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Current Developments for Mutual Fund Audit Committees

Quarterly summary

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PCAOB concept releases – auditor reports and audit firm rotation

On June 21, 2011, the Public Company Accounting Oversight Board ("PCAOB" or the "Board") issued for public comment, its concept release Possible Revisions to PCAOB Standards Related to Reports on Audited Financial Statements. The Board additionally held a public roundtable meeting on this topic on September 15, 2011. This concept release discusses potential changes to the auditor's reporting model. Some of the possible enhancements include:

- A supplement to the auditor's report in which the auditor would be required to provide additional information about the audit and the company's financial statements in an "Auditor's Discussion and Analysis" section;
- Possibly requiring and expanding the use of emphasis of a matter paragraphs within the auditor's report;
- Having the auditor report on information outside of the financial statements; and
- Clarifying the use of certain language within the auditor's report.

The concept release discusses the possibility of using one or more of these or other enhancements, with the primary objective of providing greater transparency to investors and other users of the financial statements about the audit without compromising audit quality. Comments on the proposed standard were due on September 30, 2011.

The proposed Auditor's Discussion and Analysis ("ADA") enhancement described within the concept release is intended to provide the auditor with the ability to discuss in a narrative format the auditor's views regarding significant matters.

Some of the potential topics that could be included within this narrative relating to the audit include, discussing audit risks identified during the audit, specific audit procedures performed and the results of those procedures or information regarding the auditor's independence. The auditor could also discuss relevant matters regarding the company's financial statements, including management's judgments and estimates, accounting policies and practices and difficult or contentious issues, including "close calls." The auditor could also highlight those areas where they believe management could have applied different accounting or disclosures in the financial statements. The Auditor's Discussion and Analysis would not be intended to provide additional assurance, but rather would facilitate an understanding of the auditor's opinion on the financial statements taken as a whole to users of the financial statements.

One of the major concerns expressed about this proposal, however, was that in certain respects, such as discussing accounting alternatives that management could have employed, the "ADA" (and thus the auditor) might itself become a source of company financial information. During the roundtable, PCAOB Chairman James Doty specifically stated that the proposals "are not intended to put the auditor in the position of creating and reporting financial information for management."

Another proposed enhancement within the concept release discusses expanding, or requiring, the use of emphasis of a matter paragraphs within the auditor's report. Currently, emphasis paragraphs are not required, but may be added at the discretion of the auditor in order to emphasize a matter in the financial statements. The concept release explores use of these paragraphs within the auditor's report in order to emphasize those matters that are important in understanding the financial statement presentation, including significant management judgments and estimates and areas with significant measurement uncertainty. Audit procedures performed over these areas could also be included within the emphasis paragraph.

The concept release additionally discusses reporting on information outside of the financial statements and clarifying certain language within the auditor's report. Information outside of the financial statements, such as management's discussion and analysis, would potentially be required to be examined by the auditor, increasing the auditor's scope. The auditor would then issue a report expressing an opinion on management's discussion and analysis. The language within the auditor's existing report that is proposed to be enhanced includes further explaining what is meant by "reasonable assurance." Further, enhancements are proposed to describe the auditor's responsibility for detecting fraud, the auditor's responsibility for financial statement disclosures, management's responsibility for the presentation of financial statements, the auditor's responsibility for information outside the financial statements and that the auditor has a responsibility to remain independent of the company and has complied with the applicable independence requirements.

Separately, on August 16, 2011, the PCAOB issued for public comment an additional concept release, Auditor Independence and Audit Firm Rotation. This concept release discusses potentially requiring audit firm rotation after ten (or another possible number) years of service as the company's auditor, to enhance the auditor's ability to maintain independence, objectivity, and professional skepticism through the knowledge that an auditor/client relationship cannot be indefinite. In effect, the PCAOB could introduce rule making that would determine that the auditor is not independent if the auditor has provided an opinion on a company's financial statements for a certain number of consecutive years. The Board is considering whether to move forward with this concept, or other alternatives (e.g., mandated joint audits or periodic reproposals) and, if so, what the appropriate time period should be if they move forward with this concept. The Board will hold a public roundtable meeting on this topic in March 2012. Comments on the proposed standard are due on December 14, 2011.

Exchange-traded funds

With more than $1.1 trillion in assets at the end of July 2011, exchange-traded funds (ETFs) in the United States have experienced significant growth over the past year, easily eclipsing last year's total of $821 million. And growth is projected to continue by 20% to 30% over the next few years, as ETFs have been gaining market share at the expense of mutual funds. Much of the growth in ETF assets during the past year has been in the fixed income, international, emerging market, and commodity sectors.

A recent study by Greenwich Associates indicates that institutional investors plan to increase their investments in ETFs over the next two years. Reasons for this trend include:

- Equitizing cash – Temporary idle cash is invested in ETFs while the investment manager reviews their long-term investment strategy
- Manager transitions – Proceeds from the sale of investments by a former manager are invested in ETFs until a new manager has been selected
- Rebalancing – ETFs can make rebalancing more efficient because they provide intra-day liquidity
- Tactical adjustments – ETFs provide a broad range of investment options and are a cost-effective alternative for executing strategies

Active ETFs

Until recently, many traditional investment managers have resisted the actively managed ETF market due to transparency issues. Because ETFs are required to reveal their holdings on a daily basis, potential front-running of an active ETF portfolio is a concern. But lately interest has spiked in actively managed ETFs, which have had some success in gathering assets since they were first launched in 2008. As of March 31, 2011, there were 36 active ETF portfolios with approximately $4.2 billion in assets.

