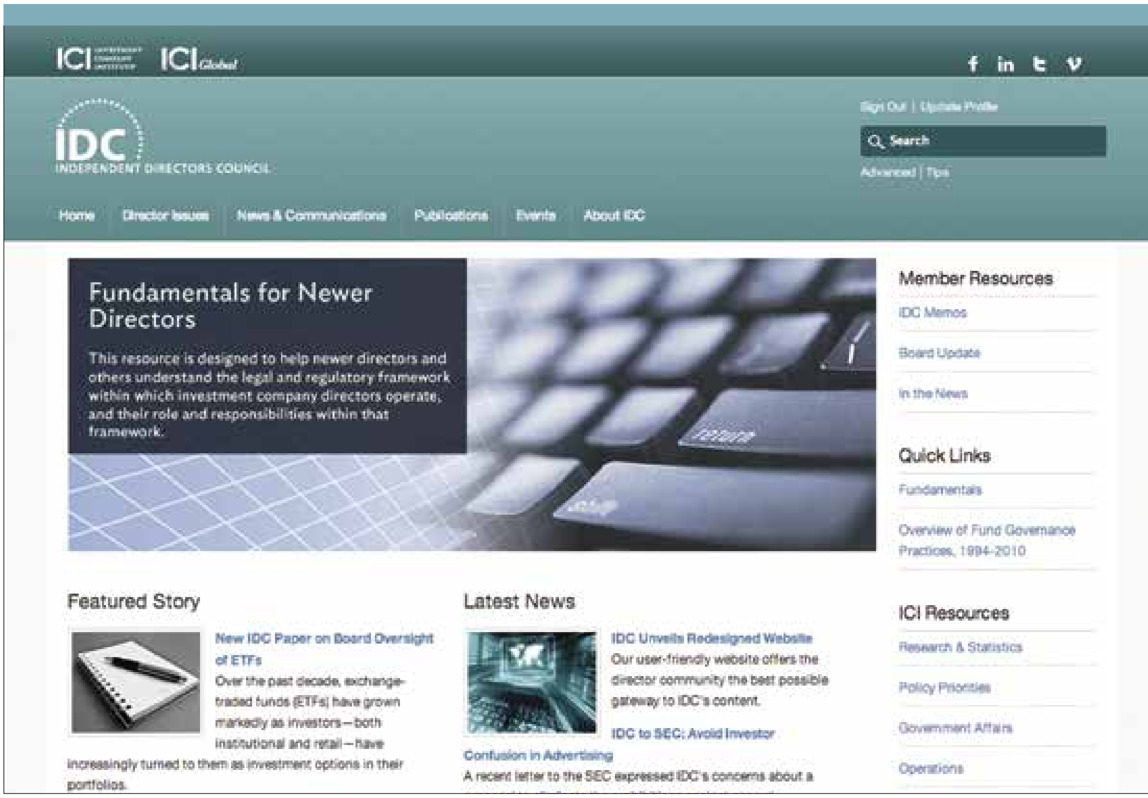
I’m also pleased about the continued growth of our chapter meetings. Annette [Capretta, Deputy Managing Director of IDC] really has developed the chapter meetings into the robust program we have today. Chapter meetings are extremely important in cultivating our member community all across the country. These meetings are informal—and free—and they offer directors an opportunity to discuss with each other important topics relating to fund board oversight, including governance practices and implementation of new regulatory requirements. The conversations that arise out of these meetings help us to identify the educational offerings directors are looking for.

The success of IDC's programs is attributable not only to the hard work of IDC's Governing Council and the staff of IDC and ICI, but also to the independent directors and other colleagues who volunteer their time to participate on a panel, contribute their expertise to a webinar, or provide input for an IDC paper. I am grateful to so many of my colleagues, who have supported—in tangible ways—IDC's mission to advance director education.

Any final thoughts for your successor, Susan B. Kerley, Independent Chair, MainStay Funds and Independent Director, Legg Mason Partners Funds?

Throughout her career, Susan has served shareholders and the independent director community with distinction. She also has been instrumental in building IDC into the organization it is today. She doesn't need any guidance from me! But she can rely upon me to continue to be involved and help her lead IDC to accomplish even more.

For more information about the Independent Directors Council, please visit www.idc.org.



QUESTION & ANSWER

With the Chair of the Small Funds Committee

SUSAN B. McGEE

Small funds, which ICI defines as fund groups with total long-term assets of less than $5 billion, remain a vital part of the fund industry's competitive landscape and a key part of the Institute's membership. Why is that?

There are several reasons, but broadly, I'd say, value to investors. Managers of small funds often excel at bringing specialized expertise to the market. Larger companies may have the advantage when it comes to innovating and developing new products, like exchange-traded funds. But from a pure money management standpoint, smaller firms can and do provide their own successful twist on some of the asset classes.

Take my firm, U.S. Global Investors. We specialize in global resources, gold, and emerging markets. In a big company, that may be some of what they do, but it's all of what we do. Our focus allows us to really dig down in those niches.

Small funds also are especially well suited to building and leveraging shareholder relationships. They're very grateful when they get investors—they want to hold on to them! Not that the larger firms do this poorly; it's just that a smaller scale gives a chance to create very personal bonds. At our shop, we have individual shareholders and advisers who have been with us for years and years. We know them personally. We know their kids.

Small funds also face a set of distinct challenges. Tell us about those.

Small funds certainly have unique challenges. One of the biggest, of course, is trying to get economies of scale, so you can better absorb costs. This is especially tough these days as costs rise with more and more regulatory requirements. Small funds have to comply just as the larger funds do.

Smaller complexes also tend to have fewer resources, and that means you're not always able to hire expertise when you might need it. Like in any smaller business, people in small funds often have to wear multiple hats. The increasing use of social media is a good example. Bigger firms could hire an expert or even create a whole team to figure out Twitter and Facebook and the rest. But that probably isn't an option for most of the smaller firms. Your social media "team" might be your head marketing person, who now has that responsibility stacked on top of his or her regular job.

In what ways does ICI help you and others in the small funds community cope with these challenges?

One way is the information that ICI provides. As I said, we in the small funds community can't always have in-house expertise, so having access to ICI's perspective is all the more important. As a lawyer, I find that the memos ICI produces are extremely valuable.

But ICI resources aren't just about law or policy. At our committee events, we've had representatives from the largest platforms come to talk about their business models, and specifically about aspects that relate to small funds. We've also gotten financial advisers to discuss what they look for in a fund before they recommend it, and we've gotten marketing and advertising folks to share ways to get your brand recognized—solutions that don't cost an arm and a leg.

Susan B. McGee, ICI Governor; Chair, Small Funds Committee; President and General Counsel, U.S. Global Investors, Inc.

> "We in the small funds community can't always have in-house expertise, so having access to ICI's perspective is all the more important."

> "I know our input is welcome for legislators and regulators in Washington, DC, too—they're very concerned about the challenges facing small business, because that's the backbone of the American economy."
>
> Susan B. McGee

I think ICI also helps foster the community of small funds complexes in a good way. Sometimes small funds can feel isolated, like David against Goliath. Through ICI and the Small Funds Committee, people with broad knowledge of the business come together to share noncompetitive ideas on how to cope with business challenges and keep costs in check in ways that don't raise competitive issues. That kind of networking is critical, particularly for small firms. I have contacts at 25 to 30 small funds complexes that I can pick up the phone and call.

