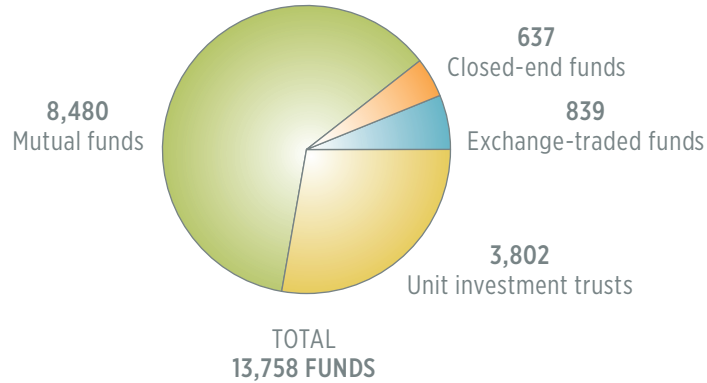




# Who Does ICI Represent?

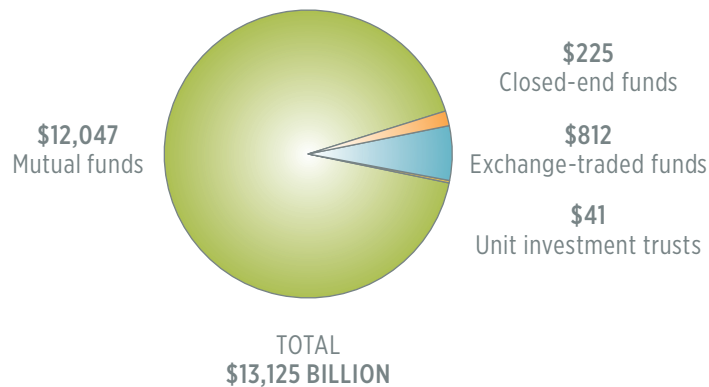
## More than 13,000 funds\*

Number of investment companies by type



## With more than \$13 trillion in assets\*

Investment company assets, billions of dollars



## Serving more than 92 million shareholders

Ownership of funds offered by investment companies, 2011

**45.0 percent**  
OF U.S. HOUSEHOLDS  
OWN FUNDS

**53.4 million**  
U.S. HOUSEHOLDS  
OWN FUNDS

**92.3 million**  
INDIVIDUALS  
OWN FUNDS

\*Data for mutual funds, closed-end funds, and exchange-traded funds are as of June 2011. Data for unit investment trusts are as of December 2010.

Source: Investment Company Institute

# Contents

<b>To Our Members: Letter from Paul Schott Stevens, ICI President and CEO</b> .....	2
<b>Question &amp; Answer With Edward C. Bernard, ICI Chairman, 2010–2011</b> .....	4
<b>Roundtable: Dodd-Frank Wall Street Reform and Consumer Protection Act</b> .....	8
<b>Preserving Money Market Funds</b> .....	12
ICI Research Illuminates Issues Facing Money Market Funds .....	16
<b>Case Study: Improving the Tax Treatment of Fund Investors</b> .....	18
<b>Impact of International Developments for Funds</b> .....	20
<b>Roundtable: Addressing the Benefits and Challenges of Social Media</b> .....	24
<b>Risk Management: IDC and ICI Lead the Way in an Evolving Landscape</b> .....	28
Ruling Highlights Need for Robust Economic Analysis .....	30
<b>Strength of the Defined Contribution Plan System</b> .....	32
<b>Question &amp; Answer With James E. Ross, Chair, ICI ETFs Committee</b> .....	36
<b>ICI Advocacy on Markets and Trading</b> .....	40
<b>ICI's Political Program: The Chairman's Council</b> .....	44
<b>53rd Annual General Membership Meeting: The Way Forward With Fund Investors</b> .....	46
<b>ICI Education Foundation: Promoting Financial Education in the National Capital Region</b> .....	48
<b>Appendices</b> .....	50
Organization and Finances .....	50
ICI Board of Governors .....	54
Governing Council of the Independent Directors Council .....	55
ICI Standing Committees and Chairs .....	55
ICI Staff .....	56
Publications and Releases .....	57
ICI and IDC Events .....	59
ICI Mutual Insurance Company .....	59
<b>Leading the Way on Policy Issues</b> .....	inside back cover

## TO OUR MEMBERS

# Letter from ICI's President



**PAUL SCHOTT STEVENS**

President and CEO, Investment Company Institute

Since the advent of the financial crisis in the summer of 2007, each year has brought new challenges to financial markets, the fund industry, and ICI. For us, 2011 will be remembered as an inflection point: a period when the Institute engaged with more U.S., foreign, and multinational policymakers on more issues of greater consequence for our members than at any time before.

Working closely with our members, we dealt with an unprecedented level of regulatory activity: implementation of the Dodd-Frank Wall Street Reform and Consumer Protection Act; ongoing efforts to make money market funds more resilient; continuing close scrutiny of trading and market structure issues; and challenges to the key roles that funds, recordkeepers, and financial advisers play in assisting retirement savers.

These issues have brought us into contact with an expanded set of policymakers—both here and abroad. Under Dodd-Frank, established regulators like the Commodity Futures Trading Commission and new ones like the Financial Stability Oversight Council are writing rules that affect funds and their advisers. And worldwide, policymakers are adopting a more global stance. The Institute has worked to ensure that policymakers understand the functioning and vital role of our funds.

As always, our approach has been highly substantive and constructive. At its core is ICI Research, which achieved new levels of stature and visibility in 2011. Whether working with the task force convened by the Federal Reserve to improve the



repurchase agreement market or briefing Capitol Hill on the federal debt ceiling, ICI Research brought solid data and penetrating insights, enhancing the credibility of the Institute and its members.

Another of ICI's key missions is to promote public understanding of funds and their investors. To that end, we stepped up our outreach to the media and the public. Two key developments were the launch of *ICI Viewpoints*, a forum providing our commentary on key issues as they emerge, and our increased profile in the broadcast media. Through these and other means, we have achieved some success in informing coverage and shaping opinions on key policy questions.

This new level of effort across so many fronts produced tangible results. One remarkable development was the passage of the Regulated Investment Company Modernization Act, the first update of mutual fund taxation in many years. This bipartisan legislation, adopted when many financial institutions are under the harshest scrutiny, attests to Congress's recognition of the crucial part funds play in helping Americans meet their financial goals. This in turn is a product of our continuing outreach to Congress, with the active support of our members.

The Institute also advanced its call for sound cost-benefit analysis in rulemaking. In a far-reaching decision, the U.S. Court of Appeals for the DC Circuit struck down the Securities and Exchange Commission's proxy access rule. ICI and the

Independent Directors Council filed an *amicus* brief challenging the rule as applied to the fund industry. The court's clear and unambiguous decision will remind regulators of the need to recognize the distinct differences between funds and public operating companies.

As I noted, the financial crisis has created an increasingly global outlook among policymakers. More and more, national regulators are influenced by policies fashioned abroad, and international bodies are stepping up policy coordination. At the same time, the extraordinary worldwide rise of asset managers as financial intermediaries has created new opportunities for funds. Responding to these and other trends, the Institute readied a new initiative—ICI Global—launched early in fiscal year 2012. We are excited about ICI Global's potential to advance the common interests and promote public understanding of global investment funds, their managers, and investors.

Our ability to serve as an effective advocate in non-U.S. markets will build upon the same strengths we have brought to bear here at home for 71 years: outstanding legal and economic analysis, deep roots in our industry, strong member involvement, and clear communications and advocacy. As we continue to move through the long aftermath of the financial crisis, we pledge to use those strengths to the utmost to advance the interests of funds and their advisers, directors, and millions of shareholders.

## QUESTION & ANSWER

# With ICI's Chairman



### **EDWARD C. BERNARD**

Chairman, Investment Company Institute  
Vice Chairman, T. Rowe Price Group, Inc.

**Last year, you said 2010 brought ICI the most challenging policy environment in its 70-year history. How did 2011 stack up?**

It was right up there, I'd say, with the three years that came before.

In 2008 and 2009, the policy challenge was all about putting out fires. It was a call to action to address a lot of issues, and ICI was deeply involved with regulators and other market participants to sort things out.

This year and last, we've been in a different phase. It's not uncommon after any financial crisis to have a regulatory response, and this one has been broad and deep. Essentially, the sprint of 2008 has turned into a marathon. You have to call on different skills and different muscles. So now, perseverance is the order of the day. And what I've seen at ICI is that the Institute's legal, economic, and government relations teams have shifted from sprint into marathon mode, and they're working quite effectively toward sensible, reasonable solutions that serve the interests of fund shareholders.

It may not have the urgency of a conference call with the Treasury at ten o'clock on a Saturday night to sort out a problem before Monday. But it's every bit as important. When you have this kind of regulatory response, the devil is in the details, and you've got to get it right.



### **Which areas have proven the toughest?**

I would say the most vexing has been the extreme scrutiny of money market funds. Regulators have made clear that they understand the important role that money market funds play in the economy, and they don't want those benefits to go away. And yet there's still concern that, perhaps, more needs to be done with these funds.

People shouldn't forget how much has already been accomplished. I'll point to the report of ICI's Money Market Working Group, a tremendous effort that preceded significant rule changes approved by the Securities and Exchange Commission in 2010. With increased credit quality standards, increased liquidity, and important provisions like the ability of a money market fund board to suspend operations and dissolve a fund, there are substantially greater protections that help either to avoid problems in money market funds or to contain any problems. So it's really not clear what additional measures can be taken that might not do more harm than good.

The Dodd-Frank [Wall Street Reform and Consumer Protection] Act is a different challenge. The challenge is to get the regulations right, and the net result is that there is an enormous amount of work to be done.

Happily, the Institute has earned a reputation for what I call "the courage to be objective." Obviously, the role of the Institute is to represent the interests of funds and their advisers. But this industry has always taken its fiduciary duty very seriously. We have a deeply held belief that if we do what's right for our shareholders, that will bode well for our businesses. So ICI has a reputation for doing very good analytical work, and then presenting the facts as they come. As a result, ICI has a seat at the table in all of these different dialogues.

### **The financial crisis vividly highlighted the global nature of finance, and regulators are increasingly emphasizing the need for international coordination. Is there a greater role for ICI to play globally?**

Absolutely. Even if you're looking at funds that are strictly U.S.-oriented, ICI has to understand the global nature of finance to advance the interests of those funds' advisers and investors, as the industries in which those funds invest become increasingly global. In addition, for quite some time, the investment operations of a number of ICI member firms have been expanding their reach to international markets, and these advisers typically want to have products that can serve clients in non-U.S. markets.

The Institute is well positioned to expand its global reach. ICI has engaged in fund issues globally for years, and has good, long-standing relationships with its counterparts around the world. My sense is that any expansion with ICI Global will be additive and complementary to ICI's efforts on behalf of U.S.-based investors.

**One signal event of your tenure was the U.S. Supreme Court's decision in *Jones v. Harris*, which affirmed the 30-year-old standard for reviewing funds' fees. What has the *Jones* case meant?**

Fund boards spend a lot of time on advisory contracts, and the litigation and differing court decisions had created ambiguity and confusion. That was clearly unsettling to advisers and to directors, both of whom, in my experience, are trying to do what is right as fiduciaries.

The *Jones* decision brought clarity. Not just clarity, but affirmation from the U.S. Supreme Court that the standards that we've applied for decades are indeed appropriate. We had it right all along. That's good for advisers and directors, and it seems to me that it should be reassuring to mutual fund investors as well.

**Investors have been challenged to meet their goals in uncertain and volatile markets. How are they coping?**

Like many advisers, we [at T. Rowe Price] stayed close to our clients in late 2008 and 2009. We found two very interesting things. Number one is that investors by and large stayed put. Whether it's because investors had thought this through or because they weren't quite sure what to do, the good news is they did the right thing. When the markets recovered, they made back their paper losses.

The other interesting thing was that when we asked clients about lessons learned, first on the list was, "I need to save more."

People generally like to have a sense of control over their lives, and they were telling us, "The one thing that I know I can control, even with volatile markets, is how much I'm putting away for my future."

As we talk to investors now, we're starting to see some shifts in risk appetite, in two forms. We obviously have a large group, the Baby Boomers, approaching retirement and getting more conservative about allocating their assets. But the other shift that's perhaps a little troubling is among younger investors who are, let's say, in their mid-thirties now. The first decade of their investing lives has been pretty tough—2000–2003 saw a severe bear market and in 2008, there was a full-blown financial crisis. So those investors' risk appetite is lower than would be expected at their age.

**What do funds need to do for this younger generation?**

The challenge for the industry is to renew and continue the messages that we've used for years. We successfully helped earlier generations understand the importance of saving, and the importance of saving in a way that would outpace inflation. We need to continue that effort so the next generation of investors gets the message. We also need to have product choices that will meet their needs. My belief is that, over time, even this generation will get more comfortable with inflation-beating investments. But it may take a while.

**There's also a great deal of concern over retirement savers.**

Well, fortunately, retirement savers have proven their ability to stay put too. And when the market recovered, the declines in their balances were in large measure recovered. In [T. Rowe Price's] data, only nine months after the trough, investors in our 401(k) plans who were in their sixties were already back to 98 percent of their 2007 balances. In 2010, they were ahead of the game.

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**“We represent the interests of Main Street, helping individuals and families invest in the instruments created by Wall Street.”**

EDWARD C. BERNARD

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“We successfully helped earlier generations understand the importance of saving, and the importance of saving in a way that would outpace inflation. We need to continue that effort so the next generation of investors gets the message.”

EDWARD C. BERNARD

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To me, it says people have come to understand that retirement saving is a long-term game, a 30- to 35-year undertaking.

**Looking forward, some plans to reform taxes or reduce the federal budget deficit have targeted tax incentives for retirement savings. What would that mean to Americans' retirement security?**

For the United States to move forward, to achieve the needed fiscal balance, every aspect of government policy needs to be examined. But the point I would make is that providing income in retirement has been, and always will be, a shared public and private responsibility. The government is going to be the provider of last resort—if people can't fund their own retirement, the cost will ultimately come back to the government. Effectively incenting private savings is likely to produce a better outcome over the long term than filling income gaps if savings fall short.

So, if you take a long-term view of the expenses of government, it's a bit shortsighted to think, well, we can help balance the budget by removing incentives for people to save for retirement. So it seems to me that should be one of the last places that legislators look to find savings.

**What does the future hold for the fund industry?**

The complexity of financial markets, the fact that they're global—those are here to stay. So the role that funds fulfill is more important than ever. We represent the interests of Main Street, helping individuals and families invest in the instruments created by Wall Street. With the nature of the professional services we provide and the fiduciary context, I think the value proposition is pretty hard to beat. You get professional management, you get broad diversification at low cost, in a vehicle that's managed to a fiduciary standard, with oversight of an independent board of directors, and priced daily, mark-to-market. No one has come up with a better way to provide investment management services to millions of individuals.

Now, it's clearly essential that fund advisers continue to live up to their fiduciary duty. But as long as the industry rises to that level of professionalism in delivering investment services, and sustains the fiduciary culture to put the client's interest first, the future for the fund industry is enormously positive.

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Edward C. Bernard served as Chairman of the Investment Company Institute for fiscal years 2010 and 2011, and is Vice Chairman of T. Rowe Price Group, Inc.

## ROUNDTABLE

# Dodd-Frank Wall Street Reform and Consumer Protection Act *A Conversation With ICI Staff*

**July 21, 2011 marked the one-year anniversary of enactment of the Dodd-Frank Wall Street Reform and Consumer Protection Act. What are ICI's priorities during Dodd-Frank's implementation?**

**Frances Stadler, Senior Counsel, Securities Regulation:** This 848-page statute touches nearly every part of the financial services industry. It doesn't target funds, because funds were not the cause of the financial crisis. Nonetheless, Dodd-Frank and the rules it requires could have important implications for funds and their advisers, and for fund investors. Despite significant progress by regulators in implementing Dodd-Frank, there's still much to do and important questions remain unanswered.

ICI members and staff have devoted enormous efforts in educating regulators and responding to rule proposals, to try to ensure that the Dodd-Frank rules don't have harmful or unintended consequences for funds. It may be quite a while before we can fully assess the impact of this sweeping legislation.

**Bob Grohowski, Senior Counsel, Investment Companies:**

Remember too, these are often very complex rulemakings with tight, and sometimes unreasonable, deadlines. In some cases, deadlines have slipped, especially in cases where regulators have received thousands of comment letters on a single

proposal. That's not necessarily bad, because it's important that the regulators take sufficient time to get the rules right.

**To regulate systemic risk, Dodd-Frank calls for designating "SIFIs"—systemically important financial institutions—for heightened regulation and oversight. What effect will this have on the fund industry?**

**Rachel Graham, Senior Associate Counsel:** Speaking broadly, the goal of systemic risk regulation is to achieve a more resilient financial system. This will benefit funds and their shareholders in the long run. Dodd-Frank gives regulators many new tools to minimize systemic risk, and SIFI designation by the Financial Stability Oversight Council, or the FSOC, is the most well known. It's a powerful tool, so it needs to be used appropriately. At ICI, we've thoroughly analyzed both the legal implications and the economic variables that should go into deciding whether a particular firm poses risk to the overall financial system. This analysis underscores our view that SIFI designation is inappropriate for funds, including money market funds, or their advisers.

**Dean Sackett, Chief Government Affairs Officer and Co-Head:** The views we've been expressing to regulators about the SIFI designation process further amplify the approach we took in advocating funds' views during the legislative process.

We've continued to recommend criteria that the FSOC should use in making a SIFI determination and to urge that leverage, for example, is a factor that should be accorded significant weight due to its ability to magnify losses, sometimes in unpredictable ways. Since mutual funds are subject to strict limits on leverage, it would be less likely that a mutual fund would be designated systemically important. We're continuing to advocate too for the FSOC to apply standards appropriate for mutual funds, rather than bank-like standards, in the event that any funds are designated as SIFIs.

**Sean Collins, Senior Director, Industry and Financial Analysis:** Our commentary on the SIFI criteria pointed out that it would be a mistake to place too much focus on whether an institution is "too big to fail." The issue is primarily leverage, not size. A critical point is that mutual funds are much less leveraged than many other financial institutions. I think regulators get that.

**Systemic risk is one of many areas where Dodd-Frank involves multiple regulators. How will this dynamic affect ICI and its members?**

**Tami Salmon, Senior Associate Counsel:** Based on my work on compliance and risk issues, I've seen the number of issues

we must address expand exponentially. In the past, our efforts focused largely on the Securities and Exchange Commission [SEC], the Financial Industry Regulatory Authority [FINRA], and the Federal Trade Commission. Today, we have to worry about more regulators and a greater variety of issues that are not "core" fund issues.

**Stadler:** I agree. While the SEC remains our primary regulator, Dodd-Frank changed the landscape. One new regulator is the FSOC, which is made up of multiple financial services regulators. Also, certain statutory provisions call for either joint or coordinated rulemaking by different regulatory agencies. We now need to build relationships with a new array of regulators and educate them and their staffs about the industry and fund regulation. And we must watch for measures that might not have been directed at funds but could affect them in some way.