Recent events suggest that market sentiment is changing in favor of active ETFs. In the United States, for example, several large investment managers have obtained exemptive relief to launch actively managed ETFs in the past year, while a number of other managers have acquired firms with active ETF relief or filed for active ETF relief from the SEC. While the promise of actively managed ETFs is intriguing, they still have much to prove to investors. For instance, because active ETFs have existed for only three years and therefore lack a consistent track record, investment managers are left to ruminate over several issues, including:

- The SEC approval process, including the current ban on the use of derivatives for actively managed ETFs, which has limited product innovation
- Transparency vs. non-transparency of active ETF portfolios
- Effectiveness of the arbitrage mechanism and other structuring issues
- Ability of actively managed ETFs to penetrate the institutional market

Regulatory

The significant growth and innovation of various ETFs in the United States and Europe has captured the attention of various regulators, including the SEC, Bank of England, Commodities Futures Trading Commission, Financial Services Authority, Financial Stability Board,

Bank for International Settlements, and the International Monetary Fund.

Most of the concerns raised by these regulators focus on the increasing complexity of various ETFs, including:

- The extent of derivatives usage, particularly for synthetic ETFs that seek to replicate the performance of a benchmark index through the use of swaps with an affiliated entity
- The extent of transparency for investors with respect to the structure of various ETFs, as well as the related costs, inherent risks, liquidity risks, counterparty risks, and collateral arrangements
- The suitability of various ETFs for retail investors

Many ETF sponsors and industry associations have responded to these regulatory reports and generally support further education and transparency of various types of ETFs. Many of the respondents also note that there are many existing regulatory provisions in the United States and Europe to help mitigate the risks outlined in the various regulatory reports on ETFs. The recent SEC concept release "Use of Derivatives by Investment Companies Under the Investment Company Act of 1940" also raises questions about the use of derivatives by ETFs and whether there should be additional protection for investors.

Evolution of ETF operating model

ETF processes, roles, automation, and controls generally lack the maturity and standardization of mutual funds, by a considerable margin. This means that providers need to continue to improve in these areas to preserve the trust given to them by investment managers.

As mutual funds became the investment product of choice in the 1990s, capabilities in people, process, and technology evolved quickly, enabling a highly scalable, risk-controlled operational environment. Front- and middle-office functions to support portfolio management and trading are well established. Likewise, a mature market of external service providers for mutual funds has also developed. These asset managers and service providers have significant experience in meeting regulatory guidelines, including 38a-1 and controls reporting requirements.

In contrast, given their relative newness, ETF-related support operations continue to evolve. Sponsors use a wide variety of operating models to rebalance portfolios, permit portfolio customizations, and report tracking errors, among other functions. Similarly, the ETF service provider market is still developing, with only four primary participants. As a sponsor, the success of your ETF strategy rests upon several operational considerations, both internal and external.

The industry continues to show exceptional growth, with no sign that investor interest is fading. Operating models, technology platforms, and distribution channels need to be able to support future volume increases and be flexible enough to accommodate product innovation.

Across much of the financial services industry, regulatory reform will put additional pressure on operating model efficiencies and restrict revenue growth opportunities. New regulations, regardless of their exact nature, will require increased transparency and expanded reporting requirements. Stakeholders will seek reassurance in the integrity and infrastructure of sponsors, reinforcing the need for increased transparency and accountability. In turn, sponsors will have expectations of transparency and accountability from their service providers.

ETF sponsors and service providers should commit to further developing the industry model by communicating frequently and sharing leading practices. Sponsors and service providers should continually assess whether their operating models can meet current and future demands.

PwC recommends five key areas of analysis to help asset managers and service providers proactively address the maturity of their ETF operating models.

Table 1: Five key areas of analysis

Capabilities and market assessment	*Fund launch*	*Service provider analysis*	*Tax reporting considerations*	*Operational risk and compliance controls*
Identification of key functions and leading practices required to support products in front and middle office	Key considerations to operationalize activities to support fund launches	Capabilities analysis of key ETF partners, including index receipt agent, distributor, authorized participants, and index provider	Considerations for appropriate treatment of securities purchases and redemptions	Thorough analysis of controls for manual and automated processes to manage operational and regulatory risks
Identification of key functions and leading practices required to serve as index receipt agent	Value-added services to support asset managers in fund launch process	Benchmark analysis of key index receipt functions to assess scope of services, service levels, and pricing	Considerations for proper recording and reporting of taxable gains and losses, with consideration for wash-sale monitoring	Analysis of index receipt agent's process controls, including financial and regulatory reporting

Taxes

Filing under the 1934 or 1940 Act does not in itself drive entity classification (and thereby investor reporting) for tax purposes for ETFs. Tax classification begins with the legal form, which can be altered by election, and ends with whether the structure and activities meet specific requirements to maintain that classification. The three entity types most prevalent in the ETF space are corporations, trusts, and partnerships. The following chart summarizes the key features of each of these structures.

