

June 30, 2011

***Current Developments
for Mutual Fund Audit
Committees***
Quarterly summary

Table of contents

PwC articles & observations for the three months ended

June 30, 2011

Current trends in risk management	3
Pricing vendor due diligence	6
Spotlight on complex securities: Swaps	9

Regulatory developments 14

Tax developments

Preparing for the implementation of the RIC Modernization Act	19
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Summary of industry developments for the six months ended 21

June 30, 2011

<i>Publications of interest to mutual fund directors issued during the three years ended June 30, 2011</i>	24
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PwC articles & observations for the three months ended June 30, 2011

Current trends in risk management

The topic of risk management as it relates to a mutual fund's Board of Directors is certainly not new. However, over the past couple of years there has been a renewed and reinvigorated focus on the topic. Simply stated—the world is different now than it was a few years ago in terms of the markets and the swiftness and correlation of risks as well as regulatory and investor expectations. Consequently, a fund's approach to risk management should likewise be different than a few years ago. This article explores some current thoughts and approaches to risk management in the mutual fund arena in the current environment.

What is risk management?

Enterprise risks can be broadly categorized into two areas: financial risks and non-financial risks. Financial risks include investment/portfolio risks, credit/counterparty risks, valuation risks and liquidity risks. Non-financial risks include operational risks, compliance risks, legal risks, financial reporting risks and reputational/franchise risks. Typically, compliance, legal and investment/portfolio risks are the ones management and directors are most familiar with and are often top of mind when the topic of risk management is discussed. Given the nature of the products a Board oversees, a focus on compliance with prospectus and other regulatory requirements as well as on a fund's portfolio is understandable and expected. However, addressing all the key enterprise risks

is critical to a sound risk management framework. In fact, some non-financial risks could have an even larger adverse impact on an organization than poor performance if one thinks about such risks as reputational risk. In a recent webcast on risk management, PwC asked directors what risk is the top concern in their organizations. Reputational or franchise risks received the most responses at 30% with investment/portfolio risk receiving 23% of the responses. Legal and compliance risk received 14% while credit/counterparty risk, operational risk and financial reporting risk each received about 11% of the responses.

Emerging trends in risk management

Certainly, the regulatory climate over the past couple of years has changed significantly and will continue to be a key area of focus going forward. The impact of the Dodd-Frank Wall Street Reform Act (the "Act") is still not completely clear for mutual fund managers but the Act emphasizes changes around disclosure and reporting and registration. Additionally, there is the still recent implementation of the proxy disclosure rules which require Boards of Directors to make enhanced disclosures surrounding risk oversight. All of these factors lead to a heightened awareness of risk management and emphasize the need for a robust risk management framework.

A proactive risk management framework should place more emphasis on new and emerging risks that

could affect an organization. Recent history has proven that risks are now changing swiftly and are sometimes unpredictable; therefore, focusing on historical approaches and information may leave an organization exposed and ill-equipped to handle future risks. A successful risk framework needs to be able to adapt to swiftly changing circumstances and risks as the industry changes. While the traditional approach to risk management tended to focus on investment risk only with a clear emphasis on quantifiable risks, the emerging framework has a more holistic view of the enterprise with a heightened focus on governance and controls. The enterprise wide approach includes privacy, information technology, operational controls, disclosure and transparency and of course, valuation. Further, a sound risk framework must contemplate that not all risks are readily quantifiable. An important point to note is that risk cannot be avoided in an investment organization; risk is a part of doing business in the mutual funds' industry.

Roles & responsibilities

Traditionally, the Chief Financial Officer and/or the Chief Operating Officer were largely accountable for risk in mutual fund companies. However, the existence of a Chief Risk Officer, a dedicated risk manager and/or an independent risk team are becoming more common in the industry. In the PwC webcast mentioned previously, directors were asked, who within their organizations is recognized as being the primary catalyst for their organization's risk management program: 31% responded that this lies with the Chief Compliance Officer while 25% with a risk management committee, 21% with various individuals or relevant business leaders 19% with a Chief Risk Officer and 2% each with the Chief Executive Officer/Chief Operating Officer and Chief Investment Officer. The responses highlight a trend toward establishing a dedicated risk management group.

While the tendency is to look to the risk management department to assume accountability for risk in the organization, the reality is that business managers, risk managers, senior management and the Board all have a role to play in maintaining a "risk aware" organization. Senior management sets the tone at the top in an organization and is responsible for talent management, transparency and compensation. Further, senior management is also responsible for the implementation of risk management programs as well as monitoring and reporting on them. The Board has the duty to understand and ensure the appropriateness of the alignment of the interests of the fund shareholders and those of the advisor. Both senior management and the Board should ensure that the funds and advisor have the proper focus on risk, which includes a clear definition of the risk appetite and the constant monitoring of the risk profile in relation to that appetite. In another question to directors, we asked how the Board has defined its scope of responsibility as it relates to the organization's risk management program: 32% responded that it is currently unclear and still evolving. 24% noted that the scope only includes those activities impacting the operations of the mutual funds while another 24% responded the scope is enterprise wide and takes into consideration all lines of business of the organization as a whole. Finally, 20% responded they are taking a broader view by taking into consideration the firm's total asset management business.

Alignment of risk framework with fiduciary role of the Board

Regardless of how the roles and responsibilities are defined at an organization, it is important to align the risk management framework with the role of the Board.

A sound risk framework process ideally includes:

- An alignment of risk appetite, strategy and asset allocation,
- Risk identification and assessment,
- Risk measurement and analysis,
- Risk mitigation, control and monitoring,
- Reporting and performance measurement,
- Periodic review.

If a sound framework is in place, the following principles can help directors as they fulfill their fiduciary roles surrounding risk management:

- Fully understand the risk management practices, have a process to periodically validate those practices and, where necessary, challenge management on their sufficiency.
- Consider all relevant conflicts of interest in risk oversight reporting and related risks and risk management of the funds.
- Appropriately document the process the Board undertakes to evidence the extent and timeliness of its involvement in and responses to risk oversight matters.
- Be definitive and articulate the tone and expectations for risk management practices. Conversely, management should be able to clearly articulate to the Board emerging trends in risks.
- Ensure that the Board understands fully all material risks and the extent of its role in risk oversight.
- Ensure that risks identified include those related to sub-advisors, custodians and other third party service providers, as appropriate.

- Consider relevant trends within the industry to determine their impact, if any, from such trends on the risk profile and related risk management practices.
- Determine the adequacy and sufficiency of the Board's risk oversight practices through periodic self-assessment reviews, independent assessments or peer group comparisons and amend practices to the extent necessary.
- Consider the quality, independence and completeness of management's risk oversight reporting to the Board.

A key lesson learned from the recent financial crisis is that the risk management process should be dynamic and change when appropriate to respond to a changing environment. Certainly, there are no "silver bullets" in terms of risk management design, methodology, or technology. However, common aspects of firms with effective risk organizations include change agility, a focus on emerging risks, a focus on continuous improvement, and, of course, accountability. The structure of the risk management function and the role of risk management related to oversight of risks varies among organizations. Of utmost importance is to strike an appropriate balance amongst three factors:

1. Communication between the Board and management around risks and how the firm should be assessing risk,
2. The quantity versus quality of information provided to the Board to understand the risk environment,
3. And the need to balance the role of the Board and management.