**Graham:** The FSOC has great potential. It brings together an array of regulators with different perspectives to work on issues that cut across the financial system. But the FSOC is dominated by the banking regulators. We will want to be sure it is not viewing funds and their advisers through the lens of banking regulation.

**Grohowski:** That's true of some joint rulemakings, as well. The proposed executive compensation rules essentially were built upon preexisting banking guidelines. We've urged regulators to recognize that an adviser's business is quite different from a bank's.

#### **Are ICI's messages resonating with the regulators?**

**Sackett:** By and large, I think regulators are taking our views into account. In analyzing and commenting on rule proposals, we take a very thoughtful approach, and certainly those regulators we've worked with extensively know this. But, there's a process of familiarization between us and some new regulators, and that process is still underway.

**Heather Traeger, Associate Counsel:** A prime example is in the derivatives space, where ICI members have become engaged with the Commodity Futures Trading Commission [CFTC]. We've seen shifts in the CFTC's thinking between proposed and final rules that are consistent with views expressed by ICI and its members. In some CFTC proposals, regulatory thresholds are set high enough that most funds' activity would not be affected by the rule. This doesn't exempt registered funds from the rules, but nonetheless seems to recognize that funds are already comprehensively regulated. In all of these instances, our message apparently has resonated with the CFTC. We've seen similar receptiveness at the SEC. Both agencies have recognized ICI as the fund industry's voice and tried to incorporate funds' perspective in their roundtables and rulemaking. This is a great foundation for our relationship going forward.

**Graham:** I'll offer another example. The FSOC's rule proposal in January analyzed the various criteria for SIFI designation in much the same way as we did in our lengthy comment letter

the previous November. Similarly, Treasury Secretary [Timothy F.] Geithner's remarks at ICI's General Membership Meeting in May are consistent with our message that leverage should be a primary consideration.

**Collins:** But although regulators in general are listening and hearing our message, it's an uphill climb in some instances. This underscores the need for our continued efforts.

#### **Aside from rulemakings and studies, are there other, less obvious implications of Dodd-Frank?**

**Graham:** Certainly there seems to be more pressure on individual regulators to be vigilant. This may stem from the fact that they're working together in the FSOC and also from Dodd-Frank's focus on reducing risk across all areas of the financial system. No regulator wants to be the one who misses the next big problem. This does leave the door open, though, for regulatory overreach in some cases.

For example, ICI has deep concerns about a CFTC proposal, known as Rule 4.5, that was not part of Dodd-Frank but that the CFTC describes as "consistent with the tenor" of Dodd-Frank. Under the proposal, many funds that invest in commodity futures, options, or swaps could become subject to both CFTC and SEC regulation, leading to duplicative and conflicting requirements. ICI has highlighted this proposal's far-reaching implications and strongly advocated for a more measured approach.

#### **Congressional interest in Dodd-Frank did not end with its passage. What are lawmakers doing, and what has this meant for ICI?**

**Sackett:** Implementation of Dodd-Frank is of great interest to Congress. Bipartisan bills aiming to slow the pace of rule-making have been introduced, reflecting the belief that getting

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**“Dodd-Frank implementation will bring changes to financial services and the markets in which funds invest. Certainly, ICI stands ready to help members understand and adapt to those changes.”**

FRANCES M. STADLER, SENIOR COUNSEL, SECURITIES REGULATION, INVESTMENT COMPANY INSTITUTE

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ICI staff working on Dodd-Frank: SEATED: Sean S. Collins, Senior Director, Industry and Financial Analysis; Rachel H. Graham, Senior Associate Counsel; Dean R. Sackett III, Chief Government Affairs Officer and Co-Head  
STANDING: Frances M. Stadler, Senior Counsel, Securities Regulation; Heather L. Traeger, Associate Counsel; Robert C. Grohowski, Senior Counsel, Investment Companies; Tamara K. Salmon, Senior Associate Counsel

it done right is more important than getting it done quickly. Significantly, the political climate has changed since Dodd-Frank's passage in July 2010, so we can expect aggressive congressional oversight of regulators' activities. We're also seeing some moves to modify or even repeal parts of Dodd-Frank.

ICI and its members have taken advantage of opportunities to provide our views and expertise to lawmakers. We've expressed support, for example, for bills to require sufficient cost-benefit analyses and to ensure that rulemaking in the swaps area is thoughtful and not rushed. In fact, [ICI General Counsel] Karrie McMillan testified in Congress that a logical process for swaps rulemaking would benefit funds and their shareholders. We've also actively supported bills related to swap execution facilities and assisted in drafting bills on credit rating agency reform.

We will continue to monitor and work with Congress on any Dodd-Frank-related legislation that could potentially affect mutual funds, in an effort to shape the legislation to ensure a positive outcome for mutual funds and their shareholders.

#### What lies ahead in the next year or two?

**Salmon:** From my perspective of working with chief compliance officers [CCOs], we're still waiting for the dust to settle on many of the issues emerging from Dodd-Frank. Once rules affecting mutual funds become final, we can assist CCOs by working with regulators to address any concerns our members have or to obtain interpretive guidance they need. We'll be providing members a forum, through committee meetings and conference calls, to discuss new requirements and how members are implementing them. Members can talk through the issues and learn from the experiences of their colleagues dealing with the same issue.

**Stadler:** Looking more broadly, Dodd-Frank implementation will bring changes to financial services and the markets in which funds invest. Certainly, ICI stands ready to help members understand and adapt to those changes.

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For more information, please visit ICI's Financial Services Regulatory Reform Resource Center, [www.ici.org/reg\\_reform](http://www.ici.org/reg_reform).

# Preserving Money Market Funds

Money market funds continued to prove their value to American investors, businesses, and governments in 2011. Bolstered by the comprehensive regulatory reforms of the preceding year, these funds weathered the extraordinary market turbulence brought about by financial instability in Europe and fiscal uncertainties in the United States. Still, money market funds remained squarely in the spotlight, as regulators, legislators, and the media examined the important role played by these funds in the financial system, their possible vulnerabilities in times of severe market stress, and the potential for further reform in the comprehensive rules that govern them.

Equipped with data and policy perspective from its membership, ICI stayed at the forefront of the discussion, pressing the case to key audiences that money market funds work for America and that their fundamental characteristics must be preserved. The Securities and Exchange Commission (SEC) and other key financial regulators were certainly an important audience.

Progress on the regulatory front had already been substantial—and effective. In early 2010, the SEC promulgated regulations that tightened standards for credit quality, maturity, disclosure, and liquidity of money market funds—thus increasing money market funds’ resilience—and required more detailed and more frequent disclosure. As one measure of the success of these changes, the money market fund industry in August 2011 had at least \$140 billion available to meet redemptions on any given day and \$531 billion available to meet redemptions within five business days—a level of liquidity far above that held by money market funds during the financial crisis of 2008–2009.

Still, regulatory activity did not abate after the January 2010 rulemaking. Particularly significant was the October 2010 publication of a report, “Money Market Fund Reform Options,” from the President’s Working Group on Financial Markets (PWG), which analyzed eight further changes regulators could make to increase the resiliency of these funds. ICI welcomed the publication of the report, which appropriately took into account the strengths, weaknesses, and potential consequences of various regulatory proposals.

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**“Money market funds represent a clear case where market discipline reinforces strong regulatory standards.”**

PAUL SCHOTT STEVENS, PRESIDENT AND CEO, INVESTMENT COMPANY INSTITUTE

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In early January 2011, ICI filed its response to the PWG report with the SEC. Weaving together extensive ICI research and legal analysis, the 59-page letter proceeded from a few simple principles. ICI stressed that money market funds' essential characteristics must be retained, given the tremendous benefits that these funds provide to investors and the broader economy. The Institute also urged policymakers to stay focused on their objectives of strengthening money market funds even further against adverse market conditions and enabling them to meet extraordinarily high levels of redemption requests.

In response to one policy option featured prominently in the PWG report, ICI described a concept of a new, private facility to provide a liquidity backstop for prime money market funds, thereby bolstering the resilience of these funds in difficult market conditions. ICI's comment letter also reiterated the Institute's strong opposition to proposals that would eliminate the ability of money market funds to use the amortized cost method of valuation, forcing them to switch from a stable \$1.00 net asset value (NAV) to floating NAVs. Such a change would be unlikely to reduce systemic risk to any meaningful extent, ICI noted, registering the Institute's deep concerns about the impact such a change would have on financial markets, both during a transition period and afterward.

ICI President and CEO Paul Schott Stevens had a chance to discuss these concerns in a colloquy with Treasury Secretary Timothy F. Geithner at ICI's 53rd General Membership Meeting

in May. Geithner emphasized the necessity of a measured approach to reforms around money market funds, noting that regulators were working toward the goal of adding resilience "without depriving the economy of the broader benefits that those funds provide."

Later that month, regulators considered floating NAVs and other policy proposals at an SEC roundtable on money market funds. ICI Chief Economist Brian Reid participated in the roundtable, which brought together SEC commissioners and staff, representatives of agencies in the Financial Stability Oversight Council, and participants from academia, the fund industry, the business community, and state and local governments.

Complementing the SEC's roundtable, ICI also convened experts from the private and public sectors for a May 2011 Money Market Funds Summit in Washington, DC. The daylong event featured panels discussing the importance of money market funds for investors and issuers, the development of these funds' regulatory framework over the past four decades, and the best path forward for reform.

"We must get the balance right," said Edward C. Bernard, ICI Chairman and Vice Chairman at T. Rowe Price Group, Inc., in the opening remarks for the conference. "Fundamental changes to this product will cause severe market disruptions." In his keynote address, ICI Governor F. William McNabb III, Chairman and CEO of Vanguard, underscored the need to consider fully these

likely disruptions, and the ramifications for investors large and small, should money market funds as the world knows them disappear. “While the choices for individuals will be limited in a world without money market funds,” he noted, “the cash management options for institutional investors could actually become more expansive and exotic: unregulated offshore accounts, unregistered funds, cash pools, and other novel Wall Street products still yet to be dreamed up.”

As these events took place, ICI tracked still another regulatory development with implications for money market funds: implementation of the Dodd-Frank Wall Street Reform and Consumer Protection Act. For example, consistent with a broader Dodd-Frank requirement, the SEC proposed eliminating credit ratings as a required element in determining which securities are permissible investments for money market funds. ICI alerted the SEC that the proposal could weaken credit standards, thus increasing risks to shareholders. The Institute recommended changes to the proposal that would help avoid this outcome.

The unfolding regulatory process helped drive a vigorous discussion in the public arena over money market funds. Leveraging the expertise of its members and the deep support for stable NAV money market funds across a wide range of constituencies, ICI moved forward with several communications initiatives around money market funds. As part of these initiatives, ICI launched [www.preservemoneymarketfunds.org](http://www.preservemoneymarketfunds.org), a website providing the public with facts, news articles, commentary, and other material on money market funds. The site’s “What Others Are Saying” section, for example, showcases the multitude of groups—from AARP to the U.S. Chamber of Commerce—who have expressed strong support for stable NAV money market funds.

To be sure, the public heard from proponents of both sides of this debate in 2011. The editorial board of the *Wall Street*

*Journal* proved especially vocal on the topic, publishing two editorials arguing that money market funds should be forced to float their NAVs. ICI responded immediately to the editorials, pointing out their serious analytic and factual flaws in responses published in the newspaper, at [WSJ.com](http://WSJ.com), and on the Institute’s website. “Money market funds represent a clear case where market discipline reinforces strong regulatory standards,” wrote ICI President and CEO Paul Schott Stevens in a June 2011 letter to the editor.

ICI, its members, and like-minded groups further pressed the case for money market funds in several longer commentaries published in the opinion pages of the world’s leading publications. “Businesses and governments have sounded the alarm,” wrote ICI Governor Mark R. Fetting, Chairman and CEO of Legg Mason, Inc., in the *Financial Times*. “Forcing money market funds to float will drive away so many investors that the current efficient channel they depend on for critical financing could be cut off.”

Capitol Hill also expressed interest in the policy issues surrounding money market funds. The House Financial Services Committee’s Subcommittee on Capital Markets and Government-Sponsored Enterprises held a June 2011 hearing, “Oversight of the Mutual Fund Industry: Ensuring Market Stability and Investor Confidence,” in which legislators and witnesses discussed at length the issues surrounding money market funds. Testifying at the hearing, Stevens conveyed to legislators both the fund industry’s support of the regulatory process and its view that regulatory changes should not undercut the enormous advantages that money market funds bring to the economy and shareholders.

Echoing Stevens’s views were a number of organizations that submitted comments for the hearing record. Mandating floating NAVs “would dampen investor demand for the securities we offer and deprive state and local governments





Treasury Secretary Timothy F. Geithner and ICI President and CEO Paul Schott Stevens discuss money market funds in a colloquy at ICI's 53rd General Membership Meeting.

of much-needed capital,” said a joint letter to Subcommittee Chairman Scott Garrett (R-NJ) from 12 groups representing municipalities, states, financing authorities, and government officials. The Association for Financial Professionals (AFP), which counts a membership of 16,000 finance and treasury professionals at businesses and nonprofits, also weighed in. “The move to a floating NAV would also create significant disruptions in the corporate funding market,” said AFP. “Many organizations issue commercial paper to meet their short-term financing needs, such as funding payroll, replenishing inventories, and financing expansion.”

U.S. policymakers were not alone in their examination of the role of money market funds. Regulatory bodies overseas were also active on the issue, and ICI engaged accordingly. For example, the Institute provided information and views on money market funds to the Financial Stability Board (FSB), a regulatory organization based in Basel, Switzerland. In an April 2011 paper, the FSB placed money market funds within

the definition of “shadow banking.” Addressing the FSB’s apparent assumption that regulatory standards are necessarily weaker outside the banking sector, ICI clarified for the FSB the stringent rules contained in the Investment Company Act of 1940, how those rules address systemic risks, and how money market funds must go beyond those requirements if they want to offer investors a stable \$1.00 share price.

In the months ahead, the spotlight will continue to shine on money market funds as policymakers around the world pursue their reform efforts. With the help of its members, ICI will advance fund industry positions and the view shared by so many—money market funds are an essential component of America’s finances. Efforts to further strengthen the product are certainly worth examining, but any reforms must preserve the key features that have made these funds so important for the U.S. economy and investors.

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For more information on money market funds, please visit [www.ici.org/mmfs](http://www.ici.org/mmfs) and [www.preservemoneymarketfunds.org](http://www.preservemoneymarketfunds.org).

# ICI Research Illuminates Issues Facing Money Market Funds

A series of unprecedented regulatory and market developments in 2011 generated tremendous demand for high-quality information on money market funds. Collaborating with both members and Institute colleagues, ICI Research delivered both data and analysis to aid investor and policymaker understanding on new disclosures on the pricing of money market funds; the impact of the financial turmoil in Europe; and implications for funds of the impasse over the U.S. debt ceiling.

The first of these challenges came in January 2011, when the Securities and Exchange Commission (SEC) began to publish monthly snapshots of money market funds' per-share market values. The new disclosure was required by the SEC's January 2010 amendments to money market fund regulations.

The new disclosure would bring attention to the fact that money market funds' per-share market values fluctuate around the funds' stable \$1.00 net asset value (NAV), raising the risks of misperceptions or faulty data interpretation. So ICI worked to ensure clarity around a key point: deviations in per-share market values of money market funds from \$1.0000 are

common and are not generally a cause for investor concern. Under securities laws, a money market fund can offer shares at a stable \$1.00 NAV as long as its per-share market value stays within one-half cent of \$1.00—between \$0.9950 and \$1.0050.

Ahead of the new disclosure, ICI economists prepared "Pricing of U.S. Money Market Funds," an in-depth report explaining funds' per-share market value and examining trends in historical pricing data. The report illustrated how fluctuations in taxable money market funds' per-share market values are typically small. As the report showed, money market funds' average per-share market value moved between \$0.9980 and \$1.0020 during the decade from 2000 to 2010, a period when the financial markets experienced wide variations in interest rates and asset prices.

As explained by "Pricing of U.S. Money Market Funds," any of four factors can account for changes in a fund's market value: falling or rising interest rates, a portfolio's dollar-weighted average maturity, investors selling or purchasing shares, and a credit event (such as a ratings downgrade or a default) affecting a security in the fund's portfolio.

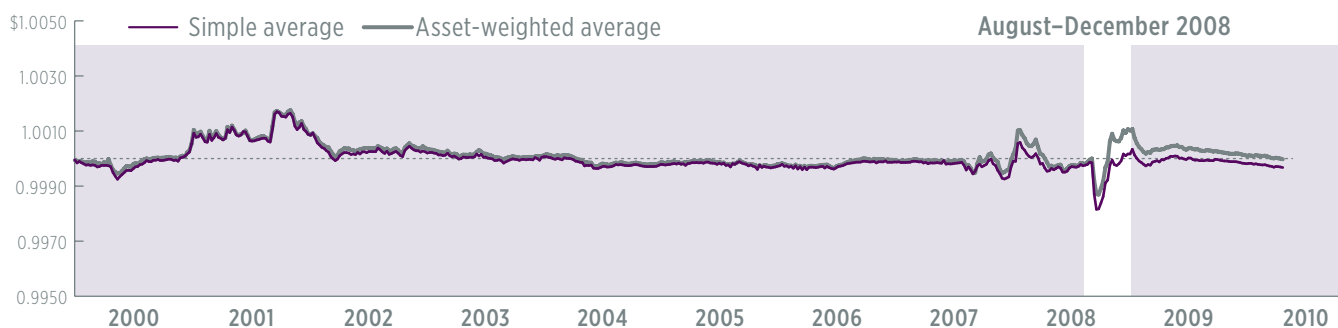
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A series of unprecedented regulatory and market developments in 2011 generated tremendous demand for high-quality information on money market funds.

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## Per-Share Market Values, January 2000–April 2010

Prime money market funds



Source: Investment Company Institute

The report discussed how extreme and sudden changes in market conditions are necessary before a money market fund's market value would change by as much as \$0.0050 and force the fund to consider whether to reprice its shares to less or more than \$1.00 per share—a development known as “breaking the dollar.” For example, ICI modeling showed that under plausible assumptions about fund portfolio composition and maturity, short-term interest rates must rise by more than 300 basis points (3 percentage points) in one day, absent any other changes in market conditions, to reduce a fund's per-share market value to \$0.9950.

Six months after the publication of “Pricing of U.S. Money Market Funds,” ICI confronted another issue requiring good data and incisive analysis: the debt crisis gripping Europe. Related concerns around money market funds focused largely on a few questions. Were U.S. money market funds invested in the “periphery countries”—Greece, Italy, Spain, Portugal, and Ireland—that were deemed particularly at risk in a debt crisis? Why were U.S. money market funds investing in European banks? Finally, what risks did those investments pose for U.S. money market funds and their investors?

