

FRANKLIN RESOURCES INC  
Form 10-Q  
February 01, 2012

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549  
FORM 10-Q

(MARK ONE)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT  
OF 1934

For the quarterly period ended December 31, 2011

OR  
 TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT  
OF 1934

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number: 001-09318

FRANKLIN RESOURCES, INC.

(Exact name of registrant as specified in its charter)

Delaware  
(State or other jurisdiction of  
incorporation or organization)

13-2670991  
(I.R.S. Employer  
Identification No.)

One Franklin Parkway, San Mateo, CA  
(Address of principal executive offices)

94403  
(Zip Code)

(650) 312-2000  
(Registrant's telephone number, including area code)

N/A  
(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.  YES  NO

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).  YES  NO

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer", "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer  Accelerated filer   
Non-accelerated filer  (Do not check if a smaller reporting company) Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).  YES  NO

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

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Outstanding: 215,942,632 shares of common stock, par value \$0.10 per share, of Franklin Resources, Inc. as of January 25, 2012.

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## PART I – FINANCIAL INFORMATION

## Item 1. Financial Statements.

## FRANKLIN RESOURCES, INC.

## Condensed Consolidated Statements of Income

## Unaudited

	Three Months Ended December 31,	
(in thousands, except per share data)	2011	2010
Operating Revenues		
Investment management fees	\$1,075,137	\$1,066,507
Sales and distribution fees	524,304	552,203
Shareholder servicing fees	75,405	72,055
Other, net	27,030	9,548
Total operating revenues	1,701,876	1,700,313
Operating Expenses		
Sales, distribution and marketing	630,618	647,153
Compensation and benefits	300,412	292,394
Information systems and technology	41,434	40,367
Occupancy	31,842	30,868
General, administrative and other	65,190	30,297
Total operating expenses	1,069,496	1,041,079
Operating Income	632,380	659,234
Other Income (Expenses)		
Investment and other income, net	71,176	46,328
Interest expense	(8,565)	(7,895)
Other income, net	62,611	38,433
Income before taxes	694,991	697,667
Taxes on income	201,265	207,550
Net income	493,726	490,117
Less: Net income (loss) attributable to Nonredeemable noncontrolling interests	10,147	(11,877)
Redeemable noncontrolling interests	2,794	837
Net Income Attributable to Franklin Resources, Inc.	\$480,785	\$501,157
Earnings per Share		
Basic	\$2.21	\$2.24
Diluted	2.20	2.23
Dividends per Share	\$2.27	\$0.25

See Notes to Condensed Consolidated Financial Statements.

FRANKLIN RESOURCES, INC.  
Condensed Consolidated Balance Sheets  
Unaudited

(in thousands)	December 31, 2011	September 30, 2011
Assets		
Current Assets		
Cash and cash equivalents	\$4,248,837	\$4,699,994
Cash and cash equivalents of consolidated variable interest entities	72,316	88,238
Receivables	781,645	772,475
Investment securities, trading	1,056,668	889,686
Investment securities, available-for-sale	756,165	990,976
Investments of consolidated variable interest entities, at fair value	10,561	10,994
Investments in equity method investees and other	20,693	21,861
Deferred taxes	106,648	107,898
Prepaid expenses and other	30,523	34,646
Total current assets	7,084,056	7,616,768
Banking/Finance Assets		
Cash and cash equivalents	590,705	410,381
Investment securities, available-for-sale	331,621	345,486
Loans receivable, net	390,120	401,860
Loans receivable of consolidated variable interest entities, net	124,529	149,386
Other	38,299	51,010
Total banking/finance assets	1,475,274	1,358,123
Non-Current Assets		
Investments of consolidated sponsored investment products	623,326	584,608
Investments of consolidated variable interest entities, at fair value	826,632	811,618
Investments in equity method investees and other	558,620	535,509
Property and equipment, net	594,668	589,748
Goodwill	1,535,602	1,536,212
Other intangible assets, net	606,625	611,979
Other	100,684	131,278
Total non-current assets	4,846,157	4,800,952
Total Assets	\$13,405,487	\$13,775,843

[Table continued on next page]

See Notes to Condensed Consolidated Financial Statements.

FRANKLIN RESOURCES, INC.  
Condensed Consolidated Balance Sheets  
Unaudited

[Table continued from previous page]

(dollars in thousands, except per share data)	December 31, 2011	September 30, 2011
<b>Liabilities and Stockholders' Equity</b>		
<b>Current Liabilities</b>		
Compensation and benefits	\$228,043	\$400,885
Commercial paper	25,000	29,997
Current maturities of long-term debt	6,589	29,656
Current maturities of long-term debt of consolidated variable interest entities, at fair value	24,924	24,858
Accounts payable, accrued expenses and other	206,684	328,303
Commissions	343,911	369,539
Income taxes	205,773	128,826
<b>Total current liabilities</b>	<b>1,040,924</b>	<b>1,312,064</b>
<b>Banking/Finance Liabilities</b>		
Deposits	1,028,343	890,189
Long-term debt of consolidated variable interest entities	135,652	164,176
Federal Home Loan Bank advances	69,000	69,000
Other	957	970
<b>Total banking/finance liabilities</b>	<b>1,233,952</b>	<b>1,124,335</b>
<b>Non-Current Liabilities</b>		
Long-term debt	974,347	1,004,381
Long-term debt of consolidated variable interest entities, at fair value	823,741	846,369
Deferred taxes	278,772	274,435
Other	93,850	91,789
<b>Total non-current liabilities</b>	<b>2,170,710</b>	<b>2,216,974</b>
<b>Total liabilities</b>	<b>4,445,586</b>	<b>4,653,373</b>
<b>Commitments and Contingencies (Note 9)</b>		
Redeemable Noncontrolling Interests	26,509	18,611
<b>Stockholders' Equity</b>		
Preferred stock, \$1.00 par value, 1,000,000 shares authorized; none issued	—	—
Common stock, \$0.10 par value, 1,000,000,000 shares authorized; 215,948,381 and 217,693,435 shares issued and outstanding, at December 31, 2011 and September 30, 2011	21,595	21,769
Retained earnings	8,198,497	8,443,531
Appropriated retained earnings of consolidated variable interest entities	40,619	18,969
Accumulated other comprehensive income	12,932	40,462
<b>Total Franklin Resources, Inc. stockholders' equity</b>	<b>8,273,643</b>	<b>8,524,731</b>
Nonredeemable noncontrolling interests	659,749	579,128
<b>Total stockholders' equity</b>	<b>8,933,392</b>	<b>9,103,859</b>
<b>Total Liabilities and Stockholders' Equity</b>	<b>\$13,405,487</b>	<b>\$13,775,843</b>

See Notes to Condensed Consolidated Financial Statements.

FRANKLIN RESOURCES, INC.  
Condensed Consolidated Statements of Cash Flows  
Unaudited

(in thousands)	Three Months Ended	
	December 31,	
	2011	2010
Net Income	\$493,726	\$490,117
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	52,624	62,478
Stock-based compensation	25,660	21,775
Excess tax benefit from stock-based compensation	(17,374)	(12,047)
Net gains on sale of assets	(13,245)	(26,968)
Net losses on non-current investments of consolidated sponsored investment products	10,077	—
Net (gains) losses of consolidated variable interest entities	(22,328)	11,458
Equity in net income of affiliated companies	(22,472)	(23,892)
Other-than-temporary impairment of investments	—	13,156
Provision for loan losses	(266)	2,845
Deferred income taxes	7,049	5,957
Changes in operating assets and liabilities:		
Increase in receivables, prepaid expenses and other	(27,820)	(135,780)
Increase in trading securities, net	(147,097)	(182,115)
Increase in income taxes payable	98,357	118,828
(Decrease) increase in commissions payable	(25,628)	26,277
(Decrease) increase in other liabilities	(70,512)	9,130
Decrease in accrued compensation and benefits	(173,011)	(135,443)
Net cash provided by operating activities	167,740	245,776
Purchase of investments	(95,640)	(43,512)
Purchase of investments by consolidated variable interest entities	(73,193)	(176,137)
Liquidation of investments	285,573	190,477
Liquidation of investments by consolidated variable interest entities	95,849	251,815
Liquidation of banking/finance investments	12,847	13,690
Decrease (increase) in loans receivable, net	13,150	(28,049)
Decrease in loans receivable held by consolidated variable interest entities, net	24,586	43,980
Additions of property and equipment, net	(26,768)	(54,003)
Cash and cash equivalents recognized due to adoption of new consolidation guidance	—	45,841
Net cash provided by investing activities	236,404	244,102
Increase in deposits	138,154	21,610
Issuance of common stock	12,788	13,061
Dividends paid on common stock	(546,899)	(49,763)
Repurchase of common stock	(290,856)	(198,536)
Excess tax benefit from stock-based compensation	17,374	12,047
Decrease in commercial paper, net	(5,007)	(2,767)
Proceeds from issuance of debt	6,589	—
Payments on debt	(61,778)	—
Payments on debt by consolidated variable interest entities	(54,119)	(89,721)
Noncontrolling interests	102,326	1,357
Net cash used in financing activities	\$(681,428)	\$(292,712)

[Table continued on next page]

See Notes to Condensed Consolidated Financial Statements.



FRANKLIN RESOURCES, INC.  
Condensed Consolidated Statements of Cash Flows  
Unaudited  
[Table continued from previous page]

(in thousands)	Three Months Ended	
	December 31,	
	2011	2010
Effect of exchange rate changes on cash and cash equivalents	\$ (9,471	) \$ 148
(Decrease) increase in cash and cash equivalents	(286,755	) 197,314
Cash and cash equivalents, beginning of period	5,198,613	4,123,716
Cash and Cash Equivalents, End of Period	\$4,911,858	\$4,321,030
Components of Cash and Cash Equivalents		
Cash and cash equivalents, beginning of period		
Current assets	\$4,699,994	\$3,985,312
Current assets of consolidated variable interest entities	88,238	—
Banking/finance assets	410,381	138,404
Total	\$5,198,613	\$4,123,716
Cash and cash equivalents, end of period		
Current assets	\$4,248,837	\$4,101,724
Current assets of consolidated variable interest entities	72,316	73,236
Banking/finance assets	590,705	146,070
Total	\$4,911,858	\$4,321,030
Supplemental Disclosure of Non-Cash Information		
Decrease in noncontrolling interests due to net deconsolidation of certain sponsored investment products	\$ (5,098	) \$ (1,503
Increase in assets, net of liabilities, related to consolidation of variable interest entities	—	60,760
Supplemental Disclosure of Cash Flow Information		
Cash paid for income taxes	\$94,633	\$82,917
Cash paid for interest	18,190	16,935
Cash paid for interest by consolidated variable interest entities	11,473	9,679
See Notes to Condensed Consolidated Financial Statements.		



## FRANKLIN RESOURCES, INC.

## Notes to Condensed Consolidated Financial Statements

December 31, 2011

(Unaudited)

## Note 1 – Basis of Presentation

The unaudited interim financial statements of Franklin Resources, Inc. (“Franklin”) and its consolidated subsidiaries (collectively, the “Company”) included herein have been prepared by the Company in accordance with the instructions to Form 10-Q and the rules and regulations of the U.S. Securities and Exchange Commission (the “SEC”). Under these rules and regulations, some information and footnote disclosures normally included in financial statements prepared under accounting principles generally accepted in the United States of America have been shortened or omitted. Management believes that all adjustments necessary for a fair statement of the financial position and the results of operations for the periods shown have been made. All adjustments are normal and recurring. These financial statements should be read together with the Company’s audited financial statements included in its Form 10-K for the fiscal year ended September 30, 2011 (“fiscal year 2011”). Certain amounts for the comparative prior fiscal year period have been reclassified to conform to the financial statement presentation as of and for the period ended December 31, 2011.