Overall, the focus should be on those risks that are most impactful to an organization, its business operations, and asset classes.

Pricing vendor due diligence

This article focuses on key considerations for Boards of Directors within the valuation operations control environment with an emphasis on pricing vendor due diligence. Discussions with more than 25 entities regarding operational controls over pricing revealed that every entity had a common control framework. The following diagram depicts a controls framework specific to pricing and valuation operations.



Starting at the top of the diagram, one element of the overall control environment is the due diligence performed by management over the information provided by third-party pricing vendors. The use of third-party pricing vendor information is common practice, especially in the SEC registered fund environment. The information includes prices received from vendors on a daily basis either to be used as a primary or secondary source in the calculation of the end of day or end

of month net asset value. It also may include other market information such as foreign exchange rates, primary or principal exchange, trading volume, fair value factors for international equity securities, coupon and maturity dates for bonds, and identifier information such as the CUSIP. There are four to six major vendors who cover a wide spectrum of asset classes such as exchange-traded equity securities, fixed-income instruments including term loans, and exchange-traded futures and options. Numerous niche providers that specialize in derivative instruments and less liquid securities, such as asset-backed securities, also are available. At this time, no third-party pricing vendor has a SAS 70 report to provide controls reliance assurance over the actual valuations delivered to clients. Therefore, it's critical that fund management develop controls over the information provided by these vendors. In addition, there has been recent heightened regulatory focus on the information provided by the third-party vendors as well as both management's and external auditors' understanding of the methods, inputs, and assumptions used in the development of a valuation for non-exchange-traded securities.

Due diligence reviews are essential components of the oversight and control over information received and relied upon by management. Due diligence review practices vary from company to company but generally consist of annual visits to the vendor, monthly or quarterly calls with the vendor, and the price challenge process. The participants in these meetings and calls

with the vendors vary but commonly include the pricing operations group personnel, treasurer's group personnel, and members of the portfolio management team, depending on the particular focus areas for discussion with the vendor. The objective of the due diligence reviews is twofold. First, it establishes a basis to evaluate whether the services provided by the vendor are in accordance to the quantity, quality, and specific services agreed to in the contract. Second, it provides a vehicle for understanding the control environment employed by the vendor and also the methods, assumptions, inputs, and models employed by the vendor in providing prices most commonly associated with "evaluated" prices.

Management should discuss with the Board its process for due diligence and vendor oversight. The results and findings of due diligence visits should also be reported to the Board. Management should have controls in place over valuation that assist in assessing the accuracy of vendor pricing. These controls and the results of the procedures should also be discussed and periodically reported to the Board.

The following questions may be asked of management to address the oversight process and controls over services provided.

- What is the level of "on time" delivery of prices from the respective vendor?
- What is the level of price changes received after delivery?
- What is the level of "dropped" prices (meaning that the vendor no longer provides a price for a security)?
- What is the coverage by asset type?
- How often does a price challenge result in a price change going forward?
- What is the response time to our price challenges?
- What is the level of quality associated with the vendor's response?
- How do the coverage, availability, and price points compare between vendors?

These questions may be asked of management to address the oversight over understanding the pricing and other data points provided by the vendor.

- Does the vendor have a SAS 70 or other type of controls reliance report on any aspect of its environment?
 - If so, were there any exceptions noted in the report and if so in what areas?
 - What is management's understanding of the controls at the vendor and how is that documented and evaluated?
 - Has management reviewed the individual pricing methodology documents for each asset class subscribed to?
 - Does management understand, for any fixed income securities, what the major inputs and assumptions are based upon?
 - Where the vendor price is based upon a model, has management understood the model and determined whether that approach is reasonable for that particular asset type?
 - Has management "back tested" prices to actual trades on a periodic basis? What do the results of this testing demonstrate?
 - How frequently is management presenting price challenges to the vendor?
 - What is the trigger for sending a price challenge to a vendor? Is that trigger reasonable based upon the current market environment?
- What are the results, if applicable, of the comparison between the primary and secondary source for the same security?
 - Is an annual on-site due diligence review conducted at the pricing vendor?
 - If so, who attends?
 - What is the level of involvement from the trading or portfolio management side of the organization?
 - If the complex uses subadvisers, are the subadvisers conducting the due diligence reviews? Does management attend those reviews?
 - What documentation is maintained of these visits, questions asked, and responses from vendors?
 - Were any "deep dives" requested of the vendor during the year?
 - Are the prices from the vendor trended day over day to highlight potential changes in the methodology employed by the vendor?
 - What is the level of pricing related NAV errors by vendor?
 - What is the level of single source securities?
 - What other transparency about the prices or other data points is the vendor providing to management?

Spotlight on complex securities: Swaps

Given the fallout of the financial crisis, complex investments and their related risks have been at the forefront of both management's and directors' minds. Further, the current emphasis around risk management has directors wondering if they are asking the right questions about complex investments. The balance between management's role and the directors' role seems to become ever more blurred as the current regulatory landscape seems to be calling directors to have a deeper, more thorough understanding of the risks associated with a fund's investments. This article delves into swaps with an emphasis on what directors need to know.

What is a swap?

A swap, by definition, is a simple concept: It is an agreement between two or more parties to exchange cash flows or payment streams over a period of time. Because swaps typically are not traded on an exchange, they are referred to as over-the-counter, or OTC. Recently, however, there have been some exchange-cleared swaps. The key document that governs most swap agreements is based upon a Master Agreement created by the International Swaps and Derivatives Association (ISDA) in 1992, and subsequently amended in 2002. Typically, a Master Agreement is created between the derivatives dealer/broker and the counterparty and details the standard terms that apply to all transactions entered into between the two parties.

The Master Agreement includes, among other things, a schedule, which allows customization of some terms between the two parties, and Confirmations, which highlight the terms (e.g., rates and dates) of any specific transactions entered into that fall under the Master Agreement. Once the Master Agreement is set up, each transaction has its own Confirmation to document the terms specific to that transaction.

One of the key components of most Master Agreements is the permissibility of netting. The counterparties are allowed to exchange one payment stream based upon the net amount due from one party to the other. The ability to net payments makes the contract operationally simple to execute.

Types of swaps

The most commonly used types of swaps in mutual funds are interest rate swaps, credit default swaps, and total return swaps.

Interest rate swap: Agreement between counterparties to exchange net cash flows based on the difference between two interest rates, applied to a notional principal amount for a specified period. The most common interest rate swap involves trading a floating rate of interest for a fixed rate, or vice versa.

Credit default swap: Agreement between counterparties where the seller agrees, for an upfront or continuing premium or fee (or some combination of both), to compensate the buyer upon the occurrence of a specified credit event on the referenced bond

(i.e., the underlying security upon which the contract is based), such as default or downgrading of the obligor. Credit default swaps can be written on a single fixed-income instrument (called a “single-name” swap) or on a “basket” of fixed-income instruments (often based on a fixed-income index, but sometimes a tailored portfolio). Credit default swaps are often explained as one party selling insurance and the other party buying insurance against the default of the referenced entity.

