

2005

# ANNUAL REPORT

TO MEMBERS



*The Investment Company Institute (ICI) is the national association of U.S. investment companies. ICI seeks to encourage adherence to high ethical standards, promote public understanding, and otherwise advance the interests of funds, their shareholders, directors, and advisers.*

*ICI members include 8,518 open-end investment companies (mutual funds), 663 closed-end investment companies, 148 exchange-traded funds, and 5 sponsors of unit investment trusts. Mutual fund members of the ICI have total assets of approximately \$8.5 trillion (representing more than 95 percent of all assets of U.S. mutual funds); these funds serve approximately 90 million shareholders in more than 51 million households.*

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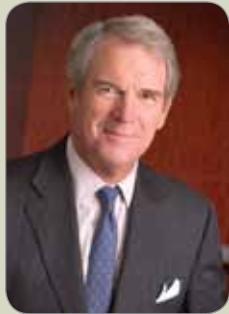
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## LETTER FROM THE CHAIRMAN



James S. Riepe  
Institute Chairman

I take this opportunity to express my thanks to all of you for allowing me to serve as ICI Chairman this past year and to congratulate my successor, Marty Flanagan, for taking on this important role. I have every confidence

that Marty will be an outstanding ICI Chair.

The last 12 months have been a year of notable progress for mutual funds and the Institute. It was particularly gratifying to see how funds continue to be embraced by the constituency that matters most—our shareholders.

Mutual funds have experienced remarkable growth in my 36-year tenure in the industry. Since 1969, when I

first started in the fund business, assets have grown from \$48 billion to nearly \$8.6 trillion. In just the last 10 years, mutual fund assets have nearly tripled—from less than \$3 trillion in 1995. And the number of investors who depend on funds to help meet their financial goals—now 91.3 million—has exceeded all reasonable expectations for growth and success. Fully half of all households in this country now own funds.

Throughout this period of growth, we have benefited from ICI's strong representation in Washington, DC. The Institute has served as an important unifying force in our industry, building consensus when it was needed and representing the interests of funds, their shareholders, directors, and advisers, with both regulators and legislators. And this was no easy task, since we faced such challenges as a technology revolution, corporate restructurings, ethical lapses,

**"James S. Riepe has again demonstrated those leadership qualities for which he is and has been so widely known and admired ... including the unwavering loyalty to shareholder interests that is the hallmark of a true fiduciary."**

—RESOLUTION OF THE ICI BOARD OF GOVERNORS, ON THE OCCASION OF MR. RIEPE'S RETIREMENT  
AS ICI CHAIRMAN, OCTOBER 7, 2005

global economy growth pains, and restructuring of our capital markets.

We all owe a special debt of gratitude to the many participants in the fund industry who volunteer their time and expertise on the Board of Governors of ICI and various Institute committees. Because of their input and participation, fund shareholders have been well served and ICI has become a source of information and knowledge for regulators and legislators alike.

I think it is safe to say that the health of the industry has been nourished by the culture of fiduciary responsibility that has been communicated through our engagement with the Institute. Maintaining this strong fiduciary culture in the industry will be crucial—for funds and investors—in the future, as the need for investors to grow their savings becomes even more important. It is widely understood that the Social Security and employer pension schemes will not accommodate the influx of Baby Boomers who will soon start retiring. Thus, it is encouraging that our policymakers are taking steps to promote greater saving in our nation. We can do our part by continuing to do what we do best: responding to the needs

of the millions of Americans who desire to save, and motivating the still millions more who must begin saving.

Just as important, we must continue to encourage and support an educated investor. Millions of Americans already access the securities markets through funds. To those investors, we have not only a fiduciary obligation, but also a responsibility to help them better understand investing. If we are successful, the public will not only approach retirement in an improved position, but will also have even more confidence in the mutual fund model.

Funds combine all of the ingredients—diversification, convenience, and cost-effective service—that make investing a successful proposition for savers and would-be savers. They continue to be the most efficient and effective way for individual investors to access our securities markets. I have no doubt that funds and the investors they serve are in good hands, through the work you perform everyday and through your participation in and support of ICI's efforts.

James S. Riepe

November 2005

#### ICI ACTIVITIES, 1974–2005

Supported Legislation Creating IRAs	Promoted Legislation Creating Tax-Exempt Funds	Defeated Efforts to Prohibit Money Market Funds	Helped Create Universal IRAs	Supported Mutual Fund Prospectus Simplification	Helped Standardize Fund Performance Disclosure	Helped Enhance Money Market Fund Credit Standards	Issued Industry Best Practices on Personal Investing	Began Formal Educational Programs for Fund Directors
1974	1976	1980–1981	1981	1983	1988	1991	1994	1995

## LETTER FROM THE PRESIDENT



**Paul Schott Stevens**  
*Institute President*

Our 2005 Annual Report marks the conclusion of my first full year as President of ICI. Looking back, it has been a year of very important transitions—in both the affairs of the Institute and the policy environment in Washington.

At ICI, we completed the recruitment of a new senior management team as well as key new members of our government affairs, legal, public communications, and research staffs. I am immensely pleased with the quality of the personnel that ICI continues to attract at all levels. This is a tribute to the Institute's membership, to the strong culture of this organization over many years, and to the importance and impact of our work.

Integrating these varied capabilities and working closely together as a team, we are poised to build on our progress this past year:

- Further strengthening our relationships with key policymakers and opinion leaders;
- Engaging the SEC under its new leadership, and the regulatory community at large, on issues of critical importance to our investors, to the vibrancy and competitiveness of mutual funds, and to the integrity of the securities markets;
- Executing a strategy designed to more closely inform the public debate on mutual fund issues, through our communications and research activities; and
- Providing continued strong support to the Independent Directors Council in its activities on behalf of independent directors.

**“A host of difficult new issues began to crowd the nation’s agenda in 2005—many of them immensely important to our industry and the investing public.”**

—INSTITUTE PRESIDENT PAUL SCHOTT STEVENS

As for the policy environment, much has changed since 2004. A host of difficult new issues began to crowd the nation's agenda in 2005—many of them immensely important to our industry and the investing public. These include the future shape of public and private pension arrangements, how to provide for future health care costs, how to return the U.S. personal savings rate to positive territory, how best to equip individuals to assume greater responsibility for their financial security, proposals for far-reaching reforms of the federal tax system, and the long-term implications of all these for U.S. economic growth and international competitiveness.

These are issues that demand our industry's attention, both as stewards for about one-quarter of the nation's retirement assets and as investors. The Institute's role is to help our members understand these challenges and assist policymakers as they formulate appropriate responses to them. That role has never been more important—whether it concerns sound tax policies to stimulate capital formation and economic growth, options for retirees to better manage longevity risk, measures like the GROWTH Act to encourage long-term savings

outside retirement plans, or ways for working Americans to take even better advantage of employer-sponsored plans and Individual Retirement Accounts.

The focus and priorities of public policy change over time. We, however, can never afford to forget the lessons of our recent past. The famous American newspaper editor Horace Greeley observed that only one thing endures and that is character. All our future success hinges upon the strength of our character as fiduciaries—and remaining loyal to the trust of our investors.

In closing, let me express my deep gratitude to Chairman Jim Riepe for his leadership of our Board over the past year, and for the generous assistance and wise counsel he has provided to me since I became President.

I appreciate the support that all our members provide to ICI. With all my colleagues here, I pledge we will work hard in the year ahead to continue to earn your confidence.

Paul Schott Stevens

November 2005

#### **ICI ACTIVITIES, 1974–2005 *continued***

Supported Uniform Federal Regulation for Funds	Supported Simplified IRAs for Small Businesses	Supported Creation of Roth IRAs	Supported Fund Disclosure Simplification	Opposed Efforts to Weaken Investor Protections	Issued Industry Best Practices for Fund Directors	Supported Increased IRA and 401(k) Plan Contributions	Worked for Legislation Lowering Dividend, Capital Gains Tax Rates	Promoted Fair Taxation of Mutual Fund Capital Gains
1996	1996	1997	1998	1999	1999	2000	2003–2004	2005

## SECTION I: ADDRESSING THE SAVINGS CRISIS IN AMERICA

According to statistics released by the U.S. Commerce Department, the rate of personal savings in the United States, for the first time since the depths of the Great Depression, dipped below zero in June 2005. This continued a steady decline since 1982 when the savings rate stood at 11.2 percent. At the same time, U.S. household debt increased by double-digit growth rates in 2003 and 2004. These alarming trends in savings and debt rates are occurring when 79 million Baby Boomers are in their peak earning years, with many reaching 65 as early as six years from now. The numbers paint a vivid picture of America's savings crisis and the risk to our economy of diminished capital available for the business investment that fuels economic growth.

Although the nation faces the sobering challenge of large continuing budget deficits, policymakers must devise ways to address this savings crisis. When President Bush focused national attention on the future of Social Security during the past 12 months, he initiated a broader, timely review of national policy in this area. Because millions of investors rely on mutual funds and other investment companies to meet long-term savings goals, the Institute has been a longtime proponent of efforts that encourage saving and investing, consistently urging that policymakers support solutions that facilitate and promote the efforts of fund investors and other Americans to achieve personal financial security.

**“A very important piece of legislation introduced this month would provide tax relief for millions of Americans who invest in mutual funds for long-term savings goals.”**

—INVESTMENTNews, MAY 30, 2005

In FY 2005, the Institute sought to address this savings crisis in three ways.

- **HELPING DEFINE THE SAVINGS CHALLENGES FACING AMERICANS.** In its research and policy commentary, ICI pointed up concerns over Social Security solvency, the evolution of the retirement plan market, and changes in savings trends and U.S. demographics.
- **PROMOTING INITIATIVES TO HELP INVESTORS SAVE.** ICI urged that policymakers take concrete steps to facilitate saving, including making permanent provisions in already enacted legislation and enacting a new proposal to allow mutual fund investors to save more.

- **ENCOURAGING POLICIES THAT MAKE INVESTING AND SAVING MORE CONVENIENT, FLEXIBLE, AND UNDERSTANDABLE.** ICI called on policymakers to support measures—such as automatic 401(k) plan enrollment, greater access to investment advice within defined contribution plans, and flexible asset withdrawal—that encourage Americans to make the best use of the savings incentives at their disposal.

## A LOOK AT THE SAVINGS CHALLENGES

Many Americans rely on mutual funds to help meet retirement and other long-term savings objectives. At year-end 2004, mutual funds accounted for 24 percent of the \$12.9 trillion U.S. retirement market.

### 2005 BILL ENCOURAGES PERSONAL SAVINGS

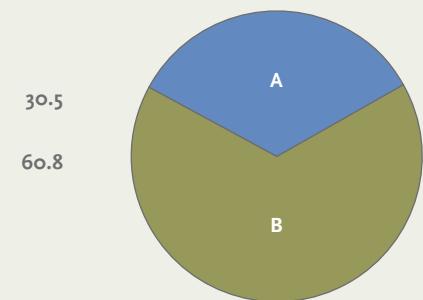
Congress is considering a proposal—introduced in both the House and Senate—that would encourage more personal savings by allowing investors to keep more dollars invested longer. This important piece of legislation, the GROWTH Act (H.R. 2121/S. 1740), provides a sensible way for millions of Americans—most of them middle class—to create a more secure financial future for themselves and their families.

For more information on the GROWTH Act and other solutions to the savings crisis in America, visit [www.FundingYourFuture.org](http://www.FundingYourFuture.org).

### NEARLY 31 MILLION CURRENT MUTUAL FUND SHAREHOLDERS WOULD BENEFIT FROM THE GROWTH ACT (number of mutual fund shareholders)

- A: Shareholders with long-term mutual fund assets in taxable accounts  
B: Shareholders without long-term mutual fund assets in taxable accounts

Total mutual fund shareholders = 91.3 million



The \$3.1 trillion retirement market assets invested in funds represent nearly 40 percent of total mutual fund assets, with investors holding most of these assets through 401(k) plans and Individual Retirement Accounts (IRAs). In total, mutual funds now make up roughly half of the savings built up in 401(k) plans and 43 percent of savings held in IRAs.

Despite the effectiveness of the fund model in meeting savings challenges, more needs to be done. Only about half of the 153 million American workers have coverage under 401(k) and other employer-sponsored plans. Meanwhile, assets in IRAs have grown primarily due to the investment performance of the underlying securities and through rollovers into IRAs from employer-sponsored retirement plans.

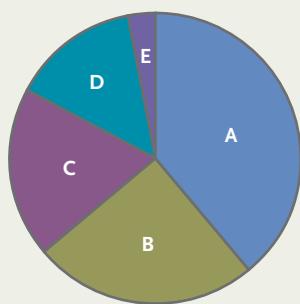
As the Baby Boomer generation heads into their retirement years, policymakers must address the solvency of Social Security and make employer-sponsored pensions, IRAs, and other savings opportunities more effective for an American public increasingly called upon to be self-reliant when it comes to planning for retirement and other future needs.

Why? Because life expectancies continue to rise, because many workers are not offered any pension or retirement plan at work, because many Americans rely too heavily on Social Security, and because many must pay an increasing share of their health coverage at the same time they're funding their children's education or supporting elderly parents.

### How Current Retirees Fund Their Retirement

(U.S. retirees age 65 and older)

A: Social Security	39%
B: Employment Earnings	25%
C: Employer-Sponsored Pension & Retirement Plans	19%
D: Income from Assets	14%
E: Other	3%



Source: Social Security Administration, *Income of the Population 55 or Older in 2002* (released March 2005)



## SPEAKER OF THE HOUSE HASTERT ADDRESSES FIRST EVER ICI LEADERSHIP DINNER

Speaker of the House Dennis Hastert (R-IL) discussed the savings challenges that face Americans and the vital role that mutual funds can play in meeting those challenges at ICI's first Mutual Fund Leadership Dinner on May 4, 2005. Nearly 40 members of Congress, senior Bush Administration officials, the SEC Chairman, representatives from other federal agencies, and about 80 mutual fund leaders attended the event, held in the historic Library of Congress.

"We have to face the facts," Hastert remarked in his keynote address. "The pension system is in major need of reform. ... Part of getting Americans to invest more and invest wisely is having access to good advice and financial literacy. Your industry has done an exemplary job of offering these services and I want to applaud you on your efforts."

"This gathering," ICI Chairman James S. Riepe observed in closing, "signals our determination to strengthen lines of communication

*"We need to use some of the innovative strategies out there in the business and investment communities to keep employers engaged and offering retirement plans to their employees," Speaker of the House Dennis Hastert (R-IL) tells an ICI gathering of fund industry leaders, Members of Congress, and government officials.*

between the leadership of America's mutual funds and senior policymakers throughout government. It is safe to say that effective dialogue between leaders of mutual funds and government policymakers has never been more important than it is today. Never has it been more important for Americans to strengthen their own long-term financial capacity."