Table 2: Key features of most prevalent ETF entity types

	Corporation	*Trust*	*Partnership*
Level of tax	Entity	Flow-through to investor	Flow-through to investor
Investments	Unrestricted	Fixed	Unrestricted
Distributions	Taxable to the extent of E&P	Generally not taxable	Generally not taxable
Allocations	Pro rata	Pro rata	Based on investor economics and holding period
Investor reporting	Form 1099	Form 1099 equivalent	Schedule K-1
Sale of interest	Sale of capital asset	Sale of share of underlying assets	Sale of capital asset with exceptions

Tax efficiency

Entities under a corporate structure have the potential for double taxation at the corporate and investor levels. Special dividend-paid deduction rules generally permit regulated investment companies (RICs) to avoid entity-level taxation. And there are limitations on deductibility at the individual investor level of trust and partnership administrative expenses. Partnership allocations match investor economics—investors don't step into unrealized gains or losses.

Ease of reporting

Pro rata allocations allow corporations and trusts to leverage broker reporting infrastructure. Cost and responsibility of issuing 1099's rests with the brokers. Grantor trust ETF investors are deemed to own an undivided interest in trust assets and have to calculate their own gains and losses. To facilitate, grantor trust ETFs provide additional information on gross income and expenses that brokers must report to investors. Partnership economic allocations result in unique allocations for each investor, making the broker reporting framework unsuitable. Therefore, the cost and responsibility of issuing K-1s rests with partnerships. Entities operating under a corporate structure block the need for investor multi-state reporting (more relevant to a non-financial partnership).

Investor behavior

Fund sponsors have limited visibility into corporate and grantor trust investor buy/sell transactions and behavior. By contrast, because they collect and own the information, fund sponsors have high visibility into partnership investor buy/sell transactions and ownership behavior. While investors generally perceive that K-1s are complex and/or are not timely relative to Forms 1099, ETF K-1s typically have four to five income and expense items and are often provided to investors at approximately the same time as 1099's.

Publicly traded partnerships

The key financial benefit to investors in publicly traded partnerships is exposure to a diversified asset class otherwise not available in RIC ETFs. For example, commodity-related gross income is non-qualifying gross income for RICs, but is qualifying gross income for a publicly traded partnership. Special rules also exist for a RIC to invest up to 25% of its assets in such publicly traded partnerships without an adverse impact on its qualification requirements. However, redemptions are in cash and typically require the fractional liquidation of holdings, thus increasing the potential for capital gain allocations. Tax reporting items reflected on a typical Schedule K-1 are limited in number and relatively easy to include in an investor's tax return.

Grantor trusts

Key non-financial benefit to investors is efficient exposure to a "physical" commodity asset class. This structure eliminates storage, insurance, etc., related costs if physical commodities are bought directly. Grantor trusts are also tax efficient, and the trust structure is suited to a "buy and hold" strategy. Only limited trading occurs to generate cash to pay expenses. Realized long-term capital gains are taxed at a maximum 28% collectibles capital gain rate. Investor tax information is provided in tables often available on websites in compliance with widely held fixed investment trust HFIT) reporting rules.

Regulated investment companies

RIC ETFs are generally tax efficient. Better tax efficiency arises from less frequent "forced selling" as shareholder redemptions are reduced, special tax treatment of in-kind redemptions, tax lot selection strategies, and tax equalization. RIC ETFs generally have smaller distributions than other types of RICs, and exchange trading affords investors greater flexibility for investment decisions.

ETFs investing in master limited partnerships

ETFs investing in master limited partnerships (MLPs) do not qualify for RIC status and therefore elect to be taxed as corporations. Key non-financial benefit to investors is exposure to the asset class without exposure to the federal and multi-state tax filing obligations. However, there is a trade-off as the entity-level taxation reduces the investors' overall return. Although, most MLPs shield 80% to 100% of cash flow through hard asset cost recovery deductions (depreciation), thus mitigating some of the exposure to entity-level taxation. Dividends are taxable to investors to the extent of corporate earnings and profits.

Despite a turbulent economy, ETFs continue to gain significant market share and have many aspects that are attractive to investors and advisors alike. Not surprisingly, with an increase in ETF popularity, we are seeing a corresponding increase in regulator focus. And although the ETF environment still has a ways to go to reach the operational maturity of traditional RICs, with their continued growth, the development of the operational aspects specific to ETFs is likely to follow.

Regulatory developments

Investment companies were on the Securities and Exchange Commission's (SEC's) radar during the third quarter. During late summer, the SEC published two concept releases that examine certain aspects of investment companies. One release reviews investment companies' use of derivatives; the other focuses on an exemption available under the Investment Company Act of 1940 (Investment Company Act) to companies engaged in acquiring or purchasing mortgages or related instruments. The SEC also issued a no-action letter providing additional guidance on the pay-to-play rule as it relates to recordkeeping requirements for government plans. However, the SEC was dealt another legal defeat, as a federal appellate court vacated its proxy access rule.

This regulatory update summarizes the court decision, the SEC's recent concept releases and rulemakings, and recent regulatory developments from the Commodities Futures Trading Commission (CFTC) and Department of Labor.