Total return swap: Agreement between counterparties in which one party makes payments based upon an agreed interest rate (fixed or variable) on a notional amount while the other party makes payments based upon the return, including dividends, of a specific security or a basket of securities or commodities. Such returns could also be tied to the return of a particular index.

Why do portfolio managers invest in swaps?

Portfolio managers employ swaps as a part of the investment strategy of a fund for a variety of reasons, including speculation, arbitrage, lower cost market exposure, diversification, hedging, insurance, and to manage duration.

For example, a portfolio manager may seek to hedge against declining interest rates by entering into an interest rate swap whereby the fund receives payments based on a fixed interest rate and makes payments based on a floating interest rate. The fund would not have to enter into transactions to sell off its variable interest rate holdings, which could potentially generate unwanted gains or losses in the portfolio, and then purchase fixed interest rate securities.

As it relates to credit default swaps, a portfolio manager may want to hedge against the potential default on a bond in a fund’s portfolio by entering into a swap contract as a buyer of protection against such default. Further, credit default swaps are traded on an unfunded basis, which allows a manager to leverage the exposure to a specific issuer. Trading on an unfunded basis

can also quickly and efficiently add or reduce credit exposure to a single issuer or index without having to buy or sell large amounts of bonds in the secondary (cash) market.

For a total return swap, the party receiving the return of the specific security or basket of securities derives the economic benefit of owning the security or securities without actually purchasing the securities and incurring transaction costs from the broker. Typically, entering into a total return swap requires less cash at the onset than purchasing the actual securities the return is based upon. A fund may choose to write a total return swap on particular positions held by the fund where the portfolio manager wants to “time out” of the market for a period, for example in a specific industry.

Overall, through interest rate swaps, credit default swaps, and total return swaps, as this discussion highlights, various investment strategies can be achieved as a fund gains or reduces exposure to the returns or payment streams of specific securities without actually owning or selling them.

What are the risks of investing in swaps?

While there is much to be said for the advantages discussed previously of investing in swaps, those advantages also come with a variety of risks. As directors, understanding the portfolio manager’s strategy with respect to utilizing swap agreements in a fund involves not just understanding what types of swaps are in a fund, but also what risks are involved with those particular agreements and what management does to mitigate and manage those risks.

Valuation: Valuation of swaps may be more challenging than the valuation of other holdings in a fund. There may be a lack of readily available sources from which to obtain prices for the swaps. Therefore, it is important to understand how swaps are valued. Quite simply, a swap’s value is intended to represent the net present value of anticipated

future cash flows arising from the agreement. Funds may value swaps by using standard models, broker quotes, or internal tailored fair valuation models. Each valuation method comes with its own set of risks that must be addressed. For example, if standard models are used, correct inputs must be used. This can be complex, particularly for certain long-term interest rate swaps where “swap curves” (i.e., term structures of interest rates) may not be easily observable at all maturities. If broker quotes are used, it is important to understand how many brokers are supplying quotes and the process for determining the “best” value if multiple brokers supply quotes. If internal models are used, it is important that not only the inputs but the assumptions embedded in the model are correct, as well as that the model has been properly constructed and is free of logical error. Simple programming errors can result in significant misvaluations. Further, it is critical that the individuals in the organization responsible for the model valuation have the requisite knowledge to perform this function.

Directors clearly look to management to perform the day-to-day valuation. Directors therefore should understand how swaps are valued, who is performing the valuation (i.e., outsourced or internal model), and what procedures management has in place to assess whether the valuation is appropriate. Discussions with management should explain the valuation process and also highlight where the swaps fall in the US GAAP fair valuation hierarchy (i.e., Level 1, 2, or 3). If they fall in Level 2 or 3 (which typically they would), the complexity increases. Of particular importance is that directors should discuss with

management the appropriate process for issue escalation in a timely manner respective to valuation. Swap valuation reporting should be at least as rigorous as the reporting for nonderivative investments and, if necessary, more detailed and more frequent.

Accounting: Accounting for swaps may require some manual processing. Given the customized nature of swap contracts, manual accounting is not uncommon and spreadsheets are often used. Some accounting systems are designed to handle certain types of swaps better than others. In some circumstances, workarounds are employed within the accounting system to enter the swaps into the accounting records, with reclassifications necessary in order to perform financial reporting or certain Subchapter M taxable income calculations. Under US GAAP, swap payments are recognized as realized gains and losses to the fund, not as investment income or expense. In any situation involving manual entries, clearly the risk of error increases. Management should explain to directors the controls in place over accounting for swaps, with likely more detail provided if the process is manual. Directors may wish to establish a periodic reporting process with management related to the frequency of errors. Additionally, with manual controls, it is important to understand management’s process for ensuring segregation of duties is in place.

Counterparty credit risk: Counterparty risk is the risk that the counterparty the fund entered into the swap agreement with may not uphold its obligation. Therefore, it is important to understand what management will do to assess the creditworthiness of the counterparties—

not just when a contract is entered into, but on an ongoing basis. While this may sound evident, management should truly understand which specific legal entity is counterparty to the contract. For example, many investment banks and intermediaries trade swaps in financial centers worldwide, and a swap entered into with a US subsidiary of an investment bank may come under a completely different legal regime than the same swap negotiated with its UK subsidiary. Management may determine that counterparty risk would be better managed if multiple counterparties were used. Collateral arrangements are also key to helping mitigate counterparty credit risk. Based on the level of counterparty risk, management should assess and monitor collateral balances. Further, management should apprise directors as to internal and external legal counsel's involvement in negotiating any contracts with counterparties.

Liquidity risk: Liquidity risk is the risk that the fund may not be able to sell securities to meet redemption requests or otherwise raise cash when needed if the investments held are considered illiquid. Depending on the type and volume of swaps in a portfolio and their liquidity, the fund may be required on short notice to post significant amounts of cash collateral to cover adverse price movements. Management could stress test the portfolio periodically and report results to the directors. The Investment Company Act of 1940 also provides for a maximum amount of illiquid holdings, which helps to reduce the liquidity risk to some extent.

Market risk: Market risk is the risk that changes in market conditions can result in the swaps not meeting their specified objective. Additionally, some swaps may involve movements in valuation similar to short sales where there could be no cap on the potential liability incurred by the fund. For example, if a fund writes a total return swap, to the extent the reference entities rise in value, a fund's liability increases. The financial crisis of 2007–2008 clearly showed that market risk cannot be overlooked. Market risk not only impacts the value of the derivatives but also increases the risk that collateral pledged may not be recovered. Management should discuss with directors the monitoring procedures in place to assess the potential impact of both negative and positive market movements on the portfolio as well as on the overall investment strategy. Similar to liquidity risk, management could potentially perform stress testing and report the results periodically.

Tax matters

One of the most critical aspects of investing in swaps is understanding the impact on RIC qualification. In terms of asset diversification, it is important to identify who the issuer is and what the value is for purposes of the test. Additionally, a determination is needed regarding whether the swap produces qualifying income. The IRS has ruled that commodity swaps produce nonqualifying income; most other swaps likely produce qualifying income. To properly assess qualifying income, it is essential to understand the terms of the swap, its relation to the fund's investment objectives, and the counterparty.