Finally, ICI acts as a channel from our community to the regulators. Participating on panels, going up on Capitol Hill, testifying before the Securities and Exchange Commission—it's so important to provide our input on how proposals will affect small funds complexes. I know our input is welcome for legislators and regulators in Washington, DC, too—they're very concerned about the challenges facing small business, because that's the backbone of the American economy.

You've served on the Small Funds Committee for several years, including as its Chair since 2009. How has the committee changed in your experience?

What's changed is how members interact on the committee. When I first joined, it seemed like few members were eager to speak up and share. Now I see a lot more sharing. That's a testament to the strong, talented group of people we have on the committee. I also think it's a result of ICI paying more attention to helping the small funds and including them in various aspects of ICI activity, whether it's receiving information or sharing our views with regulators.

What will be the key topics for the Small Funds Committee in the coming months?

We'll focus on a number of regulatory concerns, such as changes in advertising rules. I'm sure fund distribution also will remain at the top of the agenda. This is a perennial challenge for small funds, which don't have the brand recognition of bigger companies. That said, I see the distribution issue changing a bit for the better for small funds, thanks to the growth of registered investment advisers (RIAs). RIAs want to find undiscovered managers for their clients.

Changes in social media also must have had a positive impact, in terms of name recognition.

Huge. I look at the experience of our firm. We've always created educational materials, because we're in specialty areas. And we've always educated people on coping with market volatility and other topics. In the old days, we'd print out the material and mail it. Now we not only can put it on our website, we can also post it on our blog, tweet it, and put it on Facebook. We can reach a much wider audience, and it's all very low cost. We have 60 sites where we syndicate our blog, and together they reach about 25 million viewers. This really has helped us to increase our footprint.

So how do small funds grow their way out of being small funds?

That's the funny thing about the Small Funds Committee—it's the only one at ICI that members are hoping to graduate from! I think the formula is pretty simple: have a very good product and get recognition to attract flows and good people. And I see very talented people going to small firms. They want to make a difference, and you definitely can make a difference in a small company. You can see the impact that your work has immediately on the bottom line or in development of the business strategy. You get the simple fulfillment of building something.

To learn more about ICI's Small Funds Committee, please contact Peter G. Salmon, ICI Senior Director of Operations and Technology, at salmon@ici.org or 202-326-5869.

Andrew J. Bowden, U.S. Securities and Exchange Commission; ICI Governor and Small Funds Committee Chair Susan B. McGee, President and General Counsel, U.S. Global Investors, Inc.; and Peter G. Salmon, Senior Director, Operations and Technology, ICI participate in a panel discussion at the Small Funds Committee Meeting in May 2012.

Engaging Politically: The Chairman's Council and ICI PAC

Whether advancing legislation, holding hearings, or corresponding with regulators, lawmakers on Capitol Hill can have a significant—and sometimes an immediate and decisive—impact on investors. Accordingly, the fund industry must participate actively in the political process by supporting those who understand funds and fund investing, and who support public policies that benefit fund shareholders.

Since 1995, ICI has developed the fund industry's political engagement through the Chairman's Council. Taking a systematic, transparent, and bipartisan approach, the Chairman's Council provides several ways for ICI members to make their presence felt in the political arena. At the beginning of each year, the Chairman's Council sets fundraising goals for all aspects of the political program and approves a list of members of Congress who will be eligible to receive contributions from the ICI Political Action Committee, or ICI PAC. ICI Governor Robert S. Dow, Chairman, Lord Abbett Mutual Funds, has chaired the Chairman's Council since 2011.

At ICI, the work of the Chairman's Council is now managed by George F. Shevlin IV, ICI's Political Affairs Officer. Shevlin joined ICI in June 2012, succeeding James R. Hart, who retired after six distinguished years with the Institute. Shevlin brings to his role at ICI more than 20 years of experience in tax, financial services, and other business issues on Capitol Hill. Notably, he served as Staff Director for the Committee on House Administration, which has jurisdiction over campaign finance and election laws. Over his career, Shevlin and worked for Representatives John Larson (D-CT), Jay W. Johnson (D-WI), and Doug Applegate (D-OH). Shevlin was a member of the senior leadership staff in the last three Congresses.

With Dow and Shevlin at the helm, the Chairman's Council has built on its successful track record of fundraising. Thanks to support from ICI member companies and their employees, the Chairman's Council has raised more than $1 million so far in 2012 and is well on its way to meeting its goal for the year, $1.3 million.

To accomplish its goals, the Chairman's Council offers ICI members several flexible options for participation, one of which is donating to ICI PAC. By aggregating funds to contribute to the campaigns of incumbent members of Congress, ICI PAC can provide support to lawmakers who have expressed strong interest in the fund industry.

ICI members also can contribute directly to a member of Congress on the Chairman's Council list of recommended candidates. This list includes one Democrat and one Republican from each house of Congress. They are selected because of their knowledge of the fund industry and their presence on committees of importance to ICI.

Finally, ICI members can participate in one or more of the fundraising events hosted each year by ICI PAC in support of incumbent members of Congress, with all contributions generated by those events going directly to the candidates. By the end of calendar 2012, ICI PAC will have hosted fundraisers for six Democrats and six Republicans seeking reelection to the House or Senate.

To find out more about the Chairman's Council and ICI PAC, please contact ICI Political Affairs Officer George F. Shevlin IV at george.shevlin@ici.org or 202-326-5892.

CLOCKWISE FROM TOP LEFT:
Representative Paul D. Ryan (R-WI) gives a political overview at an ICI event held on his behalf on June 20, 2012.
Senator Mark Warner (D-VA) and ICI General Counsel Karrie McMillan chat at an event held in his honor at ICI on October 9, 2012.
Senator Patrick J. Toomey (R-PA) gives the keynote speech at the Eighth Annual ICI Leadership Dinner on May 9, 2012.
Senator Kirsten Gillibrand (D-NY) addresses attendees at an event hosted by ICI PAC on February 28, 2012.

> "The Chairman's Council has proven very helpful in establishing and maintaining an effective dialogue with members of Congress who understand the importance of funds to America's investors."

Robert S. Dow
ICI Governor and Chairman, Chairman's Council
Chairman, Lord Abbett Mutual Funds

Lasting Values—Challenging Times

With the 54th Annual General Membership Meeting (GMM), ICI once again hosted the world's premier fund industry gathering. Building on ICI's stellar record, the 2012 event offered the broad perspective of GMM with specialized programming at three concurrent conferences—the Operations and Technology Conference, the Mutual Fund Compliance Programs Conference, and IDC's Investment Company Directors Workshop.

Each year, this robust program draws record crowds and engages industry leaders. But there's more to GMM than the conferences: GMM has grown to become mutual fund week in Washington, DC. ICI's Eighth Annual Leadership Dinner, an invitation-only event, provided an opportunity for members to connect with key Administration officials, and featured a keynote address by Patrick J. Toomey, U.S. Senator from Pennsylvania. The event provided an opportunity for industry leaders to build relationships and to share perspectives with key policymakers. Many members of Congress attended from both chambers and both parties. In addition, ICI's Board of Governors, IDC's Governing Council, and numerous ICI committees gathered to analyze governance issues and to set ICI's policy agenda.

ICI Governor Mellody Hobson, President of Ariel Investments and Chair of the 2012 GMM Planning Committee, underscored the theme—Lasting Values, Challenging Times—in her opening remarks. In challenging times, she noted, it is more important than ever to adhere to the values that made the fund industry great. The values the industry encourages in investors—thrift, patience, and prudence—must be reflected in the way the fund industry conducts itself, Hobson said. She urged attendees to ensure good corporate citizenship and to continue to put investors first. "We also need to renew our commitment to a cause that's near to my heart—the challenge of financial education for all Americans," Hobson said.