SEC issues concept release on use of derivatives by mutual funds

The SEC and its staff have been reviewing the use of derivatives[1] by management investment companies and business development companies registered under the Investment Company Act (collectively referred to as "funds"). To obtain input on a wide range of issues relevant to the use of derivatives by funds, the SEC issued on August 31, 2011 a highly detailed concept release that focuses on the use of derivatives under a number of provisions of the Investment Company Act.

The stated goal of the review by the SEC and its staff is to evaluate whether the regulatory framework, as it applies to funds' use of derivatives, continues "to fulfill the purposes and policies underlying the Act and is consistent with investor protection." The purpose of the concept release is to assist with this review and solicit public comment on the current regulatory regime under the Investment Company Act as it applies to funds' use of derivatives. The SEC intends to use the comments to help determine whether regulatory initiatives or guidance are needed to improve the current regulatory regime and the specific nature of any such initiatives.

Background

Funds employ derivatives for a variety of purposes, including increasing leverage to boost returns; gaining access to certain markets; achieving greater transaction efficiency; and hedging interest rate, credit, and other risks. At the same time, derivatives can raise risk management issues for a fund relating to, for example, leverage, illiquidity (particularly with respect to complex OTC derivatives), and counterparty risk, among other issues.

1 The concept release broadly describes "derivatives" as instruments or contracts whose value is based upon, or derived from, some other asset or metric (referred to as the "underlier," "underlying," or "reference asset").

The release

A key impetus for the concept release appears to be the dramatic growth in the volume and complexity of derivatives investments over the past two decades, and funds' increased use of derivatives. The SEC staff generally has been exploring the benefits, risks, and costs associated with funds' use of derivatives and issues relating to the use of derivatives by funds, such as, for example, whether funds' boards of directors are providing appropriate oversight of the use of derivatives by the funds and whether existing prospectus disclosures adequately address the particular risks created by derivatives.

In its concept release, the SEC first describes common uses of derivatives by funds and seeks input on the costs and benefits associated with the use of derivatives, whether different types of funds use derivatives for different purposes and whether exchange-traded funds (ETFs) use derivatives, among other questions. A large portion of the concept release, however, analyzes the use of derivatives in light of several key statutory provisions of the Investment Company Act, with most of the discussion focused on Section 18, which essentially limits the ability of a fund to borrow by issuing "senior securities" (debt securities and preferred stock). The SEC's longstanding position has been that funds can remain in compliance with Section 18 if they "cover" senior securities by maintaining "segregated accounts" to limit the risk of loss. Under this "segregated account approach," a fund would establish and maintain with the fund's custodian a segregated account containing liquid assets equal to the indebtedness incurred by the fund with the issuance of the senior security.

However, the SEC's approach to the valuation of segregated assets has engendered criticism, and the release discusses several other possible approaches to valuation, including one recommended in the 2010 ABA Derivatives Report as well as approaches in a number of other jurisdictions for measuring and limiting risk, including the EU, Singapore, Hong Kong, and Canada. The SEC is seeking specific detailed comments on the segregated account approach and the ways in which it can be improved.

In briefer discussions, the concept release reviews and seeks input on:

- Derivatives valuation issues as they arise in determining whether a fund is classified as "diversified" or "non-diversified" based on its total assets

  Whether Section 12(d)(3), which prohibits a fund from investing in "securities-related issuers" (e.g., broker-dealers, underwriters, or investment advisors), should apply when a securities-related issuer is a counterparty to a fund in a derivatives transaction or the issuer of a reference asset in a derivatives transaction with the fund
- How derivatives transactions with funds should be valued for purposes of determining application of fund concentration provisions in a particular industry or group of industries
- In determining a fund's net asset value, how funds determine the value of derivatives for which market quotations are not readily available

The SEC will accept public comments on the concept release until November 7, 2011.

SEC issues concept release on interpretations of Section 3(c)(5)(C) of the Investment Company Act

On September 7, 2011, the SEC published in the Federal Register a concept release seeking public comment on the interpretation of Section 3(c)(5)(C) of the Investment Company Act. Section 3(c)(5)(C) generally excludes from the definition of investment company any person who is primarily engaged in, among other things, "purchasing or otherwise acquiring mortgages and other liens on and interests in real estate." Many companies engaged in the business of acquiring mortgages and mortgage-related instruments, such as some real estate investment trusts, rely on this statutory exclusion.

Given the evolution of mortgage-related pools and the development of new and complex mortgage-related instruments, the SEC is reviewing interpretive issues relating to the status of mortgage-related

pools under the Investment Company Act and whether mortgage-related pools might be making judgments about their status under the Act without sufficient SEC guidance on the interpretive issues that arise under that provision. The SEC also is concerned that staff no-action letters that have addressed the statutory exclusion in Section 3(c)(5)(C) may have contained, or led to, interpretations that are beyond the intended scope of the exclusion. Moreover, the SEC is concerned that certain types of mortgage-related pools today appear to resemble, in many respects, investment companies such as closed-end funds and may not be the types of companies that were intended to be excluded from regulation under the Act by Section 3(c)(5)(C).

Thus, the SEC has published the concept release to ensure that its regulatory approach is updated to reflect the current market environment while still meeting investor protection goals.