The swap market is constantly evolving and the tax law surrounding swaps is evolving as well. Management should have rigorous procedures in place to ensure the RIC qualification assessments and taxable income calculations treat swaps properly, and should certainly keep directors abreast of changes in the rules and regulations.

Pending regulations

As a result of the market turmoil of 2008, swaps—in particular, credit default swaps—have received much attention. At this point, the financial industry is waiting for rules and regulations that will come from the implementation of the Dodd-Frank Wall Street Reform and Consumer Protection Act. Among other matters, new rules and regulations should clarify what entities are considered major swap participants, swap dealers, and

the process for mandatory clearing of swaps. In recent weeks, the CFTC and SEC acknowledged that they would not meet Dodd-Frank's statutory deadline for implementing new rules and have delayed the effectiveness of most provisions until the end of 2011. Therefore, at this point the impact that any of these rulings will have on funds employing swaps in their investment strategy is unclear.

There are many more types of swaps to discuss, as well as more depth to each area highlighted in this article. However, the points above should arm directors with enough background and considerations to hold thoughtful discussions with management that will allow the conversation to hone in on the key aspects of swaps that directors should understand within their organizations.

Regulatory developments

Perhaps the most important development for mutual funds during the second quarter was the United States Supreme Court's decision in *Janus Capital Group, Inc. vs. First Derivative Traders*, which held that an adviser could not be held liable under Rule 10b-5 of the Securities Exchange Act of 1934 for statements made in a fund's prospectuses. This regulatory update summarizes this court decision, briefly discusses recent rules adopted by the US Securities and Exchange Commission (SEC) and US Commodities Futures Trading Commission (CFTC), provides an update on the SEC's focus on 12b-1 fees, and highlights recent discussions of money market fund reform.

Supreme Court ruling on Rule 10b-5 liability

On June 13, 2011, the Supreme Court ruled in a 5-4 decision, *Janus Capital Group, Inc. vs. First Derivative Traders*, that an adviser could not be held liable under Rule 10b-5 of the Securities Exchange Act of 1934 (Exchange Act) for statements made in a fund's prospectuses. The court held that because the fund, and not the adviser, made the allegedly false statements, the adviser and the adviser's parent company cannot be held liable in a private action under Rule 10b-5.

Respondent First Derivative Traders (First Derivative), representing a class of stockholders in petitioner Janus Capital Group, Inc. (JCG), filed a private action under Rule 10b-5 alleging that JCG and

its wholly owned subsidiary, petitioner Janus Capital Management LLC (JCM), made false statements with regard to its market timing practices in mutual fund prospectuses filed by Janus Investment Fund, for which JCM was the investment adviser and administrator, and that those statements affected the price of JCG's stock. The District Court dismissed the case for failure to state a claim. The Fourth Circuit Court of Appeals reversed, finding that First Derivative had sufficiently alleged that JCG and JCM had been involved in the writing and preparation of the prospectuses and thus had made the allegedly false statements.

The Supreme Court reversed. Justice Clarence Thomas, writing for the majority, held that for JCG to be held liable under Rule 10b-5, it must have "made the statement." According to the court, "[f]or purposes of Rule 10b-5, the maker of a statement is the person or entity with ultimate authority over the statement, including its content and whether and how to communicate it." While JCM may have assisted in preparing the fund's prospectuses, the court found that the fund, a legally separate entity with an independent Board of trustees, had "made" the statements for purposes of Rule 10b-5, as it had ultimate control over the prospectuses, not JCM, and there was no basis to find that a person influencing another to "make" a statement should cause the statement to be attributed under the law to that person.

SEC to refocus on 12b-1 Rule proposal

On April 30, 2011, the *Wall Street Journal* reported on remarks made by SEC Commissioner Elisse Walter before a mutual fund industry conference. According to the article, Ms. Walter stated that the SEC would move ahead as soon as this summer with its rule proposal to cap 12b-1 fees.

The proposal, issued in July 2010, would replace Rule 12b-1, which permits registered mutual funds to use fund assets to pay for the cost of promoting sales of fund shares. Unlike the current Rule 12b-1 framework, the proposed rules would limit the cumulative sales charges each investor pays, no matter how they are imposed. The rule would continue to allow funds to bear promotional costs within certain limits, and would also preserve the ability of funds to provide investors with alternatives for paying sales charges (e.g., at the time of purchase, at the time of redemption, or through a continuing fee charged to fund assets).

The SEC also proposes to require mutual funds to provide clearer disclosure about all sales charges in fund prospectuses, annual and semiannual reports to shareholders, and investor confirmation statements.

However, on June 27, Douglas Scheidt, chief counsel in the SEC Division of Investment Management, speaking at a regulatory conference, did not go so far as to state that a replacement to Rule 12b-1 would be issued by the end of 2011. He noted that there were “strong reactions” to the SEC’s proposals, but that the staff would “make progress” on reform later in the year.

SEC adopts final rules establishing a whistleblower program

On May 25, 2011, the SEC adopted final rules to implement a whistleblower program as established by the Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd-Frank Act). The whistleblower program requires the SEC to pay awards to eligible whistleblowers who voluntarily provide the agency with original information about a violation of federal securities laws that leads to a successful enforcement action in which the SEC obtains monetary sanctions totaling more than \$1 million.

Of note, the final rules do not require a whistleblower to first report information internally to an entity’s compliance program before reporting to the SEC in order to qualify for an award. To address industry concerns that internal corporate compliance programs would only survive with a mandatory reporting requirement, the SEC included several provisions in the final rule that it believes will encourage whistleblowers to first report internally:

- *Lookback period.* The final rules provide that a whistleblower who reports a possible violation internally may report it to the SEC within 120 days and still be treated as if he or she reported to the SEC at the earlier reporting date.
- *Credit for cooperating with compliance.* In determining the amount of an award to a whistleblower, the final rules provide that the SEC may consider a whistleblower’s voluntary participation in a company’s internal compliance as a factor in increasing the amount of an award. On the other hand, a whistleblower’s interference with a company’s compliance program may decrease the amount of an award.

- *Bundling with company report.* A whistleblower who first reports information to his or her company's internal compliance program may be eligible for an award if the company then reports the information to the SEC and the information leads to a successful action. Under this provision, all information submitted by the company will be attributed to the whistleblower even if he or she did not report it to the SEC.

SEC adopts amendments to the pay-to-play rule

On June 22, 2011, the SEC amended the pay-to-play rule as part of its adoption of rules and amendments that implement key provisions of Title IV of the Dodd-Frank Act. The new rules will require, among other things, advisers to hedge funds and other private funds to register with the SEC, establish new exemptions from SEC registration and reporting requirements for certain advisers, and reallocate regulatory responsibility for advisers between the SEC and the states.