Continuing the theme of education, U.S. Secretary of Education Arne Duncan joined ICI President and CEO Paul Schott Stevens for a dialogue about the state of the American educational system in the Eighth Annual Policy Forum. Focusing on the role American business can play in improving our educational system and preparing students to compete in a global economy, Duncan also encouraged the business community to help students become financially literate.

In a question-and-answer session with Hobson, SEC Chairman Mary Schapiro also discussed financial literacy, arguing that both policymakers and the industry must do a better job of providing financial education for Americans of all ages. In addition, Hobson and Schapiro debated market structure and the SEC's approaches to further regulatory changes to money market funds. Schapiro reiterated her belief that although the SEC, working with the industry, made great strides with the 2010 reforms to money market fund regulation, "We have a long way to go."

In his opening remarks, ICI President and CEO Paul Schott Stevens spoke about ICI's role in the policy arena, asserting that funds' obligations to investors include for ICI a duty to advance shareholders' public policy interests. "One result of putting shareholders first is that ICI and its members have always taken an affirmative approach to regulation," he said. "Nonetheless, there are occasions when we have fundamental differences with

ICI Governor Mellody Hobson, President of Ariel Investments and Chair of the 2012 GMM Planning Committee, engages in a question-and-answer session with SEC Chairman Mary Schapiro.

> "We can meet the challenges so long as we are constantly guided by the values that serve investors, the values that build our economy and our nation—the values that are lasting."

Mellody Hobson

the SEC or other regulators. We work especially hard, in those cases, to substantiate our views; to demonstrate how investor interests will be best served; to commend a sensible balance between the costs and benefits of regulation; and to demonstrate how regulators might best fulfill their statutory mandates—in the SEC's case, to promote efficiency, competition, and capital formation."

Howard Schultz, Chairman, President, and CEO of Starbucks, addressed the GMM luncheon. He recalled the turning point in the company's comeback: focusing on values, especially community service, was critical. He argued that more companies should follow in the footsteps of Starbucks. "We can't wait for Washington, and we have to recognize that we have a responsibility to the country, to the communities we serve. Shareholder value is not only based on making a profit."

Attracting representatives from government, the media, and the wider business community—including financial industry leaders from 22 countries—GMM's comprehensive program provided attendees the opportunity to consider pressing issues from different points of view. Several of the sessions were joint endeavors of the concurrent conferences. In "Minimizing the Risks of Litigation, Regulatory Proceedings, and Operational Errors," a joint session of the Investment Company Directors Workshop and the Mutual Fund Compliance Programs Conference, panelists agreed that well-established processes are indispensable. "It is remarkable how much a focus on process can do to reduce risk of regulatory, litigation, and even operational errors," said Daniel T. Steiner, Executive Vice President and General Counsel at ICI Mutual Insurance Company.

Social media was a hot topic this year, with many panels debating its proper use for funds. In a joint GMM–Operations and Technology Conference session, for example, Paul Hatch, Head of Investment Strategy and Client Solutions at Morgan Stanley Smith Barney, said, "I think it will fundamentally change everything we do. It's not a fad; it's changing the way we as humans communicate with each other."

GMM also hosted representatives of the entertainment media and the press. In "Managing Chaos," the closing session of the 2012 GMM, Hobson interviewed George Lucas, founder of Lucasfilm and director of the *Star Wars* trilogy. They reflected on the similarities and differences between the film and investment industries. The differences may seem obvious, but both industries must deal with one important problem: unpredictability.

In "The Media, the Medium, and the Message," Hobson engaged with Arianna Huffington, President and Editor in Chief of the *Huffington Post*; Gillian Tett, U.S. Managing Editor of the *Financial Times*; and ICI Governor F. William McNabb III, Chairman and CEO of Vanguard. The panel discussed how the industry could best enlist the media to educate and inform investors, and how to incorporate "new media" strategies. One challenge, Huffington said, is to rebuild trust after the financial crisis, and social media can be a great way to do that.

Indeed, the importance of maintaining investors' trust during challenging times was a recurring theme. As Stevens noted, "We wouldn't deserve that trust if we didn't devote our energies ceaselessly and tirelessly to providing the skills, the services, and the advocacy on vital public policy issues that our investors need. I'm confident that, working together, we all will continue to earn that trust." He quoted ICI Governor Paul G. Haaga Jr., former ICI Chairman and Chairman of Capital Research and Management, as saying, "As soon as shareholders don't come first, mutual funds won't be the investment of choice—and we won't deserve to be."

For information on ICI's 55th Annual General Membership Meeting, please visit http://gmm.ici.org.

CLOCKWISE FROM TOP LEFT:

Arianna Huffington, President and Editor in Chief of the *Huffington Post*; ICI Governor F. William McNabb III, Chairman and CEO of Vanguard; and Gillian Tett, U.S. Managing Editor of the *Financial Times,* participate in a panel discussion titled “The Media, the Medium, and the Message.”

Howard Schultz, Chairman, President, and CEO of Starbucks, gives the keynote address at the GMM luncheon.

Paul G. Haaga Jr., ICI Governor and Chairman, Capital Research and Management, moderates the GMM Leadership Panel with Marie A. Chandoha, President and CEO, Charles Schwab Investment Management, Inc.; Gregory Fleming, President, Morgan Stanley Smith Barney and President, Morgan Stanley Investment Management; Ronald O’Hanley, President, Asset Management and Corporate Services, Fidelity Investments; and Kenneth Olivier, Chairman and CEO, Dodge & Cox.

U.S. Secretary of Education Arne Duncan joins ICI President and CEO Paul Schott Stevens for a dialogue about the state of the American educational system in the Eighth Annual Policy Forum.

“[SOCIAL MEDIA] WILL FUNDAMENTALLY CHANGE EVERYTHING WE DO. IT’S NOT A FAD; IT’S CHANGING THE WAY WE AS HUMANS COMMUNICATE WITH EACH OTHER.”

Paul Hatch
Head of Investment Strategy and Client Solutions
Morgan Stanley Smith Barney

Appendices

APPENDIX A

Organization and Finances

Organization

ICI is a 501(c)(6) organization that represents registered investment companies on regulatory, legislative, and securities industry initiatives that affect funds and their shareholders.

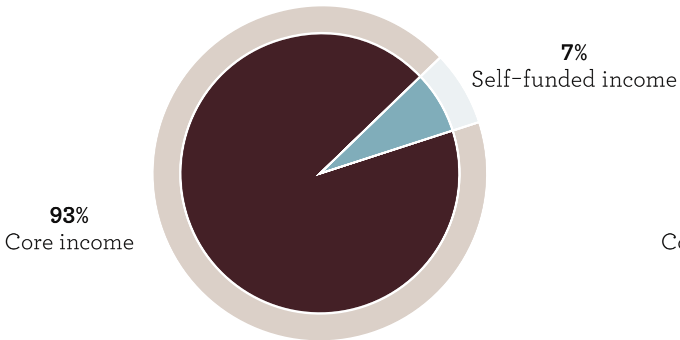
ICI members include mutual funds, exchange-traded funds, closed-end funds, sponsors of unit investment trusts, and their investment advisers and principal underwriters. The ICI president and staff report to the Institute's Board of Governors, which is responsible for overseeing the business affairs of ICI and determining the Institute's positions on public policy matters (see Appendix B, page 48).

