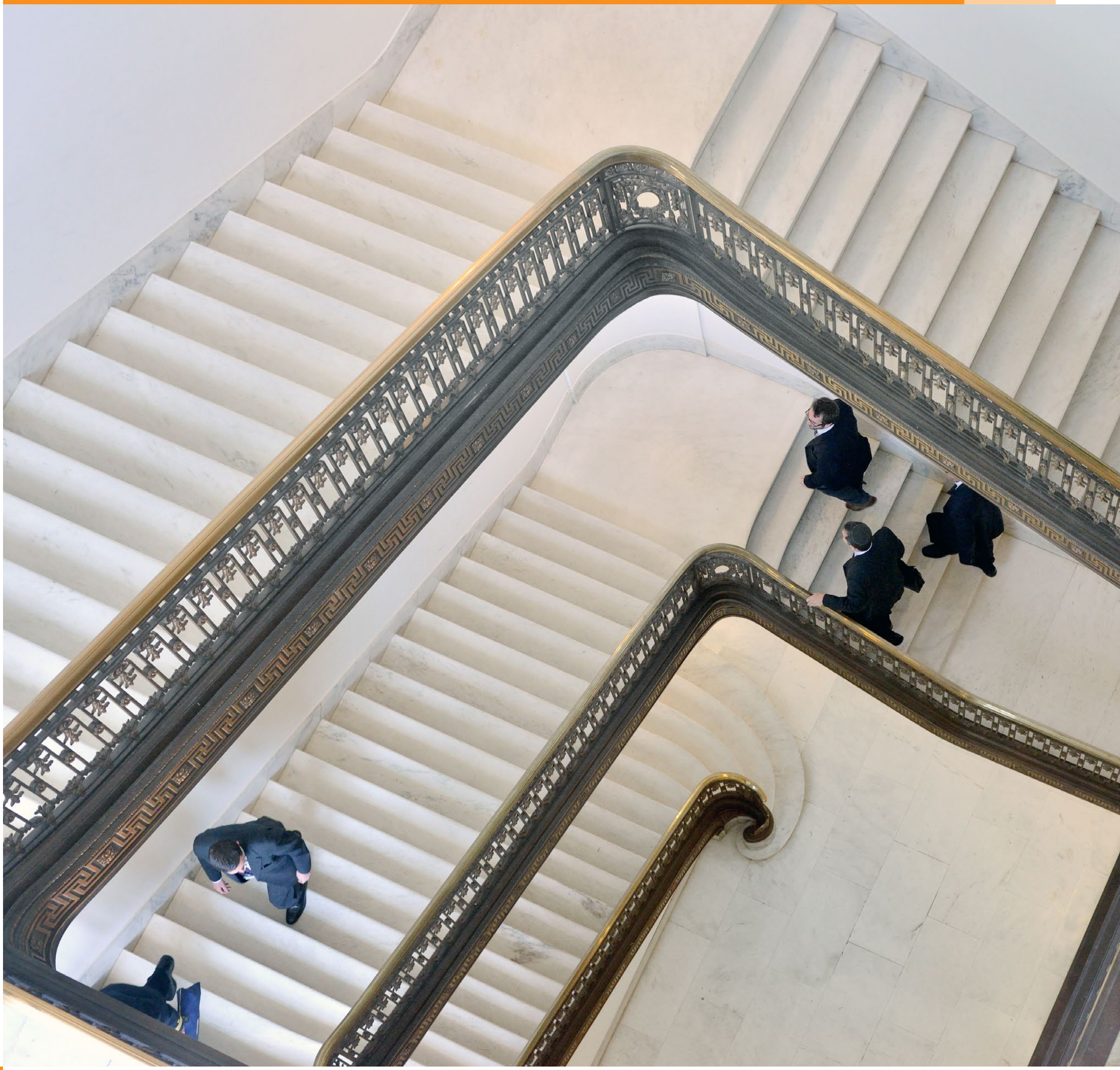
Current developments for mutual fund audit committees

A quarterly summary

June 30, 2014



Introduction

Dear clients, colleagues and friends,

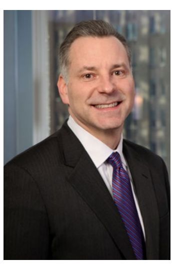
We are pleased to provide you with the most recent Current Developments for Mutual Fund Audit Committees – quarterly summary.

The latest compilation of PwC articles and observations on developments for the three months ending June 30, 2014, includes the following topics:

- Money market fund reform developments
- Liquid alternatives – Operational and regulatory considerations
- FATCA – Mutual funds may need to identify a responsible officer for certain non-US entities
- Investment spotlight on sovereign debt
- Summary of developments and articles of interest

We hope that you will find this material to be informative. If you have questions or would like additional information, please contact any of our subject matter specialists noted in the publication.

We would like to hear from you! In an effort to bring you insights on the topics that matter to you most, we invite you to provide feedback on topics we are considering for the next issue. ***Click here to provide feedback.***



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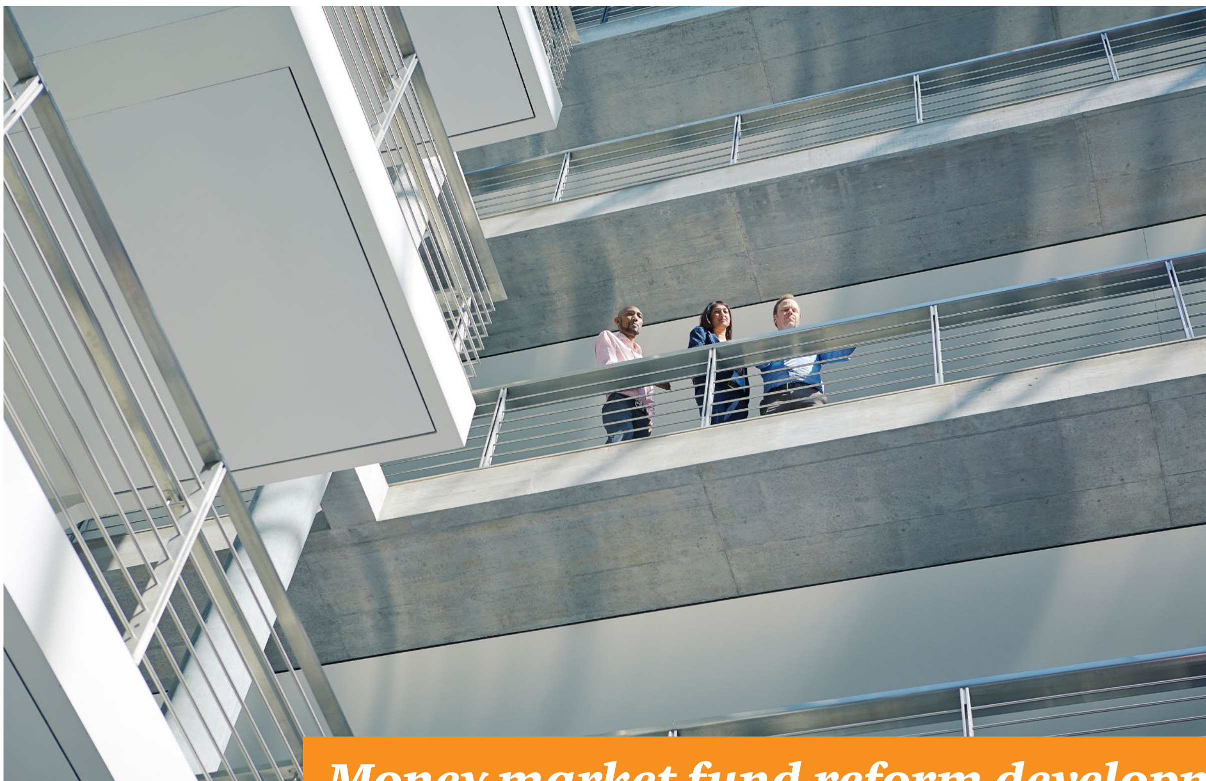

Money market fund reform developments

Liquid alternatives – Operational and regulatory considerations

FATCA – Mutual funds may need to identify a responsible officer for certain non-US entities

Investment spotlight on sovereign debt

Money market fund reform developments

At a glance

The current operations of institutional prime money market funds will be significantly impacted by new SEC rules, and all non-governmental funds will need to comply with new liquidity fee and gate redemption provisions. However, the rules are not expected to alter the designation of money market funds as cash equivalents.

After six years of debate over the risks and operations of money market funds (MMFs) – and events such as the fall of Lehman Brothers, breaking the buck at the Reserve Primary Fund, rancor between financial regulators, and over one thousand industry comment letters – the SEC finally adopted MMF reform on July 23, 2014. The final rules will fundamentally alter certain aspects of MMF operations and accounting and the way these funds are viewed by investors.

The final rule combines approaches set forth in the SEC's proposal last summer to: (1) require institutional prime MMFs to float their Net Asset Values (NAV) and (2) provide tools to all MMF boards to discourage and prevent runs by investors through the use of redemption fees and gates. A key necessity for reaching the SEC's 3-2 vote in favor of the rule was the Treasury Department's and IRS's concurrent issuance of rule proposals mitigating the tax compliance and accounting costs for institutional prime MMFs and their investors (whose investments will be subject to a floating NAV).

SEC-registered MMFs are a $2.5 trillion[1] plus business in the US (measured in terms of assets under management). These funds are popular with retail and institutional investors as a safe haven for cash, and have historically returned slightly better yields than other cash-equivalent products. Much of their popularity is owed to their accounting treatment under Investment Company Act Rule 2a-7, which has allowed these funds to maintain stable net asset values (NAVs), typically $1.00 per share, by valuing portfolio investments at amortized cost rather than at market value. In return for this accounting accommodation, MMFs must adhere to strict risk-limiting conditions around portfolio credit quality, maturity and liquidity.

The final rules will likely present substantial operational and business challenges for MMFs and non-registered MMF-like products that currently reference SEC rules in their legal documents. On top of the obvious business pressures caused by the current low interest rate environment and the fee subsidies that most MMF sponsors currently provide, existing and future sponsors will have to decide whether it will be economically viable to manage MMFs. The floating NAV requirement may drive institutional prime MMF shareholders to move their cash to government MMFs or non-MMF alternatives that offer reasonable principal protection and slightly higher yield. This would likely cause industry repositioning as traditional sponsors – and new market entrants – innovate new products to meet investors' short-term cash management needs. Furthermore, institutional prime MMF advisers may decide that Rule 2a-7's risk-limiting provisions are not worth the headaches without the availability of the stable NAV their funds have traditionally enjoyed. While some fund groups may stop offering or advising MMFs, others will likely conclude that MMFs are a part of a full suite of fund offerings that they will need to maintain. Some fund groups may separate funds which currently have both retail and institutional share classes. Thus, they will need to take the necessary steps to meet the final rules' requirements and work through their implementation. The SEC's Division of Investment Management has formed a working group to monitor the rules' impact and consider pragmatic solutions to assist with implementation challenges. There may be opportunities for engagement with SEC staff to work through these issues.