The SEC's amendments to the pay-to-play rule address certain consequences arising from the Dodd-Frank Act's amendments to the Investment Advisers Act of 1940 and the Exchange Act. First, the SEC amended the scope of the existing pay-to-play rule so that it applies to exempt reporting advisers and foreign private advisers. The amendments also add municipal advisers (referred to in the rule as "regulated persons") to the categories of registered entities excepted from the rule's prohibition on advisers paying third parties to solicit government entities. Under the amendment, an adviser will be permitted to pay a registered municipal adviser to act as a placement agent to solicit government entities on its behalf, if the municipal adviser is subject to a pay-to-play rule adopted by the Municipal Securities Rulemaking Board (MSRB) that is at least as stringent as and consistent with the objectives of the investment adviser pay-to-play rule.

The SEC also extended the date by which advisers must comply with the ban on third-party solicitation from September 13, 2011, to June 13, 2012, to allow time for the MSRB and FINRA to adopt pay-to-play rules if they choose to do so, and give third-party solicitors additional time to come into compliance with the rules.

SEC holds money market roundtable

On May 10, 2011, the SEC held a money market roundtable with government and industry participants to discuss the potential for money market funds to pose a systemic risk to broader financial markets and possible options for further regulatory reform.

The panel discussed several regulatory options and their implications, but focused a substantial part of its discussion on a proposal that would require money market funds to abandon a fixed \$1 share price and instead adopt a floating net asset value ("NAV"). Some panelists opined that money market funds with a floating NAV would not be any more stable, and argued that the funds would still be susceptible to runs in times of market crisis. Others expressed the view that the implementation of a floating NAV would lead to a migration of the money currently invested in money market funds to banks or unregulated structures, and thus lead to a loss of transparency. At least one panelist expressed support for a floating NAV, stating that it would provide incentive for money market fund shareholders to remain invested with the fund.

In support of retaining a stable NAV, panelists argued that such a stable value is important to the safety of investor assets, and that the current money market structure and governance relating to NAV calculation provides transparency to investors.

US House Financial Services Subcommittee holds hearing titled “Oversight of the Mutual Fund Industry: Ensuring Market Stability and Investor Confidence”

On June 24, 2011, the US House Financial Services Subcommittee on Capital Markets and Government-Sponsored Enterprises held a hearing to discuss issues impacting the mutual fund industry, including a focus on different regulatory proposals relating to money market funds. Witnesses included representatives of the Investment Company Institute, Fidelity Management and Research Company, and the Vanguard Group, among others.

In his opening remarks, Subcommittee Chairman Scott Garrett (R-NJ) seemed to signal a lack of Republican support for a floating NAV proposal for money market funds. In particular, Chairman Garrett stated that he is “not convinced that ‘floating the NAV’ is the proper ... [means by which] to address the perception by some that money markets represent a systemic risk.” He also voiced his concerns about the impact a floating NAV would have on investors and on the broader economy.

In addition, Chairman Garrett stated that while he understood “some level of concern about money market funds... [he] can’t ignore concerns about banks.” In his view, banks would be the likely recipients of money currently invested in money market funds if a floating NAV is instituted.

CFTC adopts final rule providing relief to commodity pool operators of commodity ETFs from certain disclosure, reporting, and recordkeeping obligations

On May 18, 2011, the CFTC published in the Federal Register a final rule adopting amendments to its regulations that provide relief from certain disclosure, recordkeeping, and reporting requirements for commodity pool operators (CPOs) of commodity pools with units of participation listed on a national securities exchange (commodity ETFs). Under the rule, which codifies a series of recent no-action letters, commodity ETFs are exempt from the disclosure document and account statement delivery requirements, provided that they make the information readily accessible on their websites and provide the website URL to pool participants. A commodity ETF also can claim an exemption from books and records requirements provided that such records are maintained by the pool’s administrator, distributor, or custodian; or bank or broker-dealer; and it files a notice with the National Futures Association setting forth the contact information of the person(s) who will be keeping the required books and records.

The rules also provide an exemption from CPO registration for independent directors or trustees of actively managed commodity pools. Under the rule, a director or trustee of a pool whose operator is registered as a CPO is eligible to claim relief from registration if the person, among other things, has no power or authority to manage or control the operations or activities of the pool, and the CPO would be liable for any of that person’s violations of the Commodities Exchange Act or the CFTC’s regulations while serving as a director or trustee.

The rule became effective June 17, 2011.

CFTC and SEC propose temporary relief from Title VII requirements for swaps and security-based swaps

The CFTC and SEC have offered relief from Title VII requirements of the Dodd-Frank Act that would apply to swaps and security-based swap (SBS) transactions and to swap/SBS market participants as of July 16, 2011. Both agencies are granting exemptive relief directed at provisions that would, absent agency action, apply to swaps or SBS activities and market participants. The CFTC plans a December 31, 2011, expiration date for its relief, while the SEC exemption does not expire on a specific date.

This targeted relief would not apply to all Title VII provisions, including provisions that are not automatically effective on July 16, that relate to anti-fraud or anti-manipulation, or that do not apply to swaps or SBS. The goal of both regulatory actions is to permit swap and SBS markets to continue to operate largely on a business-as-usual basis even with Title VII provisions in effect, until final derivatives regulations are in place and compliance is phased in.

As expected, the second quarter of 2011 was certainly not quiet on the regulatory front. Continuing to look ahead, the finalizing of the potential changes to the 12b-1 rules and of course any changes to the current money market stable NAV are of particular importance to the mutual fund industry. While much is unknown as the regulatory landscape continues to unfold, not all changes are worrisome, as evidenced by the CPO relief granted to ETFs for certain disclosure, reporting, and recordkeeping requirements, as well as the Supreme Court ruling in *Janus Capital Group, Inc. vs. First Derivative Traders*.

Tax developments

Preparing for the implementation of the RIC Modernization Act

Key developments

The Regulated Investment Company Modernization Act of 2010 (the Act) reflects the most significant tax changes to affect regulated investment companies (RICs or funds) since the Tax Reform Act of 1986. Implementing the Act's 17 provisions will require changes to various RIC tax processes, including the excise and fiscal income distribution calculations. A RIC's management and tax service providers will need to understand how these processes are impacted and take necessary steps to update them. For example, it will be necessary to modify the fiscal and excise distribution calculation templates and affected policies and procedures supporting these calculations. For most funds, these changes will need to be completed no later than November 1, 2011, as the Act's changes impacting excise distribution calculations are effective for 2011. Fiscal taxable income calculations are effective for fund years beginning after December 22, 2010.

Why it's important

RIC management teams and tax service providers have a limited amount of time to understand and implement changes required under the Act. The key objective of the implementation process should be the accurate update of templates, policies, and procedures that support RIC tax processes. A RIC's management team should consider adopting an implementation plan to ensure the timely completion of this

important project. Failure to do so could adversely impact a fund's compliance with the fiscal and excise distribution requirements and shareholder reporting obligations.

A RIC Modernization Act implementation plan should start with establishing a diverse implementation team. In most cases a RIC's tax service preparer(s) will have primary responsibility for the implementation. However, it may be appropriate for other parties, such as fund reporting and shareholder reporting, to participate on the implementation team as well. For service providers that rely heavily on computer applications to perform RIC tax processes, technology staff will also be critical members of the team. Key elements of the implementation team's plan may include:

- Establishing a deadline driven plan

As mentioned earlier, there is a limited amount of time to modify RIC tax processes to implement the Act. The plan needs to provide sufficient time, prior to November 1, 2011, for analysis of law changes, modification and testing of policies and procedures, and training for staff and other parties.