ICI's Board of Governors is composed of 61 members, representing ICI member companies and independent directors of investment companies. Governors are elected annually to staggered three-year terms. The Board is geographically diverse and includes representatives from large and small fund families as well as fund groups sponsored by independent asset managers, broker-dealers, banks, and insurance companies. This broad-based representation helps to ensure that the Institute's policy deliberations consider all segments of the fund industry and all investment company shareholders.

Five committees assist the Board of Governors with various aspects of the Institute's affairs. These five include an Executive Committee—responsible for evaluating policy alternatives and various business matters and making recommendations to the Board of Governors—as well as Audit, Compensation, Investment, and Nominating Committees. Other than the Institute's president, who is a member of the Executive Committee, all members of these committees are Governors. The Board also has appointed a Chairman's Council to administer the Institute's political programs, including the political action committee, ICI PAC (page 38). The Chairman's Council includes seven Governors and the Treasurer of ICI PAC. The Institute's president serves as an ex officio member. The Institute employs a staff of 163 (see Appendix E, page 50).

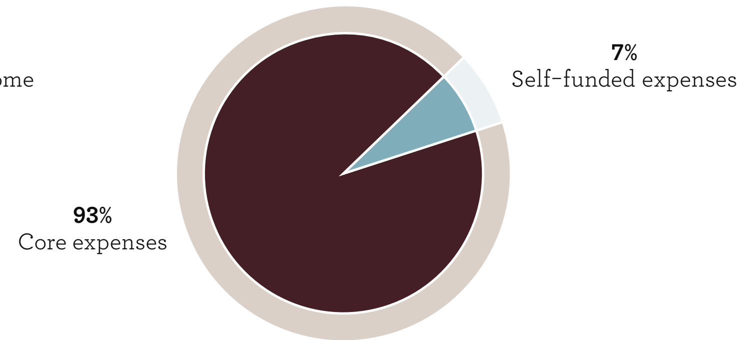
ICI addresses the needs of investment company independent directors through the Independent Directors Council (Appendix C, page 49). IDC organizes educational programs, keeps directors informed of industry and regulatory developments, and assists in the

FIGURE 1



TOTAL REVENUES
FY 2012 = $60,756,597

FIGURE 2



TOTAL EXPENSES
FY 2012 = $56,407,656

development and communication of policy positions on key issues for fund boards.

Seventeen standing committees, bringing together more than 1,700 industry professionals, guide the Institute's policy work. ICI standing committees perform a number of important roles, including assisting with formulation of policy positions as well as gathering and disseminating information on industry practices (see Appendix D, page 49). In addition, 29 industry advisory committees, task forces, forums, and working groups with more than 2,300 participants tackle a range of regulatory, operations, and business issues. In all of its activities, ICI strictly observes federal and state antitrust laws, in accordance with a long-standing and well-established compliance policy and program.

Finances

Throughout its history, the Institute has sought to prudently manage its financial affairs in a manner deemed appropriate by the Board of Governors, which is responsible for approving ICI's annual budget and its member net dues rate. The Board of Governors considers both the Institute's core and self-funded activities when approving the annual net dues rate.

Core activities are related to public policy and include regulatory, legislative, operational, economic research, and public communication initiatives in support of investment companies and their shareholders, directors, and advisers. Reflecting the Institute's strategic focus on issues affecting investment companies, the Board of Governors has chosen to fund core activities with dues rather than seek alternative sources of revenues, such as sales of publications. The significant majority of ICI's total revenues, 93 percent, comes from dues, investment income, royalties, and miscellaneous program sources (see Figure 1). Similarly, by design, 93 percent of the Institute's total resources are devoted to core activities (see Figure 2).

Core expenses support the wide range of initiatives described in this report. Self-funded activities (e.g., conferences, special surveys) are supported by separate fees paid by companies and individuals who participate in these activities. The financial goal for self-funded activities is that fees should cover all direct out-of-pocket costs and provide a margin to cover associated staff costs to ensure that these activities are not subsidized by member dues.

ICI Unaudited Financial Statements

Statement of Financial Position

as of September 30, 2012

ASSETS	
Cash and cash equivalents	$1,414,047
Investments, at market value	50,997,554
Accounts receivable	655,289
Prepaid expenses	2,174,410
Other assets	955,556
Furniture, equipment, and leasehold improvements; net (less accumulated depreciation of $9,453,007)	5,332,998
Total assets	$61,529,854
LIABILITIES AND NET ASSETS	
Liabilities	
Payroll and related charges accrued and withheld	28,615,397
Accounts payable and accrued expenses	3,422,017
Deferred revenue	1,417,745
Rent credit	3,974,533
Deferred rent	2,769,704
Total liabilities	40,199,396
Net Assets	
Undesignated net assets	21,108,218
ICI Global net assets	(777,760)
Board designated net assets	1,000,000
Total net assets	21,330,458
Total liabilities and net assets	$61,529,854

Statement of Activities and Changes in Net Assets

for the year ended September 30, 2012

CORE INCOME	
Membership dues	$52,864,754
Investment income	1,248,709
Royalty income	865,093
Program income	1,239,337
Total core income	56,217,893
CORE EXPENSES	
Administrative expenses	43,440,926
Program expenses	6,202,255
Depreciation and lobby proxy tax	2,773,444
Total core expenses	52,416,625
Change in net assets—core	3,801,268
SELF-FUNDED INCOME	
Conferences	3,590,555
Other self-funded income	948,149
Total self-funded income	4,538,704
SELF-FUNDED EXPENSES	
Conferences	3,256,782
Other self-funded expenses	734,249
Total self-funded expenses	3,991,031
Change in net assets—self-funded	547,673
Change in net assets from operations	4,348,941
ICI Global, net	(537,448)
Non-operating expenses	(972,399)
Actuarial pension/postretirement plan loss	(2,802,490)
Change in net assets	36,604
Net assets, beginning of year	21,293,854
Net assets, end of year	$21,330,458

These financial statements are preliminary unaudited statements as of September 30, 2012. Audited financial statements for the fiscal year ended September 30, 2012, will be available after February 1, 2013. To obtain copies of the audited statements, please contact Mark Delcoco at 202-326-5974.

2012 ICI Executive Committee

SEATED: Susan B. Kerley, George C. W. Gatch, John F. Cogan Jr., Martin L. Flanagan, John W. McGonigle

STANDING: Robert S. Dow, Mark R. Fetting, F. William McNabb III, Paul Schott Stevens, Gregory E. Johnson, Dorothy A. Berry, James A. McNamara, Jacques P. Perold

NOT PICTURED: Edward C. Bernard, Mellody Hobson

> "By pooling our resources, we have built an organization that brings outstanding skills in economic analysis, legal insight, operational expertise, and advocacy to bear....The strong involvement of ICI's members allows us to leverage our individual firms' knowledge and talents to attain far greater results."

Gregory E. Johnson
Chairman, Investment Company Institute
President and CEO, Franklin Resources, Inc.

APPENDIX B

ICI Board of Governors

As of September 30, 2012

Gregory E. Johnson[2,3,4,6,7]
ICI Chairman
President and CEO
Franklin Resources, Inc.

Edward C. Bernard[2,6,7]
ICI Vice Chairman
Vice Chairman
T. Rowe Price Group, Inc.

Paul L. Audet
Senior Managing Director
BlackRock, Inc.