This article summarizes the final rules and provides practical considerations.

Final rules

Floating net asset value

Institutional prime MMFs, including institutional municipal MMFs, will be required to float their Net Asset Values (NAV) and value their portfolio investments each day based on market values. These MMFs will be required to calculate their NAVs and process share transactions out to the nearest 1 basis point (1/100th of a percent). For example, an MMF attempting to maintain a price near $1/share would calculate NAV out to four decimals ($1.0000), and an MMF

1 Source: ICI Research & Statistics for June 2014

maintaining a price near $10/share would calculate NAV out to three decimals ($10.000). Amortized cost accounting will no longer be permitted for institutional prime MMFs.

Instead of distinguishing between retail and institutional MMFs based on maximum daily redemptions allowed (as proposed), a "retail MMF" will be one that has policies and procedures reasonably designed to limit its shareholders to natural persons. This change meets an industry request, but funds will likely still have to work with omnibus account holders (e.g., brokers and pension administrators) to make this definition workable. The final rule defines a "government MMF" as one that invests at least 99.5% (increased from 80% in the proposal) of its total assets in government securities, cash, or repos that are collateralized solely by government securities or cash. This significant decrease in the ability to invest in non-government securities will impact investment strategies and returns for these funds. In addition, the SEC stated its position that funds will be able to undertake one-time reorganizations to distinguish between retail and institutional MMFs without seeking separate exemptive relief from the Commission.

NAV calculations and transaction processing based on amortized cost accounting will still be allowed for MMFs other than institutional prime MMFs (the SEC proposal would have done away with amortized cost accounting for all MMFs). This will allow intra-day NAV calculations and settlements, thus permitting retail and government MMFs to continue offering desirable features like check writing and ATM withdrawals. The SEC's logic in maintaining these exemptions is that in times of stress investors have typically run towards government MMFs and not from them. These funds hold securities that trade in deeply liquid markets and are the type of securities that are sought after in a crisis. In addition, the SEC noted that most of the run activity in 2008 involved institutional and not retail investors.[2]

Liquidity fees and gates

The final rules provide tools to all MMF boards to discourage and prevent runs by investors through the use of redemption fees and gates.

Once an MMF's weekly liquid assets decline to less than 30% of total assets (the regulatory minimum, as opposed to 15% in proposal), an MMF board would be able to institute up to a 2% fee for withdrawing funds (i.e., a liquidity fee), and/or halt redemptions (i.e., impose a gate) for up to 10 business days in a 90 calendar day period (instead of a maximum of 30 business days as proposed). The SEC views the change in percentage for weekly liquid assets to 30% as giving more flexibility to MMF boards and making it more difficult for shareholders to out-guess and front-run the timing of board decisions. The hope also is that the shorter maximum gate of 10 business days will reduce run incentives. However, the MMF's board would retain discretion to not take these actions or, in the case of liquidity fees, to impose a smaller fee.

A 1% default redemption fee would be required if weekly liquid assets fall below 10%, but the board would still have the ability to waive, increase, or decrease this fee upon determination of what fee (if any) is in the best interest of the MMF and its shareholders. The default rate changed from 2% to 1% as requested by many commenters on the SEC proposal.

Upon falling below the 10% weekly liquidity threshold and the imposition or removal of any liquidity fee or gate, an MMF would have to make prompt public disclosure, whether or not its board decides to impose a liquidity fee or gate. The fund would also have to disclose the reasoning for the board's actions or decision not to act. Government funds can still opt into the gates and fees provisions if this is disclosed to investors.

The SEC's logic behind the liquidity fees and gates proposal is that investors may redeem for reasons other than "first mover advantage" or try to redeem shares at $1 that are worth less than $1. Fees may take away incentives for redemptions in times of stress when it is costly for funds to raise liquidity, and/or compensate funds for providing liquidity in stress periods. Redeeming investors would have to decide whether immediate access to their funds is worth the cost, and such fees will require those redeeming to share costs and potential losses with remaining investors. Retention of the fees can also help funds repair damaged NAVs. The SEC has also indicated that gates are designed to buy time, let panic subside, and raise liquidity in an orderly fashion. In addition, gates may motivate MMF sponsors to monitor investor concentration and transaction behavior.[3]

2 Money Market Fund Reform; Amendments to Form PF, Investment Company Act Release No. 31166, Pg. 30 (July 23, 2014)
3 Money Market Fund Reform; Amendments to Form PF, Investment Company Act Release No. 31166, Pg. 50 (July 23, 2014)

Disclosure requirements

From an operations and fund administration standpoint, the new disclosures may present some of the most challenging compliance issues.

The new disclosures are intended for two purposes: (1) to assist MMF shareholders, particularly during times of market pressure, in distinguishing between MMFs based on transparent portfolio quality and stability (potentially decreasing the incentive to run); and (2) forcing market discipline on MMF advisers with the ability for investors to better discern the risk-reward profile of each fund.

Daily website disclosure of market- based NAV and liquidity

All MMFs will have to post daily information on their websites regarding their market-based NAV, the amount of daily and weekly liquidity contained in the portfolio, and net fund flows. Investors will be able to compare these key metrics across funds, and data organizations and analysts (e.g., Lipper, iMoneyNet, etc.) will likely use this information in their reviews.

Sponsor support

MMFs will have to report any current financial support received from affiliates on their websites, on new Form N-CR, and disclose a 10-year history of all such support in their SAIs not including any instances before compliance date. Sponsor support for a predecessor fund will not have to be disclosed when the fund is no longer advised by or affiliated with the entity that previously provided the support.

Event disclosure

MMFs will also be required to promptly disclose certain events on a new Form N-CR. Such material events include the imposition or removal of fees or gates together with the primary considerations by a board of directors in its decision; security defaults; sponsor or affiliate support, including information about the amount of support and reasons; and if the market-based NAV for retail and government funds falls below $0.9975.

Removal of 60-day delay in public availability of Form N-MFP

MMFs currently provide a wealth of information, at the fund and security level, on Form N-MFP, which is not released publicly until 60 days after the report date. The final rules will make information filed on Form N-MFP available immediately to the public.

Cash equivalent assessment

The SEC noted that under normal circumstances, qualifying money market funds with floating NAVs will continue to be reported as cash equivalents. However, in the event credit or liquidity issues arise, including the increased potential for enactment of liquidity fees or redemption gates, investors will need to assess the validity of continuing to account for such money market funds as cash equivalents.

Diversification

The new rules further tighten the diversification requirements in Rule 2a-7 in several respects as described below.

Aggregation of affiliated issuers

Rule 2a-7 does not currently require an MMF to aggregate affiliated exposures when measuring compliance with diversification tests for issuers and demand/guarantee providers. Thus, while affiliated issuers may be separate legal entities, the valuation of their securities may depend on cross-group guarantees. Under the final rules, an MMF will have to aggregate affiliated issuers (defined as entities in a 50% control relationship with each other) for purposes of the 5% issuer diversification limit.

Inclusion of asset-backed security sponsors as guarantors

Rule 2a-7's diversification provisions do not require diversification of exposure to asset-backed security (ABS) sponsors even though MMFs may rely on the ABS sponsor for liquidity and other support and make investment decisions assuming that support will be forthcoming in the event of default. Thus, the final rules will require MMFs to treat the sponsors of special purpose entities issuing ABS as a guarantor subject to Rule 2a-7's diversification limits on guarantors/demand feature providers. An exception would be provided where the MMF's board (or its delegate) has determined that the fund is relying on other factors besides the ABS sponsor's financial strength to determine the ABS's credit quality. This determination would have to be documented and periodically re-evaluated.

Diversification of guarantors and demand-feature providers

Currently, MMFs cannot have more than 10% of their assets issued by, or subject to, guarantees or demand features from a single entity. However, this rule applies with respect to only 75% of an MMF's assets, meaning that for the remaining 25% of a fund's assets, a fund could concentrate its reliance on issues, guarantees or demand features from a single entity. The final rules eliminate this 25% basket and apply the 10% limit to all fund assets. However, municipal MMFs will be allowed a 15% basket for a single guarantor.

Stress testing

As part of the amendments to Rule 2 a-7 in 2010, the SEC required MMFs to periodically test their ability to transact at stable NAVs by conducting what-if analyses assuming changes in short-term interest rates, increases in shareholder redemptions, a downgrade of portfolio securities, or a change in yield spreads. The final rules further enhance these requirements.

A key focus of required stress testing will now be on the MMF's ability to maintain weekly liquid assets of at least 10% of all fund assets, consistent with the new redemption fee threshold.

Effective dates of final rules

The following dates will apply for effectiveness of the final rules:

- MMFs have 2 years from the date of adoption to implement the floating NAV and fees/gates requirements
- MMFs have 18 months from the date of adoption to implement additional requirements for diversification, stress testing, disclosure, and reporting (Form PF and Form N-MFP)
- MMFs have 9 months from the date of adoption to implement requirements for reporting material events on a new Form N-CR

Practical considerations

Noted below are practical considerations related to the final rules:

Operational considerations

Floating NAV

Many MMF sponsors already post daily market-based NAVs on their websites. Fund managers and boards will need to be prepared to fair value portfolio holdings during times of market stress, taking into account that stressful markets for short-term securities may not reflect the fair value of portfolio securities whose issuers are reasonably likely to pay at maturity, and pricing vendors may not be able to provide meaningful prices.

Current accounting and processing applications used to track MMF investments are not compatible with floating NAVs, and many may not be able to handle NAVs computed to four decimal places. Thus, institutional investors and service providers will be required to re-program their systems or manually reconcile MMF transactions, increasing staffing costs.

Liquidity fees and gates

The SEC states, and industry observers agree, that only in the most extreme circumstances will MMFs move below the 10% weekly liquidity threshold (the SEC supports this claim with analysis of historical data on Form N-MFP). Thus, from an operational perspective, effort and cost will be directed toward setting up systems, controls, confirmations and reports that are capable of accurately implementing fees and gates, but a real-world test of such systems and controls may only come with the next market crisis. That said, it may be beneficial for firms to consider safe harbor triggers that would initiate further analyses and discussions with the board prior to an actual liquidity event.

Tax considerations

Floating NAV

A switch from a stable to a floating NAV could result in the recognition of small tax gains and losses upon the redemption of MMF shares. After the release of the initial proposal last summer, the SEC received several comments indicating a floating NAV could lead to an overly burdensome tax compliance process. Understanding these tax concerns, Treasury and the IRS released guidance simultaneously with the SEC's final rule on MMF reform. There are two separate pieces of guidance, both aimed at alleviating significant tax concerns associated with the new rule.