- Understanding the law

Prior to modifying policies, procedures, and templates, the implementation team will need to have a deep understanding of the Act. Inaccurate modifications of the impacted RIC processes could occur if detailed aspects of the law are

not well understood. It is important to note that some changes, such as those that were intended to improve coordination between the excise and fiscal distribution requirements, are very complex and will require a careful analysis to understand their impact. The team will also need to understand and keep abreast of uncertainties or emerging issues related to specific law changes.

- Managing calculation risk

The team will need to properly link the Act's changes to tasks in various RIC processes. The accurate application of the changes to calculation templates, policies, and procedures is critical. Significant adverse tax consequences could result if this is not done correctly. Any modifications to calculation templates and policies should be thoroughly tested and reviewed to manage calculation risk inherent in these updates.

- Getting everyone on the same page

The Act will impact the job duties of RIC tax service provider personnel and may affect others providing services to a fund as well. To effectively execute their duties, these personnel will need training about the changes made by the Act and the specific modifications made to RIC processes by the service provider.

Implications

The update of RIC tax processes for the Act's changes is a critical project for a RIC's management and tax service provider. A failure to timely and accurately update a fund's policies could result in adverse tax consequences. A RIC's audit committee should understand whether management has adopted and is executing a plan to implement the Act's changes.

Summary of developments for the six months ended June 30, 2011

Accounting and financial reporting matters from the FASB, PCAOB, SEC, and others

On May 12, 2011, the FASB issued ASU 2011-04, *Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in US GAAP and IFRSs*. The joint project was part of the Memorandum of Understanding between the FASB and IASB. The objective of the project was to bring together as closely as possible the fair value measurement and disclosure guidance issued by the two Boards. The issuance of the final standards results in global fair value measurement and disclosure guidance, and minimizes differences between US GAAP and IFRS.

Many of the changes in the US final standard represent clarifications to existing guidance. Some changes, however—such as the change in the valuation premise, limits on the application of premiums and discounts in valuations, and new required disclosures—could have a significant impact on practice.

The US guidance is effective for interim and annual periods beginning after December 15, 2011. Subsequent to the first year of adoption, the measurement principles and certain disclosures will be applicable in interim and annual periods.

In April 2011, the FASB issued ASU 2011-03, *Reconsideration of Effective Control for Repurchase Agreements* (the ASU). The guidance removes from the assessment of

effective control (1) the criterion requiring the transferor to have the ability to repurchase or redeem the financial assets on substantially the agreed terms, even in the event of default by the transferee, and (2) the collateral maintenance implementation guidance related to that criterion. The ASU also eliminates the provision that, in effect, concluded securities were sold if sufficient collateral was not available at all times to fund the repurchase of substantially all securities sold under repurchase agreements, even in the event of default by the transferees. The guidance is effective for the first interim or annual period beginning on or after December 15, 2011. The guidance should be applied prospectively to transactions or modifications of existing transactions that occur on or after the effective date. Early adoption is not permitted.

On March 2, 2011, the SEC proposed to remove credit ratings as a required element in the determination of permissible investments for money market funds. This proposal would amend certain rules and forms under the Investment Company Act of 1940 and most specifically impacts Rule 2a-7, which governs money market funds. If the proposed rule is implemented, eligibility will be based on the fund's Board or its delegate determining that the security presents minimal credit risk, and will not be predicated on the security's credit ratings. Comments on the proposed changes were due by April 25, 2011.

On February 12, 2011, the SEC proposed to remove references to credit ratings in rules and forms promulgated under the Securities Act and the Exchange Act. Similar changes were proposed in 2008 but were not enacted. The SEC is reconsidering the proposals at this time in light of the requirements of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010. While the SEC recognizes that credit ratings play a significant role in the investment decisions of many investors, the commission wants to avoid using credit ratings in a manner that suggests in any way a “seal of approval” on the quality of any particular credit rating or nationally recognized statistical rating organization (NRSRO). The SEC is seeking to reduce the reliance on credit ratings for regulatory purposes while also preserving the use of Form S-3 (and similar forms) for issuers that the commission believes are widely followed in the market. Comments were due by March 28, 2011.

On January 28, 2011, the FASB and the IASB jointly issued an exposure draft, *Offsetting Financial Assets and Financial Liabilities*. Under the proposed guidance, a reporting entity would be *required* to offset a recognized financial asset and recognized financial liability if (and only if) it has the unconditional right of offset and intends to either settle the asset and liability on a net basis or realize the asset and settle the liability simultaneously. The proposal also clarifies that a right to offset must be legally enforceable in all circumstances (including default by or bankruptcy of a counterparty). Under the proposal, a right to offset that is exercisable only upon a contingent event would not enable a reporting entity to report an asset and liability on a net basis.

Auditing matters from the PCAOB, AICPA, and SEC

On March 22, 2011, the PCAOB discussed potential changes to the auditor’s reporting model in an open meeting. The PCAOB stated that several groups have recommended the reporting model be reexamined

and made more meaningful for investors, as the auditor’s report has not been significantly modified since the 1930s despite previous efforts and recommendations for change. The PCAOB staff reached out to more than 80 investors, auditors, preparers, audit committee members, and other interested parties to seek their views. Changes to the auditor’s reporting model are also being discussed globally, including by the European Commission. On June 16, 2011, the PCAOB announced that it would hold an open meeting on June 21, 2011, to formally approve the issuance of a concept release seeking public comment on a variety of alternatives to the current reporting model.

Compliance and regulatory matters from the SEC and others

On June 10, 2011, the SEC proposed rules that would provide certain clearing agencies with exemptions from the registration requirements of the Securities Act of 1933 and the Securities Exchange Act of 1934 for security-based swaps that they issue. The proposed rules would exempt transactions by clearing agencies in these security-based swaps from all provisions of the Securities Act, other than the Section 17(a) anti-fraud provisions, as well as exempt these security-based swaps from Exchange Act registration requirements and from the provisions of the Trust Indenture Act, provided certain conditions are met. Comments on the proposed rules were due by July 25, 2011.

On April 27, 2011 the SEC voted unanimously to propose rules further defining the terms “swap,” “security-based swap,” and “security-based swap agreement.” The Commission also proposed rules regarding “mixed swaps” and books and records for “security-based swap agreements.” The rules were proposed jointly with the Commodity Futures Trading Commission (CFTC) and stem from the Dodd-Frank Wall Street Reform and Consumer Protection Act. Comments were due by July 22, 2011.

On April 5, 2011, the SEC adopted rules and forms to implement Section 21F of the Securities Exchange Act of 1934 (Exchange Act) titled “Securities Whistleblower Incentives and Protection.” The Dodd-Frank Wall Street Reform and Consumer Protection Act, enacted on July 21, 2010 (Dodd-Frank), established a whistleblower program that requires the Commission to pay an award, under regulations prescribed by the Commission and subject to certain limitations, to eligible whistleblowers who voluntarily provide the Commission with original information about a violation of the federal securities laws that leads to the successful enforcement of a covered judicial or administrative action, or a related action. Dodd-Frank also prohibits retaliation by employers against individuals who provide the Commission with information about possible securities violations.