Ashok N. Bakhru
Independent Chair
Goldman Sachs Funds

Jonathan R. Baum
Chairman and CEO
The Dreyfus Corporation

Dorothy A. Berry[2,5]
Independent Trustee
PNC Funds
Independent Chair
Professionally Managed Portfolios

James H. Bodurtha[1,3]
Independent Director
BlackRock Funds

Mary K. Bush
Independent Director
Pioneer Funds

Marie A. Chandoha
President and CEO
Charles Schwab Investment Management, Inc.

John F. Cogan Jr.[2]
Chairman
Pioneer Investment Management USA Inc.

Michael J. Cosgrove
President of Mutual Funds and Global Investment Programs
GE Asset Management, Inc.

Patrick P. Coyne
President
Delaware Investments

Bruce L. Crockett[1]
Independent Chair
Invesco Funds

James E. Davey[1]
President, Hartford Mutual Funds
The Hartford Financial Services Group, Inc.

Robert S. Dow[1,2,4,6]
Chairman, Lord Abbett Mutual Funds
Lord, Abbett & Co. LLC

Kenneth C. Eich
Chief Operating Officer
Davis Selected Advisers, L.P.

Ralph C. Eucher[1]
Chairman
Principal Funds

Thomas E. Faust Jr.[4]
Chairman and CEO
Eaton Vance Corporation

Mark R. Fetting[2,6]
Chairman and CEO
Legg Mason, Inc.

Martin L. Flanagan[2,7]
President and CEO
Invesco Ltd.

George C. W. Gatch[2,3,6]
CEO, JPMorgan Funds
JPMorgan Asset Management

C. Gary Gerst
Independent Chair
Henderson Global Funds

William F. Glavin Jr.
Chairman, President, and CEO
OppenheimerFunds, Inc.

John T. Hailer
President and CEO, U.S. and Asia
Natixis Global Asset Management, L.P.

Peter A. Harbeck[1]
President and CEO
SunAmerica Asset Management Corp.

Brent R. Harris[4,6]
Chairman
PIMCO Funds

Diana P. Herrmann
President and CEO
Aquila Investment Management LLC

Mellody Hobson[2,6]
President
Ariel Investments, LLC

Robert M. Keith
Executive Managing Director
AllianceBernstein

Susan B. Kerley[2]
Independent Chair
MainStay Funds
Independent Director
Legg Mason Partners Funds

John Y. Kim
Chief Executive Officer
New York Life Investments

Robert J. Manning
Chairman and CEO
MFS Investment Management

Susan B. McGee
President and General Counsel
U.S. Global Investors, Inc.

John W. McGonigle[2,6]
Vice Chairman
Federated Investors, Inc.

F. William McNabb III[2]
Chairman and CEO
Vanguard

James A. McNamara[2]
President and CEO
Goldman Sachs Mutual Funds

Thomas M. Mistele[1]
Chief Operating Officer
Dodge & Cox

Catherine L. Newell
General Counsel
Dimensional Fund Advisors LP

Stuart S. Parker
President
Prudential Investments

Jacques P. Perold[2]
President
Fidelity Management & Research Company

Donald H. Pratt
Independent Chair
American Century Funds, Kansas City Board

Karla M. Rabusch
President
Wells Fargo Funds Management, LLC

J. Alan Reid[1]
Chief Executive Officer
Forward Management LLC

Robert L. Reynolds
President and CEO
Putnam Investments

James E. Ross
Senior Managing Director and Global Head of ETFs
State Street Global Advisors

Thomas S. Schreier Jr.[3]
Vice Chairman, Wealth Management
Nuveen Investments

Michael D. Strohm[3]
Chief Executive Officer
Waddell & Reed, Inc.

Jonathan S. Thomas
President and CEO
American Century Investments

Garrett Thornburg
Chairman
Thornburg Investment Management, Inc.

William F. Truscott[4]
CEO, Global Asset Management
Columbia Management

Mary Ann Tynan
Independent Director
Oppenheimer Funds

Robert W. Uek
Independent Trustee
MFS Funds

Lloyd A. Wennlund
Executive Vice President and Managing Director
Northern Trust Global Investments

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[1]Governor on Sabbatical
[2]Executive Committee member
[3]Audit Committee member
[4]Investment Committee member
[5]Chairman of the Independent Directors Council
[6]Chairman's Council member
[7]ICI Education Foundation Board member

APPENDIX C

Governing Council of the Independent Directors Council

As of September 30, 2012

Ashok N. Bakhru*
Independent Chair
Goldman Sachs Funds

Dorothy A. Berry*
IDC Chair
Independent Trustee
PNC Funds
Independent Chair
Professionally Managed Portfolios

James H. Bodurtha*
Independent Director
BlackRock Funds

Robert P. Bremner
Independent Chair
Nuveen Funds

Mary K. Bush*
Independent Director
Pioneer Funds

Bruce L. Crockett*
Independent Chair
Invesco Funds

Diana M. Daniels
Independent Director
Goldman Sachs Funds

Dennis J. Dirks
Independent Director
Fidelity Equity & High Income Group of Funds

Peter S. Drotch
Independent Director
ING Funds

Paul K. Freeman
Independent Chair
DWS Funds

C. Gary Gerst*
Independent Chair
Henderson Global Funds

Cynthia A. Hargadon
Independent Director
PAX World Funds

Karen N. Horn
Independent Director
T. Rowe Price Funds

Leonade D. Jones
Independent Director
American Funds

John P. Kavanaugh
Independent Trustee
MFS Funds

Susan B. Kerley*
Independent Chair
MainStay Funds
Independent Director
Legg Mason Partners Funds

Garry L. Moody
Independent Director
AllianceBernstein Funds

Joel W. Motley
Independent Director
Oppenheimer Funds

Steven J. Paggioli
Independent Director
Aston Funds
Managers Funds
Professionally Managed Portfolios

Donald H. Pratt*
Independent Chair
American Century Funds, Kansas City Board

Davey S. Scoon
Independent Chair
Allianz Funds

Erik R. Sirri
Independent Director
Natixis Funds

Laura T. Starks
Independent Director
TIAA-CREF Funds

George Sullivan Jr.
Independent Director
SEI Funds
State Street Navigator Trust

Mary Ann Tynan*
Independent Director
Oppenheimer Funds

Robert W. Uek*
Independent Trustee
MFS Funds

Ralph F. Verni
Independent Chair
Eaton Vance Funds

Gary N. Wilner
Independent Director
Oakmark Funds

Jonathan F. Zeschin
Independent Director
Matthews Asia Funds

* On ICI Board of Governors

APPENDIX D

ICI Standing Committees and Chairs

As of September 30, 2012

Accounting/Treasurers
Brian W. Wixted
Senior Vice President and Treasurer
OppenheimerFunds, Inc.

Chief Compliance Officer
Pauline C. Scalvino
Chief Compliance Officer
The Vanguard Group, Inc.

Closed-End Investment Company
Keith A. Weller
Executive Director and Senior Associate General Counsel
UBS Global Asset Management (Americas) Inc.

ETFs (Exchange-Traded Funds)
James E. Ross
Senior Managing Director and Global Head of ETFs
State Street Global Advisors

International
Liliane Corzo
Vice President and Senior Counsel
Capital Research and Management Company

Investment Advisers
Vacant

Operations
Basil Fox
President
Franklin Templeton Investor Services LLC

Pension
Douglas O. Kant
Senior Vice President and Deputy General Counsel
Fidelity Investments

Public Communications
Mary Athridge
Managing Director, Corporate Communications
Legg Mason

Research
Gary Blank
Senior Vice President for Public Affairs and Policy
Fidelity Investments

Risk Management
Joseph A. Carrier
Chief Risk Officer
Legg Mason, Inc.