*Sen. Paul Sarbanes (D-MD) and ICI Chairman James S. Riepe participate in ICI's Leadership Policy Forum where the legislator discussed the Sarbanes-Oxley Act of 2002.*

## **MOVING FROM THE DEFINED BENEFIT TO THE DEFINED CONTRIBUTION PLAN MODEL**

Workplace employee benefit plans and the responsibilities they place on employees have changed significantly in the United States. Traditional employer-sponsored pension plans—‘defined benefit’ (DB) pension plans that promise a guaranteed benefit based largely on years of service and compensation—are becoming less available to today’s workforce.

Many plans have not recovered from economic setbacks, and several of the largest plans, sponsored by employers in troubled industries like airlines and steel, have been taken over by the federal agency that backs up defined benefit pension promises, the Pension Benefit Guaranty Corporation (PBGC). For hundreds of thousands of people, this will mean a cut in promised benefits.

As defined benefit plans have fallen in number, defined contribution (DC) plans have increased. From 1975 to 2000, the number of defined contribution plans more than tripled and the number of participants in defined contribution plans more than quintupled. Assets held in these plans soared from a 1975 level of \$74 billion to \$3.2 trillion at the end of 2004, including \$2.1 trillion in 401(k) plans. With the shift came a tremendous growth in individuals’ responsibility: in defined contribution plans, individual employees decide whether to participate, how much to save, how to invest given the options provided, when to rebalance, and when and how to withdraw.

How workers fare under this system will depend on how they exercise these responsibilities. Research conducted by ICI and the Employee Benefit Research

## **IMPROVING DEFINED CONTRIBUTION PLAN DISCLOSURE**

The Institute has long been a strong proponent of efforts to enhance defined contribution plan disclosure standards. In 1997, for example, ICI supported the disclosure of detailed fee information for all plan investment alternatives during testimony at a Department of Labor (DOL) hearing on 401(k) plan expense disclosure. Subsequently, the Institute was instrumental in the development of a model 401(k) plan fee disclosure form made available to plan sponsors on the DOL’s website since 2000.

Over the past 13 months, ICI remained active in support of policies enhancing the effectiveness of 401(k) and other defined contribution plan disclosure. In September 2004, ICI General Counsel Elizabeth Krentzman testified before the DOL Advisory Council about needed improvements to participant and sponsor disclosures. The Advisory Council adopted many of ICI’s recommendations. For example, it agreed that plan participants should receive a “profile prospectus” for each plan investment option, and also amended a DOL worksheet for plan sponsors in order to incorporate information concerning investment-level fees as well as revenue-sharing arrangements. With input from Institute members, ICI has since taken the lead in developing a model disclosure schedule for service provider compensation that has proven particularly important in light of regulatory concerns surrounding revenue sharing in the retirement plan marketplace.



Institute President Paul Schott Stevens (l.),  
House Ways and Means Committee  
Chairman Bill Thomas (R-CA), and ICI  
Chairman James S. Riepe (r.) interact  
at a September 2005 ICI Executive  
Committee Meeting.

Institute (EBRI) suggests that employees who make full use of 401(k) plans and other similar defined contribution plans should be prepared for retirement. But many people who are offered the chance to participate in these plans do not do so. Employees who participate in their plans also face challenges in understanding and appropriately using the investment options provided to them to build a diversified account that reflects their age, risk tolerance, and other individual factors.

### FINDING SAVINGS SOLUTIONS

In FY 2005, ICI called for legislative action in two key areas to improve saving: making permanent existing incentives enacted over the past four years and addressing tax inequities that unfairly target mutual fund investors who save for long-term goals through taxable accounts.

### MAKING CURRENT SAVINGS ENHANCEMENTS PERMANENT

Policymakers recently enacted two important laws to encourage saving. In 2001, Congress rejuvenated retirement and educational savings planning options with a number of provisions enacted as part of the Economic Growth and Tax Relief Reconciliation Act (EGTRRA). Congress needs to take an even bolder step, however, by making permanent these 401(k), IRA, and educational savings enhancements (see *Making Recent Savings Solutions Permanent* on page 12).

## MAKING RECENT SAVINGS SOLUTIONS PERMANENT

### RECENTLY ENACTED SAVINGS LEGISLATION

#### *The Economic Growth and Tax Relief Reconciliation Act of 2001<sup>1</sup>*

### IMPORTANT SAVINGS INCENTIVES SET TO EXPIRE

- Increased the annual IRA contribution limit, in steps, from \$2,000 in 2001 to \$4,000 today (and increasing to \$5,000 in 2008);
- Increased income limits for the phase-out of the deductibility of contributions to traditional IRAs;
- Increased annual contribution limits for employer-sponsored retirement plans such as 401(k) plans;
- Allowed individuals age 50 or older to make special “catch-up” contributions of \$500 a year (increasing to \$1,000 in 2006) to IRAs and to increase contributions in steps to certain retirement plans, from \$1,000 a year in 2002 to \$5,000 in 2006, recognizing workers may not have been able to make adequate contributions earlier in their careers;
- Increased the ability of workers moving from job to job to transfer retirement savings without encountering tax penalties;
- Allowed tax-free distributions from “Section 529” qualified tuition plans, so long as the funds are used to pay for certain higher education expenses; and
- Increased the annual contribution limit to Coverdell Education Savings Accounts from \$500 a year to \$2,000.

#### *The Jobs and Growth Tax Relief Reconciliation Act of 2003<sup>2</sup>*

- Reduced the tax rates on long-term capital gains from 20 percent (for taxpayers facing tax rates of 25 to 35 percent on ordinary income) and 10 percent (for taxpayers in the 15 percent and 10 percent brackets) to 15 percent and 5 percent, respectively. The 5 percent rate will be reduced to zero in 2008.
- Reduced the tax rate on qualified dividend income, which was previously taxed at ordinary rates, to the 15 percent and 5 percent capital gains tax rates.

<sup>1</sup> All provisions set to expire after 2010.

<sup>2</sup> These lower rates expire at the end of 2008; the higher rates will be reinstated beginning in 2009.

Similarly, Congress should consider permanent action on taxation of investment earnings. Because taxation of investment earnings creates a drag on savings and economic growth, Congress reduced capital gains and dividend tax rates and enhanced savings incentives in 2003 with the enactment of the Jobs and Growth Tax Relief Reconciliation Act (JGTRRA).

Since the JGTRRA provisions took effect in 2004, dividend increases have exceeded all increases between 1994 and 2002 combined—greatly helping seniors who receive almost half of all dividend income. The U.S. Treasury estimates that 24 million Americans saved an average of \$950 on their taxes in 2004 as a result of lower tax rates on dividends and capital gains. The provisions also have contributed to job creation, an enhanced tax base, and better corporate stewardship of investors' capital. And they are vital to strengthening the ability of those without access to employer-sponsored retirement plans—tens of millions of working Americans—to save and invest on their own for retirement.

### **DEFERRED TAX TREATMENT FOR MUTUAL FUND CAPITAL GAINS**

At a time when individual Americans are being called upon to contribute more to their retirement, the tax code should spur, not hinder, saving. ICI strongly supports bipartisan legislation introduced in both the House and Senate in 2005 that would keep more retirement savings invested longer and growing larger by deferring taxation of automatically reinvested capital gain distributions until fund shares are sold—rather than taxing these long-term gains every year.

One of the most frustrating aspects of U.S. tax law for millions of Americans is the requirement that long-term capital gain distributions to mutual fund investors in taxable accounts be taxed every year, even if they are automatically reinvested. Fund shareholders, like other investors, should be taxed when they sell their shares—not before, while they are still building savings for retirement.

Passing the GROWTH Act (H.R. 2121/S. 1740) would send a positive message to investors about saving.

The GROWTH Act would assist tens of millions of Americans over the course of their working lives—and make a real difference in the retirement readiness of American families. In particular, the GROWTH Act would encourage savings among middle-income taxpayers.

### MAKING INVESTING AND SAVING MORE CONVENIENT, UNDERSTANDABLE, AND FLEXIBLE

Promoting savings requires saving vehicles and investments that are convenient, understandable, and flexible enough to use. ICI supports measures—such as automatic enrollment features and simpler eligibility rules—that help expand participation in 401(k)

plans and IRAs. ICI also supports solutions that give savers flexible options for drawing down their assets once they reach retirement age, and efforts to improve plan disclosure standards so that plan participants have all the necessary information to make informed investment decisions.

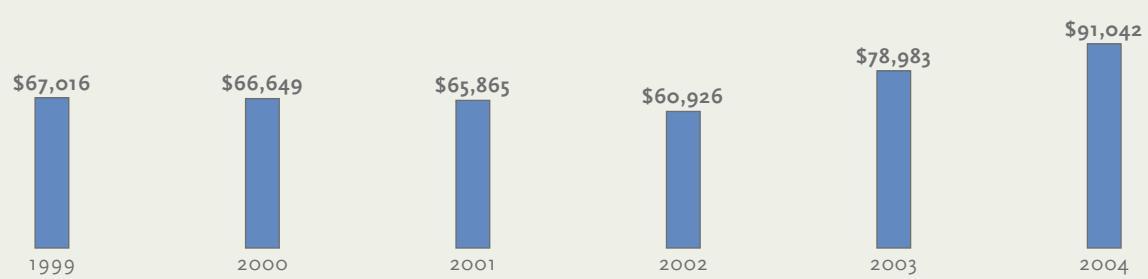
### INCREASING 401(K) PLAN EFFECTIVENESS: AUTOMATIC ENROLLMENT, INVESTMENT ADVICE

A recent study by ICI and EBRI shows that millions more Americans would benefit from 401(k) plans if Congress and federal regulatory agencies act to expand the availability and effectiveness of automatic enrollment programs.

#### CONSISTENT 401(K) PARTICIPATION REMAINS ESSENTIAL

(average plan participant account balance, 1999–2004)

Individuals who consistently participated in their 401(k) plans from 1999 to 2004 saw their account balances rise by 36 percent despite experiencing one of the worst bear markets for stocks since the Great Depression.



Source: 401(k) Plan Asset Allocation, Account Balances, and Loan Activity in 2004 ([www.ici.org/pdf/per11-04.pdf](http://www.ici.org/pdf/per11-04.pdf))

Research shows that automatic enrollment plans boost worker participation rates from about 66 percent to more than 90 percent, a substantial increase that can be expected to have a significant impact on retirement lifestyle for those remaining in a plan throughout their working lives. Furthermore, the ICI and EBRI study found that automatic enrollment would have the greatest impact on lower-income workers because members of this group are least likely to participate in a 401(k) plan of their own volition. Among eligible workers in the lowest income group, the median salary replacement from 401(k) accumulations at retirement would more than double from 23 percent without automatic enrollment to 52 percent of salary when the default contribution rate is 6 percent of salary invested in a lifecycle fund.

Employers who sponsor plans and fiduciaries responsible for investment options under plans need guidance on how to implement automatic enrollment and structure appropriate default investment options under applicable law. As a result, the Institute was actively involved in FY 2005 in discussions with the Department of Labor concerning possible safe harbor guidance on default investments.

Workers covered by 401(k) plans, meanwhile, also would benefit from additional assistance with the investment decisions these plans typically call upon them to make. ICI has consistently urged Congress to update the rules governing 401(k) plans to make sure that participants have the kind of investment options and professional advice they need. The law governing professional advice to retirement plan participants is more than 30 years old.

Studies show that many 401(k) investors would like access to financial counseling programs that offer personalized assistance, and that these programs could significantly increase plan savings and participation rates. Many plans do not offer any investment advisory service, and Employee Retirement Income Security Act (ERISA) rules effectively prohibit financial institutions that provide investment options to retirement plans from offering specific, individually tailored advice to plan participants—no matter how prudent or objective the advice. The Institute has consistently called for legislation to allow 401(k) investors to turn for advice to professionals most familiar with their 401(k) plan investment options.

## INCREASING IRA EFFECTIVENESS: CLARIFY AND SIMPLIFY ELIGIBILITY RULES

The use of IRAs likely would increase if Congress restored simplicity and clarity to contribution and eligibility rules. In the early 1980s, Congress made IRAs “universal,” allowing any taxpayer under age 70½ with earned income to make a deductible IRA contribution regardless of coverage by an employer plan.

IRA contributions soared until 1986, when Congress limited the deductibility of IRA contributions.

Although that limit has since been liberalized, annual

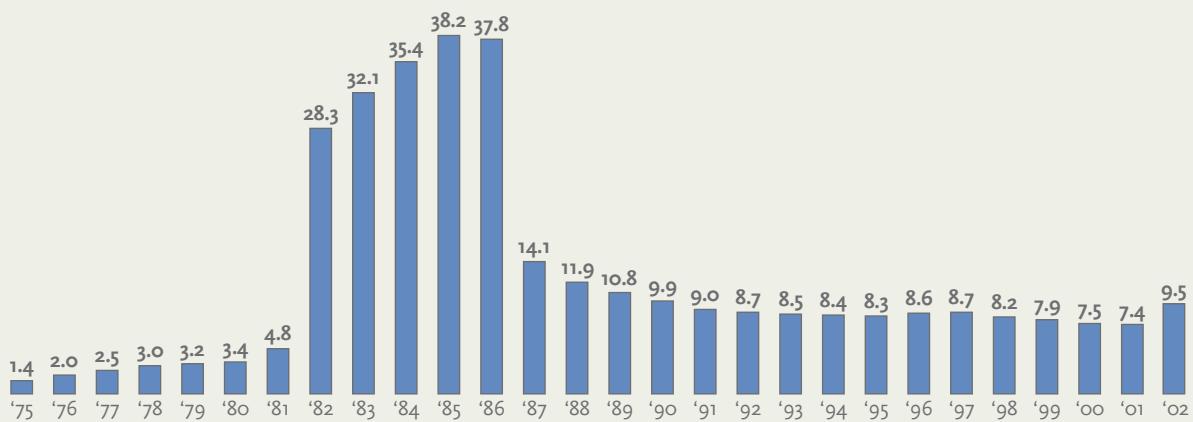
IRA contributions remain far below the level reached in the mid-1980s. The rules regarding who is eligible to contribute, how much, and on what basis are complex and, as a result, only a small fraction of those households eligible to contribute to IRAs do so.

If policymakers expect individual savings to represent a more significant and growing part of retirement income, then the IRA rules need to be consistent and simple. One way to achieve this is for Congress to restore universal eligibility to IRAs.

## IRAs CAN BE AN EFFECTIVE SAVINGS TOOL

(deductible contributions to traditional IRAs, billions of dollars)

Incentives to investing in IRAs work best when the rules are simple, understandable, and predictable. Individuals reacted negatively to the elimination of the “universal” IRA in 1986.



Source: The Individual Retirement Account at Age 30: A Retrospective ([www.ici.org/pdf/per11-01.pdf](http://www.ici.org/pdf/per11-01.pdf))

## **MANAGING ASSETS IN RETIREMENT: REQUIRED WITHDRAWALS AND ANNUITIZATION**

Steady accumulation of retirement savings is one important phase of retirement security—steady withdrawal is the other challenge. From the Institute's perspective, retirees need options that help them make retirement income last. No one savings plan is right for every individual needing to save for retirement, and no one approach to drawing down assets is right for every individual during retirement. Both insurance products and lifetime payment accounts (LPAs) from mutual funds—which systematically withdraw assets over an investor's life expectancy—enable individuals

to secure a lifetime stream of payments in retirement. If Congress considers tax incentives to encourage retirees to annuitize their retirement income, they should cover LPAs as well as annuities.