On March 31, 2011, the SEC, along with several other government agencies, proposed rules to implement Section 956 of the Dodd-Frank Wall Street Reform and Consumer Protection Act. The proposed rules would require the reporting of incentive-based compensation arrangements by a covered financial institution and prohibit incentive-based compensation arrangements at a covered financial institution that provides excessive compensation or that could expose the institution to inappropriate risks that could lead to material financial loss. Comments must be received by within 45 days of publication in the Federal Register.

On January 26, 2011, the Commodity Futures Trading Commission (CFTC) issued proposed changes to the existing exemptions under Rules 4.5, 4.13(a)(3), and 4.13(a)(4). The proposed changes, which are based on a petition for rulemaking issued to the CFTC in August 2010 by the National Futures Association (NFA), are related to commodity pool operators (CPO) and, if adopted, may result in requiring full CPO registration by registered and private funds. Rules 4.13(a)(3) and

4.13(a)(4) relate to private funds. Rule 4.5 is related to operators of registered investment companies (RICs) and currently provides an exemption from CPO registration requirements. The stated intent of the proposed changes is to prohibit mutual fund operators offering futures-only investment products without CFTC oversight and to create additional transparency and consistency in regulation of similar products regardless of status with other regulators.

On January 25, 2011, the SEC adopted rules concerning shareholder approval of executive compensation and “golden parachute” compensation arrangements as required under the Dodd-Frank Wall Street Reform and Consumer Protection Act. The SEC’s new rules specify that say-on-pay votes required under the Dodd-Frank Act must occur at least once every three years beginning with the first annual shareholders’ meeting taking place on or after January 21, 2011. Companies also are required to hold a “frequency” vote at least once every six years to allow shareholders to decide how often they would like to be presented with the say-on-pay vote. Following the frequency vote, a company must disclose on an SEC Form 8-K how often it will hold the say-on-pay vote.

Under the SEC’s new rules, companies also are required to provide additional disclosure regarding “golden parachute” compensation arrangements with certain executive officers in connection with merger transactions. The SEC also adopted a temporary exemption for smaller reporting companies (public float of less than \$75 million). These smaller companies are not required to conduct say-on-pay and frequency votes until annual meetings occurring on or after January 21, 2013.

Publications of interest to mutual fund directors issued during the three years ended June 30, 2011

Independent Directors Council/Affiliates

[\(www.idc1.org\)](http://www.idc1.org)

Board Oversight of Subadvisers, January 2010

The report discusses the business reasons for retaining a subadviser and industry trends in the use of subadvisers. The report also explores Board oversight of subadvisers, starting from the time a principal adviser recommends hiring a subadviser, through Board approval of the subadvisory agreement and ongoing Board oversight of the subadviser, to possible termination of the subadviser. At each step, the report explores potential issues and considerations of particular interest to Boards overseeing subadvised funds. A task force composed of independent directors, in-house fund lawyers, and compliance personnel developed the report.

Mutual Fund Directors Forum

www.mfdf.com

Practical Guidance for Fund Directors on Effective Risk Management Oversight, April 2010

This report provides guidance for directors on effective risk management and the Board's oversight role.

PwC

www.pwc.com

Audit committee effectiveness: What works best, 4th edition, June 2011

This publication is intended to be a convenient guide, providing information on topics that are most relevant to the audit committee. It is a collection of leading practices that supports audit committee performance and effectiveness. It captures insights and points of view from audit committee members, financial reporting experts, governance specialists, and internal audit directors. It also incorporates survey trends, allowing you to understand the financial reporting environment and how audit committees are responding. Just as importantly, it includes lessons learned from the cumulative years of experience of PwC professionals from around the world.

Each chapter is intended to stand alone so you can read and understand the guidance without having to refer to other chapters. Appendix A captures the leading practices from each section and is a useful tool for audit committees when assessing their performance. The keyword index allows readers to find discussions about specific topics throughout the book.

Additionally, the practices and procedures described in the book represent suggestions for enhancing

the overall performance of the committee and often go beyond applicable rules. A committee should take into consideration its own facts and circumstances when applying these practices.

The Quarter Close—Directors Edition, June 2011

This quarterly publication is designed to keep directors informed about the latest accounting and financial reporting issues. In response to directors' requests, we have developed this version specifically for audit committee members and financial experts, basing it upon *The Quarter Close*, which is intended primarily for chief financial officers and controllers. The Q2 2011 edition spotlights the FASB and IASB's continued deliberations on the joint standard-setting projects, the SEC's latest release on the possible incorporation of IFRS into the US financial reporting system, and more on Dodd-Frank and other key topics.

Avoiding the Headlines: How Financial Services Firms Can Implement Programs to Prevent Insider Trading, June 2011

Insider trading has become a top priority of prosecutors, with increased cooperation among civil and criminal regulators, both in the United States and abroad. Recent civil and criminal investigations have implicated all types of firms—including hedge funds, mutual funds, and other types of asset management firms—banks, broker-dealers, public companies, law firms, and accounting firms. While it's good business, the law also requires firms to have robust compliance, supervisory, surveillance, and control measures in place to prevent and detect possible illegal insider trading. Regulators can bring enforcement action for the failure to have an adequate insider trading prevention program—even if no insider trading has occurred. With insider trading a top priority, leading firms are reviewing their existing protocols to prevent insider trading, and making changes. This publication explores how financial services firms can implement

programs to prevent insider trading.

Boardroom Direct, May 2011 **Issue in focus: Understanding critical trends and the CEO's agenda**

One of a Board's most important obligations is to engage in meaningful strategy discussions with the CEO and other senior executives. These discussions should include understanding critical trends, their impact, and how they could create opportunities for growth. The Spring 2011 edition of *Boardroom Direct* outlines key themes from PwC's 14th Annual Global CEO Survey and provides insight on what directors may want to ask the CEO, enhancing the quality of those discussions.

Spring Ahead or Fall Behind: Create a Market Ready ETF Model, May 2011

Mutual funds are no longer the only game in town. While the United States has historically been the global trendsetter for the investment management industry, the formerly white-hot enthusiasm for mutual funds has begun to cool down. In recent years, the growth of US-listed ETFs has rapidly outpaced that of traditional investment products—a trend that is likely to continue in the United States, with Europe and Asia-Pacific following suit. This surge in ETF popularity in the eyes of both investors and sponsors is due to several factors, but it pretty much boils down to this: With investors seeking lower-cost options, asset managers that do not offer ETF products may lose assets to those who do. As a result, asset managers are making ETFs a strategic component of their investment-product offerings so as to attract new assets. This publication discusses the market readiness of ETF models to meet current and future demands.

A Closer Look: Impact on Swap Data Reporting, May 2011

Swap data reporting is a cornerstone of the new derivatives regime created by the Dodd-Frank Act. In an effort to

increase transparency and integrity in the derivatives markets, proposed Dodd-Frank regulations will require information about every swap or security-based swap (SBS) transaction to be sent to new swap data repositories or a government agency. This *A Closer Look* describes the proposed swap data reporting rules and suggested responses for swap market participants.