Sales Force Marketing
Dwight D. Jacobsen
Executive Vice President and Head of Intermediary Distribution
Dreyfus Investments

SEC Rules
Amy Doberman
General Counsel
ProShares Advisors LLC

Small Funds
Susan B. McGee
President and General Counsel
U.S. Global Investors, Inc.

Tax
Gregory K. Hinkle
Vice President and Funds Treasurer
T. Rowe Price Group, Inc.

Technology
Michael L. Radziemski
Partner and Chief Information Officer
Lord, Abbett & Co. LLC

Unit Investment Trust
W. Scott Jardine
General Counsel
First Trust Advisors, L.P.

APPENDIX E

ICI Staff

As of September 30, 2012

Executive Office

Paul Schott Stevens[1, 2, 6]
President and CEO

Peter H. Gallary[3]
Chief Operating Officer

Government Affairs

Donald C. Auerbach
Chief Government Affairs Officer and Co-Head

Dean R. Sackett III
Chief Government Affairs Officer and Co-Head

Peter J. Gunas III
Government Affairs Officer, Retirement Security and Tax Policy

Allen C. Huffman
Director, Retirement Security and Tax Policy

Netonis E. Wybensinger
Director, Financial Services

George F. Shevlin IV
Political Affairs Officer

Independent Directors Council

Amy B. R. Lancellotta
Managing Director

Annette M. Capretta
Deputy Managing Director

Lisa C. Hamman
Senior Associate Counsel

Law

Karrie McMillan
General Counsel

Dorothy M. Donohue
Deputy General Counsel, Securities Regulation

Sarah A. Bessin
Senior Counsel, Securities Regulation

Ari Burstein
Senior Counsel, Capital Markets

Robert C. Grohowski
Senior Counsel, Securities Regulation

Frances M. Stadler[4]
Senior Counsel, Securities Regulation

Jennifer S. Choi
Senior Associate Counsel

Rachel H. Graham
Senior Associate Counsel

Jane G. Heinrichs
Senior Associate Counsel

Tamara K. Salmon
Senior Associate Counsel

Mara L. Shreck
Associate Counsel

David M. Abbey
Senior Counsel, Pension Regulation

Howard M. Bard
Associate Counsel

Elena B. Chism
Associate Counsel

Anna A. Driggs
Associate Counsel

Keith D. Lawson[5]
Senior Counsel, Tax Law

Karen L. Gibian
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Michelle M. Kretsch
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ICI Global

Dan Waters
Managing Director

Giles S. Swan
Director, Global Funds Policy

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[1] Executive Committee of ICI's Board of Governors
[2] Chairman's Council (ex officio)
[3] Chairman's Council and Treasurer to ICI PAC
[4] Secretary to ICI
[5] Secretary to ICI's Chairman's Council, Assistant Treasurer to ICI PAC, Political Compliance Counsel
[6] ICI Education Foundation Board

APPENDIX F

Publications and Statistical Releases

Publications

ICI is the primary source of analysis and statistical information on the investment company industry. A complete list of ICI research publications and statistical releases is available on the Institute's website at www.ici.org/research. Participant-funded studies are not listed.

Industry and Financial Analysis

- *SEC Valuation and Liquidity Guidance for Registered Investment Companies*; 2011 Update, December 2011
- Trends in the Expenses and Fees of Mutual Funds, 2011, *ICI Research Perspective*, April 2012
- *The Implications of Capital Buffer Proposals for Money Market Funds*, May 2012
- Commodity Markets and Commodity Mutual Funds, *ICI Research Perspective*, May 2012
- *Operational Impacts on Proposed Redemption Restrictions on Money Market Funds*, June 2012

Investor Research

- Ownership of Mutual Funds, Shareholder Sentiment, and Use of the Internet, 2011, *ICI Research Perspective,* October 2011
- Characteristics of Mutual Fund Investors, 2011, *ICI Research Perspective*, October 2011
- *America's Commitment to Retirement Security: Investor Attitudes and Actions*, January 2012
- Profile of Mutual Fund Shareholders, 2011, *ICI Research Report*, February 2012
- The Closed-End Fund Market, 2011, *ICI Research Perspective*, March 2012
- *The IRA Investor Profile: Traditional IRA Investors' Withdrawal Activity, 2007 and 2008*, July 2012

Retirement Research

- Who Gets Retirement Plans and Why, 2010, *ICI Research Perspective*, October 2011
- Defined Contribution Plan Participants' Activities, First Half 2011, *ICI Research Report*, October 2011
- *Inside the Structure of Defined Contribution/401(k) Plan Fees*, November 2011
- The Role of IRAs in U.S. Households' Saving for Retirement, 2011, *ICI Research Perspective*, November 2011
- A Look at Private-Sector Retirement Plan Income After ERISA, 2010, *ICI Research Perspective*, December 2011
- 401(k) Plan Asset Allocation, Account Balances, and Loan Activity in 2010, *ICI Research Perspective*, December 2011
- Defined Contribution Plan Participants' Activities, 2011, *ICI Research Report*, April 2012
- Defined Contribution Plan Participants' Activities*, First Quarter 2012*, *ICI Research Report*, July 2012
- *The Tax Benefits and Revenue Costs of Tax Deferral,* September 2012
- Who Gets Retirement Plans and Why, 2011, *ICI Research Perspective*, September 2012

Investment Company Fact Book

ICI's annual data and analysis resource, *2012 Investment Company Fact Book*: *A Review of Trends and Activity in the U.S. Investment Company Industry*, provides current information and historical trends for U.S.-registered investment companies, reporting on retirement assets, characteristics of mutual fund owners, use of index funds, and other trends. It is available in both PDF and HTML versions at www.icifactbook.org. The HTML version provides downloadable data for all charts and tables.

ICI Viewpoints

At *ICI Viewpoints*, ICI publishes analysis and commentary from in-house experts in economics, law, fund operations, and government affairs on the key issues facing funds, their shareholders, directors, and investment advisers. *ICI Viewpoints* also offers short recaps of select ICI comment letters, as well as notes on ICI news and events. *ICI Viewpoints* is available on the Institute's website at www.ici.org/viewpoints.

Statistical Releases

The most recent ICI statistics and an archive of statistical releases are available at www.ici.org/research/statistics.

» **Trends in Mutual Fund Investing:** A monthly report that includes mutual fund sales, redemptions, assets, cash positions, exchange activity, and portfolio transactions for the period.

» **Estimated Long-Term Mutual Fund Flows:** A weekly report that provides aggregate estimates of net new cash flows to equity, hybrid, and bond mutual funds.

» **Money Market Fund Assets:** A weekly report on money market fund assets by type of fund.

» **Retirement Market Data:** A quarterly report that includes individual retirement account and defined contribution plan assets and mutual fund assets held in those accounts by type of fund.

» **Exchange-Traded Fund Data:** A monthly report that includes assets, number of funds, issuance, and redemptions of ETFs.

» **Closed-End Fund Data:** A quarterly report on closed-end fund assets, number of funds, issuance, and number of shareholders.

» **Unit Investment Trust Data:** A monthly report that includes the value and number of deposits of new trusts by type and maturity.

» **Worldwide Mutual Fund Market Data:** A quarterly report that includes assets, number of funds, and net sales of mutual funds in countries worldwide.