The first piece of guidance is proposed regulations that would simplify the method of accounting for tax gains and losses realized on shares of a floating NAV MMF. The proposed regulations address a concern that migrating MMF accounts to existing systems that track tax lots and calculate gains and losses would be too costly to implement. The proposed regulations respond to these concerns and outline a newly prescribed method of accounting for shareholders in a floating NAV MMF (the "NAV Method"). Under the NAV Method, all transactions in a computation period, which could be the investor's taxable year or another shorter period, would be aggregated to arrive at a single gain or loss amount. This is much simpler than prior law that requires calculating gains and losses and tracking tax basis lot by lot. The tax character (ordinary or capital) of the net gain or loss would depend the character of the underlying MMF shares to the investor. Once an investor has elected to use the NAV Method, it must be used for all floating NAV MMFs in which it invests. The proposed regulations also provide relief for the reporting of such gains and losses to shareholders by extending the exception for information reporting requirements, such as reporting cost basis and corporate actions, to floating NAV MMFs.

The other significant tax concern resulting from a floating NAV was the potential for MMF investors to be subject to the tax "wash sale" rules. Along with the SEC's initial proposal, the IRS proposed guidance that would create a de minimis exception to the wash sale rule for MMFs. In response to the proposed rule, the Investment Company Institute (ICI), on behalf of the industry, argued that a full exemption from the wash sale rules for MMFs would be more appropriate.[4] Heeding this, the IRS released a revenue procedure that excludes floating NAV MMFs from the wash sale rules. The revenue procedure will be effective for redemptions on or after the effective date of the SEC MMF Reform Rules.

Liquidity fee

Although the consensus is that they will only be implemented in extreme situations, liquidity fees may create novel tax concerns. After the release of the initial proposal, the tax characterization of liquidity fees as an item of income or capital was a key question. The ICI requested the Treasury to provide guidance that the fees are excluded from taxable income.[5] While the SEC mentioned that the fees should be treated as such in the issuance of the final rule, no further guidance has been issued from Treasury or the IRS to date. Even if liquidity fees are excluded from taxable income, a MMF may be forced to distribute these amounts in order to avoid "breaking the buck" on the upside. Such a distribution would likely be treated as a tax return of capital. As a return of capital reduces a shareholder's basis in his or her shares, it could require tracking of tax basis and result in small gains upon the redemption of the shares. In light of this scenario, the ICI previously requested that Treasury issue guidance under which any distribution from a MMF that is attributable to liquidity fees be treated as ordinary income to shareholders. Although the SEC did suggest this treatment along with release of the final rules, the tax authorities have yet to issue guidance on this topic. Instead, the proposed regulations would allow for stable NAV MMFs to employ the NAV Method, as outlined above, to the extent they would recognize gain or loss as a result of liquidity fees. Treasury and the IRS have specifically requested comments on whether the NAV Method should be available to stable value MMFs that impose a liquidity fee.

A hearing on the proposed regulations has been scheduled for November 19, 2014 and any comments are due by October 27. MMF managers and advisors should consider the impact of the proposed regulations and assess whether it is in their interests to submit comments to the IRS.

4 ICI letter to Lisa Zarlenga and Michael Novy RE: Notice 2013-48 – Proposed De Minimis Exception to Wash Sale Rule Date, September 12, 2013

5 ICI letter to Lisa Zarlenga and Michael Novy RE: SEC Proposals for Money Market Reform – Liquidity Fee Tax Issues, September 12, 2013

Governance considerations

There are additional policy and procedure, oversight and documentation responsibilities that coincide with the adoption of the final rules. New or revised polices (for example, those associated with the adoption of liquidity fees and gates for certain retail money market funds) will need to be supplemented by more detailed operating, compliance and oversight procedures that consider:

- Marketing materials (including social media and website disclosures) and/or offering documentation;
- Implications of omnibus account holders in the funds, including the associated agreements with financial intermediaries (and steps associated with revised responsibilities associated with the imposition and monitoring of liquidity fees and gates);
- Monitoring and oversight of the business process and technology changes – such as the administration of liquidity fees and gates and four decimal place pricing; and
- Updating learning and education activities.

Finally, as we have seen in other situations, inadequately documented processes tend to raise more questions from stakeholders (e.g., directors, regulators), which will then require further steps and allocation of resources. It is important that sufficient documentation be maintained to provide a comprehensive and transparent view of the funds' processes.

Considerations for mutual fund directors

The final rules will present substantial operational and business challenges for funds as described in this article. In evaluating the adequacy of management's response to the final rules, there are a number of questions that directors should consider:

- Has management provided sufficient information regarding their strategic approach? Areas include:
    - » A clear business case that includes AUM and cost projections as well as definitions of the short- and long-term goals relative both to the organization as a whole and to the market and the competition;
    - » Key judgments made;
    - » Alternatives considered; and
    - » The message(s) the advisor is delivering to the market regarding the changes proposed – including the impact to the advisor's cash management business.
- Is there a clear plan for the business process and operational changes that need to take place, including capital investments?
- Has management prepared a framework for, and internal control over, developing valuations and disclosures; scenarios for stress testing; the imposition of liquidity fees and gates and the role and oversight of service providers?
- Are the operations (including those of the advisor and service providers) appropriately and adequately staffed and is there clear accountability?
- Are the current management systems and technology necessary to operate in place?
- How will management evaluate the design of stress testing and valuation policies and procedures, including adherence to formal policies?
- What is the framework for the imposition of liquidity fees and gates? Areas for consideration include:
    - » A fund investor profile assessment (e.g. could the actions of a limited number of investors result in significant changes in liquidity levels);
    - » The establishment of safe harbor triggers that initiate discussions with the board;
    - » Response plans for changes in liquidity.
- Will there be situations where a security can be held in both an institutional prime money market fund and a retail money market fund? If so, how will potential valuation differences be addressed?

Liquid alternatives – Operational and regulatory considerations

Alternative mutual funds ("liquid alts") have experienced significant growth in recent years as investors continue to seek higher returns in the current low yield environment, while seeking protection against downside risk. Illustrating the scale of the growth, at the end of March 2014, US alternative mutual fund assets totaled more than $242 billion, approximately 1.9% of total long-term mutual fund assets under management, versus $176 billion at December 31, 2012.[1]

This growth in retail demand for liquid alts presents opportunity for both specialist alternatives managers and generalist mutual fund managers. But alternative funds have more complex investment strategies than traditional mutual funds, which in turn lead to greater product management risks. As a result, launching alternative mutual funds takes a significant amount of preparation across the investment management firm. Indeed, the entire cycle from product planning to launch might take up to two years – and this is one of the occasions when every function within the investment management firm has an important part to play.

In addition, as discussed in **PwC's Regulatory Brief: *SEC Sweep: Liquid alternative funds*** (June 2014), the Securities and Exchange Commission's ("SEC") examination staff has taken notice, and recently announced a coordinated review (or "sweep") of various liquid alts managers and funds. Several factors contribute to the SEC's interest in liquid alts. First, assets under management in liquid alts have surged in recent years.[1] Second, liquid alts are a relatively new product for retail investors, so their potential risks may not be well understood. Third, many alternative fund managers who advise or sub-advise liquid alts funds may have limited experience with the regulatory requirements of the Investment Company Act of 1940 (the "1940 Act"), which are applicable to mutual funds. Similarly, many investment advisors with experience in managing mutual funds under the 1940 Act may have limited experience with the alternative assets managed in liquid alts.

Firms may prepare not only for the upcoming SEC examination sweep, but also for long-term operations under closer SEC supervision. To that end, asset managers should prepare carefully before launching alternative investment funds, if they are to capitalize on their opportunity and minimize reputational risk. When doing so, asset managers may want to look into the following ten critical touch points:[2]

1. Preliminary vetting

Test how well clients receive the new products by performing focus groups with senior distribution professionals. Hire external research and subject matter experts to understand the market – i.e., what type of alternative investments are in demand, what would draw investors to the firm and what level of fund raising is realistic.

2. Investment process & products

Assess the investment opportunity and research competitors' alternatives products. Develop an investment philosophy and process; determine potential asset classes for inclusion and, in turn, the products to be constructed. Perform due diligence on these products, and develop an appropriate long-term strategy. Acting as a selector of external asset managers to act as subadvisor(s) requires additional due diligence, including ensuring that the external asset managers are able to comply with the rules and regulations of the Investment Company Act of 1940.

3. New product approval

Alternative investment products should be vetted through the traditional process used for investment strategies but should also include specific approval from other key stakeholders (such as risk management and compliance), senior management, and the Board of Directors. The Federal Reserve, SEC and FINRA expect to see evidence of this process. As alternative products are new for the retail buyer, they require greater due diligence by the new products committee, which focus on the reputational, regulatory and legal risks.

1 Figures are based on specific strategies classified as 'alternative' within the Strategic Insight Simfund MF database. Some industry observers use a wider definition, including strategies such as flexible global asset allocation and unconstrained global bond. If this broader definition is used, the magnitude to the 'alternatives' opportunity becomes much greater.

2 Source: PwC Global's *US retail alternatives: Ten significant touch points for success* (2014).

4. Regulatory "buy-in"

Given the complexity of these products, and the marketing to retail investors, the investment management firm may consider discussing the products with the SEC and FINRA in advance in order to obtain guidance, in addition to functional regulators. Regulators will be very interested in these products, helping to address any questions regarding suitability, sales process, supervision and record keeping.

5. Training and Internal Education

Management should roll out a training and education program for the sales force, supervisors and back-office personnel. A combination of portfolio specialists and compliance professionals may be the appropriate individuals to conduct this training.

6. Customer suitability

Management should build compliance with FINRA's Rule 2111, called the 'Suitability Rule', into every part of the process – including new product approval, training, marketing and surveillance. The rule requires an investment or strategy to be suitable for a customer based on his/her investment profile. If the firm acts as an investment adviser to the customer, it has a heightened fiduciary duty, including to disclose any potential conflicts of interest, and to ensure the financial advisor is recommending the best product for the customer.

7. Marketing & education

During the client marketing process, financial advisors must educate clients about the new products, including: the risks, the differences between the new products and 'traditional' mutual funds, and the fund's underlying investments. Management must be able to demonstrate the effectiveness of this education process.

8. Compliance and surveillance

Front-office supervisors (including branch compliance) and back-office compliance surveillance must understand the new products, their risks, how they fit in the customers' suitability profile and what red flags to be aware of. This requires extensive and well planned training. Management should also monitor the funds' investments to ensure that investments remain appropriate, meeting clients' objectives and risk tolerances.

9. Technology & operations

New alternative products might require new types of operational inputs and surveillance. Operations might be required to perform system updates to accept this new product (e.g., a new product code) and assess service providers (e.g., fund accounting/custody).