The tax code today effectively requires that savers begin withdrawing from IRAs and certain retirement plans at age 70½. Given the length of time many will spend in retirement, and the fact that many may still be working full- or part-time at age 70½, this rule needs to change. Congress should delay the date by which retirement savers must begin withdrawals.

## **LIFETIME PAYMENT ACCOUNTS: MAKING RETIREMENT SAVINGS LAST**

A Lifetime Payment Account (LPA) is a systematic withdrawal program that provides periodic distributions from mutual fund accounts over an investor's expected lifetime. Based on long-established IRS methodology, a mutual fund will calculate the LPA distribution for each year. Upon the investor's death, the LPA's remaining balance goes to the investor's heirs.

For many individuals reaching retirement age, LPAs may be one of the simplest and most affordable vehicles available for retirement planning. With the average 65-year-old now expected to live into his or her 80s, the market exposure of LPAs, as a piece in a retiree's diversified investment portfolio, also would offer potentially high returns while helping combat inflation risk.

## SECTION II: ENCOURAGING A FRAMEWORK OF SOUND REGULATION

Mutual funds and fund investors depend on a strong and well-run regulator. As ICI President Paul Schott Stevens observed in a speech late last year, “[e]very public company, every securities firm, certainly every mutual fund organization, has an enormous interest in a successful SEC.” In serving fund shareholders, mutual funds have a keen interest in ensuring the SEC’s continued ability to effectively regulate not just funds, but also financial intermediaries, other market participants, and the securities markets themselves.

A Government Accountability Office report three years ago noted the complexities facing the SEC in fulfilling its mission. “The securities markets have undergone tremendous change and innovation... and the [SEC] faces growing regulatory and oversight challenges to stay abreast of these advances.

[T]echnology has changed the way investors can buy and sell securities...and how investors are solicited. ... Because more individuals and families are now invested in the markets, the role SEC plays has become even more important to the investing public.”

Conscious of the vital importance to funds and fund investors of maintaining a sound regulatory framework, the Institute, during the past 12 months, continued its historic role in representing funds before the SEC and other regulators by engaging actively on current rulemaking and reform efforts. In a time of leadership transition at the SEC, the Institute also identified and sought to focus attention on several broad policy themes that should serve as guideposts for future rulemaking.

**“U.S. securities markets have grown tremendously and become more complex and international. As a result, SEC’s workload has increased in volume and complexity over the past decade.”**

—FROM SEC OPERATIONS: INCREASED WORKLOAD CREATES CHALLENGES, A 2002 GAO REPORT

Specific highlights of ICI's regulatory activities during the past 12 months included:

- **COMPLETING WORK ON PENDING REFORMS.**

ICI encouraged the SEC to complete pending rulemaking designed to address late trading and abusive market timing and worked with members and other interested parties to help the SEC identify solutions to issues raised by the "hard 4 pm" proposal and the redemption fee rule.

- **IMPROVING CONDITIONS FOR FUNDS AS INVESTORS.** ICI worked to advance the interests of the millions of Americans who participate in the markets through mutual funds. On major SEC initiatives relating to market structure, ICI was successful in promoting its views on how best to ensure that securities markets remain vibrant, competitive, and cost-effective for investors.

- **IMPROVING DISCLOSURE TO FUND SHAREHOLDERS.**

ICI sought to ensure that proposed requirements for brokers to inform fund investors at the point of sale about costs and potential conflicts of interest will result in effective disclosure and will be consistent with the model by which brokers sell fund shares.

- **ENSURING CONTINUED VIBRANCY AND COMPETITIVENESS OF FUNDS.**

ICI urged that the SEC consider broad, competitive issues in formulating new rules—in particular, that funds compete against other investment products for investor attention. ICI called on the SEC to conduct more rigorous cost-benefit analyses of rule proposals, and to make other improvements to internal operations.

### EFFECTIVE REGULATION: PROTECTS INVESTORS, MAINTAINS FUND INDUSTRY VIBRANCY

A dynamic fund marketplace operating within a strong regulatory framework helps sustain the historically high degree of public confidence in mutual fund investing, and preserves funds as an indispensable tool for investors to achieve their long-term financial objectives. In 2005, 75 percent of fund owners familiar with the mutual fund industry say they have a favorable impression of mutual fund companies, an increase from 72 percent in 2004. Meanwhile, in the past five years, net investor inflows to stock and bond mutual funds have totaled about \$1 trillion.

#### MUTUAL FUND SHAREHOLDERS' FAVORABILITY RATING OF FINANCIAL INSTITUTIONS, 2005



*Note: Favorability rating is defined as mutual fund shareholders familiar with and having a "very" or "somewhat" favorable impression of a financial institution.*

*Source: ICI Mutual Fund Tracking Survey, 2005*

## COMPLETING WORK ON MUTUAL FUND REFORMS

The SEC has finalized and put into effect most of the comprehensive set of mutual fund reforms that it projected in 2003–2004. Further work remains necessary, however, to complete SEC initiatives to guard against “late trading” of mutual fund shares and to provide funds and intermediaries with additional tools to prevent abusive market timing. ICI continued to

work with members, the SEC, and other interested parties towards appropriate resolution of the many complex issues involved.

### HARD 4 PM PROPOSAL

To combat late trading, the SEC issued a proposal in February 2004 that would require that only mutual fund trades received by a fund or its transfer agent by 4:00 pm Eastern time receive that day's price. In

## MAJOR SEC RULEMAKING AFFECTING INVESTMENT COMPANIES IN 2004–2005

PROPOSED OR FINAL REQUIREMENTS	ICI POSITION
<b><i>Mutual Fund Rulemaking</i></b> <b>*HARD 4:00 PM CLOSE:</b> Purchase or redemption orders would have to be received by a mutual fund or its transfer agent by the time the fund prices its shares (usually 4:00 pm Eastern time) in order to receive that day's price.	Supports the SEC's effort to determine if an alternative approach would provide effective safeguards for funds while offering greater flexibility to fund investors.
<b>MUTUAL FUND REDEMPTION FEES:</b> Mutual fund boards must determine whether redemption fees are appropriate for the funds they oversee; funds must enter into contracts with intermediaries concerning shareholder identity and transaction information.	Final rule fails to allocate responsibilities appropriately between funds and intermediaries. Contract requirement grossly underestimates the associated challenges, costs, and burdens.
<b>*POINT-OF-SALE DISCLOSURE:</b> Broker-dealers would have to provide information to customers, at the point of sale and in transaction confirmations, regarding fund distribution and other costs and potential conflicts of interest.	SEC must address unintended consequences that could discourage brokers from selling mutual funds. SEC should designate the Internet as the primary medium for this disclosure, which would give investors timely and convenient access to the required information without placing undue burdens on brokers.
<b><i>Rulemaking Affecting Funds as Investors</i></b> <b>REGULATION NMS:</b> Four interrelated rules modernize and strengthen the regulatory structure of the national market system for equity securities.	Reg. NMS advances the key goals of institutional investors in market structure reform, which include liquidity, transparency, and price discovery. “Order Protection” rule is consistent with ICI recommendations.
<b>*HYBRID MARKET:</b> NYSE proposes to create a “hybrid” market that would blend aspects of the traditional NYSE auction market with those of an electronic securities market.	Proposal is an important step in implementing much needed automation on the NYSE and facilitating more efficient trading of listed securities.

\*Final action pending

response to the SEC's request for comments, some funds and fund intermediaries raised concerns that a hard 4 pm trade requirement could disadvantage investors, such as those in defined contribution plans or those who are located on the West Coast, because they would have to submit their orders well in advance of 4 pm or even the day before.

Consistently, the Institute has supported rigorous regulatory requirements to combat late trading, as well as the SEC's effort to identify practical solutions that will accommodate the legitimate interests of investors. To assist the SEC in this effort, ICI formed a working group with the Securities Industry Association (SIA) to explore technology-based

### MAJOR SEC RULEMAKING AFFECTING INVESTMENT COMPANIES IN 2004–2005 *continued*

#### PROPOSED OR FINAL REQUIREMENTS

**SECURITIES OFFERING REFORM:** Modernization of the registration, communications, and offering processes under the Securities Act of 1933 for public issuers other than investment companies.

**ASSET-BACKED SECURITIES:** Establishes a registration, disclosure, and reporting framework for asset-backed securities.

**\*SELF-REGULATORY ORGANIZATIONS (SROs):** Proposals address the governance and administration of SROs and the role and operation of the SRO system.

**\*NATIONALLY RECOGNIZED STATISTICAL RATING ORGANIZATIONS (NRSROs):** Proposed definition of NRSRO.

#### *Other*

**HEDGE FUND ADVISER REGISTRATION:** Advisers to certain private investment pools must register under the Investment Advisers Act.

**DISPOSAL OF CONSUMER REPORT INFORMATION:** Funds, advisers, and other entities that dispose of consumer report information must take reasonable measures to protect it from unauthorized access or use.

#### ICI POSITION

Mutual funds, as significant investors in securities, will benefit from a more efficient offering process. Rulemaking provides a framework for considering possible improvements to the fund offering and disclosure regime, including an "access equals delivery" disclosure model.

Mutual funds, as significant investors in asset-backed securities, will receive better and more timely information about such securities both at the time of purchase and on an ongoing basis.

Strongly supports efforts to strengthen SRO governance processes and regulatory programs and increase the transparency of SRO operations. SEC should avoid unnecessarily burdensome rules that could prevent SROs from fulfilling their regulatory responsibilities.

Recommends that SEC modify the NRSRO registration process to facilitate competition among credit rating agencies.

Registration requirement is a measured and appropriate response to address the risks that hedge funds pose to the securities markets and market participants.

Supports enhanced protection of investors' personal financial information. Flexible standard will allow funds and advisers to adopt policies and procedures that take into account their particular circumstances.

\*Final action pending

alternatives that might provide effective safeguards while offering greater flexibility than a hard 4 pm limit for mutual fund trades. The ICI/SIA working group has been reviewing alternatives, such as “time-stamping” individual fund transactions, that would reflect the realities of the financial services marketplace and prevent the conditions leading to past trading abuses. The working group expects to convey its recommendations to the SEC staff before year-end.

### REDEMPTION FEE RULE

Earlier this year, the SEC adopted a new rule that requires mutual fund boards of directors to determine whether redemption fees are necessary or appropriate for the funds that they oversee. The rule also requires funds to enter into written contracts with financial intermediaries that give funds the right to obtain investor-level trading information and enforce anti-market timing policies against the intermediary’s

customers. The rule imposes significant new responsibilities and potential liabilities on funds and poses major operational challenges (see *Implementation of the New Redemption Fee Rule*, page 41), all of which involve costs far exceeding SEC estimates. ICI has communicated these concerns and urged the SEC to address them as soon as possible.

### IMPROVING CONDITIONS FOR FUNDS AS INVESTORS

Mutual funds play a dual role in the financial marketplace—first, as an intermediary for individual investors and second, as investors themselves on behalf of fund shareholders. Participation in the equity markets has increased more than threefold since the early 1980s, with half of all U.S. households now owning stocks directly or through mutual funds. The integrity, functioning, and structure of the securities markets is therefore critically important to funds, as greater

### AMERICA'S OWNERSHIP SOCIETY CONTINUES TO GROW

(millions of U.S. households owning equities directly or indirectly through mutual funds)

Research conducted by ICI and the Securities Industry Association demonstrates the American public's increasing appetite for equity market investing, particularly through the convenient and cost-effective fund model.



Source: *Equity Ownership in America, 2005* ([www.ici.org/pdf/rpt\\_05\\_equity\\_owners.pdf](http://www.ici.org/pdf/rpt_05_equity_owners.pdf))

efficiencies in the markets result in lower costs and better execution for funds and hence for their shareholders. Engaging at the level of national policy to advance the interests of millions of average investors who participate in the equity markets through mutual funds continued to be a high priority for the Institute during FY 2005.

### **SEC REGULATION NMS: COMPREHENSIVE MARKET RESTRUCTURING**

In the case of the SEC's Regulation NMS, the most comprehensive restructuring of the securities markets in almost 30 years, ICI strongly supported the goals of the proposal—to create a market structure that furthers the objectives of the national market system that are so critical for investors, most significantly, efficiency, competition, price transparency, and the direct interaction of investor orders. In particular, ICI supported the new "trade-through" rule, which represents a significant step in providing protection for limit orders. In comments to the SEC, ICI supported applying the rule uniformly across all markets, and not based solely on the type of security and market in which a security is invested. Regulation NMS, as adopted, is consistent with these views.

*John Thain, CEO of the New York Stock Exchange, speaks at the Institute's ninth annual Equity Markets Conference.*



### **NYSE HYBRID MARKET PROPOSAL**

ICI also has been an active participant in regulatory initiatives to modify the way securities are traded on the New York Stock Exchange. The past year has continued to see the restructuring of the NYSE in terms of changes to its trading systems, including its proposal to become a "hybrid" market, integrating elements of a traditional auction market with those of an electronic market. While commending the NYSE for its bold restructuring, the Institute continued to encourage efforts to increase the automatic execution of orders and to promote the ability of investors to efficiently interact with those orders. The NYSE made several changes to the proposal in response to ICI comments.

## OTHER INITIATIVES IMPACTING FUNDS AS INVESTORS

ICI was active in promoting the interests of funds as investors in additional initiatives proposed by the SEC and other securities regulators, including those relating to the modernization of the securities offering reform process, the structure of self-regulatory organizations, and the reform of anti-manipulation and short sale rules. Going forward, ICI will continue to engage on these and other important issues affecting our securities markets to help achieve the full potential and preserve the integrity of these

markets, and thereby advance the interests of fund shareholders.

ICI also urged that the SEC address concerns regarding the confidentiality of mutual fund trading information. In a letter to SEC Chairman Christopher Cox, the Institute urged, among other things, that the Commission continue to vigorously enforce existing regulations protecting against the disclosure of confidential trading information and continue focusing on issues related to the leakage of information as it engages in examinations of market participants.

## ENGAGING FOREIGN REGULATORS, OFFICIALS

ICI works with foreign regulators and other officials to remove impediments to portfolio investing abroad by U.S. funds, strengthen corporate governance standards, and protect and facilitate U.S. funds' rights as shareholders. ICI also works to ensure that foreign laws and regulations do not discriminate against U.S. funds or impede the ability of U.S. investment management firms to serve foreign shareholders.