APPENDIX G

ICI and IDC Events

October 24–26, 2011	Investment Company Directors Conference[1]	Chicago, IL
November 4–5, 2011	Small Funds Committee Meeting	San Francisco, CA
November 17, 2011	Closed-End Fund Conference	New York, NY
December 6, 2011	Equity Markets Conference	New York, NY
December 13, 2011	Securities Law Developments Conference[2]	Washington, DC
February 17, 2012	Derivatives Roundtable	Washington, DC
March 18–21, 2012	Mutual Funds and Investment Management Conference[3]	Phoenix, AZ
May 9–11, 2012	General Membership Meeting	Washington, DC
May 10, 2012	Investment Company Directors Workshop[1]	Washington, DC
May 10–11, 2012	Operations and Technology Conference	Washington, DC
May 10–11, 2012	Mutual Fund Compliance Programs Conference	Washington, DC
July 11, 2012	Independent Counsel Roundtable	Washington, DC
September 30–October 3, 2012	Tax and Accounting Conference	Phoenix, AZ

[1] Sponsored by IDC
[2] Sponsored by the ICI Education Foundation
[3] Cosponsored by ICI and the Federal Bar Association

APPENDIX H
ICI Education Foundation

The ICI Education Foundation (ICIEF) partners with schools, government agencies, and other nonprofits to promote financial education initiatives on behalf of the mutual fund industry. Under a microgrant program launched in mid-2009, ICIEF has awarded 10 grants to advance investor education within the greater Washington, DC, area. These grants fund teacher training in personal finance in Maryland, DC, and Virginia, as well as adult and youth investment education programs in workplaces, public libraries, public television, job training programs, online courses, and the unique venue known as Finance Park. In addition, ICIEF participates in nationwide coalitions, conferences, and government events devoted to financial education and capability.

APPENDIX I
ICI Mutual Insurance Company

ICI Mutual (ICIM) is an independent company formed by the mutual fund industry to provide various forms of liability insurance and risk management services to mutual funds, their directors, officers, and advisers. An organization must be an ICI member to purchase insurance from ICIM.

ICI Action on Select Policy Developments, Fiscal Year 2012

FUND REGULATION

Systemic Risk Regulation: The Financial Stability Oversight Council (FSOC) adopted a final rule and interpretive guidance concerning its authority to designate nonbank systemically important financial institutions (SIFIs) for Federal Reserve Board supervision and prudential regulation.

In comment letters and meetings with regulators, ICI expressed its firm view that SIFI designation would not be appropriate for funds, as they do not present the risks that the designation is intended to address. ICI also joined other trade groups in encouraging the FSOC to follow a transparent and open process for SIFI designation.

Derivatives: The Securities and Exchange Commission (SEC) sought input on a concept release modernizing the legal framework governing funds' use of derivatives.

At an ICI-hosted roundtable in Washington, DC, and in a comment letter, ICI commended the SEC for taking a measured approach to derivatives. The Institute offered recommendations to improve the current framework while preserving both investor protections and the benefits of derivatives for fund managers.

Rule 4.5: The Commodity Futures Trading Commission (CFTC) voted to adopt amendments to its Rule 4.5. As a result, advisers to certain registered investment companies already regulated by the SEC will be regulated by the CFTC as "commodity pool operators."

The Institute and the U.S. Chamber of Commerce filed a legal challenge to the amended rule, arguing that it imposes redundant and burdensome regulations, and that the CFTC failed to satisfy its statutory obligation to weigh the costs and benefits of the amendments.

Surprise Audits of 529 Plans: The SEC issued a no-action letter that relieved investment advisers to 529 plans from the surprise inspection requirement of the custody rule under the Investment Advisers Act of 1940.

ICI had requested the no-action relief, noting that the requirement added considerable expense to long-standing custodial arrangements for 529 plans without providing any enhancement to existing investor protections.

Advertising Rules: The SEC approved changes to Financial Industry Regulatory Authority (FINRA) rules governing communications with the public. The new rules—establishing a range of guidelines on institutional communications, retail communications, and correspondence—become effective in February 2013.

The final rules reflect ICI recommendations on rationalizing how FINRA categorizes different types of communications for purposes of applying FINRA filing, supervision, and content requirements.

Preserving Money Market Funds: See page 6.

Issues Facing Fund Directors: See page 30.

RETIREMENT

Fee Disclosure: The Department of Labor (DOL) implemented new fee disclosure regulations and issued a set of frequently asked questions (FAQs) interpreting certain aspects of the regulations.

The Institute continues to work with the DOL to ensure any interpretive guidance clarifies the regulations but does not create new law. In particular, the Institute worked with policymakers to ensure the DOL withdrew its position in Question 30 of the FAQs regarding plan sponsors' fiduciary responsibilities with respect to brokerage accounts.

Target Date Funds: Target date fund (TDF) disclosure proposals previously issued by the DOL and SEC could be complete in the near future. Both proposals would require a glide path illustrating how asset allocations would change over a TDF's life. The SEC proposal would require a tagline with the asset allocation at the target date next to the first use of the fund's name.

Responding to a survey study on investor comprehension of TDFs commissioned by the SEC, ICI filed comment letters with both agencies noting that the survey results show that investors who viewed a glide path illustration had better comprehension of a TDF's changing asset allocation. The same study showed, however, that the addition of a tagline to a glide path illustration did not increase investor comprehension of all key features of a TDF.

Lifetime Income: Congress considered the Lifetime Income Disclosure Act, which would mandate that benefit statements provide lifetime income illustrations, using the current account value, and showing monthly income only as an annuity calculation.

Meeting with key committee members and staff, ICI expressed its opposition to the mandate. ICI argued that any legislation in this area should allow for a broader, more flexible approach, including projected savings and allowing other methods of calculating income.

Extension of State Retirement Plans: The legislatures of California and Massachusetts passed bills that would create state-run retirement plans for private-sector workers. The Massachusetts bill became law; the California proposal was approved by the legislature but, as of October 2012, has not been signed into law.

ICI opposed both proposals and sent detailed letters to both legislatures outlining the potential impacts on state budgets and on private businesses of creating state-run plans for private-sector workers. The Institute worked with numerous trade groups in opposing California's proposal, including sending a "Myths and Facts" paper to proponents of the proposal.

Defending America's Retirement Savings System: See page 22.

FINANCIAL MARKETS

Market Structure: U.S. and overseas regulators continued to address issues raised by developments in the structure and operation of the securities markets.

In numerous speeches, comment letters, and testimony before Congress, ICI urged regulators around the world to take action on issues that impact funds as investors, including high-frequency trading and automated trading, potential conflicts of interest in the routing and execution of orders, the need for increased transparency of trading information, and issues associated with undisplayed liquidity.

Dodd-Frank and Swaps: The CFTC and the SEC continued to implement the Dodd-Frank Wall Street Reform and Consumer Protection Act's Title VII, which concerns regulation of the swaps market.

ICI, through comment letters and meetings with regulators, advocated for fair and efficient swaps markets for registered funds and their shareholders. ICI engaged regulators on issues including protection of customers' swap collateral, block trades to protect funds' swaps trading, schedules for implementing the new swaps regulations, and the cross-border application of U.S. derivatives regulation.

Volcker Rule: The SEC and other regulators issued a lengthy and complex proposal to implement this provision of the Dodd-Frank Act, which is intended to restrict proprietary trading and investments by banks.

In comment letters, meetings, congressional testimony, and other communications with regulators and on Capitol Hill, ICI shared its serious concerns about the harm from an overly broad reading of the Volcker Rule to registered funds and their non-U.S. counterparts, their shareholders, and the financial markets.