In the quarter ended September 30, 2011, the Company discontinued the classification of a portion of the investment management fees earned by certain of its non-U.S. subsidiaries as sales and distribution fees. Amounts for the comparative prior fiscal year period have been reclassified to conform to the current year presentation. This reclassification had no impact on previously reported net income or financial position and does not represent a restatement of any previously published financial results. See Note 1 – Significant Accounting Policies in the Company's Form 10-K for fiscal year 2011.

The following table presents the effects of the changes in the presentation of operating revenues to the Company’s previously-reported condensed consolidated statement of income:

(in thousands)	Three Months Ended		
	December 31, 2010		
	As Reported	Adjustments	As Amended
Operating Revenues			
Investment management fees	\$1,040,878	\$ 25,629	\$ 1,066,507
Sales and distribution fees	577,832	(25,629 )	552,203
Shareholder servicing fees	72,055	—	72,055
Other, net	9,548	—	9,548
Total operating revenues	\$1,700,313	\$ —	\$ 1,700,313

## Note 2 – New Accounting Guidance

On October 1, 2011, the Company adopted new Financial Accounting Standards Board (“FASB”) guidance that requires separate disclosures about purchases, sales, issuances and other settlements in the rollforward of activity in Level 3 fair value measurements. See Note 7 - Fair Value Measurements for the expanded disclosures.

There were no significant updates to new accounting guidance not yet adopted by the Company as disclosed in its Form 10-K for fiscal year 2011.

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Note 3 – Stockholders' Equity, Redeemable Noncontrolling Interests and Comprehensive Income  
The changes in total stockholders' equity and redeemable noncontrolling interests were as follows:  
(in thousands)

	Franklin Resources, Inc. Stockholders' Equity	Nonredeemable Noncontrolling Interests	Total Stockholders' Equity	Redeemable Noncontrolling Interests
for the three months ended December 31, 2011				
Balance at October 1, 2011	\$8,524,731	\$ 579,128	\$9,103,859	\$ 18,611
Net income	480,785	10,147	490,932	2,794
Net income reclassified to appropriated retained earnings	21,650	(21,650 )	—	
Other comprehensive income				
Net unrealized losses on investments, net of tax	(4,797 )		(4,797 )	
Currency translation adjustments	(22,558 )		(22,558 )	
Net unrealized losses on defined benefit plans, net of tax	(175 )		(175 )	
Cash dividends on common stock	(493,332 )		(493,332 )	
Repurchase of common stock	(290,856 )		(290,856 )	
Noncontrolling interests				
Net subscriptions		92,124	92,124	10,202
Net deconsolidation of certain sponsored investment products		—	—	(5,098 )
Other <sup>1</sup>	58,195		58,195	
Balance at December 31, 2011	\$8,273,643	\$ 659,749	\$8,933,392	\$ 26,509

<sup>1</sup> Primarily relates to stock-based compensation plans.

	Franklin Resources, Inc. Stockholders' Equity	Nonredeemable Noncontrolling Interests	Total Stockholders' Equity	Redeemable Noncontrolling Interests
(in thousands)				
for the three months ended December 31, 2010				
Balance at October 1, 2010	\$7,726,994	\$ 3,452	\$7,730,446	\$ 19,533
Adjustment for adoption of new consolidation guidance	106,601		106,601	
Net income (loss)	501,157	(11,877 )	489,280	837
Net loss reclassified to appropriated retained earnings	(11,996 )	11,996	—	
Other comprehensive income				
Net unrealized gains on investments, net of tax	849		849	
Currency translation adjustments	12,667		12,667	
Net unrealized gains on defined benefit plans, net of tax	13		13	
Cash dividends on common stock	(56,012 )		(56,012 )	
Repurchase of common stock	(198,536 )		(198,536 )	
Noncontrolling interests				
Net deconsolidation of certain sponsored investment products		—	—	(1,503 )
Net subscriptions (redemptions)		(733 )	(733 )	2,090
Other <sup>1</sup>	47,991		47,991	

Balance at December 31, 2010	\$8,129,728	\$ 2,838	\$8,132,566	\$ 20,957
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<sup>1</sup> Primarily relates to stock-based compensation plans.

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The components of comprehensive income, including amounts attributable to noncontrolling interests, were as follows:

(in thousands)	Three Months Ended December 31,	
	2011	2010
Net income	\$493,726	\$490,117
Net unrealized gains (losses) on investments, net of tax	(4,797	) 849
Currency translation adjustments	(22,558	) 12,667
Net unrealized gains (losses) on defined benefit plans, net of tax	(175	) 13
Total comprehensive income	466,196	503,646
Less: comprehensive income (loss) attributable to		
Nonredeemable noncontrolling interests	10,147	(11,877
Redeemable noncontrolling interests	2,794	837
Total Comprehensive Income Attributable to Franklin Resources, Inc.	\$453,255	\$514,686

During the three months ended December 31, 2011 and 2010, the Company repurchased 3.0 million and 1.7 million shares of its common stock at a cost of \$290.9 million and \$198.5 million under its stock repurchase program. In December 2011, the Company's Board of Directors authorized the repurchase of up to 10.0 million additional shares of its common stock under the stock repurchase program. At December 31, 2011, approximately 11.8 million shares of common stock remained available for repurchase under the stock repurchase program. The stock repurchase program is not subject to an expiration date.

#### Note 4 – Earnings per Share

The components of basic and diluted earnings per share were as follows:

(in thousands, except per share data)	Three Months Ended December 31,	
	2011	2010
Net Income Attributable to Franklin Resources, Inc.	\$480,785	\$501,157
Less: Allocation of earnings to participating nonvested stock and stock unit awards	3,342	2,126
Net Income Available to Common Stockholders	\$477,443	\$499,031
Weighted-average shares outstanding – basic	216,143	223,169
Effect of dilutive common stock options and non-participating nonvested stock unit awards	584	1,084
Weighted-Average Shares Outstanding – Diluted	216,727	224,253
Earnings per Share		
Basic	\$2.21	\$2.24
Diluted	2.20	2.23

Non-participating nonvested stock unit awards excluded from the calculation of diluted earnings per share because their effect would have been anti-dilutive were 0.5 million and 0.2 million for the three months ended December 31, 2011 and 2010.

#### Note 5 – Variable Interest Entities

The Company has interests in various types of variable interest entities (“VIEs”). It is the primary beneficiary of collateralized loan obligations (“CLOs”) and auto loan securitization trusts (“securitization trusts”) and therefore consolidates these VIEs. Other VIEs, for which the Company is not the primary beneficiary, primarily consist of certain sponsored and other investment products (collectively “other investment products”) from which the Company earns investment management and related services fees and/or has an equity ownership interest in the VIE.

#### Collateralized Loan Obligations

The Company provides collateral management services to the CLOs, which are asset-backed financing entities collateralized by a pool of assets.

During the three months ended December 31, 2011, the changes in fair values of the underlying assets and liabilities of the CLOs resulted in a \$27.7 million net gain and \$5.0 million net loss, for a combined net gain of \$22.7 million. During the three months ended December 31, 2010, the changes in fair values of the underlying assets and liabilities resulted in a \$34.2 million

net gain and \$43.3 million net loss, for a combined net loss of \$9.1 million.

The following tables present the unpaid principal balance and fair value of investments, including investments 90 days or more past due, and long-term debt of the CLOs:

(in thousands)	Total Investments	Investments 90 Days or More Past Due	Long-term Debt
as of December 31, 2011			
Unpaid principal balance	\$ 883,718	\$ 17,697	\$ 1,040,484
Excess unpaid principal over fair value	(46,525 )	(6,036 )	(191,819 )
Fair value	\$ 837,193	\$ 11,661	\$ 848,665
(in thousands)			
as of September 30, 2011			
Unpaid principal balance	\$ 887,838	\$ 21,577	\$ 1,044,863
Excess unpaid principal over fair value	(65,226 )	(10,178 )	(173,636 )
Fair value	\$ 822,612	\$ 11,399	\$ 871,227

#### Automobile Loan Securitization Trusts

The Company retained certain interests in and servicing responsibilities for automobile loan securitization trusts, which originated from securitization transactions between the Company and the securitization trusts in previous years. The following table provides details of the loans serviced by the Company that were held by the securitization trusts and the loans that were managed together with them:

(in thousands)	December 31, 2011	September 30, 2011
Principal amount of loans		
Loans receivable of consolidated VIEs	\$ 128,901	\$ 155,071
Loans receivable	75,337	83,791
Total	\$ 204,238	\$ 238,862
Principal amount of loans 30 days or more past due		
Loans receivable of consolidated VIEs	\$ 3,322	\$ 3,651
Loans receivable	1,507	1,721
Total	\$ 4,829	\$ 5,372

The Company has provided guarantees to cover shortfalls for the securitization trusts in amounts due to the holders of the asset-backed securities if the shortfall exceeds cash on deposit. The maximum potential amount of future payments related to these guarantees was \$3.8 million at December 31, 2011 and September 30, 2011. The Company did not provide any additional financial or other support to the securitization trusts or the holders of the asset-backed securities during fiscal year 2011 or the three months ended December 31, 2011.

The original amount of loans serviced for the securitization trusts that were still in existence at December 31, 2011 and September 30, 2011 totaled \$1.2 billion. At December 31, 2011 and September 30, 2011, the securitization trusts had approximately 17,200 and 19,100 loans outstanding, with weighted-average annualized interest rates of 10.56% and 10.55%.

#### Other Investment Products

The carrying values of the Company's investment management and related service fees receivable from and the equity ownership interests in the other investment product VIEs as recorded in the Company's condensed consolidated balance sheets are set forth below. These amounts represent the Company's maximum exposure to loss from these investment products.

(in thousands)	December 31, 2011	September 30, 2011
Current Assets		
Receivables	\$41,710	\$42,218
Investment securities, available-for-sale	130,807	139,981
Investments in equity method investees and other	160	154
Total Current	172,677	182,353
Non-Current Assets		
Investments in equity method investees and other	40,237	36,584
Total	\$212,914	\$218,937

The Company's total assets under management ("AUM") of the other investment products was \$31.3 billion at December 31, 2011 and \$36.1 billion at September 30, 2011.

While the Company has no contractual obligation to do so, it routinely makes cash investments in the course of launching sponsored investment products. The Company also may voluntarily elect to provide its sponsored investment products with additional direct or indirect financial support based on its business objectives. The Company did not provide financial or other support to its investment products during fiscal year 2011 or the three months ended December 31, 2011.

#### Note 6 – Investments

Investments consisted of the following:

(in thousands)	December 31, 2011	September 30, 2011
Current		
Investment securities, trading	\$1,056,668	\$889,686
Investment securities, available-for-sale		
Sponsored investment products	701,572	925,711
Securities of U.S. states and political subdivisions	35,926	41,199
Securities of the U.S. Treasury and federal agencies	600	602
Other equity securities	18,067	23,464
Total investment securities, available-for-sale	756,165	990,976
Investments of consolidated VIEs, at fair value	10,561	10,994
Investments in equity method investees and other	20,693	21,861
Total Current	\$1,844,087	\$1,913,517
Banking/Finance		
Investment securities, available-for-sale		
Securities of U.S. states and political subdivisions	\$308	\$311
Securities of the U.S. Treasury and federal agencies	1,820	1,837
Corporate debt securities <sup>1</sup>	121,231	121,634
Mortgage-backed securities – agency residential	208,180	221,611
Other equity securities	82	93
Total investment securities, available-for-sale	331,621	345,486
Total Banking/Finance	\$331,621	\$345,486
Non-Current		
Investments of consolidated sponsored investment products	\$623,326	\$584,608
Investments of consolidated VIEs, at fair value	826,632	811,618
Investments in equity method investees and other	558,620	535,509
Total Non-Current	\$2,008,578	\$1,931,735

<sup>1</sup> Corporate debt securities are insured by the Federal Deposit Insurance Corporation or non-U.S. government agencies.