Highlights of ICI's work in FY 2005 included:

- **SHAREHOLDER RIGHTS, CROSS-BORDER VOTING IN EUROPE:** Reflecting ICI comments and coordination with foreign trade associations, an EU shareholder rights proposal will remove many obstacles to cross-border voting, making it easier for U.S. funds to exercise their rights as shareholders in European companies. ICI also conducted high-level meetings and seminars with EU officials to promote appropriate shareholder voting rights concepts.
- **REPORTING RULES, TAX TREATMENT IN ASIA:** At ICI's request, Korean securities regulators issued helpful clarifications relating to filings under new beneficial ownership reporting rules. At the request of ICI and others, India reduced capital gains taxes on investments in India.
- **IMPROVING FINANCIAL SERVICES COMPETITION WORLDWIDE:** ICI worked successfully with the U.S. government to help ensure that trade agreements negotiated with Australia and various Central American nations (through CAFTA) included provisions allowing cross-border portfolio management of mutual funds and promoting opportunities for U.S. firms to manage pension assets in other nations. ICI worked for the inclusion of similar provisions in seven other sets of foreign negotiations during the year.



*ICI Senior Counsel Mary Podesta and Wolfgang Mansfeld, President of the European Fund and Asset Management Association, discuss issues impacting U.S. and European mutual funds.*

## IMPROVING DISCLOSURE TO FUND SHAREHOLDERS

ICI continued to engage with the SEC during FY 2005 on how to improve disclosure provided to fund shareholders. The main area of focus in the past year was disclosure of costs and potential conflicts of interest related to the sale of mutual fund shares. Over the past 10 years, ICI repeatedly has called for enhanced disclosure to fund investors at the point of sale concerning payments made to brokers to promote the sale of fund shares. Such disclosure will help investors assess and evaluate recommendations to purchase fund shares. In FY 2005, the SEC requested supplemental comments on a 2004 proposal that would require brokers to disclose information to investors at the point of sale about the costs and potential conflicts of interest associated with selling mutual funds.

ICI continues to believe that investors would benefit from point-of-sale disclosure that effectively communicates relevant information in a timely and

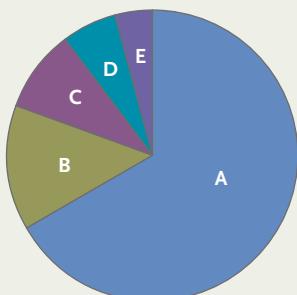
convenient manner. ICI has urged the SEC to craft rules that both recognize the widespread use of the Internet by investors and rely principally on the Internet to communicate required information. ICI also has emphasized that any point-of-sale disclosure requirement should be fully consistent with the industry's existing customer service model, one in which investors transact most business with brokers over the telephone.

In a related development, a NASD Mutual Fund Task Force issued a report last March recommending that the SEC require brokers to make available to investors at the point of sale a concise, easy to understand "Profile Plus." The document would describe a fund's material features and provide fee and expense and conflict-of-interest information similar to that required under the SEC's point-of-sale proposal. As conceived by the Task Force, brokers would make the Profile Plus available by posting it on their websites.

## MOST MUTUAL FUND SHAREHOLDERS USE THE INTERNET EVERY DAY

(percent\* of mutual fund shareholders with Internet access, by frequency of Internet use, 2005)

A: At least once a day	66%
B: 3 to 5 days a week	14%
C: 1 to 2 days a week	9%
D: Less than once a week	6%
E: Never in the past 12 months	4%



\*Components do not total 100 percent because of rounding.

Source: Investment Company Institute

Like the NASD Task Force, ICI believes that the Internet holds great promise as an innovative mechanism for furnishing fund information to investors. Not only can it facilitate disclosure that is timely, convenient, thorough, and flexible, but also it is well suited to serving a variety of needs and preferences for different levels of information. As such, the Internet could provide the needed breakthrough in what has been a repeated cycle of disclosure simplification efforts thwarted by a constant stream of new disclosure requirements.

The challenge of effectively communicating meaningful information to mutual fund investors is an ongoing one. The Institute has urged the SEC to confront this challenge head-on by undertaking a top-to-bottom review of the fund disclosure regime with the goal of improving the effectiveness of required disclosure. As part of this review, ICI has recommended that the SEC carefully study how to take full advantage of the Internet as a means of providing mutual fund disclosure.

## ENSURING THE CONTINUED VIBRANCY AND COMPETITIVENESS OF FUNDS

The transition to new leadership at the SEC provided an opportunity to reflect further on the regulatory framework for investment companies. ICI took advantage of this opportunity by offering suggestions to Chairman Christopher Cox on ways in which the Commission can promote an important objective that the SEC and the fund industry share—assuring that mutual funds remain a vibrant, competitive, and cost-effective way for average Americans to access the securities markets and realize their long-term financial goals.

In his letter to Chairman Cox, Institute President Paul Schott Stevens echoed the themes he articulated in May 2005 testimony before the Capital Markets Subcommittee of the House Financial Services Committee. In particular, he cited the need for the SEC to better inform itself about the economic consequences of its regulations and to avoid regulatory approaches that could have the effect

## REPRESENTING CLOSED-END FUNDS

The Institute has represented the interests of closed-end funds on regulatory and legislative matters since 1987. In FY 2005, the Institute asked the SEC to take into account the unique characteristics of closed-end funds when adopting final amendments to Regulation M under the Securities Exchange Act of 1934. In a presentation to a New York Stock Exchange working group reviewing the NYSE proxy rules, the Institute emphasized that eliminating brokers' ability to vote proxies in the absence of instructions from shareholders would be harmful to closed-end funds and their shareholders. Also, in response to Institute comments, NYSE determined not to modify continued listing standards for closed-end funds.

The Institute holds semi-annual closed-end fund committee meetings, providing members with a forum for discussing these and other issues and for interaction with regulators on rulemaking that affects closed-end fund operations. In 2005, the Institute organized meetings between closed-end fund members and staff from the NYSE and the American Stock Exchange to enhance working relationships and to discuss matters that members would like the exchanges to address. The Institute plans to hold these meetings annually.



### SEC LEADERSHIP TRANSITION

Christopher Cox served 17 years in the U.S. House of Representatives prior to his unanimous confirmation by the Senate to succeed William Donaldson as Chairman of the SEC this past summer. While in the House, Congressman Cox served in a leadership capacity as a senior member of every committee with jurisdiction over investor protection and the U.S. capital markets. His efforts to eliminate the double tax on shareholder dividends—the subject of his 1977 Harvard University thesis—led to the enactment in May 2003 of legislation that cut the double tax by more than half.

*Christopher Cox was sworn in as the 28th Chairman of the Securities and Exchange Commission on August 3, 2005.*

In a statement applauding his confirmation, ICI President Paul Schott Stevens observed, “The broad bipartisan support for his nomination underscores the quality of leadership and breadth of experience that Chris Cox brings to his new post.”

of making mutual funds less competitive, less innovative, less attractive to talented investment firms and professionals, and less available to investors.

In communications with legislators and regulators, ICI stressed that funds compete with a multitude of other financial products for investor dollars, and that regulators need to consider carefully the competitive realities in the financial services marketplace when proposing and enacting reforms. If regulation causes intermediaries to favor less regulated financial products over mutual funds, dissuades portfolio managers from managing mutual funds versus other investment products, or discourages investment advisers from entering or staying in the fund business, then the federal regulatory regime is not effectively serving the interests of investors. To avoid these results, it is important for regulators to take into account potential unintended consequences of rulemaking initiatives.

### IMPROVING SEC OPERATIONS

To ensure the continued effectiveness of its regulatory and enforcement efforts, ICI believes it is imperative for the SEC also to focus on internal management reforms, including improvements to the process for evaluating the economic consequences of rule proposals. ICI has emphasized the need for the SEC to engage in a more rigorous cost-benefit analysis process on several occasions over the past year. A June 2005 court decision finding that the SEC failed to meet its statutory obligation to consider the effect of proposed rules on “efficiency, competition, and capital formation” brought additional, needed attention to this issue. The court observed that the SEC has a “statutory obligation to do what it can to apprise itself—and hence the public and the Congress—of the economic consequences of a proposed regulation before it decides whether to adopt the measure,” and that this obligation extends to anticipated compliance costs and to examination of all reasonable alternatives.



Institute President Paul Schott Stevens testifies at a May 2005 House Financial Services subcommittee hearing concerning the mutual fund regulatory landscape: "The Institute applauds the Subcommittee for providing this timely forum to take stock of where we are and consider how to shape mutual fund regulatory policy going forward so that it will continue to serve the interests of fund investors."

## LEGISLATORS: ASSESSING THE REGULATORY LANDSCAPE FOR MUTUAL FUNDS

ICI testified about fund industry regulation before a House Financial Services subcommittee in May 2005. Institute President Paul Schott Stevens stressed the need for regulation that considers the competitive realities of the marketplace.

"Developments since 2003 are reassuring," Stevens observed. "Our legal and regulatory system has worked as designed to identify, correct, and prevent misconduct, and to hold investors harmless. Strong, corrective market forces have been at work as well. The result has been to sustain the historically high degree of public confidence in mutual fund investing—and thus to preserve to average Americans an indispensable tool to achieve their long-term financial objectives."

Citing the court's decision in its submission to Chairman Cox, ICI recommended that the SEC revise its internal rules to provide for careful attention to the economic consequences of regulatory proposals, better identification and quantification of compliance costs, and more thorough consideration of alternative proposals. ICI fully intends to assist the SEC in these efforts, and is taking steps to develop the capacity to do so. These steps include forming a working group of members to provide data on the costs and benefits associated with implementation of, and ongoing compliance with, regulatory requirements. A new senior economist joined the ICI research staff this year to lead the Institute's efforts in this area (see *Understanding Fund Industry Dynamics*, on page 32, for more information on this effort).

Among the other internal reforms ICI recommends the SEC undertake are: central coordination of all SEC inspections of the same firm; more limited use of sweep examinations; and better coordination among the various SEC divisions and offices that have responsibility for mutual fund issues, to ensure appropriate and consistent application of regulatory policy.

"A strong, effective SEC is a matter of vital importance to mutual funds and their shareholders," said ICI President Paul Schott Stevens following Cox's confirmation. "We congratulate him as he undertakes his duties as SEC Chairman, and we look forward to working with him and all members of the Commission on matters affecting America's mutual funds."

## THE INDEPENDENT DIRECTORS COUNCIL

ICI has long promoted and supported the vital role of fund directors, offering outreach programs geared toward fund directors. For example, the Independent Directors Council, formally launched in May 2004, is an expansion of an Institute directors' program formed in 1995. IDC provides a forum to advance the education, communication, and policy positions of mutual fund independent directors. IDC also benefits from access to the Institute's wide array of research, data, and other resources.

The Governing Council consists of 21 independent directors, and invites all fund directors to participate in the IDC's programs and activities. In its first full year of operation, IDC has carried out its mission to promote the highest standards of fund governance, keeping investment company directors current on issues that affect their duties under federal and state law in a rapidly evolving financial services landscape.

### IDC EVENTS PROMOTE DIRECTOR AWARENESS

In the past 12 months, IDC activities provided directors with continuing professional development and education opportunities and promoted public understanding of fund governance issues and the work of directors. IDC hosted approximately 20 events and meetings for directors, including a fall conference focusing on current regulatory and policy issues affecting funds and their shareholders and a spring workshop highlighting issues of particular interest to investment company directors. IDC maintains director "chapters" across the country to further facilitate discussion among fund directors about governance issues affecting funds, their shareholders, and directors. The IDC conducted chapter meetings in nine cities during the past year, where participants focused on implementation of new rules concerning fund compliance practices, the independent chair requirement, and self-evaluation procedures.

### IDC TASK FORCES TACKLE INDUSTRY ISSUES

IDC task forces promote director views on topical issues and suggest practices to improve fund governance. In FY 2005, IDC released three task force reports. One report concerned director oversight of multiple funds, concluding such oversight is appropriate given the unique structure of mutual funds and because of the benefits to shareholders of such arrangements, including enhanced board effectiveness and efficiency. Two other reports addressed issues relating to implementation of the independent chair requirement as well as issues fund boards may wish to consider when complying with the new requirement mandating annual board self-assessments.

IDC also issued a formal statement of policy on soft dollars, recommending a narrower safe harbor under Section 28(e) so that only brokerage services and bona fide research are covered, and collaborated with ICI and ICI Mutual Insurance Company on the first installment in a series of papers on issues funds and fund directors should consider in developing and administering valuation policies and procedures.

IDC maintains a website ([www.idc1.org](http://www.idc1.org)) with more information on its history, activities, and mission.



*James Bodurtha, Independent Director at Merrill Lynch Funds, speaks at the 2004 Investment Company Directors' Conference, which was attended by 242 independent directors from 127 fund complexes.*

## SECTION III: COMMUNICATING WITH THE PUBLIC

Mutual fund assets reached a record nearly \$8.6 trillion as of September 2005, demonstrating the continued tremendous popular appeal of an investment model that has enabled American households to harness the potential of the world's securities markets. Given the sheer size of the mutual fund sector—and the importance of funds in the U.S. economy—accurate public information on funds, fund shareholders, and fund investing is crucial.

The Institute has served as the authoritative source for such information. The centerpiece of ICI's public communications effort is a wide-ranging research program that analyzes data and compiles reports on more than 15,000 investment companies, on U.S. households and individuals who own funds, on the

channels through which they invest, and on other fund industry economic topics.

In diverse ways—interacting daily with the media, through speeches, op-eds, press conferences, and other public events; in outreach to opinion leaders, policymakers, and academics; and through public policy websites and other educational sites and programs—the Institute provides a broad audience with comprehensive and authoritative data on investment companies and their shareholders. ICI statistical releases examine asset and cash flow trends, and provide a reliable gauge of fund and fund shareholder activity. Research publications take a broader look at ICI's massive data collections, offering detailed examinations of the economics of the fund industry.

**"I am a 28-year-old black male, out of college three years. This website has given me so many ideas on ways I can put my money to good use. Thank you so much!"**

—RESPONSE FROM A USER OF THE *INVESTING FOR SUCCESS* INTERACTIVE WEBSITE, FEBRUARY 2005

In 2005, highlights of the Institute's public communications activities included:

- **INFORMING POLICY DISCUSSIONS AFFECTING FUND INDUSTRY DYNAMICS.** ICI research and statistics helped inform policymakers about the realities of the financial services marketplace in which funds operate. ICI research also promoted public understanding of competitive forces in the industry, including investor demand and its impact on fund services and costs.
- **ENHANCING THE BODY OF STATISTICS AND RESEARCH ON FUND SHAREHOLDERS.** ICI continued to play a leading role in promoting understanding of fund shareholders. ICI research

focused on the important role funds play in promoting savings opportunities for Americans, particularly through 401(k) plans and IRAs, and fund shareholders' use of professional financial advisers to meet their investment objectives.

- **OFFERING A WIDE RANGE OF INVESTOR EDUCATION RESOURCES TO THE PUBLIC.** ICI continued to promote or enhance investor education initiatives on behalf of the mutual fund industry, primarily through the work of the ICI Education Foundation.

### **ICIEF PARTNERSHIP INTRODUCES MUTUAL FUNDS TO STUDENTS AND TEACHERS NATIONWIDE**

As the result of a partnership between the Institute's Education Foundation and the Foundation for Investor Education (FIE), this past year, for the first time in its 28-year history, funds were included in the Stock Market Game™ program (SMG), an Internet simulation used by half a million students in grades 4–12 each year. In addition to selecting individual stocks, students can now also choose from among all mutual funds. Curriculum materials developed by the partnership emphasize the importance of a long-term perspective while the simulation teaches the “mechanics” of investing.