Becoming FATCA Compliant— Why asset managers should prepare now, May 2011

Beginning January 1, 2013, the provisions of the Financial Account Tax Compliance Act (FATCA) will impose a 30% US withholding tax on any US-sourced income and the gross proceeds from the sale of investments that produce US-sourced interest or dividends (withholdable payments) received by any offshore fund or other foreign financial institution (FFI). This withholding tax is avoided if the FFI enters into an agreement with the US government and agrees to comply with new documentation requirements, due diligence procedures, and reporting obligations. These new requirements are aimed at detecting US tax residents who may be evading US federal income tax by holding investments directly or indirectly through an FFI. Initiating a program now to identify and assess the critical business, tax, and operational impacts arising from FATCA will increase an asset manager's opportunity to address the business issues and implementation challenges through a complete, effective, and cost-efficient implementation program that will permit full compliance by January 1, 2013 (the effective date of FATCA's new documentation requirements, due diligence procedures, and reporting obligations).

A Closer Look: Dodd-Frank at the Six Month Milestone, March 2011

As a part of our ongoing Dodd-Frank *A Closer Look* series, this special edition summarizes the key progress on Dodd-Frank at the six-month milestone.

14th Annual Global CEO Survey, January 2011

The 14th Annual Global CEO Survey sets out to uncover how chief executive officers (CEOs) are approaching business growth during a time when sustainable economic growth in many developed markets is far from certain. A supplementary publication, *Gearing up for renewed growth: Asset management industry summary*, is also available and summarizes the key survey findings related to the asset management sector.

In Brief: An overview of financial reporting developments, December 2010

On November 29, 2010, the Financial Accounting Standards Board (FASB) and the International Accounting Standards Board (IASB) published a progress report that outlines a revised plan and time line for their convergence projects. This publication provides an overview of the reprioritized convergence strategy.

In Brief: Boards delay timing for financial statement presentation and financial instruments with characteristics of equity projects, October 2010

At the joint Board meetings on October 21 and 22, 2010, the FASB and IASB decided to further delay the time line on two joint projects: (1) financial statement presentation and (2) financial instruments with characteristics of equity. This publication provides an overview of the projects and how they are impacted.

Asset Management Valuation Survey, November 2010

PwC conducted a survey designed to gather, analyze and share information about emerging trends in the valuation governance process. The survey was designed to gather data from industry participants to help executives and other stakeholders benchmark their valuation governance practices against their peer group across the asset management

industry, including the traditional/registered, alternative, private equity and venture capital, and real estate sectors. PwC polled more than 50 US-based managers of varying sizes, with 2 of the participating firms managing less than \$500 million in assets and 12 of the participating firms managing more than \$100 billion.

Pay to play, September 2010

The SEC voted to adopt a new rule, Rule 206(4)-5, under the Investment Advisers Act of 1940 on June 30, 2010, to address “pay-to-play” issues relating to relationships between investment advisory firms and political officials who have control over, or the ability to appoint someone to control, the investment decision-making for public pension plans. The rule limits the political contributions (federal, state, and local) that investment advisers and certain current and prospective employees can make. This publication outlines the elements of the rule, recordkeeping requirements, and effective dates as well as additional considerations chief compliance officers should consider.

Annual Corporate Directors Survey—2010 Results, November 2010

PwC’s Annual Corporate Directors Survey collects the opinions of more than 1,000 directors serving on the Boards of the top 2,000 publicly traded companies (by revenue) listed with the NYSE Euronext, the NYSE Amex, and the NASDAQ OMX Group stock exchanges. The survey covers issues such as risk management, compensation, director evaluations, director experience mix, and Board diversity, to name just a few. This marks the ninth year for the annual survey, formerly titled What Directors Think.

2011 Current Developments for Directors, December 2010

This annual report captures the critical governance issues directors and senior executives face. A special focus section has been added in this year’s publication to highlight some of the factors that are

influencing companies’ growth plans. It highlights how new global trends are affecting companies’ operations and international expansion opportunities. This year’s publication also covers how regulatory reform, financial reporting developments, and tax reform may affect companies.

Point of View: Slowing down the pace of standard setting, July 2010

The FASB and IASB are working on several joint projects designed to improve both US generally accepted accounting principles and International Financial Reporting Standards. These projects are part of a wider goal to converge US and International Standards in key areas by 2011. While convergence is an important component of achieving a single set of high-quality global accounting standards, some question whether the current pace and time line are realistic. PwC believes that, despite the recently announced modified strategy for certain projects, the time line is still aggressive and does not allow enough time for constituent input and the Boards’ thoughtful rigorous processes to achieve the Boards’ desire for high-quality output. Read this publication for additional background, analysis, and Q&A on these issues.

CBI/PricewaterhouseCoopers Financial Services Survey, June 2010

The 83rd survey shows a gentle further improvement in confidence and levels of activity, but with increasingly upbeat predictions for the coming quarter. Other encouraging signs include plans to expand headcount and an expectation that nonperforming loans will start to fall. On the downside, regulatory costs are rising fast and respondents are concerned about further deterioration in the financial markets.

Working Guide for an Investment Company’s Audit Committee, June 2010

The guide presents considerations for audit committees in a number of areas, with significance to open-and closed-end funds’ financial statements and their internal control, as well as matters pertaining to their relationships and communications with management and internal and independent auditors.

FS Regulatory Briefs: Fund Directors and the New Proxy Disclosure Rules, June 2010

This publication is aimed at helping directors assess how well their funds comply with the enhanced proxy and fund governance disclosure requirements. This edition addresses the actions of directors with regard to (1) proxy disclosure enhancements, and (2) the voting of proxies for portfolio companies.

Broker-Dealer and Investment Adviser Compliance Programs—Regulatory requirements, common minimum elements, other paradigms, May 2010

Investment advisers and investment companies are required to have compliance programs pursuant to rules of the Securities and Exchange Commission, and broker-dealers are required to have compliance programs pursuant to rules imposed by FINRA. These rules have certain common features—effectively creating “minimum elements” for broker-dealer and investment adviser compliance programs. The separate regulatory requirements governing advisers’ and broker-dealers’ compliance programs are summarized in this publication, as well as these common “minimum elements.”

The second generation of Global Investment Performance Standards, April 2010

The Global Investment Performance Standards (GIPS), which enable asset managers to voluntarily provide standardized and transparent measures

of their performance, have been in effect in nearly 30 countries since 2005. Compliance with GIPS can serve as an important independent source of validation for a manager’s performance. This publication provides PwC’s perspective and analysis on GIPS 2010, which became effective on January 1, 2011, introducing changes that will pose additional challenges for asset managers.

Lead Directors: A study of their growing influence and importance, April 2010

This paper discusses what directors see as the most important elements of their service now and in the future.

Contact us

For more information about any of the information shared in this newsletter, please feel free to contact any of the following practice leaders, or your local PwC representative. We would welcome the opportunity to speak with you.

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