<sup>2</sup> Consists of U.S. government-sponsored enterprise obligations.

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At December 31, 2011 and September 30, 2011, current investment securities, trading included \$443.2 million and \$361.1 million of investments held by sponsored investment products that were consolidated in the Company's condensed consolidated financial statements.

At December 31, 2011 and September 30, 2011, banking/finance segment investment securities with aggregate carrying amounts of \$147.0 million and \$156.4 million were pledged as collateral for the ability to borrow from the Federal Reserve Bank, and \$57.0 million and \$60.8 million were pledged as collateral for outstanding Federal Home Loan Bank ("FHLB") borrowings and amounts available in secured FHLB short-term borrowing capacity (see Note 8 – Debt). In addition, investment management and related services segment securities with an aggregate carrying value of \$6.9 million were pledged as collateral primarily for financing arrangements at December 31, 2011 and September 30, 2011.

A summary of the gross unrealized gains and losses relating to investment securities, available-for-sale is as follows:

(in thousands)	Gross Unrealized			
as of December 31, 2011	Cost Basis	Gains	Losses	Fair Value
Sponsored investment products	\$656,542	\$72,115	\$(27,085)	\$701,572
Securities of U.S. states and political subdivisions	34,854	1,380	—	36,234
Securities of the U.S. Treasury and federal agencies	2,397	25	(2)	2,420
Corporate debt securities	120,012	1,219	—	121,231
Mortgage-backed securities – agency residential	203,945	4,239	(4)	208,180
Other equity securities	17,651	587	(89)	18,149
Total	\$1,035,401	\$79,565	\$(27,180)	\$1,087,786

(in thousands)	Gross Unrealized			
as of September 30, 2011	Cost Basis	Gains	Losses	Fair Value
Sponsored investment products	\$877,632	\$78,013	\$(29,934)	\$925,711
Securities of U.S. states and political subdivisions	39,950	1,560	—	41,510
Securities of the U.S. Treasury and federal agencies	2,423	16	—	2,439
Corporate debt securities	120,041	1,593	—	121,634
Mortgage-backed securities – agency residential	216,736	4,905	(30)	221,611
Other equity securities	23,061	703	(207)	23,557
Total	\$1,279,843	\$86,790	\$(30,171)	\$1,336,462

The net unrealized holding gains on investment securities, available-for-sale included in accumulated other comprehensive income were \$7.8 million and \$15.3 million for the three months ended December 31, 2011 and 2010. The following tables show the gross unrealized losses and fair values of investment securities, available-for-sale with unrealized losses aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position:

(in thousands)	Less Than 12 Months		12 Months or Greater		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
as of December 31, 2011						
Sponsored investment products	\$184,370	\$(26,298)	\$6,202	\$(787)	\$190,572	\$(27,085)
Securities of the U.S. Treasury and federal agencies	560	(2)	—	—	560	(2)
Mortgage-backed securities – agency residential	16,844	(4)	—	—	16,844	(4)
Other equity securities	—	—	4,269	(89)	4,269	(89)
Total	\$201,774	\$(26,304)	\$10,471	\$(876)	\$212,245	\$(27,180)

(in thousands) as of September 30, 2011	Less Than 12 Months		12 Months or Greater		Total	
	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
Sponsored investment products	\$228,926	\$(29,731 )	\$4,658	\$(203 )	\$233,584	\$(29,934 )
Mortgage-backed securities – agency residential	18,305	(30 )	—	—	18,305	(30 )
Other equity securities	8	(1 )	4,116	(206 )	4,124	(207 )
Total	\$247,239	\$(29,762 )	\$8,774	\$(409 )	\$256,013	\$(30,171 )

The Company did not recognize any other-than-temporary impairment of investments for the three months ended December 31, 2011. For the three months ended December 31, 2010, the Company recognized \$13.2 million of other-than-temporary impairment of investments, of which \$7.3 million related to available-for-sale equity securities and none related to available-for-sale debt securities.

At December 31, 2011, contractual maturities of available-for-sale debt securities were as follows:

(in thousands)	Cost Basis	Fair Value
Due in one year or less	\$109,500	\$110,653
Due after one year through five years	38,055	39,024
Due after five years through ten years	25,161	26,927
Due after ten years	188,492	191,461
Total	\$361,208	\$368,065

## Note 7 – Fair Value Measurements

The Company records the majority of its investments at fair value or amounts that approximate fair value. The tables below present the balances of assets and liabilities measured at fair value on a recurring basis.

(in thousands) as of December 31, 2011	Level 1	Level 2	Level 3	Total
<b>Current Assets</b>				
Cash and cash equivalents of consolidated VIEs	\$14,415	\$57,901	\$—	\$72,316
Receivables of consolidated VIEs	—	16,970	—	16,970
Investment securities, trading	747,065	250,466	59,137	1,056,668
Investment securities, available-for-sale				
Sponsored investment products	701,572	—	—	701,572
Securities of U.S. states and political subdivisions	—	35,926	—	35,926
Securities of the U.S. Treasury and federal agencies	—	600	—	600
Other equity securities	13,815	4,252	—	18,067
Investments of consolidated VIEs	—	10,561	—	10,561
<b>Banking/Finance Assets</b>				
Investment securities, available-for-sale				
Securities of U.S. states and political subdivisions	—	308	—	308
Securities of the U.S. Treasury and federal agencies	—	1,820	—	1,820
Corporate debt securities	—	121,231	—	121,231
Mortgage-backed securities – agency residential	—	208,180	—	208,180
Other equity securities	—	—	82	82
<b>Non-Current Assets</b>				
Investments of consolidated sponsored investment products	6,295	191	616,840	623,326
Investments of consolidated VIEs	—	823,150	3,482	826,632
Life settlement contracts	—	—	11,123	11,123
<b>Total Assets Measured at Fair Value</b>	<b>\$1,483,162</b>	<b>\$1,531,556</b>	<b>\$690,664</b>	<b>\$3,705,382</b>
<b>Current Liabilities</b>				
Current maturities of long-term debt of consolidated VIEs	\$—	\$—	\$24,924	\$24,924
Other liabilities of consolidated VIEs	—	37,010	—	37,010
<b>Non-Current Liabilities</b>				
Long-term debt of consolidated VIEs	—	763,374	60,367	823,741
<b>Total Liabilities Measured at Fair Value</b>	<b>\$—</b>	<b>\$800,384</b>	<b>\$85,291</b>	<b>\$885,675</b>

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(in thousands)	Level 1	Level 2	Level 3	Total
as of September 30, 2011				
<b>Current Assets</b>				
Cash and cash equivalents of consolidated VIEs	\$ 14,700	\$ 73,538	\$—	\$ 88,238
Receivables of consolidated VIEs	—	11,953	—	11,953
Investment securities, trading	579,225	279,308	31,153	889,686
Investment securities, available-for-sale				
Sponsored investment products	925,711	—	—	925,711
Securities of U.S. states and political subdivisions	—	41,199	—	41,199
Securities of the U.S. Treasury and federal agencies	—	602	—	602
Other equity securities	19,365	4,099	—	23,464
Investments of consolidated VIEs	—	10,994	—	10,994
<b>Banking/Finance Assets</b>				
Investment securities, available-for-sale				
Securities of U.S. states and political subdivisions	—	311	—	311
Securities of the U.S. Treasury and federal agencies	—	1,837	—	1,837
Corporate debt securities	—	121,634	—	121,634
Mortgage-backed securities – agency residential	—	221,611	—	221,611
Other equity securities	—	—	93	93
<b>Non-Current Assets</b>				
Investments of consolidated sponsored investment products	7,084	92	577,432	584,608
Investments of consolidated VIEs	—	809,762	1,856	811,618
Life settlement contracts	—	—	10,813	10,813
<b>Total Assets Measured at Fair Value</b>	<b>\$ 1,546,085</b>	<b>\$ 1,576,940</b>	<b>\$ 621,347</b>	<b>\$ 3,744,372</b>
<b>Current Liabilities</b>				
Current maturities of long-term debt of consolidated VIEs	\$—	\$—	\$ 24,858	\$ 24,858
Other liabilities of consolidated VIEs	—	32,315	—	32,315
<b>Non-Current Liabilities</b>				
Long-term debt of consolidated VIEs	—	787,301	59,068	846,369
<b>Total Liabilities Measured at Fair Value</b>	<b>\$—</b>	<b>\$ 819,616</b>	<b>\$ 83,926</b>	<b>\$ 903,542</b>

There were no significant transfers between Level 1 and Level 2 during the three months ended December 31, 2011 and 2010. The changes in Level 3 assets and liabilities measured at fair value on a recurring basis were as follows:

(in thousands)	Securities			Total	Long-term
for the three months ended December 31, 2011	Held by Consolidated Sponsored Investment Products	Investments of Consolidated VIEs	Other <sup>1</sup>	Level 3 Assets	Debt of Consolidated VIEs
Balance at October 1, 2011	\$ 608,585	\$ 1,856	\$ 10,906	\$ 621,347	\$ (83,926 )
Realized and unrealized gains (losses) included in investment and other income, net	(9,948 )	40	890	(9,018 )	(2,938 )
Purchases	80,808	—	471	81,279	—
Sales	(3,954 )	(1 )	(11 )	(3,966 )	—
Settlements	(237 )	—	(1,051 )	(1,288 )	—
Transfers into Level 3	—	1,587	—	1,587	—
Effect of exchange rate changes	723	—	—	723	1,573
Balance at December 31, 2011	\$ 675,977	\$ 3,482	\$ 11,205	\$ 690,664	\$ (85,291 )
Change in unrealized gains (losses) included in net income relating to assets and liabilities held	\$ (9,948 )	\$ 40	\$ 330	\$ (9,578 )	\$ (2,938 )

at December 31, 2011<sup>2</sup>

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<sup>1</sup> Other primarily consists of life settlement contracts.

<sup>2</sup> Included in investment and other income, net.

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(in thousands)	Securities Held by Consolidated Sponsored Investment Products	Residual Interests from Securitization Transactions	Investments of Consolidated VIEs	Other <sup>1</sup>	Total Level 3 Assets	Long-term Debt of Consolidated VIEs
for the three months ended December 31, 2010						
Balance at October 1, 2010	\$ 3,330	\$ 23,362	\$ —	\$ 9,365	\$ 36,057	\$ —
Adjustment for adoption of new consolidation guidance	—	(23,362 )	1,738	—	(21,624 )	(71,382 )
Realized and unrealized gains (losses) included in investment and other income, net	154	—	193	703	1,050	(14,899 )
Purchases, sales and settlements, net	1,417	—	—	(522 )	895	—
Transfers into Level 3	35	—	—	—	35	—
Effect of exchange rate changes	—	—	—	—	—	1,028
Balance at December 31, 2010	\$ 4,936	\$ —	\$ 1,931	\$ 9,546	\$ 16,413	\$ (85,253 )
Change in unrealized gains (losses) included in net income relating to assets and liabilities held at December 31, 2010 <sup>2</sup>	\$ 401	\$ —	\$ 193	\$ 314	\$ 908	\$ (14,899 )

<sup>1</sup> Other primarily consists of life settlement contracts.

<sup>2</sup> Included in investment and other income, net.