10. Transparency & valuation

Finally, transparency into the investment strategy and valuation of the investments that the fund holds create issues that should be addressed. Ensuring that the board understands the investment strategy and valuation processes should be a focus early on.

Areas of focus for fund boards

Given the growth of these products, and continued SEC scrutiny in this area, the following items may be of importance to the fund boards:

- **Education** – One of the areas the board may consider is to understand the education programs in place for each of sales and distribution; the back office; and risk management, in order to ensure that those who are selling and servicing the product understand the nature and risks.
- **Investment process and product selection** – The board may also consider the a) investment process employed in developing the product; b) its pro forma historical returns; c) the competitive landscape, i.e. other products that operate in the asset class; d) composition of the portfolio management team; e) valuation process for the product; f) importance of the transparency of the holdings; and, g) the profile of the prospective investors.
- **Technology, operations and compliance** – As discussed above, complex alternative products require a different or enhanced approach which may present a challenge or, at a minimum, require innovation in technology and operations, as well as broadened responsibilities in compliance. Specifically, taking a look at the fees being charged and the due diligence of any sub-advisors may be top considerations.

Given the growth trend of liquid alts addressing the touch points highlighted may help asset managers to prepare a path to success.

FATCA, Mutual funds may need to identify a responsible officer for certain non-US entities

Key development

In early 2014, the US Department of Treasury and the Internal Revenue Service (IRS) released the last substantial package of regulations necessary to implement the provisions of the Foreign Account Tax Compliance Act (FATCA Regulations). These regulations contain numerous changes with the impact varying depending on the products or services offered by funds and whether a fund's activities are onshore or offshore. Broadly speaking, the guidance provided is a compilation of many smaller changes and clarifications to previous issued FATCA regulations. However, a number of new responsibilities and requirements were introduced to the existing information reporting obligations for payments to US and non-US persons.

FATCA was enacted with the primary goal of providing the IRS with an increased ability to detect United States tax evaders concealing their assets directly in foreign accounts or indirectly through offshore entities. It aims to accomplish this goal by requiring US and non-US entities to comply with a new set of tax information reporting and withholding rules as well as investor due diligence and documentation requirements. The FATCA regulations will require a number of non-US or foreign financial institutions (FFIs), including foreign investment funds that a mutual fund may use in their structure (e.g., blocker corporations, master feeder structures), to register and in some cases sign an agreement with the IRS stating their willingness to report certain tax-related information, as well as periodically certify to the IRS their compliance with the provisions of FATCA. FFIs that are subject to the FATCA regulation and choose not to adhere to them or fail to register with the IRS will be subject to or liable for a 30% withholding tax on income from US sources, and eventually on the gross proceeds from the sale of certain US-registered securities.

The impact of intergovernmental agreements (IGAs)

In order to address local law restrictions related to complying with the FATCA regulations and to promote international tax compliance, the US has initiated intergovernmental agreements (IGAs) with over 75 countries. FFIs resident or established in a jurisdiction with a Model 1 IGA with the US are required to report information to their local tax authority that will then pass such information onto the US. FFIs resident or established in a jurisdiction that have signed a Model 2 IGA, will report information directly to the IRS. Generally, an FFI may be required to register with the IRS and obtain a Global Intermediary Identification Number. In order to register with the IRS, an FFI will need to designate an individual as a responsible officer (RO).

Understanding the role of the responsible officer

In FATCA parlance, the term RO has two meanings: 1) for an entity in a Model 1 IGA country, the person who has authority under local law to register the entity with the IRS and state that the entity and its branches will comply with FATCA, often referred to as the Registration Responsible Officer and 2) for an entity in a Model 2 or non-IGA country, the person that will ensure the entity complies with FATCA and will make required certifications to the IRS, commonly referred to as the Certification and Oversight Responsible Officer. The Registration RO and Certification and Oversight RO may be the same or different persons, but each comes with its own set of responsibilities discussed in more detail below.

Registration responsible officer

All entities required to register with the IRS will need to designate a Registration RO, regardless of location. The Registration RO is responsible for all entities required to register with the IRS and will also sign the form to register the entity with the IRS as an FFI.

By signing the form to register an entity, the RO certifies that:

- To the best of his or her knowledge, the information provided is accurate and complete, and
- The individual is authorized to agree that the FFI (including its branches, if any) will comply with its FATCA obligation either under the regulations, IGA or other administrative guidance.

Certification and oversight responsible Officer

FFIs that are not located or resident in a Model 1 IGA jurisdiction or exempted under the FATCA regulation will also need a Certification and Oversight RO who has sufficient authority to fulfill the duties of an RO as outlined in the FATCA rules. Duties of the Certification and Oversight RO require various certifications, which include:

- Certification of a participating FFI's compliance with due diligence requirements for pre-existing accounts (one time certification)
- Certification that a participating FFI did not have formal or informal practices or procedures to assist account holders in avoiding FATCA (one time certification)
- Certification of effective internal controls (tri-annual certification)

The importance of selecting the right RO

FATCA's rule are far reaching and complex, affecting many legal entities, lines of business, and various functions, all of which must be analyzed and potentially modified to achieve compliance. If an FFI fails to become FATCA compliant it will be subject to 30% withholding on any US source interest and dividends as well as proceeds from investments starting in 2017. Designating an employee as an organization's Registration or Certification and Oversight RO should not be taken lightly, as such person will play a critical role in maintaining compliance and avoiding the withholding penalty. The person chosen should have a broad view of the entity's operations, sufficient authority to enable compliance across a wide variety of functions, and the ability to implement change over functional areas that may be outside of his or her direct control. The organization must have an understanding of the type of authority required under local laws to register entities and support compliance by providing certifications. This may require board resolutions, powers of attorney or other documentation to grant sufficient authority to act on behalf of the entities with respect to their FATCA requirements.

In addition to reporting and certifying to the IRS, the RO should play a critical role in developing the organization's approach to FATCA compliance. An important decision for the RO will be to determine whether the organization will take a centralized or decentralized approach to compliance. The RO must consider the level of support needed to maintain strong internal controls and oversight. Some organizations have already determined that a support structure consisting of multiple competencies is needed, even though the requirement is one certification and oversight RO per FFI.

The take-away

While FATCA impacts many different functional areas and may involve many individuals, the ROs will be the main point of contact for the IRS. The RO will have the ultimate responsibility for an organization's compliance with the rules and ensuring the proper certifications are made timely. The individual(s) designated as RO will need to understand their respective roles in FATCA compliance as well as their company's expectations by selecting them for the role. It is important that an FFI identifies the right resource(s) to serve as RO to best position the organization to adhere to FATCA's regulations and avoid the withholding penalties.

Investment spotlight on sovereign debt

The Investment Spotlight series is a periodic look at types of investments which funds may use to achieve the investment goals outlined in fund prospectuses. We will ask a series of questions to not just look at the mechanics behind a specific investment, but also to consider why these investments may be held by funds and what the benefits and risks may be that directors/trustees should be aware of.

What is sovereign debt?

Bonds issued by a country's government as a method of financing the country's operations. Sovereign debt can be denominated in the government's local currency or another selected currency and is generally categorized as follows:

G20 – debt issued by 20 members (also known as the G20 and Group of Twenty): 19 countries plus the European Union. Collectively, the G20 members account for approximately 85% of the global gross domestic product and over 75% of global trade and two thirds of the population.[1]

G7 (G8 prior to March 24, 2014) – debt issued by 7 countries in the Group of Seven (G7), which is considered to have less risk than debt issued by a country outside of the G7.

Emerging markets – debt issued by emerging market nations, with social or business activity in the process of rapid growth and industrialization. This category typically encompasses debt issued by countries outside of the G7 and G20.

Frontier – a subset of emerging market debt, issued by smaller non-G20 nations that either are newly-growing or do not have a demonstrated record of economic growth. Many of these countries may have restructured their debt within the past 10 years.

Supranational – debt issued by an international organization or union not restricted to country boundaries, e.g. the European Union, the World Bank, International Monetary Fund, in which decision making responsibility is shared.

Why would a fund invest in sovereign debt?

A fund could invest in sovereign debt to achieve many particular strategies but generally investors are attracted to what they see as a positive risk/return tradeoff and diversification from domestic bond holdings. Like any potential investment, investors calculate potential returns and compare them with what they perceive as the risk. With interest rates near all-time lows in the United States over the past several years, investors have been looking at sovereign debt as a way to increase returns. Additionally, including sovereign bonds in an investment portfolio can provide geographic diversification and reduces exposure in case of a shock to the domestic economy.

Like domestic bonds, sovereign bonds have credit risk (risk that a country will not make all scheduled payments, due either to unfavorable economic trends, especially for commodity-based economies; political events; or "exogenous shocks" such as natural disasters or civil unrest), interest rate risk (risk that interest rates will rise, decreasing the value of the bonds) along with, in many cases, an added risk: currency risk – the risk that the currency that the bond is denominated in will lose value resulting in a loss when the bond holding is translated back to the investor's currency. A fund may have a strategy for exposure to credit risk, interest rate risk, and/or currency risk (or a combination of the three). By implementing a hedging strategy, with foreign currency forwards, credit default swaps, and/or interest rate swaps (or other various derivatives) one or more of those risks can be mitigated.

Debt from Emerging Markets may offer higher yields (as a result of lower credit ratings and higher currency risk), while on the other hand, debt from G7 and G20 countries may provide exposure to different markets and countries with less perceived credit risk.

How is sovereign debt traded and issued?

Sovereign debt investments trade over the counter (OTC) similar to US Debt, and require a fund to know who is making the market for a specific issuer. This OTC secondary market is common for most of the sovereign debt issued; however, some debt issued from emerging markets countries

1 https://www.g20.org/about_g20/g20_members

may trade less frequently, and could require a fund being part of a new issue in order to add it to its portfolio. Similar to some equity markets, countries may restrict who can hold its debt, and thus regulatory approval could delay a fund from being able to purchase the debt of a certain issuer.

How is sovereign debt valued?

Usually, a fund receives pricing information for sovereign debt holdings from third party pricing vendors, who provide an evaluated price using proprietary models. Generally, pricing vendors value sovereign debt using discounted cash flow models, incorporating option-adjusted spread (OAS) features as appropriate. In the OAS and non-OAS valuation models, benchmark curves for treasuries, swaps, and credit ratings with sufficient issuance are critical inputs to the evaluation process. The important thing to remember when utilizing pricing vendors to obtain valuations for sovereign debt is that the valuations are predominately model based. As such, an assessment of the inputs and assumptions utilized by the pricing vendor to arrive at the price should be undertaken.

What are the challenges to valuing sovereign debt?