The inclusion of mutual funds in the SMG program recognizes the increasing participation in securities markets through these investment vehicles. “We get feedback that many SMG discussions revolve around mutual funds since a majority of working families have 401(k)s. Teachers in their own TIAA-CREF retirement plans must decide on which funds to invest in and they, in turn, benefit from learning more about mutual funds,” FIE’s Executive Director Kathleen Floyd reports. Both the Maryland and Virginia Councils on Economic Education will be piloting a mutual-fund only SMG program in the 2005–06 school year.



*Students participating in the nation's oldest and best-known market simulation can now choose from among mutual funds, as well as individual stocks.*

*ICI's new Chief Public Communications Officer Greg Ahern (c.) participates in a panel discussion of the media's role in, and perceptions of, the fund industry at the 2005 General Membership Meeting. Journalist Myron Kandel (l.) moderated the panel, which also included Bloomberg News columnist Chet Currier (r.), Kiplinger's Personal Finance senior editor Manuel Schiffres, and MONEY senior editor Walter Updegrave.*



## UNDERSTANDING FUND INDUSTRY DYNAMICS

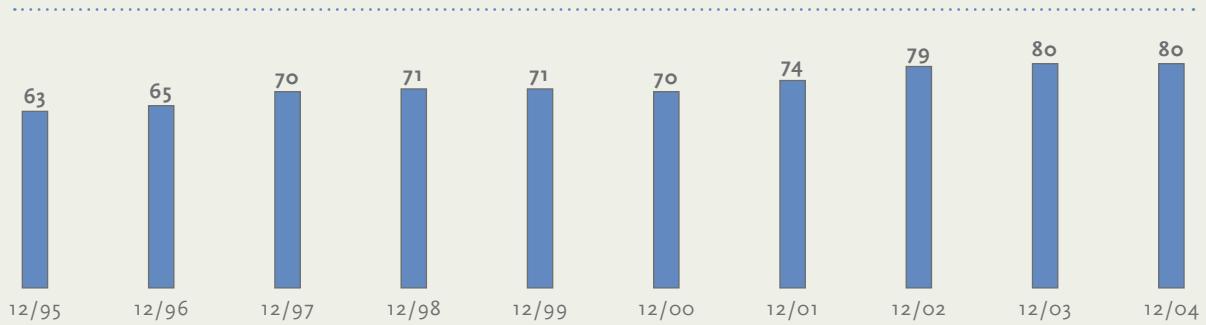
ICI research makes a uniquely important contribution to the body of knowledge that informs public policymaking. In interaction with Congress and the Administration, and in submissions to the SEC, other regulators, and federal agencies, ICI relies on the wide body of its research to inform and support its policy positions.

For example, academic researchers have generally advocated that rigorous cost-benefit analysis is crucial to an effective regulatory process. In April 2005, ICI

enhanced its expertise in this area with the addition of a new PhD economist to engage in cost-benefit analyses of fund regulatory and legislative initiatives. As a result, beginning in FY 2005, ICI has sought to comment on these aspects of rule proposals. For example, ICI research helped point out the potential costs of a new mutual fund redemption fee rule. While ICI supported the SEC in its effort to curb harmful short-term trading, it noted that the costs entailed in its rule far exceeded the agency's estimate. Working with its members, ICI anticipates conducting selected cost-benefit studies of enacted rules as well as future rule proposals.

## INVESTORS TEND TO OWN FUNDS WITH LONG PERFORMANCE RECORDS

(percent of stock and bond fund assets in funds with 10-year performance record, year-end)



Source: Investment Company Institute

## FUND COMPETITION AND INVESTOR DEMAND

ICI research also serves to promote public understanding of the highly competitive and dynamic marketplace for fund investing: hundreds of mutual fund sponsors compete to attract and retain the loyalty of millions of investors who can “vote with their feet” in search of funds or other investment products that best deliver performance and service at a competitive cost. For example, ICI research found that, in 2004, shareholders redeemed about one-quarter of their stock and bond mutual fund assets and, in every year since 1990, between one-quarter and one-half of fund sponsors experienced net outflows from their long-term funds.

## EXAMINING FUND COSTS

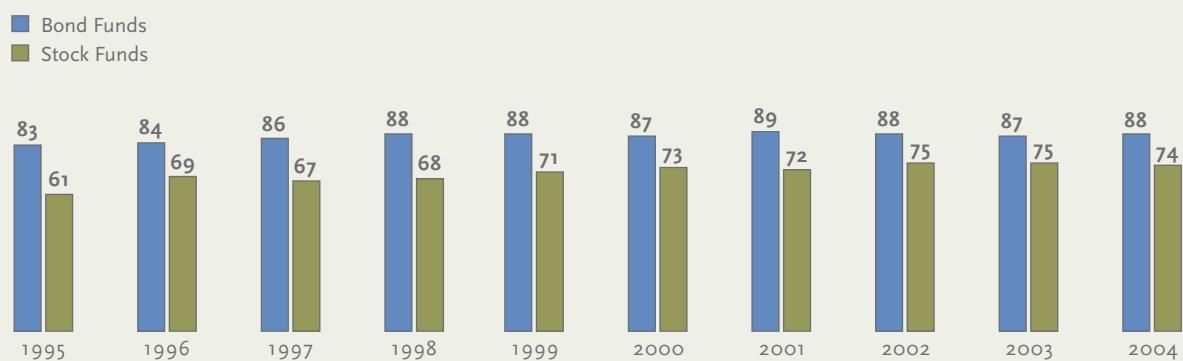
ICI has long examined trends in the cost of fund ownership. Institute research clearly demonstrates that, although shareholders pay attention to fund performance and service, they also focus on fund

fees and expenses. Investors hold most of their stock and bond fund assets in funds charging below-average operational and management expenses. The demand for lower-cost stock funds seems particularly notable in recent years. ICI research in FY 2005 observed that about 90 percent of the net “new cash” flowing into stock funds in 2003 and 2004 went to funds with costs lower than the median fund, compared with 75 percent of the flows to funds below the median in the mid-1990s.

Not surprisingly, the overall cost of fund ownership has trended downward as well: ICI research finds the fees and expenses incurred by investors who purchase mutual funds have been on the decline since 1980. For example, the average fees and expenses that shareholders incurred by investing in equity funds declined 113 basis points, a reduction of 49 percent, between 1980 and 2004.

### INVESTORS HOLD LOWER COST STOCK AND BOND FUNDS

(percent of stock and bond fund assets invested in funds with operating expense ratios below the median)



Sources: Investment Company Institute; Lipper; Value Line Publishing, Inc.; CDA/Wiesenberger Investment Companies Service; © CRSP University of Chicago, used with permission, all rights reserved (773.702.7467/www.crsp.com); Primary datasource & © Standard & Poor's Micropal, Inc. 1998 (617.451.1585/www.micropal.com); and Strategic Insight Mutual Fund Research and Consulting, LLC

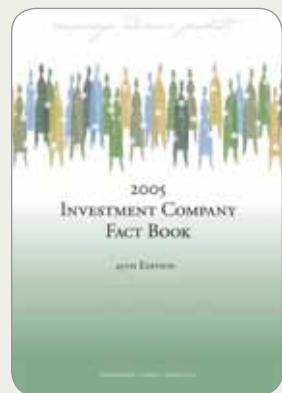
## THE ICI RESEARCH PROGRAM

ICI is an authoritative source of statistical information on mutual funds and other investment companies, compiling and analyzing data on more than 15,000 investment companies as well as the U.S. households and individuals who own funds. In FY 2005, the Institute released roughly 100 statistical releases and reports to increase public understanding of funds and fund shareholders.

Highlights of ICI's research effort in FY 2005 included:

- “401(k) Plan Asset Allocation, Account Balances, and Loan Activity in 2004,” *Perspective*, September 2005
- “Mutual Funds and the U.S. Retirement Market in 2004,” *Fundamentals*, August 2005
- “Are S&P 500 Index Mutual Funds Commodities?” *Perspective*, August 2005
- “The Influence of Automatic Enrollment, Catch-Up, and IRA Contributions on 401(k) Accumulations at Retirement,” *Perspective*, July 2005
- *Investment Company Fact Book*, May 2005
- “Ownership of Mutual Funds Through Professional Financial Advisers,” *Fundamentals*, April 2005
- “How Mutual Funds Use 12b-1 Fees,” *Fundamentals*, February 2005
- “The Individual Retirement Account at Age 30: A Retrospective,” *Perspective*, February 2005
- “IRA Ownership in 2004,” *Fundamentals*, February 2005
- “Total Shareholder Cost of Mutual Funds, 2003,” *Fundamentals*, December 2004
- “Mutual Funds and Portfolio Turnover,” *Research Commentary*, November 2004
- “Shareholder Sentiment of the Mutual Fund Industry,” *Fundamentals*, October 2004
- “U.S. Household Ownership of Mutual Funds in 2004,” *Fundamentals*, October 2004
- “Profile of Mutual Fund Shareholders,” *Research Series*, Fall 2004

For a more complete, updated list of ICI research publications and statistical releases, visit the Institute's public website at [www.ici.org/stats/index.html](http://www.ici.org/stats/index.html).



In May 2005, the Institute published the 45th annual edition of its Investment Company Fact Book, a comprehensive look at trends in the fund industry and a ready source of historical statistics on funds and their shareholders.

## UNDERSTANDING FUND OWNERS: NEEDS AND OBJECTIVES

More than 90 million individuals, with a wide range of financial objectives and service needs, currently own mutual fund shares. Evidence compiled by the Institute indicates these investors are knowledgeable about their investments, serving as a potent force that drives fund industry competition, innovation, and product and service differentiation. ICI engages in multiple research projects each year to improve understanding of fund owners, including the role that funds play in investors' pursuit of short- and long-term financial objectives, investors' confidence in fund services, and, more generally, how and why investors choose funds.

Increasingly, ICI research finds, investors purchase fund shares through intermediaries: retirement plan sponsors and financial advisers. In FY 2005, ICI research helped provide an accurate picture of the investors who owned fund shares purchased through these two major distribution channels.

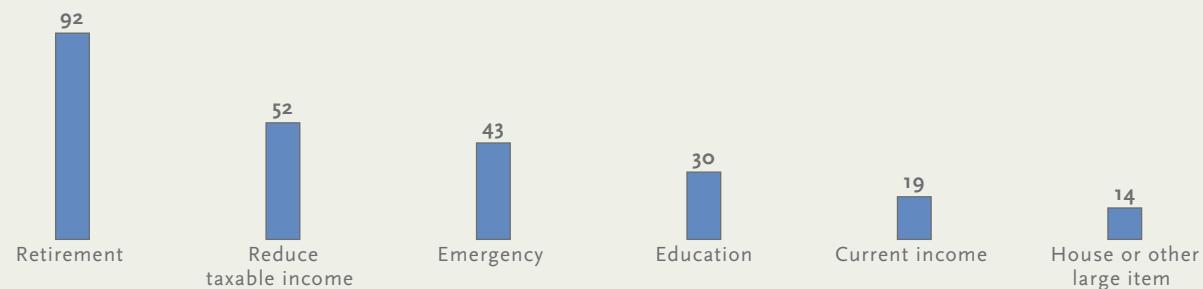
## ENCOURAGING UNDERSTANDING OF THE RETIREMENT SAVING MARKET

ICI research has long indicated that funds play a central role in Americans' retirement saving. With the growth of 401(k) plans, retirement plans at work have become a common source through which individuals invest in mutual funds. More than 60 percent of mutual fund shareholders currently hold funds through these plans.

To increase understanding of 401(k) plan participants, ICI has collaborated for several years with the Employee Benefit Research Institute (EBRI) to maintain the world's largest repository of information about individual 401(k) plan participant accounts. At year-end 2004, the EBRI/ICI database included statistical information about 16.3 million 401(k) plan participants in 45,783 employer-sponsored 401(k) plans. Analysis of the database in FY 2005 indicates that consistent participation has had a significant impact on individuals' ability to accumulate sizeable gains in 401(k) account balances since 1999.

## FINANCIAL GOALS FOR MUTUAL FUND INVESTORS

(percent of mutual fund shareholders, 2004)



Source: Profile of Mutual Fund Shareholders ([www.ici.org/pdf/rpt\\_profile04.pdf](http://www.ici.org/pdf/rpt_profile04.pdf))

ICI research in FY 2005 also pointed out the valuable role IRAs can play in helping Americans save. With proper policy direction, IRAs successfully promote and sustain retirement saving among many Americans. IRAs were the largest component of the \$12.9 trillion U.S. retirement market, representing more than one out of every four retirement dollars. ICI noted that individuals' strong response to IRA rollover policies underscores the importance of simplicity in IRA design. For example, 91 percent of U.S. households with rollover assets transferred the entire balance from their employer-sponsored account when making their most recent rollover, a sign that they are aware of the importance of maintaining these assets for retirement. Furthermore, ICI finds increased use of new types of IRAs introduced in the late 1990s, representing a positive response to the savings opportunities they offer.

## USE OF ADVISERS TO PURCHASE FUNDS

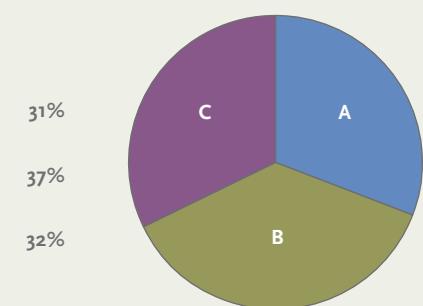
ICI has consistently pointed to the assistance that professional financial advisers provide as an intermediary between funds and shareholders. ICI finds that, among investors owning fund shares outside defined contribution plans, more than 80 percent currently own fund shares through financial advisers, including full-service brokers, independent financial planners, insurance agents, bank or savings institution representatives, and accountants. Nearly half own funds solely through advisers, while another third own funds purchased from advisers as well as from fund companies, fund supermarkets, or discount brokers. Fourteen percent solely own funds purchased without the help of a financial adviser.

In FY 2005, this research helped provide an industry context for the SEC's consideration of a "point-of-sale" disclosure requirement. ICI research also

### WHERE SHAREHOLDERS OWN FUNDS

(percent of all mutual fund shareholders, 2004)

- A: Inside and outside defined contribution retirement plans
- B: Outside defined contribution retirement plans only
- C: Inside defined contribution retirement plans only



Source: Ownership of Mutual Funds Through Professional Financial Advisers ([www.ici.org/pdf/fm-v14n3.pdf](http://www.ici.org/pdf/fm-v14n3.pdf))

helped increase policymaker understanding of the current use of 12b-1 fees—now overwhelmingly used to compensate financial advisers and other financial intermediaries for assisting fund investors before and after they purchase fund shares.