The Company's financial instruments that were not measured at fair value were as follows:

(in thousands)	December 31, 2011		September 30, 2011	
	Carrying Value	Estimated Fair Value	Carrying Value	Estimated Fair Value
<b>Financial Assets</b>				
Cash and cash equivalents	\$4,839,542	\$4,839,542	\$5,110,375	\$5,110,375
Other investments	54,220	59,511	51,259	56,908
Loans receivable, net	390,120	393,955	401,860	403,116
Loans receivable of consolidated VIEs, net	124,529	126,393	149,386	153,175
<b>Financial Liabilities</b>				
Commercial paper	\$25,000	\$25,000	\$29,997	\$29,997
Deposits	1,028,343	1,030,496	890,189	892,719
FHLB advances	69,000	73,001	69,000	72,575
Long-term debt	980,936	1,010,180	1,034,037	1,059,301
Long-term debt of consolidated VIEs	135,652	138,148	164,176	167,877

## Note 8 – Debt

Outstanding debt consisted of the following:

(dollars in thousands)	December 31, 2011	Effective Interest Rate	September 30, 2011	Effective Interest Rate	
Current					
Commercial paper	\$25,000	0.13	% \$29,997	0.16	%
Current maturities of long-term debt of consolidated sponsored investment products	6,589	2.25	% 29,656	4.39	%
Current maturities of long-term debt of consolidated VIEs, at fair value	24,924	8.49	% 24,858	8.49	%
Total Current	56,513		84,511		
Banking/Finance					
Long-term debt of consolidated VIEs, due fiscal years 2014-2016	135,652	6.61	% 164,176	5.86	%
FHLB advances	69,000	3.30	% 69,000	3.30	%
Total Banking/Finance	204,652		233,176		
Non-Current					
Senior notes					
\$300 million 2.000% notes due fiscal year 2013	299,754	2.28	% 299,710	2.28	%
\$250 million 3.125% notes due fiscal year 2015	249,814	3.32	% 249,800	3.32	%
\$350 million 4.625% notes due fiscal year 2020	349,674	4.75	% 349,664	4.75	%
	899,242		899,174		
Long-term debt of consolidated sponsored investment products, due fiscal years 2014-2017	75,105	5.56	% 105,207	5.54	%
Long-term debt of consolidated VIEs, at fair value, due fiscal years 2015-2019	823,741	1.01	% 846,369	0.88	%
Total Non-Current	1,798,088		1,850,750		
Total Debt	\$2,059,253		\$2,168,437		

The current and non-current long-term debt of consolidated sponsored investment products has both fixed and floating interest rates ranging from 1.98% to 7.32%. The repayment of amounts outstanding under certain debt agreements is secured by the assets of the consolidated sponsored investment products and, in some cases, a pledge of a right to call capital.

The current and non-current long-term debt of consolidated VIEs consists of debt of the consolidated CLOs and has both fixed and floating interest rates ranging from 0.61% to 11.18%. The banking/finance long-term debt of consolidated VIEs consists of debt of the consolidated securitization trusts and has both fixed and floating interest rates ranging from 2.18% to 8.18%. See Note 5 – Variable Interest Entities.

The debt holders of the consolidated sponsored investment products and VIEs have no recourse to the Company's assets beyond the level of the Company's direct investment in these entities.

The banking/finance segment secures advances from the FHLB to fund its retail banking and consumer lending services. The outstanding advances are subject to collateralization requirements.

The Company's senior unsecured and unsubordinated notes have an aggregate face value of \$900.0 million and contain an optional redemption feature that allows the Company to redeem each series of notes prior to maturity in whole or in part at any time, at a make-whole redemption price. The indenture governing the notes contains limitations on the Company's ability and the ability of its subsidiaries to pledge voting stock or profit participating equity interests in its subsidiaries to secure other debt without similarly securing the notes equally and ratably. The indenture also includes requirements that must be met if the Company consolidates or merges with, or sells all or substantially all of its assets to, another entity. As of December 31, 2011, the Company was in compliance with the covenants of the notes.





At December 31, 2011, contractual maturities for FHLB advances, senior notes, long-term debt of consolidated sponsored investment products, and long-term debt of consolidated VIEs were as follows:  
(in thousands)

for the fiscal years ending September 30,	FHLB Advances and Senior Notes	Long-term Debt of Consolidated Sponsored Investment Products and Consolidated VIEs	Total
2012	\$—	\$31,513	\$31,513
2013	318,254	—	318,254
2014	—	19,232	19,232
2015	260,314	83,335	343,649
2016	8,000	90,420	98,420
Thereafter	381,674	841,511	1,223,185
Total	\$968,242	\$1,066,011	\$2,034,253

The consolidated VIEs may prepay their debt obligations prior to contractual maturity dates as a result of collateral asset repayments.

At December 31, 2011, the Company had \$475.0 million of short-term commercial paper available for issuance under an uncommitted private placement program, and \$14.7 million available in uncommitted short-term bank lines of credit. The banking/finance segment had \$270.0 million available in uncommitted short-term bank lines of credit under the Federal Reserve system, \$144.1 million available through the secured Federal Reserve Bank short-term discount window and \$15.0 million available in secured FHLB short-term borrowing capacity.

#### Note 9 – Commitments and Contingencies

##### Guarantees

The Company is obligated to cover shortfalls for the automobile loan securitization trusts in amounts due to the holders of the asset-backed securities up to certain levels (see Note 5 – Variable Interest Entities).

At December 31, 2011, the banking/finance segment had issued financial standby letters of credit totaling \$11.8 million on which beneficiaries would be able to draw in the event of non-performance by its customers, primarily in relation to lease and lien obligations of these banking customers. These standby letters of credit were fully collateralized by marketable securities as of December 31, 2011.

##### Legal Proceedings

Beginning in 2003, Franklin and certain related parties were named in civil lawsuits related to industry-wide market timing and late trading investigations by regulators. Two of the lawsuits, a consolidated class action (Sharkey IRO/IRA v. Franklin Resources, Inc., et al., Case No. 04-cv-01310) and a consolidated derivative action brought on behalf of certain Franklin Templeton Investments mutual funds (the “Funds”) (McAlvey v. Franklin Resources, Inc., et al., Case No. 04-cv-01274), were dismissed in December 2011, as described below, and one final lawsuit, a derivative action brought on behalf of Franklin (Hertz v. Burns, et al., Case No. 04-cv-01624), remains pending.

With respect to the class action, as previously reported, the Company and lead plaintiff reached agreement-in-principle on December 21, 2010 to resolve that action, pursuant to which the Company agreed to pay \$2.75 million towards distribution of settlement amounts reached in lead plaintiff’s settlements with other, non-Company defendants, and towards class counsel’s fees, with any unspent amount to be distributed to relevant Funds. The parties documented the terms of the agreement in a stipulation (the “Stipulation and Releases”). The court issued its final approval of the Stipulation and Releases on December 9, 2011, and dismissed the consolidated class action. The dismissal is now final and the action is resolved.

Pursuant to stipulation, the consolidated Fund derivative action was stayed beginning in December 2010, pending a decision of appeal in another case involving a different mutual fund complex. Following issuance of the decision of appeal in the other case, on December 20, 2011, the plaintiffs in the consolidated Fund derivative action filed a

voluntarily dismissal of the action with prejudice, with no settlement by any Company-related defendants. The court entered the dismissal as its order on December 23, 2011. The dismissal is now final and the action is resolved.

The derivative action brought on behalf of Franklin against certain current and former Franklin directors was stayed, pursuant to stipulation, since 2004. On January 18, 2012, plaintiff filed a notice of voluntary dismissal without prejudice in the action. Defendants are seeking a dismissal of the action with prejudice and raised the issue with the court. The court has since set a briefing schedule to enable the defendants to move for summary judgment, with all briefing to be completed by April 18, 2012. The action does not seek any recovery from Franklin and therefore the Company does not anticipate any additional losses relating to market timing litigation.

The Company is from time to time involved in litigation relating to other claims arising in the normal course of business. Management is of the opinion that the ultimate resolution of such claims will not materially affect the Company's business, financial position, results of operations or liquidity. In management's opinion, an adequate accrual has been made as of December 31, 2011, to provide for any probable losses that may arise from these matters for which the Company could reasonably estimate an amount.

#### Other Commitments and Contingencies

At December 31, 2011, the banking/finance segment had commitments to extend credit in an aggregate amount of \$51.3 million, primarily under secured credit lines.

The Company, in its role as agent or trustee, facilitates the settlement of investor share purchase, redemption and other transactions with affiliated mutual funds. The Company is appointed by the affiliated mutual funds as agent or trustee to manage, on behalf of the affiliated mutual funds, bank deposit accounts that contain only (i) cash remitted by investors to the affiliated mutual funds for the direct purchase of fund shares, or (ii) cash remitted by the affiliated mutual funds for direct delivery to the investors for either the proceeds of fund shares liquidated at the investors' direction, or dividends and capital gains earned on fund shares. As of December 31, 2011 and September 30, 2011, the Company held cash of \$403.2 million and \$124.5 million off-balance sheet in agency or trust for investors and the affiliated mutual funds.

At December 31, 2011, there were no changes that would have a material effect on the other commitments and contingencies reported in the Company's Form 10-K for fiscal year 2011.

#### Note 10 – Stock-Based Compensation

Stock awards generally entitle holders to the right to sell the underlying shares of the Company's common stock once the awards vest. Stock unit awards generally entitle holders to receive the underlying shares of common stock once the awards vest. Certain performance-based long-term stock and stock unit awards have been granted that generally vest based on the achievement of predetermined Company financial performance goals. In the event a performance measure is not achieved at or above a specified threshold level, the portion of the award tied to such performance measure is forfeited.

Total unrecognized compensation cost related to nonvested stock and stock unit awards, net of estimated forfeitures, was \$181.3 million at December 31, 2011. This cost is expected to be recognized over a remaining weighted-average vesting period of 2.2 years.

The following table summarizes nonvested stock and stock unit award activity:

(shares in thousands)	Shares	Weighted-Average Grant-Date Fair Value
Nonvested balance at September 30, 2011	1,085	\$ 114.57
Granted	1,092	106.65
Vested	(166)	) 110.26
Forfeited/canceled	(14)	) 109.95
Nonvested Balance at December 31, 2011	1,997	\$ 110.63

#### Note 11 – Segment Information

The Company has two operating segments, investment management and related services and banking/finance. The Company derives substantially all of its operating revenues from providing investment management and related services to its sponsored investment products and the sub-advised accounts that it manages. This is the Company's primary business and operating segment. The Company's investment management and related services are marketed to the public globally under six distinct brand names: Franklin, Templeton, Mutual Series, Bissett, Fiduciary and Darby.

The Company's secondary business and operating segment is banking/finance. The banking/finance segment offers select retail banking, private banking and consumer lending services through its bank subsidiaries. The consumer lending activities

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include real estate equity lines, and home equity/mortgage and automobile lending.

Financial information for the Company's two operating segments is presented in the table below. Inter-segment transactions are immaterial and excluded from segment income and assets. Operating revenues of the banking/finance segment are reported net of interest expense and the provision for loan losses.

(in thousands)	Three Months Ended	
	December 31, 2011	2010
Operating Revenues		
Investment management and related services	\$ 1,694,723	\$ 1,693,721
Banking/finance	7,153	6,592
Total	\$ 1,701,876	\$ 1,700,313
Income Before Taxes		
Investment management and related services	\$ 691,472	\$ 693,961
Banking/finance	3,519	3,706
Total	\$ 694,991	\$ 697,667

Operating revenues of the banking/finance segment were as follows:

(in thousands)	Three Months Ended	
	December 31, 2011	2010
Interest and fees on loans	\$ 7,497	\$ 10,889
Interest and dividends on investment securities	1,716	2,423
Total interest income	9,213	13,312
Interest on deposits	(843	) (1,136
Interest on long-term debt	(3,055	) (4,642
Total interest expense	(3,898	) (5,778
Net interest income	5,315	7,534
Other income	1,572	1,903
Provision for loan losses	266	(2,845
Total	\$ 7,153	\$ 6,592

Operating segment assets were as follows:

(in thousands)	December 31,	September 30,
	2011	2011
Investment management and related services	\$ 11,930,213	\$ 12,417,720
Banking/finance	1,475,274	1,358,123
Total	\$ 13,405,487	\$ 13,775,843

The investment management and related services segment incurs substantially all of the Company's depreciation and amortization costs and expenditures on long-lived assets.