To address these questions, ICI Research staff examined the portfolio holdings of prime money market funds. They found that, as of July 2011, U.S. prime money market funds had no direct exposure to Greek, Portuguese, or Irish government or

bank debt. Moreover, their holdings of Spanish and Italian bank debt were minimal and had fallen substantially since autumn 2010. In September 2011, ICI updated its findings, reporting that money market funds had virtually no direct exposure to public or private debt in the periphery countries, while 60 percent of these funds' holdings in European bank securities would mature in 30 days or less.

The impasse over the ceiling on U.S. government borrowing likewise raised questions about implications for money market funds. As an August 2011 deadline for congressional action approached, ICI's Law, Operations, and Research staffs analyzed the implications of a possible downgrade or default of U.S. sovereign debt. The Institute's analysis, published on ICI's website and disseminated on Capitol Hill by ICI's Government Affairs team, showed that these developments would be unlikely to destabilize money market funds. In one of several *ICI Viewpoints* items, ICI Senior Economist L. Christopher Plantier and Sean S. Collins, ICI's Senior Director for Industry and Financial Analysis, returned to the four factors explained in “Pricing of U.S. Money Market Funds” to demonstrate why the U.S. debt limit crisis was unlikely to cause a money market fund to break the dollar.

To find “Pricing of U.S. Money Market Funds” and other resources, please visit [www.ici.org/mmfs](http://www.ici.org/mmfs). To find *ICI Viewpoints*, visit [www.ici.org/viewpoints](http://www.ici.org/viewpoints).

## CASE STUDY

# Improving the Tax Treatment of Fund Investors

Taxes are a key factor that households should consider in making decisions to save, invest, and manage their money. Tax policy also can bolster capital formation—crucial to the growth and prosperity of our nation’s economy. Fiscal year 2011 brought two legislative developments that strengthened tax policy to the benefit of fund investors: the Regulated Investment Company Modernization Act of 2010 (RIC Modernization), and the extension of favorable tax rates on capital gains and dividends.

Mutual fund tax rules date back to 1936. Over seven decades, those rules had not kept up with changes in the structure of the fund industry, the way mutual funds are distributed, or the markets in which funds operate. ICI had long supported Congress’s efforts to update tax laws governing mutual funds.

“Most of the current-law mutual fund rules were last collectively updated more than two decades ago. [This bill] would update certain technical tax rules...in order to make them better,” said

Representative Dave Camp (R-MI), then Ranking Member (now Chairman) of the House Ways and Means Committee, in a September 28, 2010 statement.

Those efforts bore fruit on December 22, 2010, when President Barack Obama signed into law RIC Modernization, a bill designed to modernize and streamline the tax laws governing mutual funds. Enactment of the legislation significantly benefits U.S. mutual funds and their 90 million shareholders. “The Regulated Investment Company Modernization Act streamlines and updates technical tax rules, allowing fund companies to focus on innovating and serving shareholders,” ICI’s President and CEO Paul Schott Stevens said in a statement.

Some of the law’s provisions benefit investors directly. For example, the law provides tax benefits for international investments made through funds of funds and updates tax reporting requirements so shareholders should need to file fewer amended tax returns.

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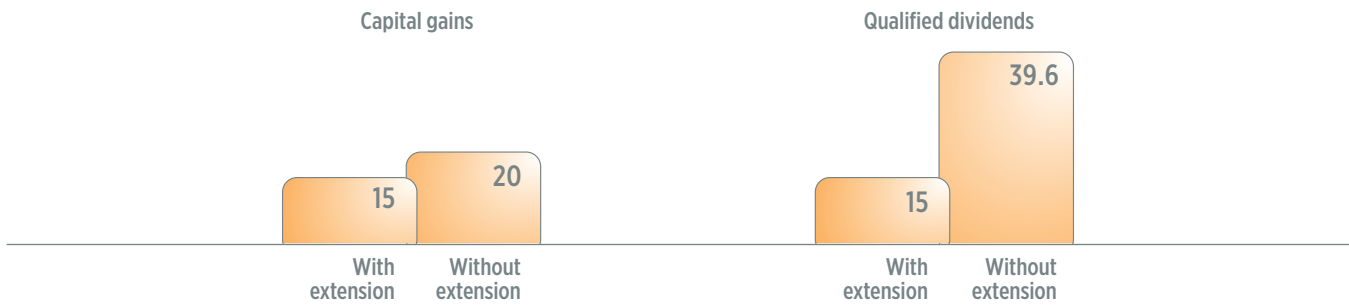
“Most of the current-law mutual fund rules were last collectively updated more than two decades ago. [This bill] would update certain technical tax rules...in order to make them better.”

REPRESENTATIVE DAVE CAMP (R-MI)

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## 2010 Extension Kept Tax Rates on Investment Income Down

Top tax rates, percent, 2011–2012



*Note: Long-term capital gains are net gains on assets held more than one year. Qualified dividends are dividends from U.S. corporations and certain foreign corporations.*

*Data: Congressional Joint Committee on Taxation*

“ICI has long supported Congress’s efforts to clarify mutual fund tax rules, and we are pleased that Congress acted expeditiously and in a bipartisan manner to modernize these laws,” commented Stevens.

Fund investors also benefited from the enactment of a tax law extending current tax rates on investments. In December 2010, in strong bipartisan votes, the Senate and House of Representatives approved a tax law that maintains and extends the current tax rates on capital gains and dividends for two years. ICI supported extension of the current rates on capital gains and dividends because of the benefits it will provide to investors and the economy.

“The two-year extension prevents tax increases on investments by Americans saving for retirement, a home, higher education, or other personal and financial goals. We will continue to work with Congress and the Administration next year as they consider broader U.S. fiscal and tax policy,” said Stevens.

Had this legislation not been enacted, the tax rates on investment income would have increased on January 1, 2011. The top tax rate for capital gains would have increased from 15 percent to 20 percent. Qualified dividends would have been taxed as ordinary income and would have been subject to a top tax rate of 39.6 percent.

ICI will continue to support sound tax policy that encourages and rewards saving, investment, and capital formation. It is imperative to preserve a tax system that recognizes the importance of mutual funds in helping Americans save and prepare for retirement. Tax incentives that promote retirement savings are of particular importance. ICI will remain engaged as policymakers continue to debate various deficit reduction and tax reform initiatives.

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For more information on RIC Modernization and the extension of favorable tax rates on capital gains and dividends, please visit [www.ici.org/taxation/ric](http://www.ici.org/taxation/ric) and [www.ici.org/taxation/cap\\_gains](http://www.ici.org/taxation/cap_gains).

# Impact of International Developments for Funds

Increasingly, serving as the voice of the U.S. fund industry involves making ICI's voice heard abroad, as national and multinational regulatory bodies take a greater interest in activity across borders. On this global stage, ICI has continued to build upon its record of legal and economic expertise to serve as an informed, vigorous advocate for funds before a growing range of authorities. The Institute and its members bring their resources to bear to inform and enhance the regulatory dialogue throughout the world on behalf of U.S. funds, their advisers, and their investors.

In the aftermath of the global financial crisis, financial authorities empowered a variety of multinational bodies to consider trends and activities in the financial markets and identify areas of risk. ICI has engaged with many of these bodies to help them better understand the history and structure of U.S. capital markets and registered investment companies, emphasizing the strengths of the regulatory and governance systems under which U.S. funds operate.

For example, the Institute responded vigorously to a paper by the Financial Stability Board (FSB)—a body charged by the Group of Twenty with a mandate to promote global financial stability—on the topic of “shadow banking.” In its paper, the FSB broadly defined a system of shadow banking that would encompass nearly all mutual funds. It stated that nonbank financial institutions that provide maturity, liquidity transformation, and leverage could create systemic risks by offering credit intermediation outside of the banking system.

In its response, ICI traced the tandem development of banking and capital markets in the United States. The parallel operations of these distinct sectors have added resiliency to the financial system, ICI said, and critical differences between banks and nonbank financial intermediaries should be respected. Simply characterizing funds and other capital market products as shadow banks would do little to address risks or other issues, ICI said. Instead, the FSB should work to identify any specific features or activities of nonbank financial intermediaries that

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On this global stage, ICI has continued to build upon its record of legal and economic expertise to serve as an informed, vigorous advocate for funds.

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pose potential risks to the global financial system, analyze why such risks arise, and explain how existing regulation does not address those risks. In addition to its written reply, ICI has engaged in extensive outreach efforts with regulators represented on the FSB to ensure an accurate understanding of mutual funds, money market funds, and exchange-traded funds (ETFs) operated under the Investment Company Act of 1940.

Continuing to build understanding of mutual funds among non-U.S. regulators is vital. For example, ICI has maintained a strong dialogue with European Union (EU) policymakers as those authorities develop new regulations for the Alternative Investment Fund Managers Directive to oversee the managers of alternative funds, including those not governed by the Undertakings for Collective Investment in Transferable Securities (UCITS) framework. ICI is seeking to ensure that European policymakers understand the unique challenges that the directive may pose for registered investment companies that are marketed to EU investors. In particular, ICI has focused on provisions that are inconsistent or incompatible with U.S. requirements in such areas as custody and disclosure to investors and regulators. The Institute also has addressed concerns that the directive raises for global asset managers and the delegation of portfolio management.

ETFs likewise drew attention from overseas regulators, including those more familiar with banking rather than securities regulations. The Institute engaged to clarify misunderstandings about risks posed by ETFs in an FSB paper focused primarily on the growth of “synthetic” ETFs—funds that gain market exposure through a single swap with an affiliated counterparty. In its response, ICI explained that the vast majority of ETFs globally do not operate through a single-swap portfolio with an affiliated counterparty—the structure of concern to the FSB. ICI’s letter further explained why such an affiliated structure is not permitted under the Investment Company Act.

Following the FSB’s paper, the European Securities and Markets Authority (ESMA) published a discussion paper regarding possible guidelines for ETFs and structured funds operating under the UCITS framework. The paper discusses options for additional disclosure for index-tracking, synthetic, leveraged, and active ETFs. In its response, ICI endorsed ESMA’s consideration of enhanced disclosure for UCITS ETFs to ensure that investors and potential investors have an accurate understanding of any fund they are considering. The Institute cautioned, however, against requiring “disclosure that inappropriately suggests or insinuates that a particular type of UCITS ETF is less desirable” or that could lead investors to inaccurate conclusions about an ETF.



In their papers on ETFs, both ESMA and the FSB also raised concerns about securities lending by ETFs. In response, the Institute urged that regulators be cautious in attributing potential systemic, market, or shareholder risks to ETFs' securities lending activities, because other types of collective investment vehicles also engage in securities lending. ICI accordingly urged that ESMA and the FSB not address the impact of securities lending on the broader markets as an issue specific to ETFs.

Promoting the interests of U.S. funds and their advisers in Asia remains a high priority. The Institute continues to participate actively in Engage China, a coalition of U.S. financial services trade associations that advocates for a more open and effective financial system in China. Through high-level engagement with Chinese and U.S. officials, the Institute has provided Chinese regulators with insight into U.S. mutual fund trends and regulatory developments, helping to inform regulatory reform and promote the interests of the U.S. asset management industry in China.

As major institutional investors, funds also take a deep interest in issues surrounding trading and market structure. ICI continued its strong support of the International Organization of Securities Commissions (IOSCO), the umbrella group for securities regulators around the world, by commenting on IOSCO's studies of dark liquidity and technological developments in the financial markets. The Institute's comments addressed the impact of these developments on, among other things, market structure and market participants' behavior. ICI anticipates monitoring ongoing work by IOSCO on market structure issues and such fund topics as valuation, money market funds, and ETFs.

In Europe, ICI submitted a lengthy letter in response to the European Commission's proposed revision of the Markets in Financial Instruments Directive, the EU law that provides harmonized regulation for investment services across 30 countries. ICI's letter covered such issues as transparency and trade reporting, data consolidation, automated trading, and high-frequency trading. ICI followed up on its concerns with a series of meetings with European regulators, policymakers, and securities exchanges.

ESMA pursued similar issues in a consultation paper on direct market access, sponsored access, and organizational requirements for trading platforms and investment firms. The paper addressed electronic trading systems, fair and orderly trading, and market abuse.

ICI expressed strong support for ESMA's review. As funds increasingly execute intricately linked trading strategies through global trading desks, the Institute said, issues raised by technological changes in markets are no longer purely domestic. The Institute strongly supported guidelines for organizational requirements for electronic trading systems and cooperation with regulators, and added that robust compliance and risk management programs are critical given the prominence of automated trading. ICI cautioned regulators, however, to be careful not to impede funds' use of new and innovative trading tools.

ICI also spoke out against the decision by several European regulatory authorities to impose or extend bans and restrictions on short selling in their respective countries. While ICI strongly supports regulatory action to address abusive and manipulative short selling, it does not support a ban or

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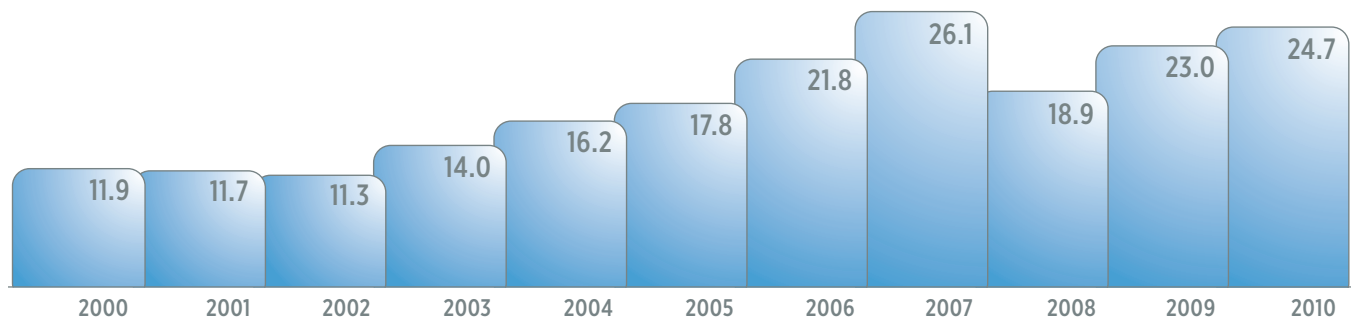
**“The sheer scale of the investment capital [shareholders] entrust to [global funds] has helped shape our world, driving progress and innovation, creating jobs and opportunities, building communities—indeed, developing nations and transforming whole economies.”**

PAUL SCHOTT STEVENS, PRESIDENT AND CEO, INVESTMENT COMPANY INSTITUTE, AT THE ALFI GLOBAL DISTRIBUTION CONFERENCE, SEPTEMBER 27, 2011, KIRCHBERG, LUXEMBOURG



## Worldwide Total Net Assets of Mutual Funds

Trillions of U.S. dollars, year-end



Sources: Investment Company Institute, EFAMA, and national mutual fund associations

substantial restrictions on short selling as the means to address regulators' concerns about the impact of recent market events on investor confidence and the stability of financial markets.

ICI likewise brought its research and deep expertise in retirement issues to bear on the European Commission's (EC) examination of the key challenges facing European pension systems and how the EU can support the delivery of adequate and sustainable pensions. The Institute submitted a letter explaining how the U.S. retirement savings framework has sought to address issues raised in the EC's paper. The letter described the critical role of U.S. defined contribution (DC) plans in providing retirement income and discussed important DC plan design features, such as automatic enrollment and default investment options. ICI's letter stressed the importance of meaningful and effective disclosure to DC plan participants and employers. It also noted that U.S. plan sponsors and service providers are instrumental in facilitating informed participant decisions as they provide education tools and new products, such as target date funds.

The Institute also lent its expertise to efforts to halt money laundering and terrorist financing in global markets. ICI closely monitors the work of the Financial Action Task Force (FATF), an

intergovernmental body that establishes standards for combating illicit money flows. During an industry hearing and in comment letters, the Institute provided the views of member funds on FATF's proposed revisions to recommended standards on customer due diligence, reliance on third parties, and the risk-based approach to combating money laundering and terrorist financing. The Institute will continue to engage with FATF during its review process.

As fund managers increasingly respond to issues that are transnational and even global, ICI has recognized the need for a global voice for the fund industry. During the past year, ICI's Board leadership urged the Institute to fill that need. As a result, at the start of the Institute's new fiscal year in October 2011, ICI launched ICI Global, the first industry body exclusively focused on the global investment fund industry.

ICI Global will build upon ICI's long-standing international advocacy on behalf of U.S. funds, their advisers, and their investors. Its mission is to advance the common interests and promote public understanding of global investment funds, their managers, and investors.

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For more information on ICI's international activities, please visit [www.ici.org/policy/regulation/international](http://www.ici.org/policy/regulation/international). For more information on ICI Global, please visit [www.ici.org/iciglobal](http://www.ici.org/iciglobal).

## ROUNDTABLE

# Addressing the Benefits and Challenges of Social Media *A Conversation With ICI Staff*

### How is the use of social media by funds evolving?

**Peter Salmon, Director, Operations and Technology:** It's just remarkable to see how our members have been putting social media tools to work. Generally, I tend to think of social media as a set of technologies that enable a large community to collaborate—not just services like Facebook and Twitter, but also wikis, blogs, and other modes of electronic communication. More and more, these social networks help funds communicate with investors during turbulent market conditions, or even just normal market conditions. We also see members using social media for shareholder education, for advertising and marketing, to find new ways to interact with business partners and distributors, and to enhance collaboration among their own employees.

And I'm not talking only about the largest ICI members. Smaller fund complexes have been particularly active with social media, because it enables them to connect with audiences that they might not otherwise reach, due to cost constraints or other factors. They've got blogs set up. They use social networks to answer shareholder questions. Social media have opened a whole new window for funds across the spectrum.

**Ianthé Zabel, Senior Director, Media Relations:** Peter's point on adoption shows up in the research on how funds use social media. Last July, Cerulli Associates released a survey that found nearly 70 percent of asset managers are using social media tools, versus 31 percent a year prior. Another research organization, kasina, found last May that 80 percent of asset managers were active in at least one social media channel.

### ICI member committees have focused intently on social media issues. Can you tell us a bit about that work?

**Zabel:** ICI's Public Communications Committee [PCC] has taken a close look at the adoption and use of social media. ICI worked with Tiller, a marketing firm, to conduct a survey for the committee. One interesting finding from that survey was that 82 percent of the participating ICI members agreed, either somewhat or strongly, that social media would likely become as important as traditional news media in the next few years. We heard a presentation on this survey at our PCC meeting in New York last December. It generated quite a lively discussion.

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**“It's just remarkable to see how our members have been putting social media tools to work.”**

PETER G. SALMON, DIRECTOR, OPERATIONS AND TECHNOLOGY, INVESTMENT COMPANY INSTITUTE

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**Salmon:** And it's been interesting to see how the discussions have evolved as the technology has evolved. Social media have been an agenda item at our Technology Committee's meetings for a number of years. That work culminated this year in the creation of a Technology Committee task force to serve as a resource on how social networks are being used, how the technology is developing, and how members can use tools to solve compliance challenges. The committee has also interacted with the Financial Industry Regulatory Authority [FINRA], which has provided us with a good view into how regulations are being crafted.