## PROMOTING INVESTOR EDUCATION

The Institute created the ICI Education Foundation (ICIEF) in 1989 to underscore its continuing commitment to shareholders by partnering with government agencies and other nonprofit organizations to develop, support, and enhance investor education initiatives. For example, this past year, in partnership with the Foundation for Investor Education, ICIEF introduced mutual funds into the Stock Market Game™ curriculum, which reaches half a million students and their teachers nationwide. The Foundation also participated:

- in the White House Conference on Aging “mini-conference” on financial literacy,
- in “Financial Literacy Day” on Capitol Hill,
- in the Financial Literacy and Education Commission’s development of a national strategy to promote financial literacy,
- in the National Endowment for Financial Education’s Financial Literacy Symposium,
- in the FNMA Foundation’s study on financial literacy education in the U.S., and
- on the boards of the American Savings Education Council and Alliance for Investor Education.

## FUNDING YOUR FUTURE: NEW ICI WEBSITE EDUCATES ABOUT SAVINGS CHALLENGES



ICI launched a website in September 2005 ([www.FundingYourFuture.org](http://www.FundingYourFuture.org)) to increase public awareness about the need to improve personal savings in America and encourage support for measures that would help Americans save more.

In addition, the Foundation continued its work with the National Urban League, Hispanic College Fund, and Society for Financial Education and Professional Development to bring investor education programs to underserved communities through nationwide workshops, at Historically Black Colleges and Universities, and through interactive web courses available in English ([www.investingforsuccess.org](http://www.investingforsuccess.org)) and Spanish ([www.invertirconexito.org](http://www.invertirconexito.org)).

## SECTION IV: SERVING ICI MEMBERS

Mutual funds have always operated in a highly regulated environment, yet the pace of regulatory reform in recent years has been unprecedented. Since September 2003, the SEC has adopted or proposed a multitude of new fund industry regulations. As a result, ICI members have confronted the need to implement a host of new requirements while ensuring ongoing compliance with a wide variety of existing rules. Some of the new and pending rules pursued by the SEC highlight the complexity of a fund's relationships with a range of intermediaries—an enormous and vitally necessary architecture in which thousands of broker-dealers, banks, insurance companies, and retirement plans help facilitate fund investing.

The Institute worked proactively throughout FY 2005 to support members' efforts to conduct their business activities in an ethical, compliant, and efficient manner.

Highlights of ICI efforts in these areas over the last 12 months included:

- **HELPING MEMBERS IMPLEMENT NEW REGULATORY REQUIREMENTS.** ICI continued to assist with implementation of the SEC's fund compliance rule, and also worked with members and intermediaries to address implementation issues surrounding the new redemption fee rule.
- **SUPPORTING ONGOING REGULATORY COMPLIANCE EFFORTS.** ICI held special programs and provided other resources and tools to assist mutual funds, their directors, and investment advisers in complying with applicable laws and regulations.

**"Our fiduciary duty is something that never changes. ... As you in your compliance roles work through the thicket of laws and regulations and procedures that govern our business, always take time to consult this basic principle. If you abide by it, you cannot go far wrong."**

—PAUL SCHOTT STEVENS, WELCOMING REMARKS AT ICI'S 2005 COMPLIANCE PROGRAMS CONFERENCE

- KEEPING MEMBERS INVOLVED AND INFORMED.** ICI continued its ongoing efforts to facilitate vitally important member participation in—and awareness of—ICI's policy and other activities. The Institute provides a wide range of resources—conferences, workshops, publications, and other communications efforts—to keep members informed of, and involved with, legal, regulatory, legislative, and other developments that impact fund operations and shareholder services.

## HELPING MEMBERS IMPLEMENT NEW REGULATORY REQUIREMENTS

When the SEC adopted a mutual fund compliance rule in December 2003, its decision set into motion one of the most labor-intensive rule implementation efforts for funds in recent years. Indeed, the obligations imposed by the compliance rule affect—and will continue to affect—fund operations each and every year. While funds have cleared the initial hurdles of the rule, there is much yet to be done.



*At the ICI's 2005 Mutual Funds and Investment Management Conference, Oliver Quinn (l.), Enterprise Business Ethics Officer at Prudential Financial, and Hal Liebes, formerly Chief Compliance Officer at AMVESCAP PLC, participated in a panel discussion on the ethical obligations of fund lawyers and compliance professionals.*

## ENCOURAGING HIGH ETHICAL STANDARDS

The bylaws of the Institute set forth an ICI mission of encouraging adherence to high ethical standards by all participants in the investment company industry. This has never seemed more important than in the aftermath of the trading abuses first uncovered in 2003.

Financial institutions, because they are so extensively regulated, are given to thinking in terms of “compliance” or “risk management”—not “ethics,” observed ICI President Paul Schott Stevens in a December 2004 address at the Exchequer Club in Washington, DC. Stevens noted that these institutions develop compliance policies and procedures and train their workforces to implement and adhere to them. By contrast, “ethics” is something that resides in a culture or ethos, not a policy or procedure. Fund advisers stand in a trusted fiduciary relationship to their funds and shareholders. Such a relationship

implies far higher obligations and exacts far stricter loyalty than the morals of the marketplace generally. If a fund firm is to succeed, it must develop an ethical culture in which these truths are deeply embedded.

How can a trade association help its members on an issue of this nature? One approach is to use the Institute’s numerous conference programs, on a continuing basis, to put ethical obligations and issues on the table for our members. This past year, for example, ethics panels, roundtable discussions, and presentations by experts on this topic were featured at the Investment Company Directors’ Conference, the Mutual Funds and Investment Management Conference, the Mutual Fund Compliance Programs Conference, and the General Membership Meeting.

In FY 2005, effective implementation of the mutual fund compliance rule continued to be a high priority for both ICI and its members. ICI devoted significant resources to programs and initiatives designed to assist members in their implementation efforts. For example, ICI launched a new Chief Compliance Officer (CCO) Committee—made up exclusively of fund and adviser CCOs—to provide a forum to bring compliance challenges into sharper focus for CCOs by discussing issues and procedures with their peers. The committee held its initial meeting in Washington, DC last fall and a second round of meetings in various regions of the country in March 2005. The opportunity to discuss issues of common concern attracted more than 250 attendees to these meetings.

To provide information to members about how different fund complexes are implementing the compliance

rule, ICI developed and fielded an industry-wide compliance survey. The Institute expects to make the results available to survey participants in late 2005. In addition, ICI continues work on a white paper addressing possible methods that funds might use to test the effectiveness of their compliance programs.

ICI compliance workshops in Boston, Chicago, and San Francisco during FY 2005 featured both experienced CCOs and SEC staff members as speakers. In addition, ICI held its second annual Mutual Fund Compliance Programs Conference in Washington, DC. In conjunction with the conference, members of the CCO Committee and the Compliance Advisory Committee had an opportunity to meet with staff of the SEC's Office of Compliance Inspections and Examinations to discuss issues arising under the compliance rule.



From left to right, Barbara H. Kipp, chief privacy officer at PricewaterhouseCoopers LLP, Robert M. Gates, president of Texas A&M University; Dawn-Marie Driscoll, an independent director at Scudder Funds; Dr. James Weber, business ethics professor at Duquesne University; and John J. Brennan, CEO with the Vanguard Group, Inc. discuss actions that can be taken to foster and enhance an ethical culture throughout a fund organization at ICI's 2005 Mutual Fund Compliance Programs Conference.

## IMPLEMENTATION OF THE NEW REDEMPTION FEE RULE

The mutual fund redemption fee rule adopted by the SEC in March 2005—scheduled to go into effect in October 2006—represents yet another new rule posing significant implementation issues and

challenges for mutual funds. The rule requires fund boards to determine whether redemption fees are necessary or appropriate to recoup the costs of short-term trading or prevent dilution in the funds that they oversee. It also requires mutual funds and financial intermediaries to enter into written “transparency

## IMPLEMENTATION OF BREAKPOINT TASK FORCE RECOMMENDATIONS PROGRESSES

At the request of the SEC, the NASD spearheaded a task force in 2003—including representatives from ICI and its members—to ensure that financial intermediaries provide appropriate sales load discounts to investors. Since 2003, the Institute organized several working groups to implement task force recommendations, which included efforts to improve disclosure to investors and develop procedures and standards that facilitate proper breakpoint calculations. Of the 13 separate task force recommendations, all but two—which present the largest operational challenges—are fully implemented.

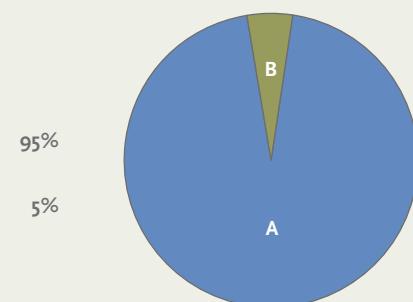
Over the past 12 months, ICI continued its efforts to facilitate implementation of the central database of funds' breakpoint schedules and policies and improved transparency of shareholder account data. With ICI's assistance—in particular the special efforts of Kathy Joaquin of the Institute's operations group led by Don Boteler—ICI member firms that together accounted for more than 90 percent of last year's sales of front-end load shares populated Depository Trust and Clearing Corporation's Profile Service. The Profile Service provides mutual fund intermediaries with a centralized source of information about breakpoint opportunities for their clients.

ICI's operations group also continues to lead the effort to facilitate improved transparency of account information between funds and their intermediaries to further ensure that fund investors receive sales load discounts to which they are entitled. Work on this final recommendation is now two-thirds complete, with the remaining work expected to be completed in early 2006.

## MUTUAL FUND PARTICIPATION IN NEW BREAKPOINT DISCLOSURE SERVICE

(percent of 2004 front-end load fund new sales represented by participating fund complexes)

- A: Sales of complexes participating/planning participation in Mutual Fund Profile Service
- B: Sales of complexes not yet participating in Mutual Fund Profile Service



Source: Investment Company Institute

## HURRICANE KATRINA: ASSESSING THE EFFECTS ON FUND SHAREHOLDERS AND FUND OPERATIONS

ICI serves as a focal point for developing the fund industry's response to operational issues, particularly in times of crisis. In the past, this role was critically important when the Institute spearheaded the fund industry's involvement in a multi-year effort to prepare for the Y2K transition in the financial services industry and following the September 11 terrorist attacks. This role re-emerged this past August when Hurricane Katrina battered the Gulf Coast region of the United States.

The scale of the humanitarian crisis following Katrina's devastation quickly became apparent, and set into motion an industrywide effort to consider the ramifications for those fund shareholders affected and the best way for funds to respond to their needs on an operational level.

At about the time the first evacuees were entering the Houston Astrodome on Thursday, September 1, ICI staff organized an industry conference call to assess operations issues, discuss the actions funds could take, and formulate a request for guidance from the SEC. For example, funds had to consider the effects of United States Postal Service decisions to reroute first-class mail deliveries (including fund statements as well as redemption and dividend checks) to bulk-storage trailers in Texas and suspend third-class mail deliveries (including shareholder reports and prospectuses) indefinitely. The implications for fund shareholders in the region became apparent—access to their assets and account information would be severely hampered at a time of great need.

Concerns in the fund industry soon arose about the security of confidential shareholder information and the ability of the Postal Service to expeditiously deliver forwarded mail—and much-needed sources of income—to recipients. For example, fund operations personnel debated whether it would be more beneficial to hold redemption checks and reinvest dividends until shareholders themselves were in a position to access their funds.

After ICI discussed these issues with the SEC staff, the SEC granted relief from certain regulatory requirements to allow funds to halt mailings according to the postal service requests and, more importantly, to respond flexibly to the needs of affected shareholders.

ICI Mutual Insurance Company (ICIM) informed its insured funds that it would work closely with them to ensure that robust coverage remains available for losses resulting from third-party frauds associated with the displacement of fund shareholders by the hurricane. ICIM stated it would address the needs of fund groups to use alternative shareholder authentication methods, waivers of standard hold periods for address changes, and similar temporary measures for handling transaction requests from shareholders in the hurricane-stricken areas.



### Affected Populations—

Louisiana, Mississippi, and Alabama: 7.1 million residents

*ICI headed up the industry's response to the devastation caused by Hurricane Katrina. The Institute and its members assessed operations issues and discussed potential options funds could take to ensure fund shareholders had access to their assets and account information.*

contracts" with intermediaries that provide funds with the right to obtain investor-level trading information and the right to enforce anti-market timing policies against the intermediary's customers.

To help members implement the new rule, ICI has urged the SEC to significantly narrow the definition of "financial intermediary" under the rule, which would substantially reduce the number of required transparency contracts. In addition, ICI is leading an initiative, with the help of the Securities Industry Association, to develop model contract clauses that funds and intermediaries could use to satisfy the rule's requirements concerning transparency and trading restrictions. Finally, ICI is working with fund companies, banks, retirement plan recordkeepers, omnibus broker-dealers, industry service providers, and the Depository Trust and Clearing Corporation (DTCC) on the development of a standardized, centralized process that can be used by funds and intermediaries to facilitate requests for and delivery of shareholder

trading data. This solution, which the working group plans to implement prior to the rule's October 16, 2006 compliance date, will allow the information to be provided on a more cost-effective and efficient basis than is possible through non-standardized, non-centralized methods in use today.

## SUPPORTING ONGOING COMPLIANCE EFFORTS

In addition to helping members implement new rules, ICI expanded efforts to assist members in serving fund shareholders by focusing significant attention and resources on ongoing legal and regulatory compliance. ICI offered specialized programs, practical guidance, and other tools addressing a broad variety of subject areas. One such area is fair valuation.

Mutual funds must determine the value of each portfolio security every business day. Appropriate valuation of fund portfolio securities is critical to ensure that fund share prices derived from those valuations will be fair to purchasing, redeeming,

## ASSISTING FUND COMPLIANCE WITH FEDERAL AND STATE LAWS AND REGULATIONS, FY 2005

TOPIC	ICI MEMBER SERVICES
ANTI-MONEY LAUNDERING COMPLIANCE	Held an Anti-Money Laundering Workshop in Boston and offered West Coast videoconference participation
CODES OF ETHICS	Updated the <i>Drafting Guide for Codes of Ethics</i> to address new investment adviser code of ethics requirements
NON-1940 ACT INVESTMENT RESTRICTIONS	Updated the <i>Summary of Non-1940 Act Investment Restrictions</i> and made it available to members in an easy-to-navigate electronic format
SECURITIES LENDING	Issued a Securities Lending Alert highlighting regulatory obligations and areas to evaluate with respect to fund lending programs

and current shareholders. Under the Investment Company Act of 1940, securities for which market quotations are “readily available” must be valued at market value, and all other securities and assets must be valued at “fair value” as determined in good faith by the fund’s board. This simple legal framework belies the complexity underlying that valuation process, and especially fair valuation.

The topic of fair valuation received renewed focus in the wake of revelations of abusive market timing, due to concerns that the use of stale prices can make funds vulnerable to abuse. For example, in adopting the fund compliance rule, the SEC outlined four obligations relating to fair valuation. In 2004, the SEC amended fund disclosure rules to require disclosure of the circumstances under which funds will use fair value pricing and the effects of using fair value pricing.