## Note 12 – Other Income (Expenses)

Other income (expenses) consisted of the following:

(in thousands)	Three Months Ended	
	December 31, 2011	2010
Investment and Other Income (Losses), Net		
Dividend income	\$6,815	\$10,230
Interest income	2,093	2,860
Gains on trading investment securities, net	4,929	817
Losses on non-current investments of consolidated sponsored investment products, net	(10,077 )	—
Gains (losses) on assets and liabilities of consolidated VIEs, net	22,685	(9,070 )
Realized gains on sale of investment securities, available-for-sale	14,393	26,749
Realized losses on sale of investment securities, available-for-sale	(1,508 )	(307 )
Income from investments in equity method investees, net of tax	22,472	23,892
Other-than-temporary impairment of investment securities, available-for-sale	—	(7,293 )
Other-than-temporary impairment of investments in equity method investees and other	—	(5,863 )
Foreign currency exchange gains, net	5,159	904
Other, net	4,215	3,409
Total	71,176	46,328
Interest expense	(8,565 )	(7,895 )
Other Income, Net	\$62,611	\$38,433

Substantially all of the Company's dividend income and realized gains and losses on sale of investment securities, available-for-sale were generated by investments in its sponsored investment products. Interest income was primarily generated by investments in cash equivalents, trading securities and debt securities of U.S. states and political subdivisions. Proceeds from the sale of investment securities, available-for-sale were \$253.2 million and \$140.0 million for the three months ended December 31, 2011 and 2010.

Gains on trading investment securities, net included \$5.6 million and \$0.7 million of net losses on investments of consolidated sponsored investment products for the three months ended December 31, 2011 and 2010. The Company recognized net gains on trading investment securities that were held at December 31, 2011 and 2010 of \$3.8 million and \$0.6 million during the three months ended December 31, 2011 and 2010.

Substantially all of the net gains (losses) of consolidated sponsored investment products and consolidated VIEs are offset in noncontrolling interests in the Company's condensed consolidated statements of income.

## Note 13 – Banking Regulatory Ratios

Franklin is a bank holding company and a financial holding company subject to various U.S. capital adequacy requirements. Based on the Company's calculations, it exceeded the applicable U.S. Federal Reserve Board requirements as listed below.

(dollar amounts in thousands)	December 31, 2011	September 30, 2011	Capital Adequacy Minimum		
Tier 1 capital	\$5,821,484	\$6,141,354	N/A		
Total risk-based capital	5,830,876	6,152,248	N/A		
Tier 1 leverage ratio	51	% 55	% 5		%
Tier 1 risk-based capital ratio	52	% 53	% 4		%
Total risk-based capital ratio	52	% 53	% 8		%

## Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

### Forward-Looking Statements

In this section, we discuss and analyze the results of operations and financial condition of Franklin Resources, Inc. ("Franklin") and its subsidiaries (collectively, the "Company"). In addition to historical information, we also make statements relating to the future, called "forward-looking" statements, which are provided under the "safe harbor" protection of the U.S. Private Securities Litigation Reform Act of 1995. Forward-looking statements are generally written in the future tense and/or are preceded by words such as "will," "may," "could," "expect," "believe," "anticipate," "intend," "plan," "seek," "estimate," or other similar words. Moreover, statements that speculate about future events are forward-looking statements. These forward-looking statements involve a number of known and unknown risks, uncertainties and other important factors that could cause actual results and outcomes to differ materially from any future results or outcomes expressed or implied by such forward-looking statements. You should carefully review the "Risk Factors" section set forth below, which describe these risks, uncertainties and other important factors in more detail.

While forward-looking statements are our best prediction at the time that they are made, you should not rely on them. Forward-looking statements are based on our current expectations and assumptions regarding our business, the economy and other future conditions. Because forward-looking statements relate to the future, they are subject to inherent uncertainties, risks and changes in circumstances that are difficult to predict. We caution you therefore against relying on any of these forward-looking statements. They are neither statements of historical fact nor guarantees or assurances of future performance. Factors or events that could cause our actual results to differ may emerge from time to time, and it is not possible for us to predict all of them. If a circumstance occurs after the date of this Form 10-Q that causes any of our forward-looking statements to be inaccurate, whether as a result of new information, future developments or otherwise, we do not have an obligation, and we undertake no obligation, to announce publicly the change to our expectations, or to make any revisions to our forward-looking statements, unless required by law.

The following discussion should be read in conjunction with our Form 10-K for the fiscal year ended September 30, 2011 ("fiscal year 2011") filed with the U.S. Securities and Exchange Commission (the "SEC"), and the condensed consolidated financial statements and notes thereto included elsewhere in this Form 10-Q.

### Overview

We are a global investment management organization and derive substantially all of our operating revenues and net income from providing investment management and related services to investors in jurisdictions worldwide through products that include registered open-end and closed-end funds, unregistered funds, and institutional, high net-worth and separately-managed accounts (collectively, our "sponsored investment products"). Our services include fund administration, shareholder services, transfer agency, sales, distribution, custodial, trustee and other fiduciary services. Our sponsored investment products and investment management and related services are distributed or marketed to the public globally under six distinct brand names: Franklin, Templeton, Mutual Series, Bissett, Fiduciary and Darby. We offer a broad range of sponsored investment products through equity, hybrid, fixed-income and cash management funds and accounts, including alternative investment products, that meet a wide variety of specific investment needs of individual and institutional investors. We also manage certain sub-advised investment products which may be sold to the public under one of our brand names or that of other companies.

The level of our revenues depends largely on the level and relative mix of assets under management ("AUM"). As noted in the "Risk Factors" section set forth below, the amount and mix of our AUM are subject to significant fluctuations and can negatively impact our revenues and income. The level of our revenues also depends on mutual fund sales and the number of mutual fund shareholder accounts. The fees charged for our services are based on contracts with our sponsored investment products or our clients. These arrangements could change in the future.

Our secondary business is banking/finance. Our banking/finance group offers select retail banking, private banking and consumer lending services through our banking and finance subsidiaries. Our banking and consumer lending activities include real estate equity lines and home equity/mortgage and automobile lending.

During the three months ended December 31, 2011, market returns improved following the volatility and negative sentiment in the global financial markets during the previous quarter, evidenced by 8% and 12% increases in the

MSCI World Index and the S&P 500 Index. Despite the positive market results during the quarter, the European sovereign debt crisis has not been resolved and volatility is likely to continue.

Our total AUM at December 31, 2011 was \$670.3 billion, 2% higher than at September 30, 2011, and essentially unchanged from the balance at December 31, 2010. Simple monthly average AUM (“average AUM”) for the three months ended December 31, 2011 decreased 6% from the previous quarter and increased 3% from the same period in the prior fiscal year. Net new flows turned negative during the quarter, with net outflows of \$15.6 billion, as long-term sales decreased 30% to \$38.2 billion from the prior-



year period. The decreases occurred in all investment objectives with the exception of U.S. taxable fixed-income and were more significant in our global/international fixed-income and equity products which experienced strong sales during the more favorable economic environment in the prior year. Redemption activity was consistent from year to year.

The business and regulatory environments in which we operate remain uncertain and subject to change. The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the "Reform Act") may impose additional restrictions and limitations on our business. We will continue to review and evaluate the Reform Act and the extent of its impact on our business as the various rules and regulations required for implementation continue to be adopted. Uncertainties regarding economic stabilization and improvement remain in the foreseeable future. As we continue to confront the challenges of the current economic and regulatory environments, we remain focused on the investment performance of our sponsored investment products and on providing high quality customer service to our clients. While we are focused on expense management, we will also seek to attract, retain and develop employees and invest strategically in systems and technology that will provide a secure and stable environment. We will continue to protect and further our brand recognition while developing and maintaining broker/dealer and client relationships. The success of these and other strategies may be influenced by the factors discussed in the "Risk Factors" section set forth below.

#### RESULTS OF OPERATIONS

(dollar amounts in millions, except per share data)	Three Months Ended December 31,		Percent Change
	2011	2010	
Operating Income	\$632.4	\$659.2	(4)%
Net Income Attributable to Franklin Resources, Inc.	480.8	501.2	(4)%
Earnings per Share			
Basic	\$2.21	\$2.24	(1)%
Diluted	2.20	2.23	(1)%
Operating Margin <sup>1</sup>	37.2	% 38.8	%

<sup>1</sup> Defined as operating income divided by total operating revenues.

Operating income and net income attributable to Franklin Resources, Inc. decreased \$26.8 million and \$20.4 million for the three months ended December 31, 2011 primarily due to a prior year \$26.5 million reduction to operating expenses from net insurance recoveries for previous years' losses.

Diluted earnings per share decreased consistent with the decrease in net income, largely offset by a 3% decrease in diluted average common shares outstanding primarily resulting from the repurchase of shares of our common stock.

## Assets Under Management

AUM by investment objective was as follows:

(dollar amounts in billions)	December 31, 2011	December 31, 2010	Percent Change	
Equity				
Global/international	\$194.5	\$219.1	(11	)%
United States	75.7	77.0	(2	)%
Total equity	270.2	296.1	(9	)%
Hybrid	96.4	106.1	(9	)%
Fixed-Income				
Tax-free	74.1	71.4	4	%
Taxable				
Global/international	174.7	144.7	21	%
United States	48.9	45.9	7	%
Total fixed-income	297.7	262.0	14	%
Cash Management	6.0	6.5	(8	)%
Total	\$670.3	\$670.7	0	%
Simple Monthly Average for the Three-Month Period <sup>1</sup>	\$675.0	\$655.6	3	%

<sup>1</sup> Investment management fees from approximately 60% of our AUM at December 31, 2011 were calculated using daily average AUM.

AUM at December 31, 2011 remained essentially unchanged from December 31, 2010 as net new flows of \$17.6 billion and \$12.5 billion from acquisitions were offset by market depreciation of \$27.4 billion during the twelve-month period. The market depreciation mostly related to global/international equity and fixed-income products as market volatility during the quarter ended September 30, 2011 led to significant valuation decreases in these categories, which were partially offset by valuation increases in U.S. fixed-income products.

Average AUM, which is generally more indicative of trends in revenue for providing investment management and fund administration services than the year-over-year change in ending AUM, increased 3% during the three months ended December 31, 2011, as compared to the same period in the prior fiscal year.

The average mix of AUM by investment objective is shown below. The change in mix towards fixed-income products for the three months ended December 31, 2011 reflects investor preference for globally diversified fixed-income investments and significant valuation decreases in global/international equity products during the past year.