**Dorothy Donohue, Senior Associate Counsel:** As you might imagine, ICI's Advertising Compliance Advisory Committee also has been especially active on social media issues. Members have used the committee's quarterly conference calls, for example, as a forum to float questions and discuss their policies and procedures around social media. The Institute is currently surveying the committee members' policies and procedures with a view toward determining the subjects they cover, whom they apply to, and their level of detail. We hope this information, in the aggregate, will provide some insights for ICI's members as they either review or draft compliance policies and procedures relating to electronic communications or the use of social media.

### **What are some of the broader challenges that social media poses for funds?**

**Donohue:** One difficulty is the availability of social media to employees inside and outside the office. The overlap between these two worlds, particularly with respect to social networking sites, means having to really drill down into the matter of where an employee's business conduct ends and where his or her personal conduct begins.

**Zabel:** Another challenging aspect of social media is its highly interdisciplinary nature. In other words, it's not an issue our members can just hand off to their legal departments, or the compliance folks, or technology, or public relations—several departments within the organization have to be involved in developing an approach for using and overseeing social media.

These are some of the reasons why you still see a good deal of caution when it comes to firms embracing social media. The Cerulli study I mentioned earlier said that most asset managers could be described as “guarded adopters” of social media. We also saw this reflected in our research, which conveyed both the enthusiasm and the hesitancy around social media.

### **Is compliance with regulations a factor in that hesitancy?**

**Donohue:** Compliance with regulations with respect to social media certainly can be a challenge for members, but, to understand that challenge, you need to first take a step back and look at the framework of regulation around communications with the public, parts of which date back to the 1930s. Broker-dealer firms—which include principal underwriters of mutual funds as well as retail distributors of mutual funds—must supervise the activities of associated persons. To do that, they have to develop compliance policies and procedures, and they have to educate their personnel regarding those procedures. That would include training on the differences between business and nonbusiness use of communications, as well as steps necessary to preserve business communications. Those compliance policies and procedures must account for specific requirements regarding the content and filing of advertisements and other material. There are also recordkeeping requirements. Broker-dealers have to keep originals of all communications received and copies of all communications sent by the broker-dealer relating to its business.

Given this framework, you can see how challenges arise in the context of electronic communications. There must be prior principal review of static postings, for example, and risk-based supervision of interactive communications. By far the biggest challenge is recordkeeping, because the overarching requirements are so broad.

### **What have been the key recent regulatory developments on social media?**

**Donohue:** FINRA has been the most active. As of August 2011, they've issued two sets of guidance, which look at the public communications rules on the books and apply them to social media. The guidance has addressed a range of topics—such as recordkeeping, suitability responsibilities, and the supervision

of both static and interactive content—and it has clarified some key issues. For example, it's established now that firms can pay for mobile devices for their employees, but they don't have to supervise communications on those devices that are not business related. That guidance makes it easier for firms to, say, get the latest technology to their sales forces.

### **What are the challenges that regulators face as they do their jobs?**

**Salmon:** One of the biggest challenges for regulators is finding the right balance as they apply existing rules to rapidly evolving technology and practices. Look at document retention, for example. In the past, you had to keep things like newspaper advertisements, but the volume was lower. Social media, and electronic communications generally, mean a much bigger volume of information. So how do you require regulated entities to retain all this information while not imposing extraordinary costs on them?

### **As ICI members and regulators address these challenges, what is ICI's role?**

**Zabel:** One of the Institute's core strengths is its ability to bring people together. We're convening people with social media knowledge and tailoring the discussion on implications for funds in particular. Some firms, of course, are further down the road than others with social media. Members are often willing to share their expertise and experiences with those that may just be getting started. Along those lines, I'd add that the conversation doesn't just take place in committees and within the Institute. We've had some terrific panels on social media at our conferences this year, particularly at the General Membership Meeting, the Mutual Fund Compliance Programs Conference, and the Operations and Technology Conference. To have this dialogue in a more public setting is important, given the intense interest that you see on social media.



ICI staff involved in social media: Peter G. Salmon, Director, Operations and Technology; Dorothy M. Donohue, Senior Associate Counsel; and lanthé Zabel, Senior Director, Media Relations

**Salmon:** I'll echo lanthé on the value of getting people together for open conversations. One of the best parts of the committees that I coordinate is what we call "shop talk." Anyone can submit questions to the group on noncompetitive issues. It's a great way for peers to interact and address general business challenges. On social media, we've discussed application of the regulations, application of the technology, and application of the tools. The conversation that goes on around these topics is crucial not just for learning, but also building relationships throughout the business.

**Donohue:** Another benefit to gathering all members' perspective is that it allows us to engage meaningfully with regulators. To take one example, our August 2011 comment letter on FINRA's proposal to modernize its advertising rules included views from across the Institute and its members and offered a constructive message to FINRA—industry and regulators should work together to modernize the rules in a way that permits the use of today's and tomorrow's technologies in a cost-effective way, consistent with investor protection.

#### What lies ahead for social media?

**Salmon:** Regulators and our members will continue to wrestle with a fundamental question—is the present model of regulation for electronic communications, including social networks, sustainable in the face of all the innovation we see? Meanwhile, ICI members will continue to create a culture of responsible communications. They'll do that by continuing to craft their guidelines so employees know where the boundaries are. They'll also leverage tools that facilitate compliance with existing regulations. Put all these together—policies, training, tools—and I'm confident we'll see more use of the new technologies across all the different departments and in a responsible way.

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Visit ICI's social media sites at [Twitter.com/WhatsNewAtICI](https://twitter.com/WhatsNewAtICI), [Facebook.com/ICI.org](https://facebook.com/ICI.org), and [www.Linkedin.com/company/investment-company-institute](https://www.linkedin.com/company/investment-company-institute).

# Risk Management: IDC and ICI Lead the Way in an Evolving Landscape

Managing risk has always been vital for any financial business. In the aftermath of the financial crisis, regulators in the United States and around the world are putting new emphasis on risk management and oversight. This is a challenge for both funds and directors, and the Independent Directors Council and ICI are responding—building upon a solid base of activity in this area and on IDC’s commitment to education.

*Fund Board Oversight of Risk Management*, a new joint paper from IDC and ICI, emphasizes that risk management is not a new concept or function for the fund industry. Practices continue to evolve, however, and the paper offers insights on how fund advisers and boards are addressing their respective responsibilities.

*Oversight of Risk Management* marks a milestone in ICI’s and IDC’s record of engagement on risk management issues. ICI’s activities on risk management date to 2005, when it established an advisory committee on the topic. In 2007, ICI published the paper *Chief Risk Officers in the Mutual Fund Industry: Who Are They and What Is Their Role Within the Organization?* This paper contains useful information to funds that are interested in either creating the position of Chief Risk Officer (CRO) or understanding the CRO’s role.

IDC has a long tradition of advancing director education and promoting greater public understanding of the role of directors through its wealth of educational resources, and *Oversight of Risk Management* continues the tradition of practical guidance to assist fund directors in fulfilling their duties. In areas closely related to risk management, a 2009 IDC task force paper—*Board Oversight of Fund Compliance*—discusses how funds implemented new compliance requirements and the board’s relationship with the chief compliance officer. A 2008 task force paper—*Board Oversight of Derivatives*—explains, in plain English, the fundamentals of derivatives and their uses by funds.

In 2009, the Senior Supervisors Group, composed of regulators of financial institutions across the globe, released a report on the lessons learned during the financial crisis. These lessons were developed by comparing the practices of institutions that weathered the financial crisis well with those that did not. Many of the lessons learned related to risk management systems within financial institutions and effective risk management practices. The Institute shared the Group’s report and information regarding effective practices with its members. With this increasing focus on risk by the industry and regulators, ICI’s board also made ICI’s Risk Management Advisory Committee





a permanent standing committee of the Institute. In 2010, ICI assisted its members in implementing new Securities and Exchange Commission (SEC) rules that require disclosure of additional information about the board's role in the risk management process in a fund's Statement of Information (SAI). ICI sponsored a call for funds and directors to discuss the new rule and to provide implementation guidance. As funds began to implement this requirement, ICI published a white paper, *Disclosure of the Role of the Board in Risk Oversight: Samples of Fund SAI Disclosure*, which consisted of examples of the disclosure funds added to their SAIs in response to these new requirements.

This year, both IDC and ICI continued to include risk management topics in their conferences. IDC's 2010 fall conference included panel sessions on risk and IDC hosted two educational conference calls on risk oversight, "Oversight of Investment Risk" and "Risk Oversight and Governance Practices." Risk oversight was also a frequent topic of discussion among fund directors at IDC's regional chapter meetings. And ICI again included risk management as a topic at its annual Mutual Fund Compliance Programs Conference in 2011.

Regulators will continue to focus on risk management. The Dodd-Frank Wall Street Reform and Consumer Protection Act established the Financial Stability Oversight Council (FSOC)

to identify and respond to emerging threats to the financial system. The FSOC's first annual report to Congress urged market participants to "employ heightened risk management." While the FSOC did not elaborate on what that might entail, the report sends a clear message about regulators' continued interest in risk management. That interest also has been evident in remarks by SEC Chairman Mary L. Schapiro, who stated that the agency's examination group will be looking to see if registrants have embraced "a culture of compliance," including enterprise risk management, within their firms.

ICI and IDC will continue to assist funds, their advisers, and directors address and stay up to date on current thinking relating to risk management. In addition to assisting members, ICI and IDC will continue to serve as the voice for funds and their boards as regulators consider this topic.

In a further development of its educational mission, IDC this year unveiled *Fundamentals for Newer Directors*, a dedicated website targeted to directors with up to five years of experience. This important resource helps newer directors understand their role and responsibilities.

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For more information on the Independent Directors Council, please visit [www.idc.org](http://www.idc.org) and <http://fundamentals.idc.org/>. For more information on risk management, please visit [www.ici.org/policy/regulation/compliance](http://www.ici.org/policy/regulation/compliance).

## Ruling Highlights Need for Robust Economic Analysis

In July, the failure of the Securities and Exchange Commission (SEC) to evaluate adequately the costs and benefits of a new proxy access rule earned it a stinging rebuke from a federal appeals court. The court's decision emphasized, once again, the need for the SEC to conduct thorough cost-benefit analyses and consider the effects of its rules on efficiency, competition, and capital formation.

The ruling by the United States Court of Appeals for the District of Columbia Circuit vacated an SEC rule, adopted in August 2010, designed to make it easier for shareholders of operating and investment companies to nominate directors.

The case was brought by the Business Roundtable and the Chamber of Commerce of the United States, who argued that the SEC had acted arbitrarily in approving the proxy access rule. ICI and the Independent Directors Council filed a joint friends-of-the-court brief, challenging the rule's application to registered investment companies. The brief pointed out that the SEC did not take into account the unique structure of registered investment companies and the protections already afforded shareholders. A three-judge panel of the DC Circuit agreed—in very strong terms.

The court's July ruling specifically addressed the Commission's failure to assess the unique economic effects of the rule on investment companies. The panel of judges agreed with ICI

and IDC that the SEC failed to adequately address whether the regulatory requirements of the Investment Company Act of 1940 reduced fund shareholders' need for, and the benefits of, the proxy access rule.

"[W]hile the Commission acknowledged the significant degree of 'regulatory protection' provided by the Investment Company Act," the court noted, "it did almost nothing to explain why the rule would nonetheless yield the same benefits for shareholders of investment companies as it would for shareholders of operating companies." The court rejected the SEC's argument that an investment company would suffer increased costs and decreased efficiency of its board only if shareholders elect a nominee. "This rationale is tantamount to saying the saving grace of the rule is that it will not entail costs if it is not used," said the court. "[T]his is an unutterably mindless reason for applying the rule to investment companies."

The ruling marks the fifth time since 2005 that the court has struck down an SEC rule, and it is the third decision based on the agency's failure to properly weigh the economic consequences and to consider—as the law requires—the effects of its rules on efficiency, competition, and capital formation.

That requirement has been a longtime focus of ICI's advocacy, as the Institute has consistently emphasized the need for robust cost-benefit analysis. ICI has expressed concern, for example,



“[T]he Commission has a unique obligation to consider the effect of a new rule upon ‘efficiency, competition, and capital formation’...and its failure to ‘apprise itself—and hence the public and the Congress—of the economic consequences of a proposed regulation’ makes promulgation of the rule arbitrary and capricious and not in accordance with law.”

*BUSINESS ROUNDTABLE ET AL. v. SEC, 647 F.3d 1144, 1148 (DC Cir. 2011)*

over an inadequate cost-benefit analysis on a proposal from the Commodity Futures Trading Commission that could treat hundreds, if not thousands, of mutual funds or their advisers as commodity pool operators, thereby importing duplicative and fundamentally inconsistent regulatory requirements. ICI also has been critical of the cost-benefit analysis accompanying the SEC’s proposal to reform Rule 12b-1, which permits funds to compensate brokers and other financial intermediaries from fund assets. ICI’s own analysis conservatively estimates the initial costs of implementing the Commission’s proposal at more than twice the SEC’s estimate, and ongoing costs at more than eight times the SEC’s figures. The SEC’s estimates of the proposal’s benefits are also suspect, because they rely on the faulty assumption that shareholders will receive the same level of services while paying less in fees.

Most recently, ICI and IDC promoted the need for strong economic analysis as the SEC undertakes to review its existing regulations to determine which ones are working as intended and which ones should be made more effective or less burdensome, or be repealed. The SEC asked for public input after President Obama issued an order calling upon independent federal agencies, including the SEC, to modernize and

improve their regulations. ICI pointed out that the SEC’s current processes for the review of existing rules are insufficiently comprehensive and robust to ensure that the agency’s regulatory program can keep pace with market developments and changes in the regulatory landscape. ICI included suggestions for how the SEC could develop a comprehensive and workable plan for such retrospective reviews.

In its letter, IDC noted a number of the regulatory requirements imposed on fund directors that are no longer necessary or appropriate. Those requirements could be modified, eliminated, or delegated, with the goal of enhancing boards’ effectiveness.

The fund industry welcomes strong regulations that protect investors, but regulators must keep sight of the critical role of sound economics in the rulemaking process. As regulatory activities proceed, ICI will continue to work to educate regulators about the unique structure of investment companies, significant protections afforded to fund shareholders, and the costs and benefits associated with contemplated new requirements.

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For more information on the court’s decision, please visit [www.ici.org/viewpoints/view\\_11\\_pss\\_proxy](http://www.ici.org/viewpoints/view_11_pss_proxy).

# Strength of the Defined Contribution Plan System

By *Mary S. Podesta*



Mary S. Podesta has been Senior Counsel of Pension Regulation since 2005, and a member of ICI's Law Department since 1994.

While events since 2008 have stress tested all long-term saving, the system of saving in 401(k) plans and individual retirement accounts (IRAs) has weathered the storm and deserves the confidence Americans have in it. On many fronts, evidence shows that the framework under which Americans save in 401(k) plans and IRAs is resilient and sound. The challenge today for policymakers and providers—including funds and their advisers—is to focus on ways to help Americans make the best possible use of the system to achieve retirement security.

The defined contribution (DC) plan concept is a good one and is serving Americans well. DC plans provide funding predictability for employers and meet the needs of a mobile American workforce, whose median job tenure is 4.4 years before changing jobs. As of June 2011, Americans had accumulated \$4.7 trillion in 401(k) plans and other DC plans, and \$4.9 trillion in IRAs (about half of which came from rollovers from plans). Approximately half of DC plan and IRA assets are invested in mutual funds.

ICI Research has helped make the case that plan participants and IRA savers generally make good investment and distribution choices. Our data show that savers in 401(k) plans and IRAs tend to invest in lower-cost funds and have investment allocations appropriate to their ages. We find that, by and large, people act responsibly with their DC account balances at



retirement, choosing to leave the balance in the plan, reinvest a lump-sum distribution, or take installment payments or annuities. IRA-owning households similarly are responsible stewards of their IRA assets, typically making modest withdrawals. IRA withdrawals often are calculated to meet minimum distribution requirements under the Internal Revenue Code.

The crucial test of the DC system, however, is how well participants will fare at retirement. Because 401(k) plans are only 30 years old, ICI has projected, in research with the Employee Benefit Research Institute, what participants in their late thirties and early forties today—who will spend full careers with 401(k) plans—could accumulate by age 65. Using typical employee behavior and historical financial returns, the study found that projected 401(k) accumulations would replace more than half of their salary for more than 60 percent of this cohort. A full career with 401(k) plans, thus, should provide meaningful retirement security when combined with other savings and with Social Security. Social Security replaces a significant amount of income for all workers, particularly lower-income workers.

In the past three years, the resilience of the retirement system and retirement savers was tested—and, as ICI Research found, withstood the test. Retirement investors did not panic or overreact to the market downturn. Institute surveys of DC plan recordkeepers since 2008 find participants continued saving

in plans; for example, fewer than one in 25 DC participants stopped contributions in any year since 2008. And the share of participants who tapped plan accounts through withdrawals also remained low—fewer than one in 25 took withdrawals in any given year.

Throughout the downturn, Americans themselves voiced a high level of confidence in the individual account system. In fall 2010, ICI found that 91 percent of households expressing an opinion of 401(k) plans had favorable impressions, whether or not the household owned DC accounts. Among DC-owning households, more than 80 percent said the immediate tax savings from their retirement plans were a big incentive to contribute and that their DC plan offered a good lineup of investment options. Nearly all DC-owning households appreciate having choice in, and control of, the investment options in their DC plans. The survey also shows Americans pay attention to their retirement planning. In the wake of the financial market crisis, 58 percent of households owning retirement accounts or other financial investments increased their regular savings amount, shifted their investment mix away from stocks, or increased their expected retirement age—and many made more than one of these changes. These conservative changes likely reflect the reduced willingness to take investment risk that households have expressed since the financial market crisis.

Taken together, this evidence demonstrates that the system of saving for retirement in 401(k) plans and IRAs is a success. Nonetheless, there are steps we can take to improve Americans' retirement preparedness and income security. The task is to help workers use these accounts to accumulate retirement nest eggs and manage those assets in retirement. Simply put, we need to focus on providing retirement savers with information and tools to help them use the system well.

First, we need to implement the new Department of Labor (DOL) 401(k) disclosure regime, including new standards for information that plans must give to participants and that plan recordkeepers must give to plans. For more than 30 years, ICI has called for rules to require that 401(k) investors receive concise, key information about all investment options in their 401(k) plans, not just mutual funds. We are pleased that the DOL's new rules follow these recommendations and that the information for mutual funds generally corresponds to information funds already disclose under Securities and Commission rules. In 2012, participants will begin to receive key information about plan investments at enrollment and annually thereafter, with access to additional information about the investments on a plan website.

ICI has taken a leadership role in working with members, other organizations, and regulators to facilitate the flow of timely and accurate information to plans and recordkeepers on fees and expenses, performance, risks, and other required information for mutual funds used in plans. This includes working to create a centralized database of the DOL-required information using the system under which mutual funds already provide data to the National Securities Clearing Corporation (NSCC). The NSCC, in turn, would make the DOL-required information available to plans.