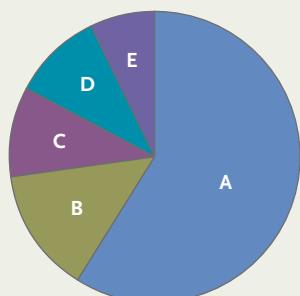
As part of its ongoing efforts to assist funds and their boards in understanding fair valuation compliance obligations, earlier this year ICI published “An Introduction to Fair Valuation,” the first installment of the Institute’s new *Fair Valuation Series*. Produced in collaboration with ICI Mutual Insurance Company and the Independent Directors Council, this paper

### ICI SUPPORTS A DIVERSE MEMBERSHIP

(percent of ICI investment adviser members by type of intermediary, 2005)

Nearly 600 financial intermediaries from around the world compete in the U.S. market. U.S. fund and trust sponsors include independent financial advisers, banks, insurance companies, securities broker-dealers, and non-U.S. firms.

A: Independent Investment Advisers	59%
B: Non-U.S. Sponsors	14%
C: Insurance Companies	10%
D: Banks or Thrifts	10%
E: Brokerage Firm “Wirehouses”	7%



Source: Investment Company Institute

provides an overview of issues funds should consider in developing and administering valuation policies and procedures.

### **KEEPING ICI MEMBERS INVOLVED AND INFORMED**

ICI provides a variety of specialized services to keep its investment company members, their directors, officers, and employees involved and informed of ICI activities. ICI hosts meetings throughout the year at its headquarters in Washington, DC to bring ICI members together to help guide and inform the Institute's policy work. Fifteen standing committees and 29 industry advisory committees, task forces, and working groups bring together industry executives and personnel from numerous disciplines to tackle the broad range of fund-related regulatory, operations, and business issues year-round. ICI also engages in regular member visits and other outreach activities to become more familiar with the issues and priorities affecting individual fund groups and the investors they serve. During FY 2005, for example, ICI staff visited more than 30 fund management companies and 12 fund boards as part of the member visit program.

### **ICI CONFERENCES, WORKSHOPS, AND OTHER RESOURCES**

ICI further facilitates member outreach and participation with various conferences, workshops, websites, publications, and other resources that provide more formal opportunities to keep abreast of industry issues, trends, and developments, and also offer the opportunity to interact with an even more diverse array of industry participants, including government regulators and legislators, and industry observers and experts.

Fourteen major Institute conferences and workshops were held during FY 2005, and ICI plans 10 more in FY 2006. An important addition to the Institute's slate in 2005 was its Mutual Fund Leadership Dinner and Policy Forum, held this past May, which offered senior fund company executives and the independent directors of leading fund boards the opportunity to interact directly with Members of Congress, SEC leadership, and senior Administration officials. Government-industry dialogue of this kind has never been more essential in view of the rapid pace of developments in the domestic and international marketplace for financial services. The Leadership Dinner and Forum will be an annual ICI event.

## SECTION V: APPENDICES

### APPENDIX A: ICI ORGANIZATION AND FINANCIALS

ICI is a 501(c)(6) organization that represents investment companies on regulatory, legislative, and securities industry initiatives that affect mutual funds and their shareholders. As of September 30, 2005, ICI members included 8,518 U.S.-registered open-end investment companies, 663 U.S.-registered closed-end investment companies, 148 exchange-traded funds, five sponsors of unit investment trust sponsors, 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 on page 51 for a list of ICI's Board). The Institute employs a staff of 166 (see Appendix E on page 56 for a description of each ICI Department). ICI's Board of Governors is composed of 46 representatives of mutual fund sponsors and independent fund directors. Governors are elected annually to staggered three-year terms and represent a broad cross-section of the fund industry. The Board is

### 2005 EXECUTIVE COMMITTEE



*Standing (l. to r.): Stephen H. Hopkins, Mitchell M. Merin, Paul G. Haaga, Jr., Paul Schott Stevens, James S. Riepe, William M. Lyons, John V. Murphy, Lynn L. Anderson, Martin L. Flanagan*

*Seated (l. to r.): Abigail P. Johnson, James H. Bodurtha, John J. Brennan, Dawn-Marie Driscoll, John W. McGonigle*

*Not pictured: John F. Cogan, Jr., Robert H. Graham, Brent R. Harris, John W. Rogers, Jr., Brian T. Zino*

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 include a 15-person 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 has also appointed a Chairman's Council to oversee the Institute's political action programs, including the political action

committee—ICI PAC. The Chairman's Council includes six Governors as well as the Institute's president and chief operating officer.

The Institute's policy work is guided by 15 standing committees that bring together more than 1,300 industry professionals. In addition, 29 industry advisory committees, task forces, forums, and working groups with more than 1,900 participants tackle a broad range of regulatory, operations, and business issues, such as mutual fund pricing, transfer agent operations, and Section 529 Education Savings Plans. Institute committees perform a number of important roles, including assisting with the analysis and formulation of policy positions, and gathering and disseminating information about industry practices (see Appendix D on page 55 for a list of Institute standing committees). In these and all of its activities, the Institute strictly observes federal and state antitrust laws, in accordance with a well-established compliance policy and program.

## 2005 INDEPENDENT DIRECTORS COUNCIL



*Standing (l. to r.): Susan B. Kerley, Samuel M. Eisenstat, C. Gary Gerst, Donald H. Pratt, James H. Bodurtha, Anthony Deering, Dawn-Marie Driscoll, Clayton K. Yeutter, Marvin L. Mann, Jock Patton, Vanessa C. L. Chang, Ranne P. Warner*

*Seated (l. to r.): Robert W. Uek, Rosalie J. Wolf, Robert D. Neary, Dorothy A. Berry, David A. Hughey*

*Not pictured: Darlene DeRemer, Howard J. Kerr, Robert E. La Blanc, C. Alan MacDonald, Thomas F. Morrissey, Thomas E. Stitzel, Roman L. Weil, James W. Zug*

## 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 the annual expense budget and the member dues rate. The Board of Governors considers both the Institute's core and self-funded activities when they approve the annual dues rate.

**CORE ACTIVITIES** (i.e., regulatory, legislative, operational, economic research, and public communication initiatives in support of investment companies, their shareholders, directors, and advisers) are public policy related. Reflecting the Institute's strategic

focus on issues affecting mutual funds, 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, approximately 90 percent, of ICI total revenues comes from dues, investment income, royalties, and miscellaneous program sources (see Figure 5.1). Similarly, by design, over 90 percent of the Institute's total resources are devoted to core activities (see Figure 5.2). Core expenses support the wide range of initiatives described in this *Annual Report*.

**SELF-FUNDED ACTIVITIES** (i.e., conferences and special surveys) are supported by separate fees paid by companies and individuals who participate in these

FIGURE 5.1

**TOTAL REVENUES: FY 2005 = \$47,194,409**

A: Self-Funded Income	13%
B: Core Income	87%

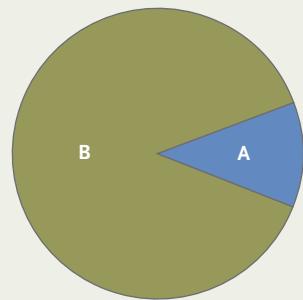
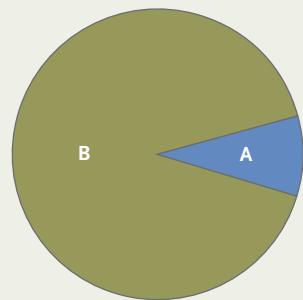


FIGURE 5.2

**TOTAL EXPENSES: FY 2005 = \$45,204,756**

A: Self-Funded Expenses	9%
B: Core Expenses	91%



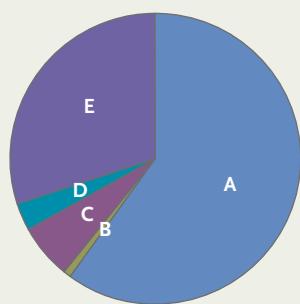
activities. The financial goal for self-funded activities is that fees should cover all direct out-of-pocket costs plus provide a margin to cover associated staff costs to ensure that these activities are not subsidized by member dues. Each year a portion of the net profit from self-funded activities is contributed to the ICI Education Foundation and to support the Institute's government affairs efforts (see Figure 5.3).

**DUES:** Between FY 1996 and FY 2004, as mutual funds experienced rapid growth, the annual dues rate declined by 33 percent as a result of a series of Board-approved discounts from the standard dues schedule. During this period, open-end fund dues declined from \$0.116 per \$10,000 of industry assets to \$0.046 per \$10,000 of industry assets (see Figure 5.4).

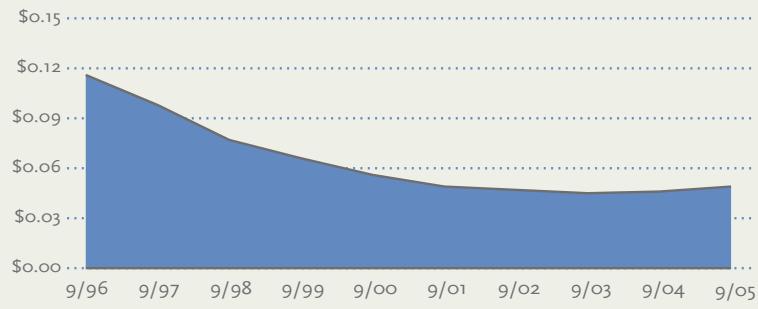
At the beginning of this year when the Board of Governors reviewed the many policy challenges and strategic goals mutual funds and the Institute would need to address, Board members approved an increase in the FY 2005 open-end fund dues rate of approximately 14 percent. This increase caused open-end fund dues to rise to \$0.049 per \$10,000 of industry assets, the same rate assessed in FY 2001. The Board earmarked the additional dues to replenish and provide the resources ICI will need to help mutual funds address the regulatory and legislative challenges that lie ahead and sustain an adequate level of financial reserves.

**FIGURE 5.3**  
**SELF-FUNDED ACTIVITIES: FY 2005**

A: Conferences	60%
B: ICIEF Contributions	1%
C: Surveys and Publications	6%
D: Government Affairs Activities	3%
E: Net Profit	30%



**FIGURE 5.4**  
**DUES PER \$10,000 OF ASSETS**



## INVESTMENT COMPANY INSTITUTE UNAUDITED FINANCIAL STATEMENTS

### **STATEMENT OF FINANCIAL POSITION (September 30, 2005)**

#### **Assets**

Cash and cash equivalents	\$545,257
Investments, at market value	37,984,073
Accounts receivable	351,529
Prepaid expenses	962,745
Furniture, equipment and leasehold improvements, net (less accumulated depreciation of \$8,276,514)	2,981,384

Total assets

\$42,824,988

#### **Liabilities and Net Assets**

Payroll and related charges accrued and withheld	\$11,666,056
Accounts payable and accrued expenses	4,010,067
Deferred revenue	551,844
Rent incentives	2,291,089
Total liabilities	18,519,056
Undesignated net assets	23,305,932
Board designated net assets	1,000,000
Total net assets	24,305,932
Total liabilities and net assets	\$42,824,988

### **STATEMENTS OF ACTIVITIES AND CHANGES IN NET ASSETS (Year Ended September 30, 2005)**

#### **Core—Income**

Membership dues	\$38,033,706
Investment income	1,125,902
Royalty income	1,059,301
Program income	1,033,842
Total core—income	41,252,751

#### **Core—Expenses**

Administrative expenses	\$31,093,434
Program expenses	7,358,084
Depreciation and lobby proxy tax	2,585,907
Total core—expenses	41,037,425
Changes in net assets—core	215,326

#### **Self-Funded Income**

Conferences	\$5,038,094
Other self-funded income	903,564
Total self-funded income	5,941,658

#### **Self-Funded Expenses**

Conferences	\$3,612,175
Other self-funded expenses	555,156
Total self-funded expenses	4,167,331
Changes in net assets—self-funded	1,774,327
Changes in net assets	1,989,653
Net assets, beginning of year	22,316,279
Net assets, end of year	\$24,305,932

These financial statements are preliminary unaudited statements as of 9/30/05. Audited financial statements for the fiscal year ended 9/30/05 will be available after 2/1/06. For information on obtaining copies of the audited statements, please contact Larry Maffia at 202/326-5800.

**APPENDIX B: 2006 BOARD OF GOVERNORS**  
*(as of October 7, 2005)*

Mr. Martin L. Flanagan<sup>1,6</sup>

*ICI Chairman &*

*President & Chief Executive Officer*

AMVESCAP PLC

Mr. James S. Riepe<sup>1</sup>

*ICI Vice Chairman &*

*Vice Chairman*

T. Rowe Price Group, Inc.

Ms. Anne F. Ackerley\*

*Managing Director*

BlackRock Investments, Inc.

Mr. Lynn L. Anderson<sup>2</sup>

*Vice Chairman*

Russell Investment Group

Mr. William L. Armstrong<sup>5</sup>

*Independent Chairman & Trustee*

OppenheimerFunds

Mr. James H. Bodurtha<sup>1,2,4</sup>

*Independent Director*

Merrill Lynch Funds

Mr. John J. Brennan<sup>1,2</sup>

*Chairman & CEO*

The Vanguard Group, Inc.

Mr. Stephen E. Canter

*Chairman & CEO*

The Dreyfus Corporation

Mr. Christopher W. Claus\*

*President & CEO*

USAA Investment Management Company

Mr. John F. Cogan, Jr.\*

*Chairman*

Pioneer Investment Management USA, Inc.

Mr. Anthony W. Deering<sup>1,5</sup>

*Independent Director*

T. Rowe Price Funds

Mr. John D. DesPrez, III<sup>1</sup>

*President & CEO*

John Hancock Financial Services, Inc.

Mr. Andrew J. Donohue

*General Counsel & First Vice President*

Merrill Lynch Investment Managers

Mr. Robert S. Dow<sup>1,6</sup>

*Managing Partner*

Lord, Abbett & Co. LLC

Mr. Kenneth C. Eich

*COO*

Davis Selected Advisers, L.P.

Mr. Ralph C. Eucher

*President & CEO*

Principal Mutual Funds

Mr. Dennis H. Ferro\*

*President, CEO & CIO*

Evergreen Investment Management Company LLC

Mr. Mark R. Fetting<sup>6</sup>

*President, Asset Management*

Legg Mason, Inc.

Mr. George C. W. Gatch<sup>6</sup>

*President & CEO, J.P. Morgan Funds*

J.P. Morgan Fleming Asset Management Inc.