- Many speculative grade/emerging Mmarket sovereigns don't have domestic yield curves or currency (FX) forwards
- For some countries, comparable US denominated bond yields and credit default swaps speak to credit risk but not to FX risk for bonds denominated in a local currency
- Cash flows are hard to model given lack of credit default swap and FX forward data for many countries
- Many funds rely solely on broker quotes (particularly for frontier debt, which can be highly illiquid). In those cases, funds may consider if back-up bids are available

What are the tax considerations related to sovereign debt investments?

In most countries, capital gain and interest income derived by non-resident investors from sovereign debt should not be subject to tax in the country of payment. Typically, it is taxed only in the investor's resident country. However, recently there has been an increasing trend in many countries to tax non-resident investors, especially when the investor is resident in a tax haven/low-tax jurisdiction. Consequently, adequate diligence on the potential tax implications of investing in sovereign debt should be undertaken prior to making the investment in order to avoid unforeseen tax implications.

What should directors consider related to sovereign debt?

1. Does the prospectus allow for investment in sovereign debt? If so, are there further limits based on credit or currency risk?
2. How does this investment, including credit and default risk of the issuing country, contribute to the investment objective of the fund?
3. Is currency risk part of the fund's objective? If not how is currency risk addressed?
4. Has the fund assessed the non-resident tax considerations of the investment?
5. Do the portfolio managers have sufficient prior experience in investing in sovereign debt?
6. Has risk management considered any political and social risks associated with the issuer?
7. How liquid are these investments, and are relevant risks e.g. those related to solvency and marketability included in the prospectus and financial statements?
8. To what extent does the fund plan to hedge some of the risks? Does management have sufficient experience in trading these vehicles?
9. When there are unique terms or structures, are the middle-office and back-office operations adequate to support the trading in, and recordkeeping of, sovereign debt?

Summary of developments for the six months ended June 30, 2014

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

On June 12, 2014, the FASB issued Accounting Standards Update No. 2014-11, *Transfers and Servicing (Topic 860): Repurchase-to-Maturity Transactions, Repurchase Financings, and Disclosures* (the "new standard"). The new standard amends the accounting guidance for "repo-to-maturity" transactions and repurchase agreements executed as repurchase financings. In addition, the new standard requires a transferor to disclose more information about certain transactions, including those in which it retains substantially all of the exposure to the economic returns of the underlying transferred asset over the transaction's term.

As a result of the new accounting guidance:

- Repo-to-maturity transactions will be reported as secured borrowings. Under current accounting rules, these transactions may qualify for sale accounting if certain conditions are met.
- Transferors will no longer apply the current "linked" accounting model to repurchase agreements executed contemporaneously with the initial transfer of the underlying financial asset with the same counterparty. Under the new standard, the accounting for each transaction instead will be evaluated on a standalone basis. This is expected to result in many of these repurchase agreements being reported as secured borrowings.

The new standard also requires additional disclosures by transferors for transactions that involve a transfer of a financial asset reported as a sale and accompanied by an agreement that results in the transferor retaining substantially all of the exposure to the economic returns of the transferred asset during the transaction's term.

In these circumstances, the transferor is required to provide the following information, by type of transaction (e.g., repurchase agreement, or a sale accompanied by a total return swap) outstanding at the reporting date:

- Carrying amount of the assets derecognized and the gross amount of proceeds received at the transfer date, and
- Related amounts reported on the balance sheet (e.g., carrying value of the total return swap)

The transferor is also required to provide information about its ongoing exposure to the economic return on the transferred assets, including a description of the arrangements and the risks associated with those arrangements.

With one exception, public business entities are required to apply the accounting changes and comply with the enhanced disclosure requirements for the first interim or annual reporting period beginning after December 15, 2014. However, for repurchase and securities lending transactions reported as secured borrowings, the new standard's enhanced disclosures are effective for annual periods beginning after December 15, 2014 and interim periods beginning after March 15, 2015. A public business entity may not early adopt the standard's provisions.

In all cases, an entity must report changes in accounting for transactions outstanding on the effective date as a cumulative-effect adjustment to retained earnings as of the beginning of the period of adoption. The new disclosures are not required for comparative periods prior to the effective date.

On May 28, 2014, the FASB and IASB issued their long-awaited converged standard on revenue recognition. The objective of the revenue standard is to provide a single, comprehensive revenue recognition model for all contracts with customers to improve comparability within industries, across industries, and across capital markets. The revenue standard contains principles that an entity will apply to determine the measurement of revenue and timing of when it is recognized.

On March 4, 2014, the FASB issued an exposure draft of the Conceptual Framework for Financial Reporting: Notes to Financial Statements (the "Proposal"). The Proposal is intended to make financial statement disclosures more effective and less redundant. It details a framework to be used by the FASB in its standard-setting activities for determining what information is relevant to the users of financial statements and should be included in the notes. The framework will not only be used as a basis for establishing future disclosure requirements, but can be used to evaluate existing disclosures. The exposure draft focuses on:

- The types of information to include in notes to financial statements
- Limitations on information in notes to financial statements
- Additional considerations for interim period disclosures

Comments were due by July 14, 2014.

Auditing matters from the PCAOB, AICPA, and SEC

On June 30, 2014, the PCAOB issued an updated standard-setting agenda, which provides a brief project overview of the board's current standard-setting agenda and outlines key milestones on various standard-setting projects.

On June 10, 2014 the PCAOB adopted Auditing Standard No. 18, *Related Parties* ("the standard") and also adopted amendments to certain PCAOB auditing standards that address the auditor's responsibilities with respect to a company's significant unusual transactions and a company's financial relationships and transactions with its executive officers ("the amendments"). The PCAOB adopted the standard and amendments substantially as they were re-proposed in May 2013 (the standard and amendments were originally proposed in February 2012).

The standard, which supersedes PCAOB interim standard AU 334, *Related Parties*, is designed to strengthen auditor performance requirements by setting forth specific procedures for the auditor's evaluation of a company's identification of, accounting for and disclosure of relationships and transactions between the company and its related parties. Among other things, the standard requires the auditor to:

- Perform specific procedures to obtain an understanding of the company's relationships and transactions with its related parties, including obtaining an understanding of the terms and business purposes (or the lack thereof);
- Evaluate whether the company has properly identified its related parties and relationships and transactions with related parties by performing procedures to test the accuracy and completeness of management's identification, taking into account information gathered during the audit;
- Obtain representation letter from management that all related party names, relationships and transactions have been disclosed to the auditor;
- Perform specific procedures if the auditor determines that a related party or relationship or transaction with a related party previously undisclosed to the auditor exists;
- Perform specific procedures regarding each related party transaction that is either required to be disclosed in the financial statements or determined to be a significant risk;
- Communicate to the audit committee the auditor's evaluation of the company's identification of, accounting for and disclosure of its relationships and transactions with related parties, and other significant matters arising from the audit regarding the company's relationships and transactions with related parties; and
- Inquire whether any member of the audit committee has concerns regarding relationships or transactions with related parties.

The amendments regarding significant unusual transactions revise PCAOB AU 316, *Consideration of Fraud in a Financial Statement Audit*, and other PCAOB auditing standards with the intent of strengthening the auditor's performance requirements for the identification and evaluation of these transactions. Among other things, the amendments require the auditor to:

- Perform specific procedures to identify significant unusual transactions and to obtain an understanding of, and evaluate, their business purpose (or lack thereof); and
- Consider additional factors in evaluating whether significant unusual transactions may have been entered into to engage in fraudulent financial reporting or conceal misappropriation of assets.

Other amendments modify Auditing Standard No. 12, *Identifying and Assessing Risks of Material Misstatement*, to require the auditor to perform specific procedures to obtain an understanding of the company's financial relationships and transactions with its executive officers, including compensation. The amendments do not require the auditor to make any determination regarding the reasonableness of compensation arrangements or recommendations regarding compensation arrangements.

The standard and amendments, if approved by the SEC, will be applicable to all audits performed pursuant to PCAOB standards. Pursuant to the JOBS Act, the standard and amendments will be subject to a separate determination by the SEC regarding their applicability to audits of emerging growth companies ("EGCs"). If approved by the SEC, the new standard and amendments will be effective for audits of financial statements for fiscal years beginning on or after December 15, 2014, including reviews of interim financial information within these fiscal years.

On May 7, 2014, the PCAOB issued a supplemental request for comment on its proposed framework for reorganization of PCAOB auditing standards and related amendments to PCAOB auditing standards and rules and reopened the comment period on the proposed reorganization which closed on July 8, 2014.

In February 2014, the AICPA Accounting Standards Board ("ASB") published Statement on Auditing Standards (SAS) No. 128, *Using the Work of Internal Auditors*. The standard was prepared as part of the ASB's effort to apply its clarity drafting conventions and to converge the SASs with International Standards on Auditing. SAS No. 128 addresses the external auditor's responsibilities if using the work of internal auditors. This includes (a) using the work of the internal audit function in obtaining audit evidence, and (b) using internal auditors to provide direct assistance under the direction, supervision, and review of the external auditor. SAS No. 128 is effective for audits of financial statements for periods ending on or after December 15, 2014.

Compliance and regulatory matters from the SEC and others

In June 2014, the SEC issued Investment Management Guidance Update, 2014-09, *Business Development Companies with wholly owned subsidiaries- asset coverage requirements*. Exemptive orders, issued by the SEC from time to time, can grant limited relief from asset coverage requirements. Subject to certain representations and conditions, the relief permits a BDC to treat certain indebtedness issued by its wholly owned subsidiary operating as a small business investment company as indebtedness not represented by senior securities for purposes of determining the BDC's consolidated asset coverage.

In June 2014, the SEC issued Investment Management Guidance Update, 2014-08, *Guidance regarding Mutual Fund Enhanced Disclosure*. This Guidance Update relates to the SEC's enhanced mutual fund disclosure amendments adopted in 2009. While this guidance does not specifically relate to compliance with Rule 498, it does relate to the content of Summary Prospectuses, through the disclosures contained in the Summary Section of the statutory prospectus.

In June 2014, the SEC issued Investment Management Guidance Update, 2014-06, *Series Investment Companies, Affiliated transactions*. This Guidance Update reminds mutual funds that are series companies about the importance of ensuring that their compliance policies and procedures are reasonably designed to prevent violations of the federal securities laws as they apply to each series. In particular, a mutual fund should review its compliance policies and procedures for the appropriate identification of "affiliated persons" with respect to each series of the mutual fund for purposes of transactions that may be prohibited under the 1940 Act.

In April 2014, the SEC issued Investment Management Guidance Update, 2014-05, *Deregistration of investment companies, applications on Form N-8F*. This Guidance Update identifies common comments on deregistration form N-8F and provides guidance for responding to these items.

In April 2014, the SEC provided via a risk alert additional information concerning its initiative to assess cybersecurity preparedness in the securities industry.