A second priority is for the DOL to give retirement plans more flexibility to use electronic delivery to provide participants with required information. Recognizing that its rules may constrain e-delivery, the DOL asked this year whether it should revisit them. The Institute has been on the forefront in urging the DOL to allow plans to make e-delivery the default, as long as

participants can request paper instead. We filed a comprehensive comment letter with the DOL and commissioned an academic white paper by Peter P. Swire of Ohio State University. The comment letter and white paper point out that Internet access is almost universal today. The paper also lays out the benefits that e-delivery brings in helping investors understand, manage, and act on information; and argues that existing law should support allowing plans to deliver required information electronically unless a participant opts out and requests paper instead.

As a third challenge, having helped retirement savers accumulate assets, the industry must work to maintain and enhance their ability to understand the distribution phase as well. Because there is no one-size-fits-all solution for the distribution phase, information, education, and advice are of paramount importance.

ICI is dedicated to improving the 401(k) system to benefit participants, sponsors, and plans. ICI works to ensure that proposed changes to the system will achieve their stated goals. For example, we took a strong stand this year on the DOL's controversial proposal that would blur the line between information and education, on the one hand, and advice, on the other hand—a line that must be clear to market participants. Under the DOL proposal, many more persons assisting retirement savers would be viewed as giving advice, which would subject them to Employee Retirement Income Security Act (ERISA) fiduciary duties. As proposed, the changes could affect routine assistance recordkeepers give to plans, communications with mutual fund call centers about rollovers from plans to IRAs, and other common interactions by financial intermediaries with IRA savers.

In comment letters and testimony, the Institute urged the DOL to redraft and repropose the changes so that ERISA fiduciary status attaches only to genuine advisory relationships where a position of trust and confidence exists. We are pleased the DOL has now announced that it will revise and repropose the rule early next year.



ICI staff working on pension issues: SEATED: Elena B. Chism, Associate Counsel; Peter J. Gunas, Government Affairs Officer, Retirement Security and Tax Policy; Allen C. Huffman, Director, Retirement Security and Tax Policy; Sarah A. Holden, Senior Director, Retirement and Investor Research  
STANDING: Anna A. Driggs, Associate Counsel; Mary S. Podesta, Senior Counsel, Pension Regulation; Peter J. Brady, Senior Economist

ICI submitted specific recommendations to the DOL on how to revise its published guidance to clarify that plans and service providers can convey the general advantages of various distribution forms without triggering fiduciary liability.

ICI also responded actively to proposals to mandate or regulate illustrations of lifetime income on benefit statements, which is currently on the regulatory agenda at the DOL and the subject of legislation introduced in both houses of Congress.

Disclosure that translates an account balance into an estimated projected monthly benefit is useful to retirement savers, and many plans provide it. Current legislative proposals, however, would only allow calculating those projections as an annuity based on a participant's current plan balance.

We have advocated to the DOL and on Capitol Hill that any mandate or safe harbor should give plans the option to include projected future investment contributions and investment growth in estimating the size of a participant's account at age 65. It also must allow plans the option to calculate an estimated monthly income stream using a percentage of the

final account reasonably designed to spread payments over retirement (such as the 4 percent method that many plans use today on benefit statements or in retirement planning tools), as an alternative to an annuity calculation. The DOL expects to issue a proposal by next year.

Despite the success of the DC retirement system, the pressures on the United States today to achieve fiscal balance and slow the growth of national debt may spark a rigorous examination of tax incentives for retirement saving. ICI's mission will be to show the economic and social value of preserving these incentives—efforts bolstered by the expertise that our Research, Law, Government Affairs, Operations, and Public Communications staffs bring to bear on pension issues.

ICI is committed to supporting policies that preserve and strengthen the resiliency of the 401(k) system, and to working with members, regulators, and policymakers to provide retirement savers with information to help them use the system well.

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For more information on ICI's work on retirement issues, please visit [www.ici.org/policy#retirement](http://www.ici.org/policy#retirement).

## QUESTION & ANSWER

# With the Chair of ICI's ETFs Committee



### JAMES E. ROSS

ICI Governor and Chair, ETFs Committee  
Senior Managing Director and Global Head of ETFs, State Street  
Global Advisors

#### **Total assets of U.S. exchange-traded funds [ETFs] surpassed \$1 trillion in January of 2011. What does that milestone mean?**

It means a lot of things, but I think it certainly speaks to the benefits that ETFs provide to both retail and institutional investors: low cost, versatility for managing portfolios, the underlying liquidity, among others. The product has grown into a great option that investors have to achieve their goals, whether those goals are retirement, or saving to buy a house, or any number of objectives.

Another key benefit of ETFs is their flexibility. So while the “core” ETFs that offer standard index strategies have continued to grow substantially, innovation in this area has also opened up new asset classes, new areas of expertise, and new strategies, from index to active.

We've seen different kinds of weighting methods when it comes to fixed income and equities. I think that's one reason why investors' financial advisers have been a driver of ETF growth for many years. The product is a useful tool for them as they find and implement the right strategy for the investor whose goals they're trying to help achieve.



## **Along with growth, ETFs have encountered new challenges.**

### **What are the top issues?**

One of our biggest challenges as an industry continues to be investor education and awareness—trying to help people really understand the product and how it works. Sure, ETFs are clearly mainstream, with more than \$1 trillion in assets, but you’ve still got newcomers and other folks out there who may need help on the basics. What are ETFs? How are they different from other investment vehicles? How are they similar?

Ironically, the innovation that I just mentioned is a factor in this challenge. As the industry has grown, we’ve seen a remarkable number of ETFs launched in relatively short order. Some of these funds are regulated under the ‘40 Act [Investment Company Act of 1940], some of them are regulated differently. Investors, financial advisers, and others need to grasp these distinctions. So education continues to be critical, and, when you think about it, that’s probably not going to change. There are more than 1,000 ETFs in the United States today, and that number will continue to grow.

An important part of this—and something we as an industry need to continue to work on—is how we can tailor information for all the potential investors in ETFs. Anyone who spends much time in this industry knows that there’s a need for

knowledge among all the constituent users of ETFs, whether that’s the retail investor, a broker, financial planner, registered investment adviser, or even the institutional community. But the needs vary for each of those groups.

Another challenge is increased regulatory scrutiny. Given the volatility of the markets that we saw during the financial crisis, regulators naturally are very focused on how financial markets work and whether they’re appropriately regulated. Those concerns cut broadly across the financial sector, but ETFs, because of their newer structure, have gotten a significant amount of attention lately from regulators both here in the United States and abroad.

Think about it—ETFs, depending on the day, can be 30 to 40 percent of the dollar trading volume on the New York Stock Exchange. You go back 20 years ago, ETFs didn’t exist. So regulators are looking at this and continue to deepen their understanding of how ETFs are part of the overall fabric of the financial markets today. How do they work from a structural standpoint? What is their interrelationship with the underlying trading markets and emerging practices, such as high-frequency trading? How are traders using ETFs in ways that they probably would have used derivatives or individual stocks in the past?

### **Is education also a part of the regulatory challenge?**

Without question. The industry and ICI have been engaging directly with policymakers to make sure they have the best information.

We also work to educate the folks who interface with the policymakers. For example, a paper was published last fall that discussed the markets and ETFs at length. Its authors were both market experts who had served as advisers to policymakers. Their paper was provocative and floated some good ideas, so it got quite a bit of attention. The problem, though, was that the authors leveled several accusations at ETFs based on fundamental misunderstandings of how the product works. ICI staff worked with members on the ETFs Committee to get that point across in commentary posted on ICI's website and used in further educational efforts.

There's also a global aspect to all this. As ETFs have emerged in different marketplaces around the world, they've come to have different structures and to operate under different regulatory regimes. Over the past year, we've seen the need to make sure the world's regulators fully grasp the implications of these differences.

Probably the clearest example of that was a paper published by the Financial Stability Board [FSB], which is based in Switzerland. The paper took issue with so-called synthetic ETFs, meaning those that enter into a single swap with an affiliated counterparty to obtain returns. As ICI suggested in its comment letter to the FSB, the paper didn't make it clear that U.S. ETFs that meet the requirements of the '40 Act, including those using derivatives, are not permitted to create that type of structure.

### **Outside the regulatory arena, how is ICI helping the ETF community?**

I'm pleased to see ETFs on the agenda at ICI Research's academic conference at the University of Texas this November [Investment Company Institute/AIM Investment Center Academic & Practices Conference]. One thing we've discussed in the ETFs Committee is the value of promoting better understanding of ETFs from a research standpoint. It's important for academics to continue to study ETFs, their role in marketplace, and how investors are using them in their portfolios.

### **Tell us more about the ETFs Committee and its agenda. What are its priorities?**

For one thing, like all of ICI's standing committees, we're bringing together viewpoints from across the industry so that we can develop industrywide positions on regulatory initiatives. We also serve as a good mechanism for direct interaction with regulators. This summer, for instance, we had an interesting back-and-forth discussion with regulators on issues such as the ETFs creation process.

And, as you might imagine, education around ETFs is at the top of our priorities list. We're working on ways to produce a better general understanding of the product, such as development of consistent sets of materials that constituents across the board can use to get a better grasp of both ETFs basics and some of the nuances of different products. ICI and its website are a logical home for some of those materials.

The committee has also focused on the media and the media landscape. ETFs offer a compelling story, and they get media attention at all levels—from TV's financial channels to the biggest print publications to bloggers whose websites do nothing

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**“While the ‘core’ ETFs that offer standard index strategies have continued to grow substantially, innovation in this area has also opened up new asset classes, new areas of expertise, and new strategies.”**

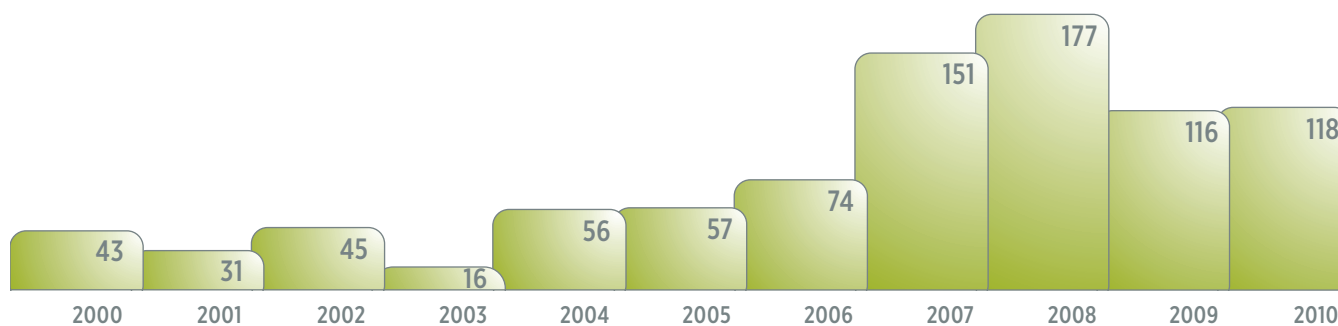
JAMES E. ROSS

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## Net Issuance of ETF Shares\*

Billions of dollars, 2000–2010



\*ETF data prior to 2001 were provided by Strategic Insight Simfund. ETF data include ETFs not registered under the Investment Company Act of 1940 and exclude ETFs that invest primarily in other ETFs.

Sources: Investment Company Institute and Strategic Insight Simfund

but track the industry. So there's quite a range of coverage, and, in the electronic age that we live in, intense pressure to break news. As stories get picked up by television outlets, getting accurate or complete information becomes even tougher, because the amount of time you have in a TV segment is often just a matter of minutes, if that.

So this is an important topic for the committee, given the media's role in educating the public, our investors. This year, working with ICI Public Communications, we devoted some of our efforts to gathering and sharing insights on the media landscape. I believe the process helped us get a better sense of steps the industry can take to improve the odds that press coverage will be well informed.

Finally, we've also spent time discussing how we as an industry react in times of crisis, whether it's broader market volatility or a more specific problem affecting ETFs. The industry has had a few such tests recently, such as the unsettled markets of this past summer or the "flash crash" that we saw in May 2010.

ETFs and the ETFs Committee have come through those events well, but the committee has tried to identify and formalize a series of steps we can take in any future times of difficulty.

The goal is to make sure we proceed carefully and consistently, developing viewpoints and common-ground solutions that we can then communicate broadly.

### Looking into your crystal ball, how do you see the ETFs industry evolving in the coming years?

Well, my crystal ball hasn't always been right over the years! But one thing I think you're going to see is continued innovation.

This is a highly competitive marketplace, and the way to succeed is to innovate. You really have to innovate, though, from the standpoint of people who want to use ETFs to work toward their financial goals. You need to look through their eyes and ask, what kind of product are they looking for? Is it passive ETFs? Active? When I look at the future, I think we will be looking at active ETFs becoming more of a mainstream product. That will lead to an even broader suite of ETF opportunities that investors will have to choose from. We just need to make sure investors have the right information so they can benefit as much as possible from that choice.

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ICI Governor James E. Ross is Chairman of ICI's ETFs Committee and is Senior Managing Director and Global Head of ETFs for State Street Global Advisors. For more information on ETFs, please visit [www.ici.org/etf\\_resources](http://www.ici.org/etf_resources).

# ICI Advocacy on Markets and Trading

Rapid technological changes in the operation of financial markets have ignited a wide-ranging debate over how best to structure institutions and mechanisms for trading stocks, bonds, and other instruments, such as derivatives. As institutional investors responsible for more than \$13 trillion in assets, the registered investment companies who are ICI's members are major players in those markets and have a vital role in how they operate, both in the United States and abroad. While these debates are complex and highly technical, the Institute's advocacy is driven by a simple principle: to ensure that markets operate efficiently, transparently, and fairly for the benefit of all market participants, including funds and the 90 million shareholders they serve.

To a great degree, the impact of new technology and innovation in trading has been positive. Overall, financial markets are

functioning better than ever before. Trading costs are lower, and technology has made trading more efficient. Investors have more tools available to make trades, whether large or small.

Yet these trends also have challenged the integrity of markets—and deeply unsettled many individual and institutional investors. New trading systems seem to spring up overnight, bringing innovations that may or may not prove to be useful. As trading has fragmented among multiple exchanges and venues, participants find it more difficult to gather information and find liquidity to support trades. Changes in rules or regulatory emphasis unleash structural and competitive changes in markets that are both powerful and unpredictable. Increasing automation has empowered new forms of trading that create new potential for market abuse. These trends have provoked fierce debates among competing interests.

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**“Most Americans engage with our financial markets through funds. They are the connection that takes Wall Street from here in Lower Manhattan to Manhattan, Illinois; Manhattan, Kansas; Manhattan, Montana; and Manhattan Beach, California. And they are the reason why ICI advocates so fiercely on the issues of market structure, trading practices, and transparency.”**

KARRIE McMILLAN, GENERAL COUNSEL, INVESTMENT COMPANY INSTITUTE

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The Institute addresses these issues by getting beyond labels and rhetoric to focus on the behavior of market centers and market participants—and the consequences of those behaviors for investors. ICI’s advocacy raises critical questions about automated trading, particularly high-frequency trading; transparency of market information; reform of short selling rules; and so-called dark pools where institutions can find liquidity. ICI is also concerned about policies—such as the potential imposition of securities transaction taxes—that could impede efficient trading and raise costs.

Increasingly, ICI’s interest in these issues goes beyond domestic markets. U.S.-based long-term mutual funds hold some \$2.4 trillion in non-U.S. securities, accounting for almost 25 percent of these funds’ assets. Jurisdictions around the world are facing a number of common issues. Given the links between financial markets and the interconnected trading strategies that funds pursue around the world, regulators need to coordinate their efforts to ensure a broad consistency of approach to market structure and trading.

Domestically and abroad, automated trading has raised concerns about fair and orderly trading and the potential for market abuse. The rapid-fire trading known as high-frequency trading appears to increase the amount of “noise” in markets—which may drown out useful information on trading volume and patterns—and creates potential for gaming trades, including

attempts to detect funds’ large-block trades to allow other participants to place orders with or ahead of those blocks.

ICI identified an immediate need for more information about such practices and called upon regulators and legislators—including the Securities and Exchange Commission (SEC), the European Securities and Markets Authority, and the European Commission—to examine the strategies employed by automated trading firms to determine whether certain strategies should be considered improper or manipulative activity. While some of these practices may not violate any specific rules, the Institute noted that they still may not be beneficial to the markets or to investors. At the same time, ICI urged regulators to take a measured approach in addressing automated trading to ensure there are no unintended consequences for investors in market efficiency and integrity.

Similarly, market participants and regulators need improved information on the incentives involved when brokers route trades to one venue over another. Enhanced information on trade execution would allow investors to make better investment decisions, while helping regulators and market participants better assess current market performance. “Sellside participants are challenged to restore confidence that their systems are serving the markets’ core functions—efficient transactions and accurate price discovery—rather than just their own interests,” ICI General Counsel Karrie McMillan told the ICI Equity Markets

Conference in December 2010. “In particular, we in the fund industry challenge you [brokers and dealers] to provide the information on trade routing and execution that we need to ensure that our orders are getting the best possible treatment, at the lowest possible costs.”

To that end, ICI has urged the SEC and the International Organization of Securities Commissions to examine the sufficiency of the information about trade execution provided to investors by brokers and other trading venues, and to improve transparency about current trading practices. Similarly, ICI is urging regulators to look at conflicts of interest that arise when brokers route trades to one venue over another.

The Institute also supports concepts such as the SEC’s consolidated audit trail, which would increase transparency of market information. At the same time, the Institute is working actively to ensure that implementation of the audit trail protects confidentiality of trade information and does not create unreasonable compliance costs.

Exchange-traded funds (ETFs) also continue to grow in popularity, bringing new strategies and approaches to trading. ICI is working to ensure that any regulatory examination of the impact of ETFs on markets is fully informed. In May, the Institute responded quickly and vigorously to a Financial Stability Board (FSB) note that failed to differentiate clearly between the structure of U.S. ETFs issued under the Investment Company Act of 1940 and “synthetic” ETFs, noting that the FSB’s broad definition “unfairly paints all ETFs with the same ‘systemic risk’ brush.” In the wake of unprecedented market volatility in August, ICI has called consistently for a thorough, empirical examination of all market changes that could affect trading volatility, without singling out particular products in the absence of sound data.

Short selling—the practice of selling borrowed securities—continues to raise controversy. In the Dodd-Frank Wall Street Reform and Consumer Protection Act, Congress ordered the SEC to conduct a study on the reporting of short sales, while European regulators are considering outright bans on short selling. ICI engaged on the issue to outline the potential negative consequences of public reporting of short sales, particularly in real time. Such real-time public reporting could destroy the confidentiality of fund trades and could allow other traders to front-run a fund’s trades, adversely affecting the price of the stock that the fund is buying or selling. The Institute also defended the positive impact that short selling can have on market liquidity and price discovery, and called upon regulators to stop any abusive or manipulative practices that may arise.