	Three Months Ended December 31,			
	2011		2010	
Equity				
Global/international	29	%	32	%
United States	11	%	12	%
Total equity	40	%	44	%
Hybrid	14	%	16	%
Fixed-Income				
Tax-free	11	%	11	%
Taxable				
Global/international	27	%	21	%
United States	7	%	7	%
Total fixed-income	45	%	39	%
Cash Management	1	%	1	%

Total	100	%	100	%
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Components of the change in our AUM were as follows:

(dollar amounts in billions)	Three Months Ended December 31,		Percent Change	
	2011	2010		
Beginning AUM	\$659.9	\$644.9	2	%
Long-term sales	38.2	54.9	(30)	)%
Long-term redemptions	(53.0	) (52.8	) 0	%
Net cash management	(0.8	) 1.1	NM	
Net new flows	(15.6	) 3.2	NM	
Reinvested distributions	7.3	5.8	26	%
Net flows	(8.3	) 9.0	NM	
Distributions	(8.5	) (7.3	) 16	%
Appreciation and other	27.2	24.1	13	%
Ending AUM	\$670.3	\$670.7	0	%

Components of the change in our AUM by investment objective were as follows:

(in billions) for the three months ended	Equity			Fixed-Income			Cash Management	Total
	Global/ International	United States	Hybrid	Tax-Free	Taxable Global/ International	Taxable United States		
December 31, 2011								
AUM at September 30, 2011	\$185.8	\$68.4	\$101.3	\$72.0	\$178.8	\$46.9	\$6.7	\$659.9
Long-term sales	9.8	3.7	4.1	2.8	14.2	3.6	—	38.2
Long-term redemptions	(10.4	) (4.3	) (15.1	) (2.2	) (17.7	) (3.3	) —	(53.0
Net exchanges	(0.7	) 0.1	0.1	0.2	(0.5	) 0.7	0.1	—
Net cash management	—	—	—	—	—	—	(0.8	) (0.8
Net new flows	(1.3	) (0.5	) (10.9	) 0.8	(4.0	) 1.0	(0.7	) (15.6
Reinvested distributions	1.5	1.3	1.2	0.6	2.3	0.4	—	7.3
Net flows	0.2	0.8	(9.7	) 1.4	(1.7	) 1.4	(0.7	) (8.3
Distributions	(1.8	) (1.4	) (1.4	) (0.8	) (2.6	) (0.5	) —	(8.5
Appreciation and other	10.3	7.9	6.2	1.5	0.2	1.1	—	27.2
AUM at December 31, 2011	\$194.5	\$75.7	\$96.4	\$74.1	\$174.7	\$48.9	\$6.0	\$670.3
(in billions) for the three months ended								
December 31, 2010								
AUM at September 30, 2010	\$204.2	\$69.5	\$110.8	\$77.7	\$130.7	\$45.4	\$6.6	\$644.9
Long-term sales	15.6	4.3	5.1	3.1	23.5	3.3	—	54.9
Long-term redemptions	(14.6	) (3.8	) (15.8	) (4.2	) (11.5	) (2.9	) —	(52.8
Net exchanges	0.4	0.2	0.3	(0.9	) 1.5	(0.2	) (1.3	) —
Net cash management	—	—	—	—	—	—	1.1	1.1
Net new flows	1.4	0.7	(10.4	) (2.0	) 13.5	0.2	(0.2	) 3.2
Reinvested distributions	1.6	1.1	1.1	0.5	1.2	0.3	—	5.8
Net flows	3.0	1.8	(9.3	) (1.5	) 14.7	0.5	(0.2	) 9.0
Distributions	(2.2	) (1.1	) (1.4	) (0.8	) (1.4	) (0.4	) —	(7.3
Appreciation (depreciation) and other	14.1	6.8	6.0	(4.0	) 0.7	0.4	0.1	24.1
	\$219.1	\$77.0	\$106.1	\$71.4	\$144.7	\$45.9	\$6.5	\$670.7

AUM at December 31,  
2010

AUM increased \$10.4 billion or 2% during the quarter ended December 31, 2011, driven by market appreciation of \$27.2 billion and partially offset by net new outflows of \$15.6 billion. The market appreciation primarily resulted from equity and hybrid products as improved market conditions led to valuation increases, evidenced by 8% and 12% increases in the MSCI World Index and the S&P 500 Index. Net new outflows resulted as long-term sales decreased 30% to \$38.2 billion as compared to the prior-year period, while redemptions remained almost unchanged. Ongoing investor concerns related to the European sovereign debt

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crisis and general negative market sentiment contributed to the lower sales and continued long-term redemptions, most notably in our global/international fixed-income and equity products. Redemptions included \$11.1 billion from an institutional advisory account in the hybrid objective.

AUM increased \$25.8 billion or 4% during the quarter ended December 31, 2010, driven by market appreciation of \$24.1 billion and net new flows of \$3.2 billion. The market appreciation primarily resulted from equity and hybrid products as the global economy recovered and generated higher returns, evidenced by 9% and 11% increases in the MSCI World Index and the S&P 500 Index. The net new flows were driven by strong sales in our global/international fixed-income products, and were partially offset by a \$12.0 billion redemption from the same institutional advisory account in the hybrid objective.

The average mix of AUM by sales region is shown below.

(dollar amounts in billions)	Three Months Ended		Percent Change
	December 31,		
	2011	2010	
United States	\$439.0	\$442.7	(1)%
Europe, the Middle East and Africa	107.4	97.3	10%
Asia-Pacific	72.4	60.4	20%
Canada	30.5	32.9	(7)%
Latin America <sup>1</sup>	25.7	22.3	15%
Total	\$675.0	\$655.6	3%

<sup>1</sup> Latin America sales region includes North America-based advisors serving non-resident clients.

Growth in our international business reflects strong new flows in Europe and Asia. Due to the global nature of our business operations, investment management and related services may be performed in locations unrelated to the sales region.

#### Investment Performance Overview

Our primary focus is on the long-term investment performance of our sponsored investment products. A standard measure of the performance of a large group of these products is the percentage of AUM exceeding benchmarks and peer group medians. The performance of our products against such benchmarks and peer group medians is presented in the table below.

As of December 31, 2011	Benchmark Comparison				Peer Group Comparison			
	% of AUM Exceeding Benchmark				% of AUM in Top Two Quartiles			
	1-Year	3-Year	5-Year	10-Year	1-Year	3-Year	5-Year	10-Year
Equity								
Global/international	54%	38%	51%	57%	76%	63%	55%	64%
United States	25%	24%	54%	77%	79%	40%	60%	54%
Total equity	45%	33%	52%	65%	77%	56%	57%	60%
Hybrid	14%	97%	14%	96%	94%	99%	95%	97%
Fixed-Income								
Tax-free	82%	65%	0%	0%	77%	25%	92%	92%
Taxable								
Global/international	2%	97%	92%	92%	6%	71%	70%	99%
United States	40%	77%	32%	52%	20%	21%	40%	45%
Total fixed-income	30%	85%	57%	56%	28%	50%	71%	87%

AUM measured in the benchmark and peer group rankings represents 83% and 80% of our total AUM as of December 31, 2011. The benchmark comparisons are based on each fund's return as compared to a market index that has been selected to be generally consistent with the investment objectives of the fund. The peer group rankings are sourced from Lipper, Morningstar or eVestment in each fund's market and asset-weighted in U.S. dollars. Private equity, certain privately-offered emerging market and real estate funds, cash management and U.K. unit trusts and Australian equity funds acquired in 2011 are not included. Certain other funds and products were also excluded because of

limited benchmark or peer group data. Had this data been available, the results may have been different. These results assume the reinvestment of dividends, are based on data available as of January 18, 2012 and are subject to revision. While we remain focused on achieving strong long-term performance, our future benchmark and peer group rankings may vary from our past performance.

## Operating Revenues

In the quarter ended September 30, 2011, we discontinued the classification of a portion of the investment management fees earned by certain of our non-U.S. subsidiaries as sales and distribution fees. Amounts for the comparative prior fiscal year period have been reclassified to conform to the current year presentation. See Note 1 – Basis of Presentation in the notes to condensed consolidated financial statements in Item 1 of Part I of this Form 10-Q. The table below presents the percentage change in each revenue category.

(dollar amounts in millions)	Three Months Ended		Percent Change	
	December 31,			
	2011	2010		
Investment management fees	\$1,075.1	\$1,066.5	1	%
Sales and distribution fees	524.3	552.2	(5	)%
Shareholder servicing fees	75.4	72.1	5	%
Other, net	27.1	9.5	185	%
Total Operating Revenues	\$1,701.9	\$1,700.3	0	%
Investment Management Fees				

Investment management fees are generally calculated under contractual arrangements with our sponsored investment products and the sub-advised products that we manage as a percentage of the market value of AUM. Annual rates vary by investment objective and type of services provided.

Investment management fees increased \$8.6 million for the three months ended December 31, 2011. The increase was driven by a 31% increase in average AUM of global/international fixed-income products, which resulted from strong sales during fiscal year 2011. The global/international fixed-income AUM increase was partially offset by average AUM decreases in global/international equity products of 6% and hybrid products of 10%, resulting in a total average AUM increase of 3%. The overall increase in global/international products led to higher investment management fees as they generally earn higher fees than U.S. products because they include fees to offset higher distribution costs.

The fee increase from higher AUM was largely offset by a decrease in the effective management fee rate (investment management fees divided by average AUM) to 63.7 basis points for the three months ended December 31, 2011 from 65.1 basis points for the prior-year period. The decrease in the rate primarily resulted from lower performance-based fees during the current quarter and lower levels and weighting of global/international equity AUM, which generally carry the highest fee rates. The rate decrease was partially offset by an increase in the U.S. hybrid rate due to the loss of an \$11.1 billion institutional advisory account that had a low fee rate.

Performance-based investment management fees were de minimus and \$10.8 million for the three months ended December 31, 2011 and 2010.

Our product offerings and global operations are diverse. As such, the impact of future changes in the market value of AUM on investment management fees will be affected by the relative mix of investment objective, geographic region, distribution channel and investment vehicle of the assets.

### Sales and Distribution Fees

We earn fees from the sale of certain classes of sponsored investment products on which investors pay a commission at the time of purchase (“commissionable sales”). Sales commissions are reduced or eliminated on some share classes and for some sale transactions depending upon the amount invested and the type of investor. Therefore, sales fees will change with the overall level of gross sales, the size of individual transactions, and the relative mix of sales between different share classes and types of investors.

Globally, our mutual funds and certain other products generally pay us distribution fees in return for sales, marketing and distribution efforts on their behalf. Specifically, the majority of U.S.-registered mutual funds, with the exception of certain of our money market mutual funds, have adopted distribution plans under Rule 12b-1 (the “Rule 12b-1 Plans”) promulgated under the Investment Company Act of 1940 (the “Investment Company Act”). The Rule 12b-1 Plans permit the mutual funds to bear certain expenses relating to the distribution of their shares, such as expenses for marketing, advertising, printing and sales promotion, subject to the Rule 12b-1 Plans’ limitations on amounts. The individual Rule 12b-1 Plans set a percentage limit for Rule 12b-1 expenses based on average daily net AUM of the mutual fund. Similar arrangements exist for the distribution of our non-U.S. funds where, generally, the distributor of



the funds in the local market arranges for and pays commissions.

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We pay a significant portion of sales and distribution fees to the financial advisers and other intermediaries who sell our sponsored investment products to the public on our behalf. See the description of sales, distribution and marketing expenses below.

Overall, sales and distribution fees decreased \$27.9 million for the three months ended December 31, 2011. Sales fees decreased 19% to \$155.5 million primarily due to a 22% decrease in total commissionable sales, partially offset by a higher mix of U.S. product sales, which typically generate higher sales fees than international products.

Distribution fees were \$368.8 million for the three months ended December 31, 2011, increasing 2% over the prior-year period primarily due to a higher mix of international AUM as discussed above in the "Investment Management Fees" section. Distribution fees on international products are generally higher than on U.S. products.