In March 2014, the SEC issued Investment Management Guidance Update, 2014-04, *Guidance on the testimonial rule and social media*. This Guidance Update considers registered investment advisers' use of social media and their publication of advertisements that feature public commentary about them that appears on independent, third-party social media sites. Through this guidance, the SEC staff seeks to clarify application of the testimonial rule as it relates to the dissemination of genuine third-party commentary that could be useful to consumers. Specifically, the SEC staff seeks through this guidance to assist firms in applying section 206(4) of the Investment Advisers Act of 1940 ("Advisers Act") and rule 206(4)-1(a)(1) thereunder ("testimonial rule") to their use of social media, and assist investment advisers in developing compliance policies and procedures. Consistent with previous guidance, the SEC staff believes that in certain circumstances, an investment adviser's or investment advisory representative's ("IAR's") publication of all of the testimonials about the investment adviser or IAR from an independent social media site on the investment adviser's or IAR's own social media site or website would not implicate the concern underlying the testimonial rule.

In February 2014, the SEC announced an initiative directed at investment advisers that have never been examined, focusing on those that have been registered with the SEC for three or more years. OCIE previously announced that examining these advisers is a priority in 2014. As part of the initiative, OCIE will conduct examinations of a significant percentage of advisers that have not been examined since they registered with the SEC. These examinations will concentrate on the advisers' compliance programs, filings and disclosure, marketing, portfolio management, and safekeeping of client assets.

In February 2014, the SEC issued Investment Management Guidance Update, 2014-03, *Multi-manager funds – aggregate advisory fee rate*. Under the multi-manager orders, among other requirements, the aggregate fee rate payable by a fund for advisory services, both primary and subadvisory (aggregate advisory rate), remains subject to fund shareholder approval. The staff periodically receives interpretive questions about circumstances that may or may not trigger an increase in the aggregate advisory rate and necessitate shareholder approval. The staff is issued this Guidance Update to assist funds in complying with this aspect of the multi-manager orders.

In February 2014, the SEC issued Investment Management Guidance Update, 2014-02, *Unbundling of proxy proposals – investment company charter amendments*. As a result of inquiries from registrants and in an effort to encourage consistent application of the rule, the SEC staff issued the Guidance Update. SEC staff has commented that proposed amendments to the charters of investment companies should be "unbundled," providing separate votes for each proposed material amendment. The Guidance Update provides examples of proposed material amendments that should be proposed separately.

In January 2014, the SEC issued Investment Management Guidance Update, 2014-01, *Risk management in changing fixed income market conditions*. After a brief examination of the developing trends in the fixed income market, this Guidance Update suggests certain steps that fund advisers may consider with respect to risk management and disclosure matters relating to changing market conditions. To assist fund boards in providing appropriate oversight of the funds, fund boards may want to consider discussing with fund advisers the steps these advisers are taking in this area. The Guidance Update discusses the types of information fund advisers may want to consider providing boards to facilitate this oversight function.

On January 9, 2014, the SEC announced its examination priorities for 2014. Corporate governance, conflicts of interest, enterprise risk management, as well as fraud detection and prevention at financial institutions are among the top areas of concern for the SEC's National Examination Program (NEP) in 2014. The SEC staff said it will continue meeting with senior management and public boards to discuss how companies identify and mitigate conflicts of interest and legal, compliance, financial, and operational risks. It also plans to evaluate companies' tone at the top. With respect to fraud detection and prevention, the NEP plans to use quantitative and qualitative tools to identify market participants engaged in fraudulent or unethical behavior.

Publications of interest to mutual fund directors issued during the two years ended June 30, 2014

Independent Directors Council/Affiliates (www.idc.org)

Investment Performance Oversight by Fund Boards, October 2013

This paper discusses some primary steps for overseeing a fund's portfolio structure and risks and its performance results. The paper also discusses board governance structures and processes for investment oversight and resources available to fund directors to enhance their understanding of investment management.

Considerations for Board Composition: From Recruitment Through Retirement, October 2013

The Independent Directors Council (IDC) prepared this paper to assist directors when considering these and related governance topics.

Overview of Fund Governance Practices, 1994-2012, September 2013

The overview provides common fund governance practices covering the period from 1994 through 2012, and is an update to the overview published two years previously. This overview includes information on fund assets managed by complexes that participated in each of the biennial studies, the average fund assets served per director, the average number of funds served, and selected independent director characteristics.

Board Oversight of Exchange-Traded Funds, October 2012

The Independent Directors Council (IDC) has prepared this document to assist directors of ETFs in performing their oversight responsibilities. The paper also may be useful for directors who do not currently oversee ETFs but wish to be more familiar with a board's oversight role, including those whose fund groups may currently invest in ETFs or intend to launch ETFs in the future. The paper includes practical guidance in the form of potential questions to ask in areas that may be of particular interest in the ETF context.

Audit Committee Annual Evaluation of the External Auditor, October 2012

This document assists audit committees in performing the annual evaluation of the auditor. This evaluation tool is scalable and specifically includes an examination of the auditor's independence, objectivity, and professional skepticism. It contains sample questions to gauge the quality of services provided, communications, and interaction. It also provides a sample form for obtaining input from company personnel.

Mutual Fund Directors Forum www.mfdf.com

Practical Guidance for Directors on Board Governance and Review of Investment Advisory Agreements, October 2013

This report offers recommendations to enhance the effectiveness of investment company independent directors and recommendations for the review of management agreements and fees.

Practical Guidance for Fund Directors on Oversight of Proxy Voting, September 2012

This report explores models of proxy voting oversight and provides context for decision points boards take into consideration when organizing their proxy oversight.

PwC www.pwc.com

In Brief: SEC issues final rules to reform money market funds, July 2014

On July 23, 2014, the SEC issued final rules aimed at reducing the risk of a run by investors on money market funds. The new rules mandate the use of a floating net asset value (NAV) for institutional prime money market funds. In addition, the rules provide boards the ability to impose liquidity fees, as well as implement redemption gates, for all non-government money market funds during periods of stress. The rules are not expected to alter the designation of money market funds as cash equivalents.

In the loop: EU audit reform – the impact beyond Europe, July 2014

This issue discusses how audit reform in the European Union (EU) doesn't directly apply to US companies—but certain European subsidiaries could be scoped in. The new requirements apply to subsidiaries that meet the definition of an EU public interest entity, including EU banks and insurers. The rules become effective in 2016, except for mandatory firm rotation, which is subject to a transition period. However, US multinationals should take steps now to understand if and how the legislation affects their EU subsidiaries. Complying with the requirements could be challenging and require advance planning, especially if EU statutory audits are performed by the same audit firm performing the US company consolidated audit.

Regulatory and standard-setting Developments, June 2014

This document provides a summary of the activities of the PCAOB, SEC, and FASB, and describes related international developments that are of interest to audit committees, companies, and their stakeholders. It includes some of the relevant regulations, standards, and guidance that were recently issued or are on the horizon.

Regulatory Brief: SEC sweep on liquid alternative funds, June 2014

This Regulatory Brief (a) provides background on liquid alts, (b) describes the SEC's concerns, (c) suggests areas of future exam focus, and (d) offers suggestions on what industry participants can do now to prepare.

Regulatory Brief: Asset manager SIFI designation, June 2014

This Regulatory Brief provides PwC's view that (a) asset manager SIFI designations will not occur this year, (b) the SEC's upcoming money market reform rule will play an important role in the debate, (c) the PSOC is facing increased political scrutiny as a result of the designation process, but (d) nevertheless PwC continues to believe two to four large asset managers will ultimately be proposed for designation as indicated in our prior briefs.

The Quarter Close – Directors' Edition Q2 2014, June 2014

The quarter close — Directors edition is designed to keep directors informed about the latest accounting and financial reporting issues.

This edition discusses the following items:

- Overseeing the process of going public
- Accounting for software costs
- An overview of the new discontinued operations guidance
- The latest private company accounting alternative for leases under common control
- Financial institutions prepare to comply with new regulations
- Corporate governance – audit committee excellence

In Brief: PCAOB adopts final standard on related parties and related amendments to other auditing standards, June 2014

On June 10, 2013 The PCAOB adopted Auditing Standard No. 18, Related Parties, and amendments to other auditing standards to strengthen auditor performance requirements in three critical areas of the audit: (1) related party transactions, (2) significant unusual transactions, and (3) a company's financial relationships and transactions with its executive officers. If approved by the SEC, the new standard and amendments will be effective for audits of financial statements for fiscal years beginning on or after December 15, 2014, including reviews of interim financial information within these fiscal years.

In Brief: FASB amends repo accounting and enhances disclosures, June 2014

FASB amends accounting for repos-to-maturity and repurchase financings. The new standard amends the accounting guidance for "repo-to-maturity" transactions and repurchase agreements executed as repurchase financings. In addition, the new standard requires a transferor to disclose more information about certain transactions, including those in which it retains substantially all of the exposure to the economic returns of the underlying transferred asset over the transaction's term. With one exception, public business entities are required to apply the accounting changes and comply with the enhanced disclosure requirements for the first interim or annual reporting period beginning after December 15, 2014. However, for repurchase and securities lending transactions reported as secured borrowings, the new standard's enhanced disclosures are effective for annual periods beginning after December 15, 2014 and interim periods beginning after March 15, 2015. A public business entity may not early adopt the standard's provisions.

In depth: The standard is final – A comprehensive look at the new revenue model, June 2014

This issue summarizes the new revenue recognition model. Accompanying the issue is an initial release of industry-specific supplements with examples and further insights into ways entities within the industry are likely to be affected by the revenue standard. Additional supplements will be released over the coming weeks.

In the loop: Reporting revenue – new model, new strategy? June 2014

This issue of discusses the newly issued revenue guidance and how it could impact a company's business practices and go-to-market strategies.

Five megatrends and possible implications: Directors edition, May 2014

PwC's Center for Board Governance released a "directors edition" of Five megatrends and possible implications. The publication looks at the complexities and interconnectedness of the megatrends, and the potential implications on business— now and in the future. It offers a high-level view of the megatrends for directors to discuss with their companies. The megatrends are:

- Accelerating urbanization
- Climate change and resource scarcity
- Demographic shifts
- A shift in economic power
- Technological breakthroughs

Audit Committee Excellence Series Achieving – excellence: Financial reporting oversight, May 2014

PwC's Center for Board Governance issued its second edition of the Audit Committee Excellence Series (ACES). The second edition is titled, Achieving excellence: Financial reporting oversight, and it discusses the importance of press releases covering preliminary results, considerations for audit committees before releasing results, and tips for reviewing actual filings.

Board oversight of risk: Defining risk appetite in plain English, May 2014

PwC's Center for Board Governance released Board oversight of risk: Defining risk appetite in plain English. This board-level report provides an overview of the risk appetite process, the board's role in risk appetite, and questions boards should consider asking management about risk appetite.