Much of the current debate over the structure of U.S. securities markets has centered on the proliferation of orders that are never displayed in the public exchanges and the venues that provide such liquidity, particularly dark pools. ICI outlined for regulators the long history of such venues in the market and highlighted the positive role they play. In a May statement to a subcommittee of the House Financial Services Committee, the Institute noted that these venues can lower the cost of implementing trading ideas and allow funds to avoid those seeking to profit, at the expense of funds and their investors, from public display of large orders. ICI is working to ensure that regulators continue to recognize the value of enabling market participants that frequently trade in large amounts, as funds do, to have access to venues that do not disclose the funds’ trading interest.

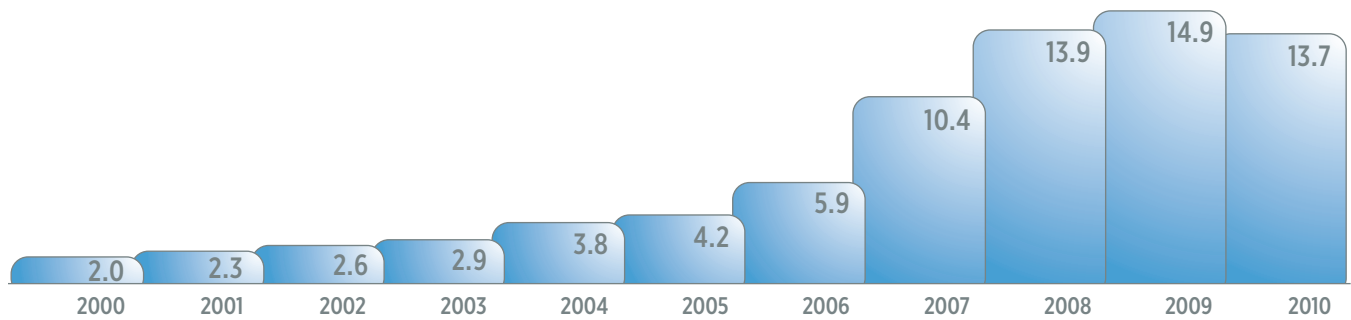
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**For the fund industry, the paramount interest must always be those of the 90 million shareholders who depend on funds to help meet their financial goals.**

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## Worldwide Trading in Equity Shares

Billions of trades, 2000–2010



Source: World Federation of Exchanges

New rules governing the venues in which most derivatives trading take place also must preserve market transparency, price efficiency, liquidity, and stability. In congressional testimony submitted in June, and in ongoing dialogue with the SEC and the Commodity Futures Trading Commission (CFTC), ICI pressed for rules that are clear, flexible, and consistent, and that minimize disruption and costs to market participants. The testimony emphasized the need for safeguards against conflicts of interest in swap execution facilities, including the addition of investor representatives on their boards of directors. ICI raised concerns that certain of the CFTC's and SEC's proposed trading restrictions could hamper the migration of swaps to swap execution facilities. ICI also advocated for block trade exemptions that help avoid market disturbances and front-running of trades.

The Institute also remained engaged in opposition to broader policies that could harm the efficiency of markets. In September, ICI joined with six other national financial and business organizations in a letter to Treasury Secretary Timothy F. Geithner, encouraging him to maintain U.S. opposition to a financial transaction tax (FTT) proposed by European finance ministers. Such a tax, the groups wrote, would “cycle through the entire

U.S. economy, harming both investors and businesses....Major economies that have adopted a FTT and FTT-like initiatives have had overwhelmingly negative results, including reduced asset prices, trading moving to other venues, market dislocation, and a decrease in liquidity. In light of the current fragile state of the global markets and the economy...the imposition of such a tax would be particularly harmful.”

The issues involved in debates over markets and trading are abstract, and the interests involved are often hard to untangle. For the fund industry, as McMillan reminded the Equity Markets Conference, the paramount interests must always be those of the 90 million shareholders who depend on funds to help meet their financial goals. “Most Americans engage with our financial markets through funds,” McMillan said. “Funds are the connection that takes Wall Street from here in Lower Manhattan to Manhattan, Illinois; Manhattan, Kansas; Manhattan, Montana; and Manhattan Beach, California. And fund investors are the reason why ICI advocates so fiercely on the issues of market structure, trading practices, and transparency.”

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For more information on policy issues surrounding markets and trading, please visit [www.ici.org/policy#financial\\_markets](http://www.ici.org/policy#financial_markets).

## ICI's Political Program: The Chairman's Council

In bipartisan fashion, ICI's political program, the Chairman's Council, fosters effective dialogue with key lawmakers in Washington, DC. The Chairman's Council provides individuals in the fund industry a targeted means to build rapport with members of Congress who work on legislative issues affecting the U.S. fund industry and the tens of millions of investors that it serves.

The Chairman's Council entered calendar year 2011 with a new chairman, Robert S. Dow, ICI Governor and Senior Partner at Lord, Abnett & Co. LLC. Under Dow's leadership, the Chairman's Council has continued to increase the resources it brings to the political program. Thanks to support from ICI members, the Chairman's Council raised nearly \$1 million in 2011. Further, fundraising for the 2011–2012 congressional election cycle is on track to exceed the Council's record of more than \$2.6 million raised during the 2009–2010 cycle.

The Chairman's Council provides several ways for ICI members to engage in the political program. First, ICI PAC, which is ICI's political action committee, is a core component of the Chairman's Council. ICI PAC aggregates donations to contribute to the campaigns of incumbent members of Congress who have expressed strong interest in the fund industry. ICI members can also contribute directly to a member of Congress on the

Chairman's Council list of recommended candidates. These candidates are selected because of their knowledge of the fund industry, their demonstrated interest in issues that matter to funds and their shareholders, and their membership on pertinent legislative committees.

Finally, ICI members can participate in one or more of the several fundraising events hosted each year by ICI PAC in support of incumbent members of Congress, with all contributions to those events going directly to the candidates. By the end of 2011, ICI PAC will have hosted more than a dozen fundraisers for Democrats and Republicans seeking reelection to either the U.S. House of Representatives or the U.S. Senate.

Each spring, a key ICI event is the Leadership Dinner, which provides fund industry leaders the opportunity to meet and exchange ideas with members of Congress and Administration officials. House Speaker John Boehner (R-OH) delivered the keynote address at the 2011 dinner, with policymakers from both houses of Congress and the Administration in attendance, including Representative Steny H. Hoyer (D-MD), the House Democratic Whip.

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To find out more about the Chairman's Council and ICI PAC, please contact ICI's Political Affairs Officer, James R. Hart, at [jhart@ici.org](mailto:jhart@ici.org) or 202/326-5892.



“The Chairman’s Council and ICI PAC are critical components of our industry’s efforts to engage in the political process and to support the reelection efforts of federal legislators who grasp the important role that funds play in the financial well-being of their constituents.”

ROBERT S. DOW



ICI Governor and Chairman of ICI’s Chairman’s Council Robert S. Dow, Senior Partner at Lord, Abnett & Co. LLC chats with House Democratic Whip Steny H. Hoyer (D-MD) at the May 4, 2011, Seventh Annual ICI Leadership Dinner.



Speaker of the House John A. Boehner (R-OH) at the Seventh Annual ICI Leadership Dinner on May 4, 2011.



ICI Governor and Independent Director of Wells Fargo Advantage Funds Michael S. Scofield talks with Representative Peter Roskam (R-IL) at an event hosted by ICI PAC on March 2, 2011.



ICI Chairman and Vice Chairman of T. Rowe Price Group, Inc., Edward C. Bernard, and Senator Ben Cardin (D-MD) at an event hosted by ICI PAC on February 16, 2011.



## 53rd ANNUAL GENERAL MEMBERSHIP MEETING

### The Way Forward With Fund Investors

ICI's 53rd Annual General Membership Meeting (GMM) brought together high-profile policymakers, thought-provoking commentators, and industry leaders. ICI enhanced the broad industry focus of the GMM again this year with three additional events—the Mutual Fund Compliance Programs Conference, the Operations and Technology Conference, and the Investment Company Directors Workshop. This structure gave attendees the opportunity to construct their own programs.

Gregory E. Johnson, Chairman of the 53rd GMM and President and CEO of Franklin Resources, Inc., evoked the theme of the conference in his opening remarks: "Don't forget that our industry thrives only when we keep our focus on our investors."

Edward C. Bernard, Chairman of the Investment Company Institute and Vice Chairman of T. Rowe Price Group, Inc., emphasized the importance of ICI's policy advocacy. "We must pursue policies that preserve and extend the incentives to save and invest that Americans rely upon."

GMM opened with the Seventh Annual Policy Forum, featuring Treasury Secretary Timothy F. Geithner. In response to questions by ICI President and CEO Paul Schott Stevens, Geithner stressed the importance of balance in the implementation of new rules under the Dodd-Frank Wall Street Reform and Consumer Protection Act.

In her remarks to attendees on the first anniversary of the "flash crash," Securities and Exchange Commission Chairman

Mary L. Schapiro emphasized the importance of monitoring high-frequency traders, because events like the flash crash undermine investor confidence.

The director community participated in a program on current issues at IDC's Investment Company Directors Workshop. A panel on "Fund Distribution and Board Oversight" discussed risk management and developments in distribution platforms and share classes.

At a joint session with the Mutual Fund Compliance Programs Conference, "Directors' Interface with Compliance, Risk Management, and Internal Audit," industry experts discussed the topics from the perspectives of both directors and compliance officers.

At the Operations and Technology Conference's Leadership Roundtable, panelists discussed the importance of keeping up-to-date despite limited resources.

Erskine Bowles and Alan Simpson, cochairs of the National Commission on Fiscal Responsibility and Reform, closed out the GMM with their recommendations for improving the economy's long-term outlook. The cochairs "slaughtered all the sacred cows in the field," in Simpson's phrase, as they tackled entitlement spending, tax reform, and the rapid growth of the national debt.

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For more information on ICI's 2012 GMM, please visit <http://gmm.ici.org>.

“First and foremost, this is a people business. The products that we offer help people retire with dignity, fund college educations, and save for important goals like buying a home. Overall they help contribute to a better quality of life for people all over the world.”

GREGORY E. JOHNSON



ICI President and CEO Paul Schott Stevens has a “Frank Talk About the U.S. Deficit” with the cochairs of the National Commission on Fiscal Responsibility and Reform, Alan K. Simpson, former Senator from Wyoming, and Erskine B. Bowles, former White House Chief of Staff.



GMM Chairman Gregory E. Johnson, President and CEO of Franklin Resources, Inc., welcomes attendees to ICI’s 53rd General Membership Meeting.



Peter De Proft, Director General of the European Fund and Asset Management Association (EFAMA) and David W. Powell, Principal of Groom Law Group, Chartered, discuss “Insights from Worldwide Private Pension Systems.”



John Rogers, Chairman and CEO of Ariel Investments, moderates the “Experience Talks” panel, with Eddie C. Brown, President and CEO of Brown Capital Management; G. Staley Cates, President of Longleaf Partners Funds; and Jack Laporte, Vice President of T. Rowe Price Associates.

## ICI EDUCATION FOUNDATION

### Promoting Financial Education in the National Capital Region

“It’s the coolest thing in Finance Park,” one eighth grader says of the new technology installed this year in ICI Education Foundation’s (ICIEF) investment “storefront.” All Fairfax County, Virginia, eighth graders—approximately 15,000 students each year—spend a day at Junior Achievement of Greater Washington Finance Park participating in a personal finance simulation.

A grant to Junior Achievement of Greater Washington in support of Finance Park is one of seven ICIEF grants to advance investor education within the Washington, DC, region. Other grantees include the Arlington County Office of Virginia Cooperative Extension, Fairfax County Public Schools, the SIFMA Foundation, STRIVE DC, UNCF, and the University of Maryland. These grants are supporting teacher training in investment education, investment education at the workplace for those who speak English as a second language, money management skills for job applicants, investment education programs for middle school and high school students, student investment competitions, online financial literacy courses for minority students, and adult investment education through public libraries.

ICIEF launched a new awards program this year to spark greater involvement by Washington, DC, high schools and students in the annual National Financial Capability Challenge, a joint initiative of the U.S. Departments of Treasury and

Education. The Challenge is designed to engage educators in the teaching of personal finance and to increase the financial knowledge and capability of high school-aged youth across the United States. ICIEF presented twelve \$1,000 awards to high-scoring Washington, DC, students and their schools, as well as to DC schools with high student participation rates. Both participation and performance in the Challenge improved significantly in the District of Columbia.

As an advocate for financial education since its formation in 1989, ICIEF builds visibility and goodwill for the Institute and its members, while pursuing programs that do not compete with ICI members’ education activities. The Foundation is a well-known participant in a variety of coalitions, conferences, and initiatives that promote financial education, saving, and investing nationwide. As part of this effort, the Foundation has engaged with many organizations, including the Securities and Exchange Commission, the North American Securities Administrators Association, the Financial Industry Regulatory Authority, the Social Security Administration, and the U.S. Departments of Education, Treasury, and Labor. ICIEF focuses its own programs regionally to maximize its cumulative impact with limited resources.

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ICIEF accepts grant applications continually and reviews them on a quarterly basis. For more information about ICI’s work on financial education, please visit [www.icief.org](http://www.icief.org).

“It’s great to see schools right here in the District making personal finance a priority. I want to applaud ICIEF for encouraging DC teachers and students to take part in the National Financial Capability Challenge, and I congratulate all of the awardees and participants.”

U.S. EDUCATION SECRETARY ARNE DUNCAN



Students from Gonzaga College High School and Theodore Roosevelt High School in Washington, DC receive \$1,000 awards from ICIEF for their performance on the National Financial Capability Challenge, an annual competition sponsored by the U.S. Departments of Education and Treasury. Their schools received matching awards.



Students from Robert Frost Middle School use their shadows to select and explore personal investing topics through motion-capture technology newly installed in ICIEF’s storefront in “Finance Park.” The Finance Park curriculum is a joint initiative of Fairfax County Public Schools and Junior Achievement of Greater Washington.



# Appendices

## APPENDIX A

### Organization and Finances

#### ORGANIZATION

ICI is a 501(c)(6) organization that represents registered investment companies on regulatory, legislative, and securities industry initiatives that affect funds and their shareholders. ICI members include mutual funds, exchange-traded funds, closed-end funds, sponsors of unit investment trusts, and their investment advisers and principal underwriters. The ICI president and staff report to the Institute's Board of Governors, which is responsible for overseeing the business affairs of ICI and determining the Institute's positions on public policy matters (see Appendix B, page 54).

ICI's Board of Governors is composed of 55 members, representing ICI member companies and independent directors of investment companies. Governors are elected annually to staggered three-year terms. The Board is geographically diverse and includes representatives from large and small fund families as well as fund groups sponsored by independent asset managers, broker-dealers, banks, and insurance companies. This broad-based representation helps to ensure that the Institute's policy deliberations consider all segments of the fund industry and all investment company shareholders.

Five committees assist the Board of Governors with various aspects of the Institute's affairs. These five include an Executive Committee—responsible for evaluating policy alternatives and various business matters and making recommendations to the Board of Governors—as well as Audit, Compensation, Investment, and Nominating Committees. Other than the Institute's president, who is a member of the Executive Committee, all members of these committees are Governors. The Board also has appointed a Chairman's Council to administer the Institute's political programs, including the political action committee, ICI PAC (page 44). The Chairman's Council includes eight Governors and the Treasurer of ICI PAC. The Institute's president serves as an *ex officio* member. The Institute employs a staff of 160 (see Appendix E, page 56).

The needs of investment company independent directors are addressed through the Independent Directors Council (Appendix C, page 55). IDC organizes educational programs, keeps directors informed of industry and regulatory developments, and assists in the development and communication of policy positions on key issues for fund boards.

Figure 1

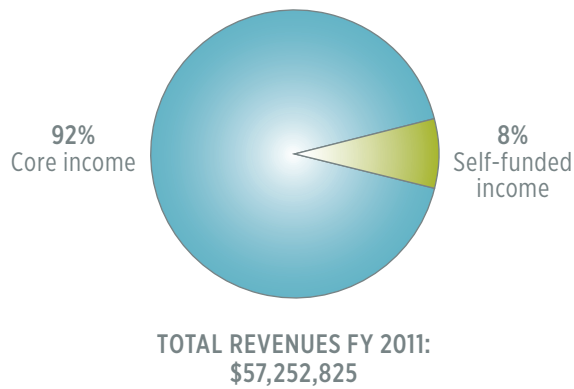
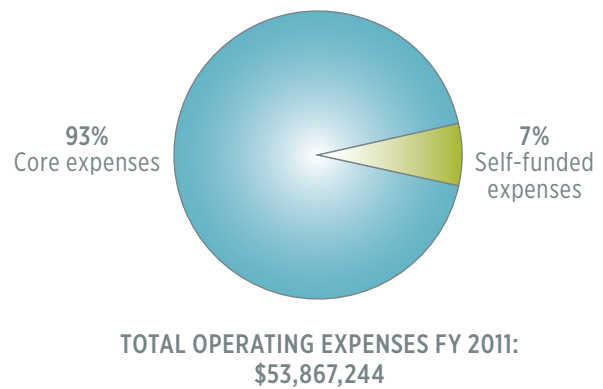


Figure 2



Seventeen standing committees, bringing together more than 1,600 industry professionals, guide the Institute's policy work. ICI standing committees perform a number of important roles, including assisting with formulation of policy positions as well as gathering and disseminating information on industry practices (see Appendix D, page 55). In addition, 27 industry advisory committees, task forces, forums, and working groups with more than 2,000 participants tackle a range of regulatory, operations, and business issues. In all of its activities, ICI strictly observes federal and state antitrust laws, in accordance with a well-established compliance policy and program.

## FINANCES

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

Core activities are related to public policy and include regulatory, legislative, operational, economic research, and public communication initiatives in support of investment companies and their shareholders, directors, and advisers. Reflecting the Institute's strategic focus on issues affecting investment companies, the Board of Governors has chosen to fund core activities with dues rather than seek alternative sources of revenues, such as sales of publications. The significant majority of ICI's total revenues, 92 percent, comes from dues, investment income, royalties, and miscellaneous program sources (see Figure 1). Similarly, by design, 93 percent of the Institute's total resources are devoted to core activities (see Figure 2). Core expenses support the wide range of initiatives described in this report.