#### Shareholder Servicing Fees

We receive shareholder servicing fees as compensation for providing transfer agency services, which include providing customer statements, transaction processing, customer service, and tax reporting. These fees are generally fixed charges per shareholder account that vary with the particular type of fund and the service being rendered. In some instances, we charge sponsored investment products these fees based on the level of AUM. In the U.S., transfer agency service agreements provide that accounts closed in a calendar year generally remain billable at a reduced rate through the second quarter of the following calendar year. In Canada, such agreements provide that accounts closed in the calendar year remain billable for four months after the end of the calendar year. Accordingly, the level of fees will vary with the change in open accounts and the level of closed accounts that remain billable.

Shareholder servicing fees increased \$3.3 million for the three months ended December 31, 2011 primarily due to a \$3.2 million increase in Europe resulting from a change in fee structures that became effective on January 1, 2011 and a 7% increase in simple monthly average billable shareholder accounts originated in Europe.

#### Other, Net

Other, net revenue primarily consists of investment income from our consolidated sponsored investment products and revenues from the banking/finance segment. Investment income from our consolidated sponsored investment products consists of dividend and interest income. Banking/finance revenues include interest income on loans and servicing income and are reduced by interest expense and the provision for loan losses.

Other, net revenue increased \$17.6 million for the three months ended December 31, 2011 primarily due to a \$17.0 million increase in investment income from our consolidated sponsored investment products, including \$10.3 million related to limited partnerships and similar structures that were consolidated as of September 30, 2011.

#### Operating Expenses

The table below presents the percentage change in each operating expense category.

(dollar amounts in millions)	Three Months Ended December 31,		Percent Change	
	2011	2010		
Sales, distribution and marketing	\$630.6	\$647.1	(3	)%
Compensation and benefits	300.4	292.4	3	%
Information systems and technology	41.4	40.4	2	%
Occupancy	31.8	30.9	3	%
General, administrative and other	65.2	30.3	115	%
Total Operating Expenses	\$1,069.4	\$1,041.1	3	%
Sales, Distribution and Marketing				

Sales, distribution and marketing expenses primarily consist of payments to financial advisers, broker/dealers and other third parties for providing services to investors in our sponsored investment products, including marketing support services. These payments are generally determined as percentages of either AUM or sales. Also included is the amortization of deferred sales commissions related to up-front commissions on shares sold without a front-end sales charge to shareholders. The deferred sales commissions are amortized over the periods in which commissions are generally recovered from distribution fee revenues and contingent sales charges received from shareholders of the funds upon redemption of their shares.



Sales, distribution and marketing expenses by cost driver are presented below:

(dollar amounts in millions)	Three Months Ended December 31,		Percent Change	
	2011	2010		
Asset-based expenses	\$457.5	\$433.5	6	%
Sales-based expenses	139.7	171.4	(18)	)%
Amortization of deferred sales commissions	33.4	42.2	(21)	)%
Sales, Distribution and Marketing	\$630.6	\$647.1	(3)	)%

Asset-based expenses increased \$24.0 million for the three months ended December 31, 2011 primarily due to a \$17.9 million increase in distribution expenses on international products resulting from an 11% increase in average international AUM. Distribution expenses on U.S. products increased \$4.0 million mainly resulting from a higher mix of Class C assets, which have higher expense rates than other U.S. product classes. Distribution expenses, which are typically higher for international products, are generally not directly correlated with distribution fee revenues due to international fee structures which provide for recovery of certain distribution costs through investment management fees.

Sales-based expenses decreased \$31.7 million for the three months ended December 31, 2011 primarily due to a 22% decrease in total commissionable sales.

Amortization of deferred sales commissions decreased \$8.8 million for the three months ended December 31, 2011 primarily due to a \$5.7 million decrease related to lower sales of U.S. Class A and C shares sold without a front-end sales charge to shareholders and a \$3.1 million decrease related to U.S. Class B shares, which were fully amortized in the prior year.

#### Compensation and Benefits

Compensation and benefit expenses increased \$8.0 million for the three months ended December 31, 2011 primarily due to an increase in salaries, wages and benefits, partially offset by a decrease in variable compensation. Salaries, wages and benefits increased \$12.5 million primarily due to a \$10.4 million increase in salaries and wages resulting from higher staffing levels and annual merit salary adjustments that were effective December 1, 2011. Variable compensation decreased \$4.2 million, mainly due to a \$3.0 million decrease related to private equity performance fees. At December 31, 2011, our global workforce had increased to approximately 8,500 employees from approximately 8,000 employees at December 31, 2010.

We continue to place a high emphasis on our pay for performance philosophy. As such, any changes in the underlying performance of our sponsored investment products or changes in the composition of our incentive compensation offerings could have an impact on compensation and benefit expenses going forward. However, in order to attract and retain talented individuals, our level of compensation and benefit expenses may increase more quickly or decrease more slowly than our revenue.

#### Information Systems and Technology

Information systems and technology costs increased \$1.0 million for the three months ended December 31, 2011 primarily due to higher investments in strategic technology projects for operational and regulatory purposes.

Details of capitalized information systems and technology costs are shown below.

(in millions)	Three Months Ended December 31,	
	2011	2010
Net carrying value at beginning of period	\$67.9	\$63.9
Additions, net of disposals	17.7	5.0
Amortization	(7.4)	(9.4)
Net Carrying Value at End of Period	\$78.2	\$59.5

Occupancy  
The Company conducts its worldwide operations using a combination of leased and owned facilities. Occupancy costs include rent and other facilities-related costs including depreciation and utilities.

Occupancy costs increased \$0.9 million for the three months ended December 31, 2011 primarily due to higher property taxes and facility improvement costs.

### General, Administrative and Other

General, administrative and other operating expenses primarily consist of fund administration services and shareholder servicing fees payable to external parties, advertising and promotion costs, corporate travel and entertainment, professional fees, and other miscellaneous expenses.

General, administrative and other operating expenses increased \$34.9 million for the three months ended December 31, 2011 primarily due to \$26.5 million of net insurance recoveries during the first quarter of fiscal year 2011 for losses incurred in previous years, \$4.2 million in current year expenses of limited partnerships and similar structures that were consolidated as of September 30, 2011 and a \$4.2 million increase in advertising and promotion expenses due to higher levels of business activity. The increases were partially offset by a \$2.6 million decrease from consulting fees incurred in the prior year related to private equity performance fees.

We are committed to investing in advertising and promotion in response to changing business conditions, and to advance our products where we see continued or potential new growth opportunities. As a result of potential changes in our strategic marketing campaigns, the level of advertising and promotion expenditures may increase more rapidly, or decrease more slowly, than our revenues.

### Other Income (Expenses)

(in millions)	Three Months Ended	
	December 31,	
	2011	2010
Investment and other income, net	\$71.2	\$46.3
Interest expense	(8.6	) (7.9
Other Income (Expenses), Net	\$62.6	\$38.4

Other income (expenses) includes net investment and other income and interest expense from our investment management and related services business. Net investment and other income consists primarily of dividend and interest income, gains (losses) from trading investments and non-current investments of consolidated sponsored investment products, gains (losses) of assets and liabilities of consolidated VIEs, realized gains (losses) on sales of available-for-sale investment securities, income from equity method investees, other-than-temporary impairments and foreign currency exchange gains.

Other income (expenses) increased \$24.2 million for the three months ended December 31, 2011 primarily due to market valuation gains. Higher valuations resulted in \$22.7 million of net gains from the changes in fair value of the assets and liabilities of consolidated collateralized loan obligations (“CLOs”) as compared to net losses of \$9.1 million in the prior-year period and in a \$4.1 million increase in net gains on trading investment securities. In addition, lower valuations during the prior year resulted in \$13.2 million in other-than-temporary impairments on certain available-for-sale and equity investments. The increases were partially offset by a \$13.6 million decrease in net realized gains on sale of available-for-sale investment securities and \$10.1 million of net losses on non-current investments of limited partnerships and similar structures that were consolidated as of September 30, 2011.

Substantially all of the net gains (losses) of consolidated CLOs and consolidated sponsored investment products are offset in noncontrolling interests in our condensed consolidated statements of income.

Our investments in sponsored investment products include initial cash investments made in the course of launching mutual fund and other investment product offerings, as well as investments for other business reasons. The market conditions that impact our AUM similarly affect the investment income earned or losses incurred on our sponsored investment product investments.

### Taxes on Income

As a multi-national corporation, we provide investment management and related services to a wide range of international sponsored investment products, often managed from locations outside the U.S. Some of these jurisdictions have lower tax rates than the U.S. The mix of pre-tax income (primarily from our investment management and related services business) subject to these lower rates, when aggregated with income originating in the U.S., produces a lower overall effective income tax rate than existing U.S. federal and state income tax rates.

Our effective income tax rate for the three months ended December 31, 2011 was 28.96%, as compared to 29.75% for the same period in the prior fiscal year. The decrease was primarily due to an increase in forecasted non-U.S. earnings

in lower tax jurisdictions, an increase in net income attributable to noncontrolling interests, and a decrease in state tax due to new legislation.

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The effective income tax rate for future reporting periods will continue to reflect the relative contributions of non-U.S. earnings that are subject to reduced tax rates and that are not currently included in U.S. taxable income. Changes in tax rates in these jurisdictions may affect our effective income tax rate and net income.

#### LIQUIDITY AND CAPITAL RESOURCES

The following table summarizes certain key financial data relating to our cash flows and uses of capital.

(in millions)	Three Months Ended	
	December 31,	
	2011	2010
Cash Flow Data		
Operating cash flows	\$167.7	\$245.8
Investing cash flows	236.4	244.1
Financing cash flows	(681.4 )	(292.7 )

Net cash provided by operating activities decreased during the three months ended December 31, 2011 despite a slight increase in net income due to decreases in other liabilities and commissions payable as compared to increases in the prior-year period, payments of accrued compensation and benefits, and net gains of consolidated VIEs as compared to net losses in the prior year. Net cash provided by investing activities decreased mainly due to higher purchases of investments, net of liquidations. Net cash used in financing activities increased primarily due to higher dividends paid on common stock and common stock repurchases, partially offset by an increase in banking deposits and higher subscriptions of noncontrolling interests.

The assets and liabilities of our consolidated VIEs and consolidated sponsored investment products in the form of limited partnerships and similar structures do not impact our liquidity and capital resources. We have no right to these entities' assets, beyond our direct investment in, and management fees generated from these entities, which are eliminated upon consolidation. The debt holders of these entities have no recourse to our assets beyond the level of our direct investment in these entities and, therefore, we bear no risks associated with these liabilities. Accordingly, the assets and liabilities of our consolidated VIEs and consolidated sponsored investment products in the form of limited partnerships and similar structures are excluded from the discussion below.

The following table summarizes certain key balance sheet data relating to our liquidity and debt.

(in millions)	December 31, 2011	September 30, 2011
Assets		
Cash and cash equivalents	\$4,798.1	\$5,033.1
Receivables	720.9	746.8
Investments	2,133.5	2,206.6
Total liquid assets	\$7,652.5	\$7,986.5
Liabilities		
Debt		
Commercial paper	\$25.0	\$30.0
Federal Home Loan Bank advances	69.0	69.0
Long-term debt	899.2	899.2
Total debt	\$993.2	\$998.2

#### Liquidity

Liquid assets consist of cash and cash equivalents, current receivables, and current and certain other investments (trading, available-for-sale, investments in equity method investees consisting of mutual fund sponsored investment products, and other). Cash and cash equivalents include cash on hand, non-interest-bearing and interest-bearing deposits with financial institutions, federal funds sold, time deposits, U.S. government-sponsored enterprise obligations, securities of the U.S. Treasury and federal agencies, debt instruments with original maturities of three months or less at the purchase date and other highly liquid investments, including money market funds, which are readily convertible into cash.