In brief: Consolidation – changes may affect all industries, May 2014

The FASB's consolidation project nears completion with more decisions made at last week's board meeting. Significant changes have been made to the principal versus agent proposal that was exposed in 2011, making the potential impacts broader than initially anticipated. The FASB's initial goal was to make a surgical fix to one aspect of the consolidation guidance (adding a new principal versus agent step in the VIE model) to avoid asset managers needing to consolidate the funds they manage. Since then, the board has made decisions that will affect several aspects of the consolidation guidance for all companies. In fact, both the VIE model and voting model for consolidation are expected to change. The article provides an overview of the FASB's tentative decisions on its consolidation project.

BoardroomDirect: Special Edition (ProxyPulse, first edition 2014)

PwC's Center for Board Governance released a Special Edition of BoardroomDirect, the Center's newsletter for directors and executives. The Special Edition announces ProxyPulse, first edition 2014 – a collaboration of PwC's Center for Board Governance and Broadridge Financial Solutions. ProxyPulse contains key trends from the 2013 fall "mini-season" covering the 1,066 shareholder meetings held between July 1 and December 31, 2013, along with comparative data from the 2012 fall mini-season.

Point of view: Financial statement disclosures – Enhancing their clarity and understandability, April 2014

Preparers can take actions today to make sure they are preparing clear and understandable disclosures based on the facts and circumstances. Other capital market participants also have a role to play by encouraging disclosure of only important, relevant information. Within established rules and legal requirements, exercising well-reasoned judgment to determine relevant disclosures should streamline financial statement presentation and provide users with the information that is most important for decision making. Organization, formatting and cross-referencing also can enhance navigation within the financial statements.

How does the recent FATCA guidance affect asset managers? February 2014

On February 20, 2014, the US Department of the Treasury (Treasury) and the Internal Revenue Service (IRS) issued extensive temporary regulations that (1) amend the existing final Treasury regulations implementing the Foreign Account Tax Compliance Act (FATCA) and (2) provide guidance to harmonize the FATCA rules with the existing US information reporting and withholding rules. Since February 20, the Treasury and IRS have also released the final W-8BEN-E (for foreign entities), guidance on certain intergovernmental agreement (IGA) jurisdictions, and the deferral of certain key registration dates.

Asset managers who have already begun their FATCA implementation activities should find these changes provide some welcomed relief and clarification. For many managers, however, who were waiting on the additional guidance to move forward, these regulations represent the final significant pieces of guidance to be issued. If a manager has not started preparing for FATCA already, now is the time to begin preparation to 'go live' with FATCA by July 1, 2014. Time is short until July 1, so managers should review their FATCA implementation plans and make sure that they will be ready by July.

Asset Management 2020: A Brave New World, 2014

The publication sets out how the operating landscape for asset managers will change by 2020 and explains how asset managers can prepare for the challenges ahead and turn them into competitive advantages.

The Quarter Close – Directors' Edition Q1 2014, March 2014

The quarter close — Directors edition is designed to keep directors informed about the latest accounting and financial reporting issues.

This edition discusses the following items:

- New accounting standards for private companies being adopted
- Assessing whether profit-sharing arrangements are accounted for as equity or a bonus
- Two class method of calculating earnings per share
- Accounting for new transaction types using old methods – gross versus net revenue analysis
- Allocating income taxes to separate company and carve-out financials
- New FASB developments relating to financial instruments, consolidations, and insurance projects
- Regulatory matters
- Corporate governance – cybersecurity, and more

BoardroomDirect: Updated on current board issues, March 2014

BoardroomDirect is an electronic newsletter sent to directors and executives from the PwC Center for Board Governance. This edition includes the inaugural edition of PwC's Audit Committee Excellence Series, which covers a company's forward-looking guidance practices and the potential risks associated with analysts' consensus estimates. It provides board-level perspectives regarding current trends as well as the advantages and disadvantages of providing guidance. The newsletter also includes briefs on 1) update on SEC no-action letters for 2014 season, 2) companies' succession planning, 3) the Conference Board task force on director-shareholder engagement, 4) accounting fraud on the rise at US companies, 5) SEC chief accountant to audit committees: audit quality top priority, 6) PCAOB to hold roundtable on auditor's reporting model in April.

In brief: FASB issues exposure draft of the Conceptual Framework for Financial Reporting: Notes to Financial Statements, March 2014

The FASB issued an exposure draft of the *Conceptual Framework for Financial Reporting: Notes to Financial Statements* (the "Proposal"). The Proposal is part of the FASB's disclosure framework project, intended to make financial statement disclosures more effective and less redundant. It details a framework to be used by the FASB in its standard-setting activities for determining what information is relevant to the users of financial statements and should be included in the notes. The framework will not only be used as a basis for establishing future disclosure requirements, but can be used to evaluate existing disclosures. Comments on the exposure draft are due by July 14, 2014.

Regulatory and standard-setting developments, March 2014

This document provides a summary of the activities of the PCAOB, SEC, and FASB, and describes related international developments that are of interest to audit committees, companies, and their stakeholders. It includes some of the relevant regulations, standards, and guidance that were recently issued or are on the horizon.

BoardroomDirect, February 2014

BoardroomDirect is an electronic newsletter sent to directors and executives from the PwC Center for Board Governance. This edition includes an article on the latest developments on cybersecurity, along with information on the new standards framework from the US Department of Homeland Security. The newsletter also includes briefs on: 1) new shareholder proposals companies are facing in 2014, 2) the creation of an engagement protocol from a group of independent directors and investors, 3) Institutional Shareholder Services targeting director tenure in its corporate governance rating system, 4) the SEC staff issuing further guidance on the "unbundling" rule for charter amendments, 5) the PCAOB extending the comment period for its proposed lead audit partner disclosure rule, 6) FASB issuing private company alternative standards for goodwill and certain interest rate swaps.

Regulatory Brief – Nonbank SIFIs: No solace for US asset managers, February 2014

Ever since the Treasury Department's Office of Financial Research ("OFR") released its report on Asset Management and Financial Stability in September 2013 ("OFR Report"), the industry has vigorously opposed its central conclusion that the activities of the asset management industry as a whole make it systemically important and may pose a risk to US financial stability. The Financial Stability Board and the International Organization of Securities Commissions issued a Consultative Document in January proposing methodologies for identifying globally active systemically important investment funds. This brief analyzes the OFR report and the Consultative Document, and concludes with our continued view that the Council will propose a few large asset managers for designation.

Key considerations for board and audit committee members, December 2013

Today's globally interconnected and competitive world means companies have ongoing challenges and opportunities. This report addresses today's changing boardroom agenda and outlines topics that can provide a basis to help enhance the quality of board and management discussions in the coming year.

The Quarter Close – Directors' Edition Q4 2013, December 2013

The quarter close — Directors edition is designed to keep directors informed about the latest accounting and financial reporting issues.

Topics featured in this edition:

- Update on the upcoming revenue recognition standard
- Structured payables programs
- Implications of government tax incentives
- Retiree health plans
- Implications of stock repurchases
- PCAOB revised proposal on disclosing information about the auditors
- SEC rule making

BoardroomDirect: The Audit Committee Report – An opportunity to enhance communication with stakeholders, November 2013

Center for Audit Quality has released a paper titled Enhancing the Audit Committee Report: A Call to Action. This edition examines the call to action on the importance of audit committees voluntarily and proactively enhancing their proxy report and other disclosures. The article includes comments from two corporate governance experts: one an audit committee chair and the other a corporate attorney, who explain the importance of this call to action.

In Brief: PCAOB reproposes amendments to disclose name of engagement partner and certain other participants in audits, December 2013

On December 4, the Public Company Accounting Oversight Board ("PCAOB" or the "Board") reproposed for public comment amendments to the PCAOB's auditing standards (the "reproposed amendments") that would require disclosure in the auditor's report of the name of the engagement partner and information about certain other participants in the audit.

10 Minutes on service provider transparency, December 2013

Service providers play an increasingly critical role in today's competitive business model, from protecting sensitive customer data and managing technology to running essential business processes. When service providers suffer breakdowns, their clients can unwittingly violate regulations or even lose customer trust. This 10Minutes highlights that businesses may know less than they realize about their service providers' controls. Service Organization Control reports can help businesses increase confidence in their providers' critical technology systems. They may request audited Service Organizational reports to assess a service provider's controls around outsourced technology and systems supporting outsourced business processes. These reports can offer greater peace of mind around service providers, and savvy businesses can use them to distinguish themselves through their outsourcing models.

PwC Dataline: A look at current financial reporting issues – accounting for centrally cleared swaps, December 2013

Dodd-Frank Title VII (Dodd-Frank) significantly changed the trading requirements for derivative instruments, such as mandating that certain derivatives be centrally cleared. A number of financial reporting implementation questions have arisen as companies consider the Dodd-Frank requirements. These include determining fair value of centrally cleared derivatives, accounting for collateral, assessing the impact on hedge accounting, and determining the appropriate presentation (gross versus net).

This *Dataline* discusses the financial reporting implications of the new requirements, primarily focusing on end-users that trade in the affected derivatives and who do not qualify for the end-user exception.

PwC Dataline: A look at current financial reporting issues –derivative valuation, December 2013

Derivative pricing practices have evolved in recent years as market participants refine their pricing approaches to capture the elements underlying the pricing of derivative transactions in a changing market. One area that has continued to evolve relates to pricing assumptions on collateralized derivatives. For many years market participants utilized collateral on bilateral over-the-counter ("OTC") derivative transactions as a means of mitigating the credit risk of their counterparties. Following the lessons learned during the financial crisis, many market participants recognized that the funding advantages from collateral that may be rehypothecated has value that should be considered in derivative pricing.

The incorporation of these funding advantages has had a broad impact on derivative pricing as a result of the increasingly common use of collateral on derivative transactions. The increased use of collateral has been driven by an increased focus in the OTC market on credit risk and funding risk management, as well as by the migration of derivative activity to clearing houses where transactions are typically fully collateralized. As a result, certain collateralized derivatives may be presumed to require valuation based on discounting at the Overnight Indexed Swap ("OIS") rate.

The derivative pricing changes also impact uncollateralized transactions as market conventions for the way prices are quoted for reference instruments, such as interest rate swaps, have changed.

This *Dataline* addresses some of the key financial reporting implications relating to these evolving pricing conventions.

PwC Dataline: 2013 year-end financial reporting considerations – Leading practices, lessons learned, and reminders, December 2013

This *Dataline* looks at aspects of financial reporting that have continued to present challenges to financial statement preparers, and transactions and arrangements prevalent in today's economic environment that have unique or complex accounting implications.