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

## ICI UNAUDITED FINANCIAL STATEMENTS

### STATEMENT OF FINANCIAL POSITION

as of September 30, 2011

#### ASSETS

Cash and cash equivalents	\$633,700
Investments, at market value	46,420,527
Accounts receivable	1,093,743
Prepaid expenses	1,290,575
Other assets	786,216
Furniture, equipment, and leasehold improvements; net (less accumulated depreciation of \$8,611,189)	5,816,670
Total assets	<u>\$56,041,431</u>

#### LIABILITIES AND NET ASSETS

##### Liabilities

Payroll and related charges accrued and withheld	22,891,955
Accounts payable and accrued expenses	3,492,523
Deferred revenue	539,272
Rent credit	4,240,344
Deferred rent	<u>2,426,782</u>
Total liabilities	<u>33,590,876</u>

##### Net Assets

Undesignated net assets	21,450,555
Board designated net assets	<u>1,000,000</u>
Total net assets	<u>22,450,555</u>
Total liabilities and net assets	<u>\$56,041,431</u>

### STATEMENT OF ACTIVITIES AND CHANGES IN NET ASSETS

for the year ended September 30, 2011

#### CORE INCOME

Membership dues	\$49,703,384
Investment income	999,368
Royalty income	887,130
Program income	<u>1,290,188</u>
Total core income	<u>52,880,070</u>

#### CORE EXPENSES

Administrative expenses	40,522,708
Program expenses	6,566,387
Depreciation and lobby proxy tax	<u>2,926,450</u>
Total core expenses	<u>50,015,545</u>
Change in net assets—core	<u>2,864,525</u>

#### SELF-FUNDED INCOME

Conferences	3,997,650
Other self-funded income	<u>375,105</u>
Total self-funded income	<u>4,372,755</u>

#### SELF-FUNDED EXPENSES

Conferences	3,690,185
Other self-funded expenses	<u>161,514</u>
Total self-funded expenses	<u>3,851,699</u>

Change in net assets—self-funded	<u>521,056</u>
Change in net assets from operations	3,385,581
Non-operating expenses	198,430
Actuarial pension/postretirement plan loss	<u>5,725,408</u>
Change in net assets	(2,538,257)
Net assets, beginning of year	<u>24,988,812</u>
Net assets, end of year	<u>\$22,450,555</u>

These financial statements are preliminary unaudited statements as of September 30, 2011. Audited financial statements for the fiscal year ended September 30, 2011, will be available after February 1, 2012. To obtain copies of the audited statements, contact Mark Delcoco at 202/326-5974.



## 2011 ICI EXECUTIVE COMMITTEE



SEATED: Mark R. Fetting, John W. McGonigle, Michael S. Scofield, George C. W. Gatch, Jacques P. Perold, Dorothy A. Berry

STANDING: Martin L. Flanagan, James A. McNamara, Mellody Hobson, Gregory E. Johnson, Paul Schott Stevens, Edward C. Bernard, F. William McNabb III, Paul G. Haaga Jr., Robert S. Dow

NOT PICTURED: Lynn L. Anderson, John F. Cogan Jr., Richard S. Davis

“As Chairman of the Institute, I’ve watched ICI’s staff and ICI’s members rally together to serve our investors and, in collaboration with regulators, to help shape policies for the benefit of our nation. Professionals throughout our industry have brought their talents and dedication to bear in a collaborative effort to address the most challenging policy agenda we have faced in decades.”

EDWARD C. BERNARD SERVED AS CHAIRMAN OF THE INVESTMENT COMPANY INSTITUTE FOR FISCAL YEARS 2010 AND 2011, AND IS VICE CHAIRMAN OF T. ROWE PRICE GROUP, INC.

## APPENDIX B

# ICI Board of Governors

as of September 30, 2011

**Edward C. Bernard**<sup>2,3,4,6,7</sup>

ICI Chairman  
Vice Chairman  
T. Rowe Price Group, Inc.

**Martin L. Flanagan**<sup>2,7</sup>

ICI Vice Chairman  
President and CEO  
Invesco, Ltd.

**Lynn L. Anderson**<sup>1,2</sup>

Independent Director  
SSgA Funds

**Ashok N. Bakhru**

Independent Chair  
Goldman Sachs Funds

**Jonathan R. Baum**

Chairman and CEO  
The Dreyfus Corporation

**Dorothy A. Berry**<sup>2,5</sup>

Independent Trustee  
PNC Funds  
Independent Chair  
Professionally Managed Portfolios

**James H. Bodurtha**<sup>3</sup>

Independent Director  
BlackRock Funds

**Mary K. Bush**<sup>1</sup>

Independent Director  
Pioneer Funds

**Marie A. Chandoha**

President and CEO  
Charles Schwab Investment Management, Inc.

**John F. Cogan Jr.**<sup>2</sup>

Chairman  
Pioneer Investment Management USA Inc.

**Michael J. Cosgrove**<sup>1</sup>

President and CEO, Mutual Funds  
GE Asset Management, Inc.

**Patrick P. Coyne**<sup>1</sup>

President  
Delaware Investments

**Bruce L. Crockett**

Independent Chair  
Invesco Funds

**James E. Davey**

President, Hartford Mutual Funds  
The Hartford Financial Services Group, Inc.

**Richard S. Davis**<sup>1,2</sup>

Managing Director  
BlackRock, Inc.

**Anthony W. Deering**<sup>1</sup>

Independent Director  
T. Rowe Price Funds

**Robert S. Dow**<sup>2,4,6</sup>

Senior Partner  
Lord, Abbot & Co. LLC

**Kenneth C. Eich**

Chief Operating Officer  
Davis Selected Advisers, L.P.

**Ralph C. Eucher**

Chairman  
Principal Funds

**Thomas E. Faust Jr.**<sup>4</sup>

Chairman and CEO  
Eaton Vance Corporation

**Mark R. Fetting**<sup>2,6</sup>

Chairman and CEO  
Legg Mason, Inc.

**George C. W. Gatch**<sup>2,3,6</sup>

CEO, JP Morgan Funds  
JPMorgan Asset Management

**C. Gary Gerst**

Independent Chair  
Henderson Global Funds

**William F. Glavin Jr.**

Chairman, President, and CEO  
OppenheimerFunds, Inc.

**Paul G. Haaga Jr.**<sup>2,7</sup>

Chairman  
Capital Research and Management Company

**John T. Hailer**<sup>1</sup>

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

**Peter A. Harbeck**

President and CEO  
SunAmerica Asset Management Corp.

**Brent R. Harris**<sup>1,4,6</sup>

Chairman  
PIMCO Funds

**Diana P. Herrmann**

President and CEO  
Aquila Investment Management LLC

**Melody Hobson**<sup>2,6</sup>

President  
Ariel Investments, LLC

**Gregory E. Johnson**<sup>2,6</sup>

President and CEO  
Franklin Resources, Inc.

**Robert M. Keith**

Executive Managing Director  
AllianceBernstein

**Susan B. Kerley**

Independent Chair  
MainStay Funds  
Independent Director  
Legg Mason Partners Funds

**John Y. Kim**

Chief Executive Officer  
New York Life Investments

**Robert J. Manning**

Chairman and CEO  
MFS Investment Management

**Susan B. McGee**

President and General Counsel  
U.S. Global Investors, Inc.

**John W. McGonigle**<sup>2,6</sup>

Vice Chairman  
Federated Investors, Inc.

**F. William McNabb III**<sup>2</sup>

Chairman and CEO  
Vanguard

**James A. McNamara**<sup>2</sup>

President and CEO  
Goldman Sachs Mutual Funds

**Thomas M. Mistele**

Chief Operating Officer  
Dodge & Cox

**Jacques P. Perold**<sup>1,2</sup>

President  
Fidelity Management & Research Company

**Donald H. Pratt**

Independent Chair  
American Century Funds–Kansas City Board

**Karla M. Rabusch**

President  
Wells Fargo Funds Management, LLC

**J. Alan Reid Jr.**

Chief Executive Officer  
Forward Management LLC

**Robert L. Reynolds**

President and CEO  
Putnam Investments

**Judy Rice**

President  
Prudential Investments

**James E. Ross**

Senior Managing Director and Global Head of ETFs  
State Street Global Advisors

**Thomas S. Schreier Jr.**<sup>1,3</sup>

Vice Chairman, Wealth Management  
Nuveen Investments

**Michael S. Scofield**<sup>2</sup>

Independent Director  
Wells Fargo Advantage Funds

**Michael D. Strohm**<sup>3</sup>

Chief Executive Officer  
Waddell & Reed, Inc.

**Jonathan S. Thomas**<sup>1</sup>

President and CEO  
American Century Investments

**Garrett Thornburg**

Chairman  
Thornburg Investment Management, Inc.

**William F. Truscott**<sup>1,4</sup>

CEO, U.S. Asset Management and President,  
Annuities  
Columbia Management

**Robert W. Uek**

Independent Trustee  
MFS Funds

**Lloyd A. Wennlund**

Executive Vice President and Managing Director  
Northern Trust Global Investments

<sup>1</sup> Governor on sabbatical

<sup>2</sup> Executive Committee

<sup>3</sup> Audit Committee

<sup>4</sup> Investment Committee

<sup>5</sup> Chairman of the Independent Directors Council

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

<sup>7</sup> ICI Education Foundation Board

## APPENDIX C

# Governing Council of the Independent Directors Council

as of September 30, 2011

### **Lynn L. Anderson\***

Independent Director  
SSgA Funds

### **Ashok N. Bakhru\***

Independent Chair  
Goldman Sachs Funds

### **Dorothy A. Berry\***

IDC Chair  
Independent Trustee  
PNC Funds  
Independent Chair  
Professionally Managed Portfolios

### **James H. Bodurtha\***

Independent Director  
BlackRock Funds

### **Robert P. Bremner**

Independent Chair  
Nuveen Funds

### **Mary K. Bush\***

Independent Director  
Pioneer Funds

### **Bruce L. Crockett\***

Independent Chair  
Invesco Funds

### **Diana M. Daniels**

Independent Director  
Goldman Sachs Funds

### **Anthony W. Deering\***

Independent Director  
T. Rowe Price Funds

### **Dennis J. Dirks**

Independent Director  
Fidelity Equity & High Income Group  
of Funds

### **Peter S. Drotch**

Independent Director  
ING Funds

### **Paul K. Freeman**

Independent Chair  
DWS Funds

### **C. Gary Gerst\***

Independent Chair  
Henderson Global Funds

### **Cynthia A. Hargadon**

Independent Director  
PAX World Funds

### **Susan B. Kerley\***

Independent Chair  
MainStay Funds  
Independent Director  
Legg Mason Partners Funds

### **Garry L. Moody**

Independent Director  
AllianceBernstein Funds

### **Joel W. Motley**

Independent Director  
OppenheimerFunds

### **Alfred E. Osborne Jr.**

Independent Director  
FPA Funds

### **Steven J. Paggioli**

Independent Director  
Aston Funds  
Managers Funds  
Professionally Managed Portfolios

### **Donald H. Pratt\***

Independent Chair  
American Century Funds-Kansas  
City Board

### **Richard A. Redeker**

Independent Director  
Prudential Retail Funds

### **Michael S. Scofield\***

Independent Director  
Wells Fargo Advantage Funds

### **Davey S. Scoon**

Independent Chair  
Allianz Funds

### **Laura T. Starks**

Independent Director  
TIAA-CREF Funds

### **Susan M. Sterne**

Independent Director  
Sentinel Funds

### **Virginia L. Stringer**

Independent Director  
Nuveen Funds

### **George Sullivan Jr.**

Independent Director  
SEI Funds

### **Robert W. Uek\***

Independent Trustee  
MFS Funds

### **Ralph F. Verni**

Independent Chair  
Eaton Vance Funds

### **Gary N. Wilner**

Independent Director  
Oakmark Funds

### **Jonathan F. Zeschin**

Independent Chair  
Dividend Capital Funds  
Independent Director  
Matthews Asia Funds

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\*On ICI Board of Governors

## APPENDIX D

# ICI Standing Committees and Chairs

as of September 30, 2011

### **ACCOUNTING/TREASURERS**

#### **Brian W. Wixted**

Senior Vice President and Treasurer  
OppenheimerFunds, Inc.

### **CHIEF COMPLIANCE OFFICER**

#### **Pauline C. Scalvino**

Chief Compliance Officer  
The Vanguard Group, Inc.

### **CLOSED-END INVESTMENT COMPANY**

#### **Keith A. Weller**

Executive Director and Senior Associate  
General Counsel  
UBS Global Asset Management  
(Americas) Inc.

### **ETFs (EXCHANGE-TRADED FUNDS)**

#### **James E. Ross**

Senior Managing Director and Global  
Head of ETFs  
State Street Global Advisors

### **INTERNATIONAL**

#### **Liliane Corzo**

Vice President and Senior Counsel  
Capital Research and Management  
Company

### **INVESTMENT ADVISERS**

Vacant

### **OPERATIONS**

#### **Basil Fox**

President  
Franklin Templeton Investor  
Services LLC

### **PENSION**

#### **Lisa H. Lattan**

Vice President and Associate  
General Counsel  
American Century Investments

### **PUBLIC COMMUNICATIONS**

#### **Mary Athridge**

Director, Corporate Communications  
Legg Mason

### **RESEARCH**

#### **Drew Elder**

Senior Vice President, Product Strategy  
and Development  
Janus Capital Group, Inc.

### **RISK MANAGEMENT**

#### **Joseph A. Carrier**

Chief Risk Officer  
Legg Mason, Inc.

### **SALES FORCE MARKETING**

#### **Peter D. Jones**

President  
Franklin/Templeton Distributors, Inc.

### **SEC RULES**

#### **Amy Doberman**

General Counsel  
ProFund Advisors, LLC

### **SMALL FUNDS**

#### **Susan B. McGee**

President and General Counsel  
U.S. Global Investors, Inc.

### **TAX**

#### **Gwen L. Shaneyfelt**

Senior Vice President, Global Taxation  
Franklin Templeton Investments

### **TECHNOLOGY**

#### **Michael L. Radziemski**

Partner and Chief Information Officer  
Lord, Abnett & Co. LLC

### **UNIT INVESTMENT TRUST**

#### **W. Scott Jardine**

General Counsel  
First Trust Advisors, L.P.

## APPENDIX E

# ICI Staff

### EXECUTIVE OFFICE

**Paul Schott Stevens**<sup>1,2,6</sup>  
President and CEO

**Peter H. Gallary**<sup>3</sup>  
Chief Operating Officer

### GOVERNMENT AFFAIRS

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

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

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

**Allen C. Huffman**  
Director, Retirement Security and Tax Policy

**Netonis E. Wybensing**  
Director, Financial Services

**James R. Hart**  
Political Affairs Officer

### INDEPENDENT DIRECTORS COUNCIL

**Amy B. R. Lancellotta**  
Managing Director

**Annette M. Capretta**  
Deputy Managing Director

**Lisa C. Hamman**  
Associate Counsel

### LAW

**Karrie McMillan**  
General Counsel

**Robert C. Grohowski**  
Senior Counsel, Investment Companies

**Dorothy M. Donohue**  
Senior Associate Counsel

**Rachel H. Graham**  
Senior Associate Counsel

**Tamara K. Salmon**  
Senior Associate Counsel

**Mara L. Shreck**  
Associate Counsel

**Ari Burstein**  
Senior Counsel, Capital Markets

**Jane G. Heinrichs**  
Senior Associate Counsel

**Sarah A. Bessin**  
Senior Counsel, Securities Regulation

**Frances M. Stadler**<sup>4</sup>  
Senior Counsel, Securities Regulation

**Mary S. Podesta**  
Senior Counsel, Pension Regulation

**Elena B. Chism**  
Associate Counsel

**Anna A. Driggs**  
Associate Counsel

**Keith D. Lawson**<sup>5</sup>  
Senior Counsel, Tax Law

**Karen L. Gibian**  
Associate Counsel

**Pinank K. Desai**  
Assistant Counsel

**Susan M. Olson**  
Senior Counsel, International Affairs

**Eva M. Mykolenko**  
Associate Counsel

### OPERATIONS AND CONTINUING EDUCATION

**Donald J. Boteler**  
Vice President, Operations and Continuing Education

**Linda J. Brenner**  
Director, Operations and Continuing Education

**Martin A. Burns**  
Director, Institutional Operations and Service

**Diane E. Butler**  
Director, Transfer Agency and International Operations

**Kathleen C. Joaquin**  
Director, Operations–Distribution and Service

**Peter G. Salmon**  
Director, Operations and Technology

**Gregory M. Smith**  
Director, Operations–Compliance and Fund Accounting

### PUBLIC COMMUNICATIONS

**F. Gregory Ahern**  
Chief Public Communications Officer

**Susan J. Duncan**  
Senior Director, Public Communications  
Vice President, ICI Education Foundation

**Mike McNamee**  
Senior Director, Policy Writing and Editorial

**Jennifer S. Smith**  
Director, Editorial

**Janet M. Zavistovich**  
Senior Director, Communications Design

**Jodi M. Weakland**  
Director, Design

**Ianthé Zabel**  
Senior Director, Media Relations

**Rachel W. McTague**  
Director, Media Relations

**Stephanie M. Ortals-Tibbs**  
Director, Media Relations

### RESEARCH

**Brian K. Reid**  
Chief Economist

**Sarah A. Holden**  
Senior Director, Retirement and Investor Research

**Peter J. Brady**  
Senior Economist

**Sean S. Collins**  
Senior Director, Industry and Financial Analysis

**Rochelle L. Antoniewicz**  
Senior Economist

**L. Christopher Plantier**  
Senior Economist

**Judith A. Steenstra**  
Senior Director, Statistical Research

**Sheila M. McDonald**  
Director, Statistical Research

**Erin H. Short**  
Director, Statistical Research

### ADMINISTRATION

**Christopher E. Boyland**  
Senior Director and Information Technology Officer

**Andrew L. Colb**  
Director, System Operations

**Paul R. Camarata**  
Director, Electronic Data Collection

**Mark A. Delcoco**  
Controller/Treasurer

**Patricia L. Conley**  
Director, Accounting

**Jane A. Forsythe**  
Senior Director, Conferences

**Mary D. Kramer**  
Vice President, Human Resources

**Suzanne N. Rand**  
Director, Human Resources

**Sheila F. Moore**  
Director, Office Services

**Lee D. Butler**  
Director, Information Services

**Sandra J. West**  
Senior Director, Membership

**Michelle M. Kretsch**  
Director, Membership

<sup>1</sup> Executive Committee of ICI's Board of Governors

<sup>2</sup> Chairman's Council (*ex officio*)

<sup>3</sup> Chairman's Council and Treasurer to ICI PAC

<sup>4</sup> Secretary to ICI

<sup>5</sup> Secretary to ICI's Chairman's Council, Assistant Treasurer to ICI PAC, Political Compliance Counsel

<sup>6</sup> ICI Education Foundation Board

## APPENDIX F

# Publications and Releases

### RESEARCH AND POLICY PUBLICATIONS

A complete list of ICI research publications, statistical releases, and policy publications is available on the Institute's website, at [www.ici.org/research](http://www.ici.org/research). Participant-funded studies are not listed.