In the concept release, the SEC provides an overview of the mortgage-related pools and solicits comment on their management styles, corporate governance, and similarities to traditional investment companies. In addition, the SEC seeks comment on a number of topics, including, but not limited to, the current state of guidance and interpretation concerning Section 3(c)(5)(C), whether there are uncertainty or differing views among companies as to the availability of the statutory exclusion, and whether use of the exclusion is generally consistent with the underlying purposes and policies. Finally, the SEC seeks views on what steps, if any, including possible rulemaking, it should take to provide greater clarity, consistency, or regulatory certainty regarding the status of mortgage-related pools under the Investment Company Act.

Public comments on the concept release should be received by the SEC by November 7, 2011.

SEC adopts large-trader reporting rule

In July, the SEC adopted a final rule establishing large-trader reporting requirements under the Securities Exchange Act of 1934. The final rule will require a “large trader,” defined as any person whose aggregate transactions equal or exceed (1) two million shares or $20 million during any calendar day, or (2) 20 million shares or $200 million during any calendar month, to identify itself to the SEC and make certain disclosures on new Form 13H. The SEC will then assign each large trader a unique identification number, which the large trader then must provide to its registered broker-dealers. The rule may affect advisors who engage in high-volume trading.

The rule also imposes recordkeeping, reporting, and monitoring requirements on broker-dealers. Broker-dealers will be required to maintain additional transaction records for each large trader, and to report this information to the SEC upon request. In addition, broker-dealers will be required to perform limited monitoring of their customers’ accounts for activity that may trigger the large-trader identification requirements.

The rule became effective October 3, 2011. Large traders must file Form 13H by December 1, 2011. Broker-dealers must maintain additional records and perform their monitoring obligations on April 30, 2012.

SEC issues advance notice of proposed rulemaking on the treatment of issuers of asset-backed securities under the Investment Company Act

The SEC is considering proposing amendments to Rule 3a-7 under the Investment Company Act, the rule that provides certain asset-backed securities issuers with a conditional exclusion from the definition of investment company. Specifically, the SEC may consider amendments to Rule 3a-7 that could reflect market developments since the

adoption of the rule in 1992, and recent developments affecting asset-backed issuers, including passage of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank) and the SEC's recent rulemakings regarding the asset-backed markets. To assist in its review, on September 7, 2011, the SEC published in the Federal Register an advance notice of proposed rulemaking. The SEC is also withdrawing its July 2008 proposal to amend Rule 3a-7.

Asset-backed issuers typically meet the definition of investment company under the Investment Company Act, but generally cannot operate under the Act's requirements and restrictions. In 1992, the SEC adopted Rule 3a-7 specifically to exclude from the Investment Company definition certain asset-backed securities that meet the rule's conditions. In particular, to rely on Rule 3a-7, an asset-backed issuer must issue fixed income securities that entitle holders to receive payments that depend primarily on the cash flow from eligible assets. The rule provides that the issuer's fixed income securities generally must be rated in one of the four highest ratings categories by a nationally recognized statistical rating agency.

The SEC indicated that it is considering the elimination of this rating requirement because it is concerned that such ratings have not served as a "proxy" to address Investment Company Act related issues, and in light of the Dodd-Frank Act provision to substitute other standards of creditworthiness in place of credit ratings in federal regulations. The SEC seeks particular comment on whether ratings criteria should be replaced by other conditions.

In addition, the SEC requests comment on the following conditions that, in its view, should be added to Rule 3a-7 to directly address investor protection under the Investment Company Act:

- Concerns about self-dealing by insiders, misvaluation of assets, and inadequate asset coverage as they relate to the structure and intended operations in addressing these concerns
- The benefits of an independent review of the asset-backed issuer's structure and intended operations in addressing these concerns
- Preservation and safekeeping of the asset-backed issuer's eligible assets and cash flow

The SEC also requests comment on whether the requirements of Regulation AB or the shelf-eligibility requirements for asset-backed securities may serve as a means to address some of the SEC's concerns with Rule 3a-7. Specifically, the SEC asks for insight on the effects of any such rule changes, including on some asset-backed issuers that privately offer their securities based on Rule 3a-7. Finally, the SEC is interested in better understanding the manner in which the exclusion provided by the rule affects the status of holders of securities issued by Rule 3a-7 issuers.

The public comment period closes November 7, 2011.

Court of Appeals strikes SEC proxy access rule

On July 22, 2011, in the case Business Roundtable and US Chamber of Commerce v. Securities Exchange Commission, the US Court of Appeals for the DC Circuit vacated SEC Rule 14a-11, which would have required public companies to provide shareholders with information about, and their ability to vote for, shareholder-nominated candidates for the board of directors. The petitioners, Business Roundtable, and the US Chamber of Commerce argued that the SEC promulgated the rule in violation of the Administrative Procedure Act, because the SEC, among other things, failed to adequately consider the rule's effect upon efficiency, competition, and capital formation, as required by federal securities laws. The court agreed, finding that the SEC "acted arbitrarily and capriciously" in its failure to consider the economic effects of a new rule, including, for example, inconsistently and opportunistically framing the costs and benefits of the rule, failing to adequately quantify certain costs (or explain why costs could not be quantified), contradicting itself, and failing to respond to substantial problems raised by commenters. The court also noted that the SEC had not justified the potential disruption that might be caused to investment companies in their use of unitary boards to govern a fund complex.

On September 6, 2011, the SEC confirmed that it would not seek review of the court's decision.