Mr. C. Gary Gerst\*

*Independent Director & Chairman*

Harris Insight Funds

Mr. Paul G. Haaga, Jr.<sup>1</sup>

*Executive Vice President*

Capital Research and Management Company

Mr. Charles E. Haldeman, Jr. <sup>3</sup> <i>President &amp; CEO</i> Putnam Investments	Ms. Abigail P. Johnson <sup>1</sup> <i>President</i> Fidelity Employer Services Corporation
Mr. Thomas L. Hansberger <sup>*3</sup> <i>President &amp; CEO</i> Hansberger Global Investors, Inc.	Mr. Gregory E. Johnson <i>President &amp; CEO</i> Franklin Resources, Inc.
Mr. Peter A. Harbeck <i>President &amp; CEO</i> AIG SunAmerica Asset Management Corp.	Mr. Peter S. Kraus* <i>Co-Head of Investment Mgmt. Division</i> Goldman Sachs & Co.
Mr. Brent R. Harris <sup>1,3,6</sup> <i>Chairman</i> PIMCO Funds	Mr. William M. Lyons <sup>1,6</sup> <i>President &amp; CEO</i> American Century Investments
Mr. James B. Hawkes <sup>2</sup> <i>Chairman, President &amp; CEO</i> Eaton Vance Corporation	Mr. John W. McGonigle <sup>*6</sup> <i>Vice Chairman</i> Federated Investors, Inc.
Mr. James M. Hennessy <i>President &amp; CEO</i> ING Funds	Mr. Mitchell M. Merin <sup>1</sup> <i>President &amp; COO, Investment Management</i> Morgan Stanley
Ms. Diana P. Herrmann <i>CEO &amp; Vice-Chair</i> Aquila Investment Management LLC	Mr. Randall W. Merk* <i>EVP &amp; President, Asset Mgmt. Products &amp; Services</i> Charles Schwab & Co., Inc.
Mr. John A. Hill <sup>5</sup> <i>Chairman of the Trustees</i> Putnam Funds	Ms. Paula R. Meyer <i>Sr. Vice President &amp; Managing Director</i> Ameriprise Financial Services, Inc.
Ms. Mellody Hobson <i>President</i> Ariel Capital Management, LLC	Mr. Brian A. Murdock <sup>3</sup> <i>President</i> New York Life Investment Management LLC
Ms. Edith E. Holiday* <i>Independent Director</i> Franklin Templeton Funds	Mr. John V. Murphy <sup>1,6</sup> <i>Chairman, President &amp; CEO</i> OppenheimerFunds, Inc.
Mr. Stephen H. Hopkins <sup>*3</sup> <i>COO</i> Citigroup Asset Management	Dr. Alfred E. Osborne, Jr. <sup>5</sup> <i>Independent Trustee</i> WM Group of Funds

Mr. William G. Papesh

*President*

WM Advisors, Inc.

Mr. Robert C. Pozen

*Chairman*

MFS Investment Management

Mr. Thomas O. Putnam

*Chairman*

Fenimore Asset Management, Inc.

Ms. Ruth H. Quigley<sup>5</sup>

*Independent Director*

AIM Family of Funds

Ms. Judy Rice\*

*President*

Prudential Investments

Mr. Lewis A. Sanders

*Chairman & CEO*

Alliance Capital Management L.P.

Mr. William N. Shiebler

*Vice Chairman, Deutsche Asset Mgmt., Americas*

Deutsche Asset Management, Inc.

Mr. Michael D. Strohm\*<sup>2</sup>

*CEO*

Waddell & Reed, Inc.

Mr. Peter E. Sundman

*President*

Neuberger Berman Management Inc.

Mr. Garrett Thornburg

*Chairman & CEO*

Thornburg Investment Management, Inc.

Mr. Robert W. Uek<sup>5</sup>

*Independent Trustee*

TT International Funds

Mr. John C. Walters

*Executive Vice President*

Hartford Life, Inc.

Mr. Lloyd A. Wennlund\*

*Exec. Vice President & Managing Director*

Northern Trust Global Investments

Mr. Christopher L. Wilson

*Head of Mutual Funds*

Columbia Management Group, Inc.

Dr. Patricia K. Woolfs

*Independent Director*

American Funds

Mr. Brian T. Zino<sup>1,6</sup>

*President*

J. & W. Seligman & Co. Incorporated

\* Governor on Sabbatical

<sup>1</sup> Executive Committee member

<sup>2</sup> Audit Committee member

<sup>3</sup> Investment Committee member

<sup>4</sup> Chairman of the Independent Directors Council

<sup>5</sup> Participant in Independent Directors Council activities

<sup>6</sup> Chairman's Council member

## **APPENDIX C: INDEPENDENT DIRECTORS COUNCIL**

(as of October 7, 2005)

### **Chairman:**

James H. Bodurtha  
*Independent Director*  
Merrill Lynch Funds

### **Governing Council:**

Dorothy A. Berry  
*Independent Director*  
Professionally Managed Portfolios

Vanessa C. L. Chang  
*Independent Director*  
New Perspective Fund

Darlene DeRemer  
*Independent Director*  
Nicholas-Applegate Funds

Samuel M. Eisenstat  
*Independent Director*  
AIG SunAmerica Funds  
*Independent Trustee*  
Anchor Series Trust

David A. Hughey  
*Independent Director*  
FAM Funds

Susan B. Kerley  
*Independent Director*  
CitiFunds  
*Independent Director*  
NY Life Eclipse Funds

Howard J. Kerr  
*Independent Director*  
Van Kampen Funds

Robert E. La Blanc  
*Independent Director*  
Prudential Mutual Funds

C. Alan MacDonald  
*Independent Director*  
Lord Abbett Funds

Marvin L. Mann  
*Independent Director*  
Fidelity Funds

Thomas F. Morrissey  
*Independent Director*  
Victory Funds

Robert D. Neary  
*Independent Director*  
Armada Funds

Jock Patton  
*Independent Director*  
ING Funds

Donald H. Pratt  
*Independent Director*  
American Century Funds

Thomas E. Stitzel  
*Independent Director*  
Columbia Funds

Robert W. Uek  
*Independent Director*  
Hillview Group of Investment Companies  
and TT International Funds

Ranne P. Warner  
*Independent Director*  
Allmerica Funds

Roman L. Weil  
*Independent Director*  
NY Life MainStay VP Funds

Rosalie J. Wolf  
*Independent Director*  
Bernstein Funds Group

Clayton K. Yeutter  
*Independent Director*  
OppenheimerFunds

James W. Zug  
*Independent Director*  
Brandywine Funds

## **APPENDIX D: ICI STANDING COMMITTEES AND CHAIRS**

(as of October 7, 2005)

### **Accounting/Treasurers**

Mr. Richard J. Thomas  
*Senior Vice President & Treasurer*  
Federated Investors

### **Chief Compliance Officer**

Mr. James M. Davis  
*Director, Global Compliance*  
Franklin Templeton Investments

### **Closed-End Investment Company**

Mr. John D. Diederich  
*Managing Director & Chief Operating Officer*  
Royce & Associates, LLC

### **International**

Mr. Murray L. Simpson  
*Executive VP & General Counsel*  
Franklin Resources, Inc.

### **Investment Advisers**

Mr. Michael F. Rosenbaum  
*Managing Director & General Counsel*  
Citigroup Asset Management

### **Operations**

Mr. Douglas L. Anderson  
*Senior Vice President*  
Delaware Investments

### **Pension**

Mr. Dennis Simmons  
*Principal—Legal*  
The Vanguard Group, Inc.

### **Public Communications**

Mr. Ivy B. McLemore  
*Director of Communications*  
AIM Investments

### **Research**

Ms. Hannah S. Grove  
*Managing Director & Chief Marketing Officer*  
Merrill Lynch Investment Managers

### **Sales Force Marketing**

Mr. Keith F. Hartstein  
*President & CEO*  
John Hancock Funds

### **SEC Rules**

Ms. Heidi Stam  
*General Counsel*  
The Vanguard Group, Inc.

### **Shareholder Communications**

Mr. David M. Maher  
*Vice President—Customer Communications*  
Fidelity Investments

### **Small Funds**

Ms. Diana P. Herrmann  
*CEO & Vice Chair*  
Aquila Investment Management LLC

### **Tax**

Mr. Donald C. Burke  
*First Vice President & Treasurer of Funds*  
Merrill Lynch Investment Managers

### **Unit Investment Trust**

Mr. Steven M. Massoni  
*Managing Director, UIT Division*  
Van Kampen Investments, Inc.

## **APPENDIX E: ICI STAFF**

(as of October 7, 2005)

### **EXECUTIVE OFFICE**

The Executive Office, under the direction of the Board of Governors, is responsible for the strategy and overall management of the Institute.

Paul Schott Stevens\*

*President*

Lawrence R. Maffia

*Executive Vice President and Chief Operating Officer*

### **GOVERNMENT AFFAIRS**

The Government Affairs Department represents the mutual fund industry before the Administration and U.S. Congress on securities, tax, pension, and other legislative initiatives that affect investment companies and their shareholders.

Daniel F. C. Crowley

*Chief Government Affairs Officer*

### **INDEPENDENT DIRECTORS COUNCIL**

The Independent Directors Council ([www.idc1.org](http://www.idc1.org)) enhances outreach and education activities for independent directors and helps communicate their views more effectively to policymakers and the media.

Marguerite Bateman

*Managing Director*

### **LAW**

The Law Department represents the Institute before various governmental bodies, including the SEC, the IRS, the Departments of Labor and Treasury, state governments, and foreign and international authorities. The Law Department also advises in securities and financial regulation, tax, pension, and other policy and legal issues of interest to ICI.

Elizabeth R. Krentzman

*General Counsel*

Robert C. Grohowski

*Senior Counsel—International Affairs*

Amy B.R. Lancellotta

*Senior Counsel—Securities Regulation*

Keith D. Lawson

*Senior Counsel—Tax Law*

Mary S. Podesta

*Senior Counsel—Pension Regulation*

### **OPERATIONS AND CONTINUING EDUCATION**

The Operations and Continuing Education Department seeks solutions to traditional back-office business problems through studies, coordination of activities with other segments of the securities industry, and guidance on mutual fund accounting, reporting, and operations. The Continuing Education Group produces self-paced education programs for industry professionals and also produces an annual directory of fund service providers.

Donald J. Boteler

*Vice President—Operations and Continuing Education*

\*Member of Executive Committee of ICI's Board of Governors; Chairman's Council member

## PUBLIC COMMUNICATIONS

The Public Communications Department disseminates information on funds, investing, and shareholders through daily interaction with the media, in regular public commentary, through speeches, op-eds, press conferences, and other public events, and through its public website.

F. Gregory Ahern  
*Chief Public Communications Officer*

Susan J. Duncan  
*Assistant Vice President—Public Communications*

Edward Giltenan  
*Head of Media Relations*

## RESEARCH

The Research Department maintains a comprehensive program of industry research and statistical data collections. The Research staff collects and disseminates industry statistics, and conducts research studies relating to issues of public policy, economic and market developments, and shareholder demographics.

Brian K. Reid  
*Chief Economist*

## ADMINISTRATION

The Administration Department provides support services for other Institute departments, including conference management, information technology, and accounting, library, membership, and office services.

Thomas S. Simmons  
*Vice President—Administration*

## HUMAN RESOURCES

The Human Resources Department is responsible for Institute recruitment and staffing, employee benefits, staff training and development, compensation, performance management, and employee relations.

Mary D. Kramer  
*Vice President—Human Resources*

## INFORMATION SERVICES

The Information Services Department is responsible for managing the Institute's member website, <http://members.ici.org>, and facilitating the electronic transmission of statistical data and other industry information between the Institute and its members.

Mark W. Walecka  
*Vice President—Information Services*

## ICI EDUCATION FOUNDATION

The ICI Education Foundation (ICIEF), a 501(c)(3) educational affiliate of the Investment Company Institute, partners with U.S. government agencies and other nonprofit organizations to help develop, promote, and enhance investor education initiatives on behalf of the mutual fund industry.

Lawrence R. Maffia  
*President*

Susan J. Duncan  
*Vice President*

## ICI MUTUAL INSURANCE COMPANY

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, and advisers. To purchase insurance from ICIM, an organization must be an ICI member.

Natalie Shirley  
*President*

## APPENDIX F: CONFERENCES, WORKSHOPS, AND LEARNING COURSES

### INSTITUTE FISCAL YEARS 2005–2006 CONFERENCES AND WORKSHOPS

October 3–6, 2004	Tax & Accounting	San Antonio, TX
October 12, 2004	Mutual Fund Compliance	Chicago, IL
October 20–22, 2004	Investment Company Directors <sup>5</sup>	Washington, DC
October 27, 2004	Mutual Fund Compliance	San Francisco, CA
November 7–10, 2004	Operations	Orlando, FL
November 18, 2004	Mutual Fund Compliance	Boston, MA
December 6–7, 2004	Securities Law Developments <sup>1</sup>	Washington, DC
February 24, 2005	Anti-Money Laundering	Boston, MA (San Mateo videoconference)
March 13–16, 2005	Mutual Funds and Investment Management <sup>2</sup>	Palm Desert, CA
May 1–4, 2005	Globalisation of Mutual Funds <sup>3</sup>	Bermuda
May 11–13, 2005	General Membership Meeting	Washington, DC
June 23–24, 2005	Mutual Fund Compliance Programs	Washington, DC
September 18–21, 2005	Tax & Accounting	Chicago, IL
September 22, 2005	Equity Markets	New York, NY
October 23–25, 2005	Operations & Technology	Austin, TX
November 2–4, 2005	Investment Company Directors <sup>5</sup>	Washington, DC
November 15–17, 2005	West Coast Investment Company Directors <sup>5</sup>	Scottsdale, AZ
December 12–13, 2005	Securities Law Developments <sup>1</sup>	Washington, DC
March 9–10, 2006	Mutual Fund Compliance Programs	Washington, DC
March 19–22, 2006	Mutual Funds and Investment Management <sup>2</sup>	Scottsdale, AZ
May 7–10, 2006	Globalisation of Mutual Funds <sup>3</sup>	Bermuda
May 17–19, 2006	General Membership Meeting	Washington, DC
September 26–29, 2006	Tax & Accounting	Orlando, FL

<sup>1</sup> Sponsored by the ICI Education Foundation

<sup>2</sup> Cosponsored by the Federal Bar Association and ICI

<sup>3</sup> Cosponsored by the International Bar Association and ICI

<sup>4</sup> Cosponsored by the Independent Directors Council and ICI

<sup>5</sup> Sponsored by the Independent Directors Council

## SIX ICI LEARNING COURSES

The Fundamentals of Mutual Funds	A two-part course covering the nature and organization of mutual funds.
Mutual Funds: Communications with the Public	A two-part course covering the rules and regulations governing a mutual fund's communications with the public.
IRA Fundamentals for Financial Industry Professionals	A detailed overview of the fundamentals of Traditional IRAs, Roth IRAs, Simplified Employee Pension (SEP) IRAs, and Savings Incentive Match Plans for Employees (SIMPLE) IRAs.
Retirement Plan Distributions, Loans, and Withdrawals	An exploration of the types of distributions available from tax-qualified retirement plans and the options a retirement plan participant has when he/she is eligible to receive a distribution. The course also covers retirement plan loans, hardship withdrawals, and qualified domestic relations orders.
Retirement Plan Fundamentals for Financial Industry Professionals	A detailed overview of the tax advantages of retirement plans, contribution limits, plan sponsor responsibilities, and the key requirements of qualified retirement plans. Specific types of plans covered by the course include 401(k) plans, 403(b) plans, profit-sharing plans, and money purchase pension plans.
The Role and Responsibilities of a Mutual Fund Transfer Agent	A detailed overview of the organization and operation of a mutual fund transfer agent.

*For more information on ICI courses, visit [www.icilearning.org](http://www.icilearning.org).*







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