OPERATIONS

Mandatory Audit Firm Rotation: The Public Company Accounting Oversight Board issued a concept release on ways to enhance auditor independence. The release considered requiring public companies, including funds, to change their auditor after a prescribed period.

ICI and IDC strongly opposed mandatory audit firm rotation and made the case that existing safeguards and recent enhancements to auditing standards are more than adequate to assure the independence of auditors. They explained that mandatory audit firm rotation could increase the cost of audits and diminish their quality, to the detriment of fund shareholders.

Investment Company Accounting: The Financial Accounting Standards Board (FASB) proposed updating accounting standards regarding the scope, measurement, and disclosure requirements for investment companies.

While supporting FASB's efforts to develop consistent criteria, the Institute opposed mandatory investment company consolidation of controlling interests in investee investment companies, given that funds of funds do not invest for control purposes. ICI recommended that FASB develop a principles-based model for determining when a fund of funds should be required to provide disclosure regarding an investee fund.

TAXES

FATCA: Implementation of the Foreign Account Tax Compliance Act (FATCA) continued, including the release in July of a model intergovernmental agreement (IGA) to help institutions in non-U.S countries comply with the law.

Working with senior Treasury Department and Internal Revenue Service (IRS) officials—and their counterparts abroad—ICI helped ensure that FATCA is applied in a manner that addresses many of the concerns with the substantial compliance burdens FATCA places on funds, their distributors, and their investors.

International Tax Issues: Tax issues posing challenges to the U.S. fund industry arose in several countries, notably France, India, Korea, and Sweden. In India, for example, legislation was enacted that could impose an unprecedented period of retroactive tax collection and an onerous tax on indirect stock transfers.

ICI engaged with tax authorities overseas to provide fund industry views and seek practical solutions to challenges. Regarding the Indian legislation, ICI urged that the rules be implemented to comport with accepted international tax norms and with a logical application to funds.

Capital Gains and Dividends: With the prospect of fundamental tax reform efforts in 2013, Congress and the Administration considered proposals addressing expiring income tax rates, including favorable tax rates on capital gains and dividends.

ICI advocated strongly for maintaining current rates favoring investment income. A steering committee member of the Alliance for Savings and Investment, ICI joined with other groups in letters to Congress, legislative briefings, and the "Defend My Dividend" ad campaign to support current rates.

Implementing Key Tax Laws: Implementation of the Regulated Investment Company Modernization Act of 2010 continued in 2012, and mandatory cost basis reporting became effective for mutual fund shares on January 1, 2012.

ICI coordinated with members, transfer agents, broker-dealers, outside counsel, and vendors to assist the industry in implementing these complex laws. The Institute continued to seek additional guidance from the IRS to address open issues.

INTERNATIONAL

ICI Global: See page 18.

Derivatives: The CFTC issued proposed guidance for cross-border transactions, and the European Securities and Markets Authority (ESMA) published draft technical standards under the European Market Infrastructure Regulation.

ICI and ICI Global filed comment letters with the CFTC, expressing concerns about the broad definition of a U.S. person in the CFTC's guidance, and with ESMA, identifying potential problems with its proposed standards.

Money Market Funds: At the request of the Financial Stability Board, the International Organization of Securities Commissions (IOSCO) released a consultation paper on the potential risks money market funds pose to systemic stability. The paper explored possible changes to money market fund regulations, including floating a fund's net asset value or imposing capital and liquidity requirements on money market funds.

ICI and ICI Global engaged with IOSCO through meetings with IOSCO's Director General and comment letters. ICI described money market funds' value to investors and the economy, explained how the SEC's 2010 amendments made money market funds more resilient, and showed how proposals for further regulation could damage funds and the global fund marketplace. ICI Global noted the tremendous differences globally among funds that would fall within IOSCO's description of a money market fund and stated that a global one-size-fits-all approach was neither advisable nor appropriate.

Exchange-Traded Funds (ETFs): IOSCO published a consultation paper, *Principles for the Regulation of Exchange-Traded Funds*, and ESMA, after two consultations, issued guidelines on Undertakings for Collective Investment in Transferable Securities (UCITs) ETFs.

ICI's comment letter generally supported IOSCO's expression of the ETF principles, but requested that IOSCO explain that most of these principles are not unique to ETFs. The Institute submitted two comment letters to ESMA expressing serious concerns with its proposals regarding secondary market investors and their ability to sell their shares directly to the funds.

India: Under a revised interpretation of India's know-your-customer (KYC) requirements, registered intermediaries began requiring U.S.-registered investment companies to provide personal information for their directors, such as copies of passports, when opening accounts in India.

In a letter, ICI urged Indian regulators to clarify that the KYC provisions do not require U.S. funds to submit directors' personal information to intermediaries. ICI explained that such requests are based on a misunderstanding of the unique role of U.S. fund directors and are outside of international norms.

Leading the Way on Policy Issues

Standing Up for Money Market Funds and Their Investors (PAGE 6)

ICI responded with vigor when regulators settled upon proposals that would require money market funds to abandon the stable net asset value or to maintain capital buffers and impose redemption holdbacks. In testimony before Congress, outreach to allies, and public communications, ICI used its extensive research to show that such structural changes would render money market funds useless as cash-management vehicles for many individual and institutional investors. ICI also endeavored to make sure the public and policymakers were aware of the array of opposition to these changes from investors, businesses, nonprofit institutions, and state and local government officials.

ICI Global (PAGE 18)

As funds and their advisers increasingly responded to an array of international regulatory and policy challenges, ICI's members and leadership recognized the industry's need for a global voice. To meet that need, the Institute launched ICI Global—the first industry body exclusively focused on the global investment fund industry. A year later, ICI Global has grown to represent a diverse group of members in North America, Europe, and Asia, who manage more than $1 trillion in registered fund assets. Leveraging ICI's traditional strengths in law, research, communications, and industry operations, and building upon its longtime involvement with international issues of consequence to U.S. funds, ICI Global gives a strong voice to the concerns and interests of regulated funds, their managers, and investors worldwide. Those interests fall into four main categories: the role of funds and fund managers in financial stability; transnational regulatory developments for funds; trading and market structure; and retirement savings and pension systems.

Defending America's Retirement Savings System (PAGE 22)

The fund industry's decades-long efforts to provide plan sponsors and participants with better disclosure achieved important results this year, including a new, standardized set of disclosures on all investment options as well as new disclosures on fees. Despite this progress, some policymakers and commentators continued to question whether the 401(k) system can help Americans achieve a secure retirement. Using empirical research, ICI defended the 401(k) system and emphasized the importance of existing tax incentives for retirement savings through speeches, in the media, and by informed advocacy on Capitol Hill.

Issues Facing Fund Directors (PAGE 30)

Acting as the voice of the fund director community to policymakers on issues affecting boards, the Independent Directors Council (IDC) weighed in through comment letters, testimony, and commentary on derivatives, mandatory audit firm rotation, and Commodity Futures Trading Commission regulations, among other issues. In light of the discussion about further changes to money market funds, IDC expressed directors' grave concerns about the negative impacts these changes could have on investors, capital markets, and the economy. Correcting misperceptions about the role of directors, IDC pointed out that the duties of directors are highly regulated and that independent directors are robustly independent.

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The Investment Company Institute is the national association of U.S. investment companies, including mutual funds, closed-end funds, exchange-traded funds (ETFs), and unit investment trusts (UITs). ICI seeks to encourage adherence to high ethical standards, promote public understanding, and otherwise advance the interests of funds, their shareholders, directors, and advisers.