SEC's final rule facilitating director nominations becomes effective

The SEC recently published notice in the Federal Register that amended Rule 14a-8(i)(8) became effective September 20, 2011. The rule requires companies to include in their proxy materials shareholder proposals regarding proxy access procedures. Specifically, shareholder proposals by qualifying shareholders that seek to establish a procedure in the company's governing documents for the inclusion of shareholder director nominees in company proxy materials would not be excludable. Although the amendments to the rule were not at issue in the Business Roundtable litigation, the SEC had voluntarily stayed the effective date pending the court's decision.

SEC issues no-action letter on pay-to-play rule

On September 12, 2011, the SEC issued a no-action letter to the Investment Company Institute (ICI) stating it would not recommend enforcement action under the recordkeeping requirements of Rule 204-2(a)(18)(i)(B) (government plan recordkeeping rule) against an advisor to a registered investment company that is an investment option of a plan or program of a government entity (covered investment pool) if such advisor makes and keeps an alternative set of records as described in the letter.

In connection with its amendments to Rule 206-4(5), or the pay-to-play rule, the SEC amended Rule 204-2 to add the government recordkeeping rule, which requires a registered investment advisor to make and keep a list or other record of all government entities that are or were investors in any covered investment pool to which the advisor provides or has provided investment advisory services, as applicable, in the past five years, but not prior to September 13, 2010.

ICI's letter noted that a government entity may hold shares in a covered investment pool through one or more omnibus accounts in such a way that the government entity is wholly unknown to the advisor, registered investment company, or its transfer agent, and that this lack of transparency impedes the ability of an advisor to comply with the government plan recordkeeping rule with respect to such accounts.

To address the lack of transparency, the staff agreed not to recommend enforcement action against an advisor, provided that the advisor must make and keep a list of other records that includes:

- Each government entity that invests in a covered investment pool where the account of such government entity can reasonably be identified as being held in the name of or for the benefit of the government entity on the records of the covered investment pool or its transfer agent
- Each government entity whose account was identified as that of a government entity — at or around the time of the initial investment — to the advisor or one of its client servicing employees, regulated persons, or covered associates
- Each government entity that sponsors or establishes a 529 plan and has selected a specific covered investment pool as an option to be offered by such 529 plan
- Each government entity that has been solicited to invest in a covered investment pool if a covered associate, regulated person, or client servicing employee of the advisor participated in or was involved in such solicitation, regardless of whether such government entity invested in the covered investment pool

MSRB withdraws pending municipal advisor rule proposals

On September 12, 2011, the Municipal Securities Rulemaking Board (MSRB) announced it has withdrawn several rule proposals it filed with the SEC in August. Citing substantial concern regarding the timing of a permanent municipal advisor definition, the MSRB stated it would delay certain of its proposed rules until the SEC adopts a permanent definition under the Securities Exchange Act of 1934. The affected rule proposals address fiduciary duty, pay-to-play, fair dealing, supervision, gifts, and assessments.

The MSRB has been given a statutory mandate by Dodd-Frank to regulate municipal advisors. In seeking to fulfill its mandate, the MSRB issued draft rules, sought public comment, and took into account the potential scope of the SEC's proposed definition of municipal advisor. However, the MSRB is concerned that because the SEC's definition has not been finalized, some firms and individuals will not participate in the SEC comment process on the MSRB proposals.

The MSRB stated that its rulemaking process for municipal advisors will continue. Once the SEC adopts a definition of municipal advisor, the MSRB will resubmit its rule proposals to the SEC for approval.

SEC proposes conflict-of-interest rules for issuers of asset-backed securities

On September 19, 2011, the SEC voted to propose a rule intended to prohibit certain material conflicts of interest between those who package and sell asset-backed securities (ABS) and those who invest in them. The SEC noted that as the securitization process has grown more complex, certain persons may in some circumstances engage in a range of activities and transactions that give rise to potential conflicts of interest, and that the existence and potential effects of conflicts of interest in that process have received increased attention.

The proposal would implement Section 621 of Dodd-Frank, which adds new Section 27B to the Securities Act of 1933. Section 27B prohibits an underwriter, placement agent, initial purchaser, or sponsor, or any affiliate or subsidiary of any such entity (collectively "securitization participants") who create and distribute an ABS, including a synthetic ABS, from engaging in transactions that would involve or result in a material conflict of interest with respect to any investor in the ABS for one year after the date of the first closing of the sale of the ABS. The prohibition applies to registered and unregistered offerings of ABS.

The proposal largely tracks the statutory language of Section 27B and, as required by Dodd-Frank, provides exemptions for three categories of activities: risk-mitigating hedging activities, liquidity commitments, and bona fide market-making.

However, the proposed rule does not define the term "material conflict of interest." Instead, the SEC has proposed a two-part test to determine whether a transaction would involve a "material conflict of interest." The first prong of the test asks (1) whether a securitization participant to the transaction would benefit directly or indirectly from the actual, anticipated, or potential decline or loss in the value of the relevant ABS; or (2) if a securitization participant who directly or indirectly controls the structure of the ABS would benefit from fees, other forms of remuneration, or future business as a result of allowing a third party to structure the relevant ABS. The second prong of the test evaluates whether there is a substantial likelihood that a reasonable investor would consider the conflict important. If a transaction's conflict of interest meets both prongs, it is "material" and thus would be prohibited under the proposed rule.