**Defined Contribution Plan Participants' Activities: First Half 2010, October 2010**

[www.ici.org/pdf/ppr\\_10\\_rec\\_survey-q2.pdf](http://www.ici.org/pdf/ppr_10_rec_survey-q2.pdf)

**Trends in Proxy Voting by Registered Investment Companies, 2007–2009, *Perspective*, November 2010**

[www.ici.org/pdf/per16-01.pdf](http://www.ici.org/pdf/per16-01.pdf)

**A Look at Private-Sector Retirement Income After ERISA, *Perspective*, November 2010**

[www.ici.org/pdf/per16-02.pdf](http://www.ici.org/pdf/per16-02.pdf)

**401(k) Plan Asset Allocation, Account Balances, and Loan Activity in 2009, *Perspective*, November 2010**

[www.ici.org/pdf/per16-03.pdf](http://www.ici.org/pdf/per16-03.pdf)

**The Role of IRAs in U.S. Households' Saving for Retirement, 2010, *Fundamentals*, December 2010**

[www.ici.org/pdf/fm-v19n8.pdf](http://www.ici.org/pdf/fm-v19n8.pdf)

**The IRA Investor Profile: Traditional IRA Investors' Rollover Activity, 2007 and 2008, December 2010**

[www.ici.org/pdf/rpt\\_10\\_ira\\_rollovers.pdf](http://www.ici.org/pdf/rpt_10_ira_rollovers.pdf)

**Commitment to Retirement Security: Investor Attitudes and Actions, January 2011**

[www.ici.org/pdf/ppr\\_11\\_com\\_ret.pdf](http://www.ici.org/pdf/ppr_11_com_ret.pdf)

**Pricing of U.S. Money Market Funds, *ICI Research Report*, January 2011**

[www.ici.org/pdf/ppr\\_11\\_mmf\\_pricing.pdf](http://www.ici.org/pdf/ppr_11_mmf_pricing.pdf)

**Profile of Mutual Fund Shareholders, 2010, *ICI Research Report*, February 2011**

[www.ici.org/pdf/rpt\\_11\\_profiles.pdf](http://www.ici.org/pdf/rpt_11_profiles.pdf)

**The Closed-End Fund Market, 2010, *ICI Research Perspective*, March 2011**

[www.ici.org/pdf/per17-01.pdf](http://www.ici.org/pdf/per17-01.pdf)

**Trends in the Fees and Expenses of Mutual Funds, 2010, *ICI Research Perspective*, March 2011**

[www.ici.org/pdf/per17-02.pdf](http://www.ici.org/pdf/per17-02.pdf)

**Who Gets Retirement Plans and Why: An Update, *ICI Research Perspective*, March 2011**

[www.ici.org/pdf/per17-03.pdf](http://www.ici.org/pdf/per17-03.pdf)

**2011 Investment Company Fact Book, April 2011**

[www.icifactbook.org](http://www.icifactbook.org)

**Defined Contribution Plan Participants' Activities, 2010, *ICI Research Report*, May 2011**

[www.ici.org/pdf/ppr\\_10\\_rec\\_survey-q4.pdf](http://www.ici.org/pdf/ppr_10_rec_survey-q4.pdf)

**The Economics of Providing 401(k) Plans: Services, Fees, and Expenses, 2010, *ICI Research Perspective*, June 2011**

[www.ici.org/pdf/per17-04.pdf](http://www.ici.org/pdf/per17-04.pdf)

**Defined Contribution Plan Participants' Activities, First Quarter 2011, *ICI Research Report*, August 2011**

[www.ici.org/pdf/ppr\\_11\\_rec\\_survey-q1.pdf](http://www.ici.org/pdf/ppr_11_rec_survey-q1.pdf)

**The IRA Investor Profile: Traditional IRA Investors' Asset Allocation, 2007 and 2008, September 2011**

[www.ici.org/pdf/rpt\\_11\\_ira\\_asset.pdf](http://www.ici.org/pdf/rpt_11_ira_asset.pdf)

## JOINT ICI AND IDC PUBLICATIONS

### ***Fund Board Oversight of Risk Management, September 2011***

[www.idc.org/pdf/pub\\_11\\_oversight\\_risk.pdf](http://www.idc.org/pdf/pub_11_oversight_risk.pdf)

### ***Overview of Fund Governance Practices, 1994–2010, September 2011***

[www.idc.org/pdf/pub\\_11\\_fund\\_governance.pdf](http://www.idc.org/pdf/pub_11_fund_governance.pdf)

## STATISTICAL RELEASES

The most recent ICI statistics and an archive of statistical releases are available at [www.ici.org/research#statistics](http://www.ici.org/research#statistics).

To subscribe to ICI's statistical releases, visit [www.ici.org/pdf/stats\\_subs\\_order.pdf](http://www.ici.org/pdf/stats_subs_order.pdf).

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

**Mutual Fund Complex Assets:** A monthly report on long-term mutual fund and money market fund assets under management by complex.

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

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

**Mutual Fund Assets in Retirement Accounts:** A quarterly report that includes individual retirement account and defined contribution plan assets and estimates of net new cash flows to mutual funds from retirement accounts.

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

**Exchange-Traded Funds:** A monthly report on ETF assets, number of funds, issuance, and redemptions of ETFs.

**Unit Investment Trusts:** A monthly report on UIT value and number of deposits of new trusts by type and maturity.

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

**Quarterly Supplemental Mutual Funds:** A quarterly report that includes statistics on mutual fund asset composition, income and capital gain distributions, and number of shareholder accounts.

**Mutual Fund Institutional Report:** An annual report that includes mutual fund assets for various types of institutional shareholders, broken out by broad investment classification.

## APPENDIX G

# ICI and IDC Events

October 25–27, 2010	Investment Company Directors Conference <sup>1</sup>	Chicago, IL
November 10–12, 2010	Small Funds Committee Meeting	San Francisco, CA
November 17, 2010	Closed-End Fund Conference	New York, NY
December 14, 2010	Securities Law Developments Conference <sup>2</sup>	Washington, DC
March 10, 2011	Cost Basis Reporting Workshop	Boston, MA
March 17, 2011	Credit Quality in the Municipal Bond Market	New York, NY
March 27–30, 2011	Mutual Funds and Investment Management Conference <sup>3</sup>	Palm Desert, CA
March 31, 2011	Cost Basis Reporting Workshop	Irvine, CA
May 4–6, 2011	General Membership Meeting	Washington, DC
May 5, 2011	Investment Company Directors Workshop <sup>1</sup>	Washington, DC
May 5–6, 2011	Operations and Technology Conference	Washington, DC
May 5–6, 2011	Mutual Fund Compliance Programs Conference	Washington, DC
May 11, 2011	IRA Research and Policy Summit	Washington, DC
May 16, 2011	Money Market Funds Summit	Washington, DC
August 3, 2011	Independent Counsel Roundtable	Washington, DC
September 11–14, 2011	Tax and Accounting Conference	Phoenix, AZ

<sup>1</sup> Sponsored by IDC

<sup>2</sup> Sponsored by ICI's Education Foundation

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

## APPENDIX H

# ICI Mutual Insurance Company

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



## Leading the Way ON POLICY ISSUES

### **DODD-FRANK WALL STREET REFORM AND CONSUMER PROTECTION ACT (PAGE 8)**

ICI worked to ensure that the myriad rules of the Dodd-Frank Wall Street Reform and Consumer Protection Act do not have harmful or unintended consequences for funds. The Institute, for example, analyzed the legal implications and economic variables that should go into deciding whether a particular firm poses risk to the overall financial system. ICI's analysis underpinned its view that designation as a "systemically important financial institution," or SIFI, by the new Financial Stability Oversight Council is inappropriate for funds—including money market funds—or their advisers.

### **MONEY MARKET FUNDS (PAGE 12)**

Regulators, legislators, and the media examined the important role played by money market funds in the financial system, their possible vulnerabilities in times of severe market stress, and the potential for further reform in the comprehensive rules that govern them. Equipped with data and policy perspective from its membership, ICI stayed at the forefront of the discussion, pressing the case that money market funds work for America and that their fundamental characteristics must be preserved.

### **INTERNATIONAL REGULATION (PAGE 20)**

The development of financial policy has become increasingly global, with a growing range of national and multinational authorities. ICI has continued to build upon its record of legal and economic expertise to serve as a vigorous advocate for funds around the world. On issues ranging from market structure to retirement savings and pension systems, ICI delivered analysis and expertise to inform the global regulatory dialogue on behalf of U.S. funds, their advisers, and their investors.

### **STRENGTH OF THE DEFINED CONTRIBUTION PLAN SYSTEM (PAGE 32)**

Maintaining the strength of the system by which Americans save for retirement in 401(k) plans and individual retirement accounts (IRAs) is vital to providing retirement security. ICI advanced this goal with research showing that Americans have a high level of confidence in the individual account system and that plan participants and IRA savers generally make good investment and distribution choices. The Institute engaged with policymakers in many areas, such as the 401(k) disclosure regime and electronic delivery of required information.

### **MARKET STRUCTURE (PAGE 40)**

Rapid technological changes in the operation of financial markets have ignited debates over how best to structure institutions and mechanisms for trading stocks, bonds, and other securities. In dealing with numerous regulators at home and abroad, ICI's advocacy has been driven by a simple principle: ensuring that markets operate efficiently, transparently, and fairly for the benefit of all market participants, including funds and the 90 million shareholders they serve.

# ICI Action on Select Policy Developments, FISCAL YEAR 2011

## FUND REGULATION

**Rule 12b-1:** Regulators continued work on the July 2010 proposal by the Securities and Exchange Commission (SEC) to replace Rule 12b-1, a rule governing distribution fees used to compensate brokers and pay for account recordkeeping and other services provided to fund investors.

*In a November 2010 comment letter, ICI called the SEC's overhaul "far more extensive and intrusive than necessary." The Institute also conducted its own cost-benefit analysis, which showed that the SEC's analysis understated the likely costs of the proposal's implementation, while overstating its benefits.*

**Rule 4.5:** The Commodity Futures Trading Commission (CFTC) proposed revising Rule 4.5, which provides an exclusion for funds from regulation as "commodity pool operators." Under the proposal, a fund would only be exempt from CFTC regulation if it adheres to trading and marketing restrictions with respect to its positions in commodity futures, commodity options, and swaps.

*ICI made clear in a comment letter, during a roundtable, and in testimony before Congress that the CFTC had failed to demonstrate the need for adding this duplicative and conflicting layer of regulation, one that could affect hundreds, if not thousands, of funds.*

**Whistleblower:** The SEC and the CFTC approved rules establishing programs to monetarily reward individuals who provide regulators with original information about a violation of the federal securities laws.

*ICI strongly opposed the portions of these rules that would undermine funds' internal compliance programs, impose burdensome new reporting obligations, and overwhelm the agencies with insignificant information. Separately, ICI expressed support for legislation that would address ICI's more-serious concerns with these rules.*

**Pay-to-Play:** By mid-September 2011, fund advisers had to comply with the SEC's new rule inhibiting "pay-to-play" practices by investment advisers through restrictions on political contributions to state and local government officials.

*Following the rule's adoption in July 2010, ICI immediately began work to address the immense reporting and recordkeeping challenges produced by the rule. The Institute held monthly conference calls with members, commissioned a legal memorandum on concerns around political giving, and vigorously pursued no-action relief from SEC staff. This relief was granted in September 2011 on the rules' compliance date.*

**State Issues:** The Montana Securities Department moved to increase mutual fund notice filing fees, effective January 2011.

*ICI filed suit challenging the fee increases. The litigation remains pending.*

**Financial Services Regulatory Reform:** See page 8.

**Money Market Funds:** See page 12.

## FINANCIAL MARKETS

**Short Selling:** The SEC and other regulators continued to examine rules relating to short sales, responding to concerns that short selling contributed to market abuses or inefficiencies.

*ICI's comments to the SEC urged caution on public disclosure of short sale information to avoid confusion and front-running of fund trades. ICI also contacted regulators outside the U.S. to express the Institute's support for action to curb abusive short selling but its opposition to outright bans that would deprive markets of short selling's contribution to efficiency and price discovery.*

**Municipal Securities Markets:** Regulators continued to examine and carry out reforms related to improving the operation of the municipal securities markets, particularly regarding transparency and regulatory oversight.

*ICI participated in the Municipal Securities Rulemaking Board's (MSRB) industry roundtable, which focused on ideas for improving disclosure and the implications of a potential repeal of tax exemption for municipal securities. ICI also arranged to have its members participate in periodic calls with the MSRB, to ensure dialogue with the fund industry, and commented on the scope of the SEC's municipal adviser proposal.*

**Volcker Rule:** The Financial Stability Oversight Council (FSOC) requested information on the Volcker Rule, which prohibits a "banking entity" from engaging in proprietary trading.

*ICI raised concerns about potential unintended consequences of the Volcker Rule for funds and their advisers and requested that the FSOC confirm that funds are not within the scope of the term "banking entities" or otherwise subject to the Volcker Rule by virtue of any relationships with banks.*

**Market Structure Issues:** See page 40.

## RETIREMENT

**E-delivery:** The Department of Labor (DOL) requested information on whether to allow employee benefit plans to make greater use of electronic delivery to communicate with participants in employee benefit and retirement plans.

*ICI urged that the DOL allow plans to make e-delivery the default method for communication, citing research from ICI and others on American workers' almost universal online access and routine use of the Internet for financial and plan-related transactions.*

**Target Date Fund Disclosure:** The DOL proposed adding new target date fund disclosure to information that participants receive about plan investments and qualified default investment alternatives, including a graphical illustration of a fund's glide path.

*ICI strongly supported the proposal and recommended a few clarifying changes. The DOL is anticipated to release final rules in November 2011.*

**Fiduciary Status:** The DOL proposed amending its regulation defining the kind of investment advice that triggers a fiduciary duty under the Employee Retirement Income Security Act.

*In comment letters and testimony before the DOL, ICI called for the DOL to narrow the proposal so that commonplace financial market interactions do not create a fiduciary duty. The Institute argued that the DOL should issue a new proposal to ensure that the final rule is clear and workable. In September 2011, the agency announced it would repropose the rule in early 2012.*

**401(k) Fee Litigation:** Federal lawsuits proceeded against large plan sponsors and plan recordkeepers. The suits challenge fees paid to 401(k) plan service providers, including using retail mutual funds in plans.

*ICI filed several friend-of-the-court briefs in support of defendants. The U.S. Courts of Appeals for the Third and Seventh Circuits issued decisions in favor of the plans and recordkeepers. In dismissing its case, the Seventh Circuit opinion incorporates data and arguments from the ICI brief.*

**Strength of the Defined Contribution System:** See page 32.

## TAXES

**Cost Basis Reporting:** Implementing the 2008 law on cost basis reporting, the Treasury Department and the Internal Revenue Service (IRS) issued regulations that would have limited shareholders' options for choosing a cost basis method other than the average cost default method provided by a fund.

*ICI asked Treasury and the IRS to change the regulations so that brokers and funds that choose average cost as their default method may allow their customers to select any other basis method for existing shares until the time of the first redemption from that account. The IRS issued guidance that amended the rules in a manner consistent with ICI's request.*

**FATCA:** Regulators proceeded with implementation of the Foreign Account Tax Compliance Act (FATCA), which aims to curtail U.S. tax evasion through offshore investments.

*ICI, in correspondence with Treasury and the IRS, discussed a range of steps that regulators should take to make FATCA more effective, easier to administer, and less likely to adversely affect ICI members and U.S. capital markets.*

**Tax Treatment of Fund Investors:** See page 18.

## OPERATIONS AND TECHNOLOGY

**Accounting for Transaction Costs:** A May 2010 proposal from the Financial Accounting Standards Board (FASB) would have required funds to characterize portfolio transaction costs as operating expenses, rather than being added to the cost basis of securities purchased and deducted from proceeds of securities sold.

*ICI opposed the proposal, arguing that it would reduce the usefulness of the expense ratio for investors. In June 2011, FASB exempted funds from the proposal.*

**Global Standards:** The SEC took steps toward a possible transition to use of International Financial Reporting Standards (IFRS) by 2016. The SEC's Office of the Chief Accountant released a paper describing an approach for this transition.

*ICI again aired its concerns to the SEC on implications of the transition for funds. Notably, ICI said that applying IFRS to mutual fund financial statements would not yield benefits to fund investors—such as the ability to better compare financial statements of issuers organized in different jurisdictions—that normally would accompany a move to global accounting standards.*

**Social Media:** See page 24.

## FUND AND CORPORATE GOVERNANCE

**Proxy Access:** In a unanimous decision, the U.S. Court of Appeals for the DC Circuit vacated the SEC's 2010 proxy access rule, which would have permitted shareholders to nominate directors on a company's proxy statement. The court found that the SEC failed to adequately consider the rule's effect upon efficiency, competition, and capital formation.

*ICI and IDC filed a joint friends-of-the-court brief in support of the parties challenging the rule. ICI and IDC argued that the proxy access rule as adopted was unsuited to the unique corporate governance structure of fund companies and boards and failed to take into account the significant economic effects of the rule on investment companies. For more, see "Ruling Highlights Need for Robust Economic Analysis," on page 30.*

**Executive Compensation:** Seven federal financial regulators proposed a joint rule restricting incentive-based compensation practices at financial institutions, including investment advisers with at least \$1 billion in assets on their balance sheets.

*While supporting the proposal's principles-based approach, ICI voiced serious concerns that the standards for prohibited conduct are not clear and that statements in the release about the role of risk management and internal control personnel are overly prescriptive.*

**Proxy Vote Disclosure:** The SEC proposed a rule requiring institutional investment managers to report annually how they voted on various executive compensation issues, including "say-on-pay" votes.

*ICI expressed its support for the concept and reiterated its long-standing position that all institutional investors should have the same proxy vote disclosure requirements as mutual funds. However, ICI's comment letter opposed parts of the proposal that would place new requirements on funds alone for more information that would be of little or no use to investors.*

**Proxy Infrastructure:** In July 2010, the SEC undertook a comprehensive review of the proxy voting system.

*ICI's comment on the SEC's review underscored its members' strong interest in a well-functioning and cost-efficient proxy system. To promote cost efficiency, ICI encouraged the SEC to take steps to increase competition related to the distribution of proxy materials. ICI also encouraged the SEC to permit client-directed voting and take other steps to help increase retail shareholder voting participation rates.*

**Risk Management:** See page 28.

## INTERNATIONAL

**Exchange-Traded Funds (ETFs) and Systemic Risk:** The Financial Stability Board (FSB) published a note, "Potential Stability Issues Arising from Recent Trends in Exchange-Traded Funds."

*ICI urged the FSB to use care in describing the perceived risks posed by growth and innovation in the ETF market. The Institute clarified that the primary characteristic of the "synthetic" ETFs described by the FSB as raising concern—i.e., a single swap with an affiliate—is by and large unique to that particular structure and is not reflected in U.S. ETFs registered under the Investment Company Act of 1940.*

**Non-European Union (EU) Funds and Rules for Alternative Investment Funds:** The European Securities and Markets Authority (ESMA) sought advice on drafting recommendations to the European Commission (EC) for implementing the Alternative Investment Fund Managers Directive. The proposed framework seeks to establish a single, stringent regulatory and supervisory framework for alternative investment funds and managers in Europe.

*ICI provided ESMA with input to ensure that rules are appropriately tailored to the structure and circumstances of U.S. investment companies registered under the Investment Company Act. Although highly regulated under U.S. law, these funds are categorized as alternative investment funds under the directive and will be subject to the directive if marketed to EU investors.*

**European Pensions:** The EC published a "Green Paper" to further a continent-wide debate on how to ensure adequate, sustainable, and safe pension systems.

*ICI submitted a letter describing its research concerning the critical role of mutual funds and defined contribution (DC) plans in supplementing retirement income. The letter also stressed that providing meaningful and effective disclosure to both DC plan participants and employers is fundamental to developing and enhancing DC plans.*

**International Regulation:** See page 20.



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