While not an all-inclusive list, the *Dataline* provides timely reminders for companies navigating the year-end financial reporting process. While many of the topics are not new, they continue to be challenging, based on SEC staff comment letters, restatements, revisions, and our own observations. Topics include: cash flows, other comprehensive income, revenue recognition, income taxes, segments, impairment of long-lived assets, goodwill – qualitative impairment test, variable interest entities, equity method investments, asset acquisition versus business, accounting changes and error corrections, use of overnight index swap rate in derivatives valuation, fair value hierarchy, equity-linked financing instruments, extinguishment gain when debt holder owns equity, contingencies, and stock-based compensation.

Dataline: Highlights of the 2013 AICPA National Conference on Current SEC and PCAOB Developments, December 2013

The 2013 AICPA National Conference on Current SEC and PCAOB Developments (the Conference) brought together presenters from across the accounting landscape: regulatory and standard-setting bodies, auditors, users, preparers, and industry experts.

The SEC staff provided an update on regulatory and financial reporting matters including areas of frequent comment and consultation trends. They emphasized the need for high quality, concise disclosures, focusing on ways registrants can improve communications throughout their filings. They also stressed the continued importance of internal controls over financial reporting, asking participants to remain vigilant in order to maintain the gains made over the past decade.

Quality and transparency were themes highlighted throughout the Conference, and were broadly applicable to the spectrum of conference participants. Topics on quality included both financial reporting and auditing, while transparency was discussed in the context of regulatory practices, audits, and disclosures. These themes were emphasized by speakers from the Center for Audit Quality, the SEC, and PCAOB, and echoed by others involved in the financial reporting process.

The *Dataline* provides highlights from the Conference and PwC observations.

The next generation of ETFs: Why every asset manager needs an ETF Strategy, November 2013

Exchange traded funds (ETFs) have enjoyed two decades of explosive growth. Evolving and proliferating as they attracted new users, ETFs went from a single vehicle providing exposure to large cap US equities to thousands of products representing a dizzying range of asset classes and strategies. As ETFs reshape their environment all over again, asset managers and intermediaries alike will want to have strategies in place to deal with the changes sweeping across the competitive landscape. This paper examines factors that attributed to ETF growth, recent developments and emerging trends impacting ETFs in the market, potential growth challenges. Strategies to help market participants differentiate and compete in this new environment.

How global tax reforms might impact ETF efficiency: A look at the implications for ETF strategy and structuring, November 2013

Due to their low costs and potentially greater tax efficiency, ETFs offer a very efficient return to investors. ETFs' tax advantages have contributed to their strong competitive position and growth. But a rapidly changing tax environment will present challenges as governments around the globe seek to bridge budget deficits. By staying on top of these changes, sponsors can mitigate adverse effects while remaining compliant with changing global tax laws. This paper examines ETF product evolution and tax reforms impacting efficiency, market infrastructure reforms across Europe and Asia, and changes in distribution and the pursuit of scale through international expansion.

In brief: Most money market funds to be scoped out of Consolidation, October 2013

At its October 24, 2013 meeting, the FASB tentatively decided to exclude money market funds that are registered with the SEC, as well as certain unregistered money market funds from the scope of the consolidation guidance. The effective date of the proposal has not yet been determined.

In brief: PCAOB other information proposal, October 2013

The proposed standard would apply to the auditor's responsibility with respect to other information in a company's annual report that is filed with the Securities and Exchange Commission (SEC) under the Securities Exchange Act of 1934 and that contains the company's audited financial statements and the related auditor's report. As a result, it applies to other information that is incorporated by reference and is available prior to the issuance of the auditor's report but does not extend to annual reports that are distributed by other means, such as corporate websites or social media. It also does not apply to other information contained in 1933 Act registration statements.

In Brief: PCAOB proposes significant changes to the auditor's report, October 2013

The proposed standard would retain the existing pass/fail model and the basic elements of the auditor's report, but would require the auditor to report a wider range of information specific to the particular audit and auditor.

ETFs: How innovators and regulators are shaping growth in the Asset Management industry, October 2013

This paper examines the interplay between innovation and the regulators across three dimensions: Products; Markets; and Distribution. Given the fragmented nature of regulation – with a series of national regulators – the paper looks into the effect of regulations in: the United States, the European Union and Asia Pacific.

PwC Mutual Fund Directors Roundtable: 2013 highlights, October 2013

Professionals from PwC's Asset Management practice and directors from the boards of some of the nation's leading mutual fund groups gathered for informal discussions of the industry's key issues and significant challenges. These talks generated important insights into what directors are thinking about in today's evolving market place regarding valuation, risk management, board effectiveness, and other key issues.

The Connected Advisor: The Rise of Digital and Social Advice in Wealth Management, August 2013

This paper examines the four forces of change that are shaping wealth management – shifting demographics, changing client behaviors and expectations, rising technological innovations and emerging disruptive competition.

The Quarter Close – Directors' Edition Q3 2013, September 2013

The quarter close — Directors edition is designed to keep directors informed about the latest accounting and financial reporting issues.

Topics featured in this edition:

- Accounting and reporting issues for private companies that could impact public companies
- Statement of cash flows
- Entities under common control
- Contingencies
- New vice-chairman at the FASB
- PCAOB proposal on improving auditor reporting
- International developments on auditor rotation and retendering

PwC's 2013 Annual Corporate Directors Survey Strategy and risk management and regulatory and governance environment, September 2013

PwC reports many directors believe recent regulatory and enforcement initiatives have failed to achieve increased investor protections, improve public trust in the corporate sector, or enhance transparency to stakeholders.

Key survey findings include:

- Directors skeptical of regulatory and enforcement initiatives. Nearly two-thirds of directors (64%) believe recent regulatory and enforcement initiatives have not increased investor protections, and 77% don't believe they have increased public trust in the corporate sector. In addition, 51% think these efforts have not enhanced transparency to stakeholders "very much" or at all.
- Costs of regulation exceed benefits. Nearly three-fourths of directors feel that increased regulation and enforcement initiatives have added costs to the company that exceed benefits, and 56% believe they have at least somewhat put excessive burdens on directors.
- Director and CEO views on who influences company strategy. CEOs see more influence by the media and supply chain partners than directors do. Directors see somewhat more influence from investors and creditors, and say they are more concerned about the government impairing growth prospects.
- More comfort with risk oversight. The percentage of directors who feel there is a clear allocation of risk oversight responsibilities among the board and its committees improved by 17 points over the prior year. Half of those who say there is clarity believe it still could be improved.

PwC's 2013 Annual Corporate Directors Survey: Information technology, stakeholder communications and executive compensation, September 2013

PwC reports that information technology is a top priority for today's boards as directors spend more time on IT and recognize the increased importance of effective IT oversight. With technology rapidly changing the way companies do business, more boards are turning to outside consultants for advice on IT strategy and risk oversight.

Key survey findings include:

- Challenges weaving IT into strategy and risk. Despite reporting increased recognition of the importance of effective IT oversight, 32% of directors still say they do not have a sufficient understanding of IT to support the company's strategy and IT risk mitigation. Additionally, only 22% of directors say they "very much" agree that the company's approach provides them with adequate information for effective oversight.

- Getting up to digital speed. The majority of directors have evolved to become more actively engaged in overseeing traditional IT issues. The status of major IT implementations and the annual IT budget reflect areas with the highest levels of director engagement (80% and 63%, respectively).

PwC's 2013 Annual Corporate Directors Survey: Board composition and behavior, September 2013

PwC provides an inside look at specific details in the core areas of board composition, structure and performance. The survey found that concerns among directors about board composition and peer performance are among the key issues cited by respondents.

Key survey findings include:

- What is so great about serving on a board? Board service is not driven by money or ego. More than half of directors (54%) say that their primary motivation for sitting on a corporate board is intellectual stimulation; 22% see board service as a way to keep engaged; and 17% indicate they simply want to give something back. Remuneration is low on the list.
- How are my fellow directors doing? Directors are becoming more critical of their fellow directors. 35% now say someone on their board should be replaced (compared to 31% in 2012). The top three reasons cited are diminished performance because of aging, a lack of the required expertise and lack of preparation for meetings.
- Replacing directors—and the impediments to doing so. Replacing a fellow board member can be difficult; nearly half of directors (48%) cite impediments to doing so. The top reason given, and cited nearly twice as often as any other factor, demonstrates the importance of board leadership. Specifically, the directors said that board leadership is uncomfortable addressing the issue.
- Sensitivity to shareholder voting. Directors are less sensitive to negative shareholder voting in director elections than they were last year. In 2012, 59% said they would be concerned about re-nomination of a fellow director if he or she received less than 75% favorable shareholder support. However, this year the number dropped to 51%.

10Minutes on whistleblower reform, July 2013

Whistleblower reform is having significant impact. The SEC's Office of the Whistleblower has one full year of operation under its belt, and with it 3,001 tips and two awards to date. Leading companies are looking closely at the Office's first-year report and drawing lessons for building stronger ethics and compliance programs. They're also considering what it takes to create a highly ethical culture. This 10Minutes highlights the importance of having an ethical culture at the workplace.

FS Viewpoint: An unsettled world: The changing world of cash equities and fixed income and how it is impacting asset managers and their service providers, January 2013

The execution to custody value chain and the players involved have remained relatively stable since the consolidation of custodial providers in the 1990s. The financial crisis and new capital and regulatory rules have forced asset managers to reduce fees and have increased the challenges for sell-side firms participating in the cash equities and fixed income execution to custody value chain. To adjust to the new market realities, asset managers are aggressively pushing to change their business models.

16th Annual Global CEO Survey

US CEOs are honing approaches for 2013: focusing on organic growth, their customers and ever more effective operational models. The results of this survey highlight the items that are top of mind for CEOs.

Key questions for board and audit committee members, 2013 edition

This publication summarizes key topics and questions board and audit committee members should ask during the year-end reporting cycle and throughout the year. Directors should consider the questions in *Key questions for board and audit committee members, 2013 edition*, as well as others they determine are relevant to the companies they serve, given their specific facts and circumstances. They should also consider questions that are routinely asked of management and the auditors at year-end.

9 New Rules of IT Strategy Asset Management, October 2012

The asset management industry is in the midst of significant structural change, with primary drivers including shifting investor preferences, pricing pressure and uncertain markets. While we see significant variation in how firms are adapting to these changes, we have identified many situations where asset management firms' business and IT strategies are at risk of misalignment.

PwC offers nine new rules for how firms can mitigate or completely eliminate misalignment risk by re-visiting commonly held and outdated wisdom on IT strategy.

10 Minutes on effective audit committees, Fall 2012

Audit committees, management, and auditors work together to meet the information needs of the capital markets and to promote quality audits and financial reporting. The audit committee's oversight role is particularly critical. The leading practices in 10Minutes on effective audit committees can help audit committees continue to improve their oversight of auditors and management, thereby enhancing the quality of audits and financial reporting.

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