Comments should be submitted to the SEC by December 19, 2011.

CFTC adopts whistleblower rule

In August, the CFTC adopted a final rule to implement its whistleblower program as established by Dodd-Frank. The final rule amends Section 23 of the Commodities Exchange Act (CEA) to require the CFTC to pay an award, subject to certain limitations, to eligible whistleblowers who voluntarily provide the CFTC with original information about a violation of the CEA that leads to the successful enforcement of a covered judicial or administrative action, or a related action. The rule also prohibits retaliation by employers against individuals who provide the CFTC with information about possible CEA violations.

In adopting the rule, the CFTC endeavored to harmonize its whistleblower rules with those of the SEC, and made certain revisions. Like the SEC whistleblower rules, the CFTC has chosen not to require whistleblowers to report information internally to a company in order to be considered for an award. In addition, the CFTC streamlined its procedures for submitting information and claims by combining the two proposed forms into one form. Finally, the final rules provide greater clarity and specificity about the scope of the exclusions applicable to senior officials within an entity who learn information about misconduct in connection with the entity's processes for identifying, reporting, and addressing possible violations of law.

The rule becomes effective October 24, 2011. The SEC's whistleblower rule, discussed in last quarter's newsletter, became effective August 12, 2011.

US Department of Labor to re-propose rule defining fiduciary

In response to requests from Congress and the public, the US Department of Labor's Employee Benefits Security Administration (EBSA) announced it will re-propose its rule on the definition of fiduciary in order to allow members of the public an opportunity to provide additional input into the rule.
The proposed rule would have imposed a fiduciary duty on financial professionals who provide advice to companies regarding their employee retirement plans.

EBSA's proposal would amend a 1975 regulation that sets forth a five-part test used to determine whether a person providing "investment advice" becomes a fiduciary under the Employee Retirement Income Security Act. According to EBSA, the agency anticipates revising certain provisions of the rule proposal, including clarifying that fiduciary advice is limited to individualized advice directed to specific parties, responding to concerns about the application of the regulation to routine appraisals, and clarifying the limits of the rule's application to arm's length commercial transactions, such as swap transactions. EBSA also plans to draft exemptions addressing concerns about the impact of the new regulation on the current fee practices of brokers and advisors, and clarify the continued applicability of exemptions that allow brokers to receive commissions in connection with mutual funds, stocks, and insurance products.

EBSA expects to issue the new rule proposal in early 2012.

New proposed regulations address swap issues

Key development

On September 15, 2011, the Internal Revenue Service (IRS) and Treasury released proposed regulations that address the tax characterization of certain swap transactions.

Why it's important

Properly characterizing swap contracts for tax purposes is critical for regulated investment companies (RICs). The tax characterization of a swap dictates the time at which income or loss is recognized with respect to the contract and the tax character (e.g., capital or ordinary) of the recognized income or loss. Thus, for each swap entered into by a RIC, the resolution of this question directly impacts the amounts a RIC must distribute to maintain compliance with the RIC distribution requirements.

The proposed regulations suggest a number of changes that, if adopted in final regulations, would impact the tax characterization of certain swaps. Significant changes proposed in the regulations include:

- Credit default swaps would be characterized as notional principal contracts. The IRS and Treasury have been formally studying the proper tax characterization of credit default swaps since 2004. In the absence of guidance, taxpayers have characterized these contracts in a variety of ways. RICs have most commonly characterized credit default swaps as notional principal contracts or as put options. A significant difference between the two approaches is the tax accounting of the payments made or received for protection. If the proposed regulations are adopted, RICs that did not previously treat credit default swaps as notional principal contracts will likely need to change the tax treatment of these payments.

- The definition of notional principal contracts would be modified in a way that expands the population of transactions that fall under these rules. The tax accounting for transactions that provide for only one payment at the end of the contract, otherwise known as bullet swaps, could be significantly impacted by this change. Under current law, these transactions are not notional principal contracts and gain or loss from these contracts is typically not recognized until the maturity or termination of the contract. Furthermore, income or loss from these transactions is capital in nature. For certain bullet swaps, this would change if the proposed regulations are adopted, perhaps making these contracts less attractive from a tax perspective.
- Swaps that are traded on an exchange are notional principal contracts and not Section 1256 contracts. This rule was set forth as part of the Dodd-Frank Act and the proposed regulations add further clarity to this point.

The rules would apply to contracts entered into on or after the date the final regulations are published. Taxpayers interested in submitting comments on the regulations must do so by December 15, 2011.

Implications

The management of mutual funds that enter into swaps should consider assessing how the proposed regulations would affect their current characterization of the contracts. If a significant impact is anticipated, management could consider exploring future alternatives for structuring swaps that minimize the consequences to a RIC.

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

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

On August 31, 2011, the SEC issued a concept release Use of Derivatives by Investment Companies under the Investment Company Act of 1940. The SEC and its staff are reviewing the use of derivatives by management investment companies registered under the Investment Company Act of 1940 (the Investment Company Act or Act) and companies that have elected to be treated as business development companies (BDCs) under the Act (collectively, funds). To assist in this review, the SEC is issuing this concept release and request for comments on a wide range of issues relevant to the use of derivatives by funds, including the potential implications for fund leverage, diversification, exposure to certain securities-related issuers, portfolio concentration, valuation, and related matters. In addition to the specific issues highlighted for comment, the SEC invites members of the public to address other matters that they believe are relevant to the use of derivatives by funds. The SEC intends to consider the comments to help determine whether regulatory initiatives or guidance are needed to improve the current regulatory regime for funds and, if so, the nature of such initiatives or guidance. Responses to the concept release are due by November 7, 2011.

On May 12, 2011, the FASB issued ASU 2011-04, Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in US GAAP and IFRS. 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.

Auditing matters from the PCAOB, AICPA, and SEC

On August 16, 2011, the PCAOB issued a concept release to solicit public comment on ways that auditor independence, objectivity, and professional skepticism could be enhanced. One possible approach on which the board is seeking comment is mandatory audit firm rotation, which is explored in detail in this release. However, the board seeks advice and comment on other approaches as well. Comments are due by December 14. 2011.

On June 21, 2011, the PCAOB issued a concept release to discuss potential changes to the auditor's reporting model. The concept release requests feedback on alternatives for changes to the auditor's reporting model that could provide investors and other users of financial statements with more transparency related to the audit process and increase the auditor's involvement with information presented outside of the financial statements. These alternatives include:

(1) A supplement to the auditor's report, such as an Auditor's Discussion and Analysis, in which the auditor provides additional information about the audit and views regarding the company's financial statements

(2) Expanded use of "emphasis paragraphs" in the auditor's report to highlight areas of critical importance to the financial statements. This might include expanded discussion of significant management judgments and estimates, areas with significant measurement uncertainty, and other areas that the auditor determines are important for a better understanding of the financial statement presentation

(3) Auditor reporting on information outside the financial statements, such as management's discussion and analysis, non-GAAP information, or earnings releases

(4) Clarification of certain language in the auditor's report (e.g., the meaning of reasonable assurance), and the auditor's responsibilities relating to disclosures, fraud, and other information presented outside of the financial statements

Comments were due by September 30, 2011, and a public roundtable was held on September 15, 2011.

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 SEC 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 SEC to pay an award, under regulations prescribed by the SEC and subject to certain limitations, to eligible whistleblowers who voluntarily provide the SEC 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 SEC 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.

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

Independent Directors Council/Affiliates

(www.idc1.org)

Board Oversight of Subadvisers, January 2010

The report discusses the business reasons for retaining a subadvisor and the industry trends in the use of subadvisors. The report also explores board oversight of subadvisors, starting from the time a principal advisor recommends hiring a subadvisor, through board approval of the subadvisory agreement, and ongoing board oversight of the subadvisor, to possible termination of the subadvisor. 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.

Navigating Intermediary Relationships, October 2009

Intermediaries such as broker-dealers, fund supermarkets, and financial advisors provide important distribution and other services to mutual funds and their shareholders. This paper describes the important roles of these intermediaries in the mutual fund industry and discusses ways their roles evolve with the changing business and regulatory environment. Appendix H provides examples of high-level potential board questions for fund management concerning these relationships.

Board Oversight of Fund Compliance, September 2009

The task force report's goal is to provide fund board members and others a comparison of the various practices used by funds to structure, evaluate, and pursue compliance. It is designed to assist them in evaluating compliance.

SEC Valuation Guidance Compendium, July 2009

The Investment Company Institute created a new site to capture SEC valuation guidance that applies to mutual funds when they calculate net asset values at which capital share purchases and redemptions are transacted. The Institute intends to keep the site evergreen, with the latest comprehensive SEC valuation information for investment companies.

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

To the Point: Current Issues for Board of Directors, September 2011

This edition addresses the recent developments on proxy access and how boards can prepare for the possibility of "private ordering" proxy access. It also presents an examination of auditor rotation and explores how directors are using more technology in the boardroom.

US Asset Management – The State of the Industry, August 2011

Faced with recovering but volatile markets and regulatory change, asset managers are striving to maximize the performance parameters they can control. With asset flows generally improving, firms are focused on operational excellence, growth, performance, people-related issues, governance, risk, and compliance.

This paper explores what we believe to be among the key challenges facing the industry, as it continues to grapple with a number of difficult issues, including product development, evolving investor expectations, merger & acquisitions, global tax risk, global sourcing, tax optimization, performance measurement, talent management, and regulatory change (including Dodd Frank, FATCA, and more).

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 support 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. Equally important, 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 are 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: Creating a Market-Ready ETF Operating 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 investors and sponsors alike 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 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 timeline 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 two 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 advisors 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 US GAAP and IFRS. 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 timeline are realistic. PwC believes that, despite the recently announced modified strategy for certain projects, the timeline 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 advisors and investment companies are required to have compliance programs pursuant to rules of the SEC, 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 advisor compliance programs. The separate regulatory requirements governing advisors' 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.

SEC

www.sec.gov

Valuation of Portfolio Securities and other Assets Held by Registered Investment Companies – Select Bibliography of the Division of Investment Management, March 2009

This bibliography lists relevant provisions of the Investment Company Act of 1940, its rules, SEC releases, staff guidance, and enforcement actions related to securities valuation. Directors, legal counsel, and others may find this information useful when researching the SEC's positions on valuations.

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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