Cash and cash equivalents at December 31, 2011 decreased primarily due to net cash used in financing activities, partially offset by net cash provided by investing and operating activities. At December 31, 2011, the percentages of cash and cash equivalents held by our U.S. and non-U.S. operations were approximately 38% and 62%, as compared to approximately 45% and 55% at September 30, 2011.

We utilize a significant portion of our liquid assets to fund operational and regulatory requirements and capital contributions relating to our sponsored investment products. Certain of our subsidiaries are required by our internal policies or applicable regulations to maintain minimum levels of capital which are partially maintained by retaining cash and cash equivalents. As a result, such subsidiaries may be restricted in their ability to transfer cash to their parent companies. Also, certain of our non-U.S. subsidiaries are subject to regulatory or contractual repatriation restrictions or requirements. Such restrictions and requirements limit our ability to transfer cash between various international jurisdictions, including repatriation to the U.S. Should we require more capital in the U.S. than is generated domestically, we could elect to reduce the level of discretionary activities, such as share repurchases, or we could elect to repatriate future earnings from non-U.S. jurisdictions or raise capital through debt or equity issuance. Certain of these alternatives could result in higher effective tax rates, increased interest expense or other dilution to our earnings. As of December 31, 2011, our U.S. and non-U.S. subsidiaries held approximately \$2,294.9 million and \$1,933.7 million of our liquid assets to satisfy operational and regulatory requirements and capital contributions to our sponsored investment products, as compared to approximately \$2,140.4 million and \$1,933.5 million held at September 30, 2011.

#### Capital Resources

We believe that we can meet our present and reasonably foreseeable operating cash needs and future commitments through existing liquid assets, continuing cash flows from operations, the ability to issue debt or equity securities and borrowing capacity under current credit facilities.

At December 31, 2011, our outstanding commercial paper had a total face value of \$25.0 million and a weighted-average annualized interest rate of 0.13%.

The banking/finance segment secures advances from the Federal Home Loan Bank (the "FHLB") to fund its retail banking and consumer lending services. At December 31, 2011, we had \$69.0 million of FHLB advances outstanding. These advances had a weighted-average interest rate of 3.30% at December 31, 2011 and are subject to collateralization requirements.

In May 2010, we issued senior unsecured and unsubordinated notes with a face value of \$900.0 million. Of the notes, \$300.0 million was issued at a fixed interest rate of 2.000% per annum and matures in 2013, \$250.0 million was issued at a fixed interest rate of 3.125% per annum and matures in 2015 and \$350.0 million was issued at a fixed interest rate of 4.625% and matures in 2020. Interest is payable semi-annually. The indenture governing the notes contains limitations on our ability and the ability of our subsidiaries to pledge voting stock or profit participating equity interests in our subsidiaries to secure other debt without similarly securing the notes equally and ratably. As of December 31, 2011, we were in compliance with the covenants of the notes.

At December 31, 2011, we had \$475.0 million of short-term commercial paper available for issuance under an uncommitted private placement program and \$14.7 million available in uncommitted short-term bank lines of credit. Our banking/finance segment had \$270.0 million available in uncommitted short-term bank lines of credit under the Federal Reserve system, \$144.1 million available through the secured Federal Reserve Bank short-term discount window and \$15.0 million available in secured FHLB short-term borrowing capacity.

Our ability to access the capital markets in a timely manner depends on a number of factors, including our credit rating, the condition of the global economy, investors' willingness to purchase our securities, interest rates, credit spreads and the valuation levels of equity markets. If we are unable to access capital markets in a timely manner, our business could be adversely impacted.

#### Uses of Capital

We expect that our main uses of cash will be to expand our core business, make strategic acquisitions, acquire shares of our common stock, fund property and equipment purchases, invest in our sponsored investment products, pay operating expenses of the business, enhance technology infrastructure and business processes, pay stockholder dividends and repay and service debt.

On December 8, 2011, our Board of Directors declared a regular quarterly cash dividend of \$0.27 per share and a special cash dividend of \$2.00 per share, both of which were paid on December 30, 2011 to stockholders of record on December 19, 2011.

During the three months ended December 31, 2011, we redeemed \$70.2 million, net of investments, from our sponsored investment products.

We maintain a stock repurchase program to manage our equity capital with the objective of maximizing shareholder value. Our stock repurchase program is effected through regular open-market purchases and private transactions in accordance with applicable laws and regulations. During the three months ended December 31, 2011, we repurchased 3.0 million shares of our common stock at a cost of \$290.9 million. In December 2011, our Board of Directors authorized the repurchase of up to 10.0 million additional shares of our common stock under our stock repurchase program. At December 31, 2011, approximately 11.8 million shares of our common stock remained available for repurchase under our stock repurchase program. Our stock repurchase program is not subject to an expiration date.

The funds that we manage have their own resources available for purposes of providing liquidity to meet shareholder redemptions, including securities that can be sold or provided to investors as in-kind redemptions, and lines of credit. While we have no contractual obligation to do so, we may voluntarily elect to provide the funds with direct or indirect financial support based on our business objectives.

#### CONTRACTUAL OBLIGATIONS AND COMMERCIAL COMMITMENTS

Our contractual obligations and commercial commitments are summarized in our Form 10-K for the fiscal year ended September 30, 2011. At December 31, 2011, there were no material changes outside the ordinary course in our contractual obligations and commercial commitments from September 30, 2011.

#### OFF-BALANCE SHEET ARRANGEMENTS

In our role as agent or trustee, we facilitate the settlement of investor share purchase, redemption, and other transactions with affiliated mutual funds. We are appointed by the affiliated mutual funds as agent or trustee to manage, on behalf of the affiliated mutual funds, bank deposit accounts that contain only (i) cash remitted by investors to the affiliated mutual funds for the direct purchase of fund shares, or (ii) cash remitted by the affiliated mutual funds for direct delivery to the investors for either the proceeds of fund shares liquidated at the investors' direction, or dividends and capital gains earned on fund shares. As of December 31, 2011 and September 30, 2011, we held cash of approximately \$403.2 million and \$124.5 million off-balance sheet in agency or trust for investors and the affiliated mutual funds.

#### CRITICAL ACCOUNTING POLICIES

Our consolidated financial statements and accompanying notes are prepared in accordance with accounting principles generally accepted in the United States of America, which require the use of estimates, judgments, and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the periods presented. Actual results may differ from those estimates under different assumptions. The following are updates to our critical accounting policies disclosed in Management's Discussion and Analysis of Financial Condition and Results of Operations in our Form 10-K for the fiscal year ended September 30, 2011.

##### Fair Value Measurements

We record the majority of our investments in the consolidated financial statements at fair value or amounts that approximate fair value. We use a three-level fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value based on whether the inputs to those valuation techniques are observable or unobservable. As of December 31, 2011, Level 3 assets represented 18.6% of total assets measured at fair value, substantially all of which related to investments of consolidated sponsored investment products in equity and secured and unsecured debt securities of entities in emerging markets which are not traded in active markets. Level 3 liabilities, comprised of long-term debt of consolidated VIEs, represented 9.6% of total liabilities measured at fair value at December 31, 2011. There were immaterial transfers into and no transfers out of Level 3 during the three months ended December 31, 2011.

##### Goodwill and Other Intangible Assets

We performed our annual impairment tests for goodwill and indefinite-lived intangible assets as of August 1, 2011. There were no impairments to these assets subsequent to the annual tests as we determined no events occurred or circumstances changed that would more likely than not reduce the fair value of a reporting unit below its carrying value, or indicate that our indefinite-lived intangible assets might be impaired.

We test definite-lived intangible assets for impairment quarterly. As of December 31, 2011, the undiscounted future cash flow projections for \$37.7 million, or 74% of our definite-lived intangible assets exceeded their carrying values by more than 25%. We estimated the future undiscounted cash flows for these assets using AUM growth rates ranging from 0% to 8%. As of December 31, 2011, a decline in their related AUM of 21% could cause us to evaluate whether their fair value is below the carrying value. There was no impairment of definite-lived intangible assets for the three months ended December 31, 2011.

##### Revenues

Investment management and distribution fees are generally determined based on a percentage of AUM. The AUM of our sponsored investment products is calculated using fair value methods derived primarily from unadjusted quoted

market prices, unadjusted independent third-party broker or dealer price quotes in active markets, or market prices or price quotes adjusted for observable price movements after the close of the primary market. The fair values of securities for which market prices are not readily available are internally valued using various methodologies which incorporate unobservable inputs as appropriate for each

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security type. As of December 31, 2011, our total AUM by fair value hierarchy level was 48.0% Level 1, 50.7% Level 2 and 1.3% Level 3.

#### NEW ACCOUNTING GUIDANCE

See Note 2 – New Accounting Guidance in the notes to condensed consolidated financial statements in Item 1 of Part I of this Form 10-Q.

#### RISK FACTORS

Volatility and disruption of the capital and credit markets, and adverse changes in the global economy, may significantly affect our results of operations and may put pressure on our financial results. The capital and credit markets continue to experience volatility and disruption worldwide. Declines in global financial market conditions have in the past resulted in significant decreases in our AUM, revenues and income, and future declines may negatively impact our performance. Such declines have had and may in the future have an adverse impact on our results of operations. Even if legislative or regulatory initiatives or other efforts successfully stabilize and add liquidity to the financial markets, we may need to modify our business, strategies or operations, and we may be subject to additional constraints or costs in order to satisfy new regulatory requirements or to compete in a changed business environment.

The amount and mix of our AUM are subject to significant fluctuations. Fluctuations in the amount and mix of our AUM may be attributable in part to market conditions outside of our control that have had, and in the future could have, a negative impact on our revenues and income. We derive substantially all of our operating revenues and net income from providing investment management and related services. The level of our revenues depends largely on the level and mix of AUM. Any decrease in the value or amount of our AUM because of market volatility or other factors negatively impacts our revenues and income. We are subject to an increased risk of asset volatility from changes in the global financial and equity markets. Individual financial and equity markets may be adversely affected by economic, political, financial or other instabilities that are particular to the country or regions in which a market is located, including without limitation local acts of terrorism, economic crises, political protests, insurrection or other business, social or political crises. Declines in these markets have caused in the past, and may cause in the future, a decline in our revenues and income. Global economic conditions, exacerbated by war, terrorism or financial crises, changes in the equity marketplace, unanticipated changes in currency exchange rates, interest rates, inflation rates, the yield curve, defaults by derivative counterparties, bond default risks, the sovereign debt crisis in Europe and other factors that are difficult to predict affect the mix, market values and levels of our AUM. The funds we manage may be subject to an unanticipated large number of redemptions as a result of such events, causing the funds to sell securities they hold, possibly at a loss, or draw on any available lines of credit to obtain cash to settle these redemptions, or settle in-kind with securities held in the applicable fund. The Company, in its discretion, may also provide financial support to a fund to enable it to maintain sufficient liquidity in such event. Our investment management services revenues are derived primarily from fees based on a percentage of the value of AUM and vary with the nature of the account or product managed. A decline in the price of stocks or bonds, or in particular market segments, or in the securities market generally, could cause the value and returns on our AUM to decline, resulting in a decline in our revenues and income. Moreover, changing market conditions may cause a shift in our asset mix between international and U.S. assets, potentially resulting in a decline in our revenues and income depending upon the nature of our AUM and the level of management fees we earn based on them. Additionally, changing market conditions may cause a shift in our asset mix towards fixed-income products and a related decline in our revenues and income, as we generally derive higher fee revenues and income from equity assets than from fixed-income products we manage. On the other hand, increases in interest rates, in particular if rapid, or high interest rates, as well as any uncertainty in the future direction of interest rates, may have a negative impact on our fixed-income products as rising interest rates or interest rate uncertainty typically decrease the total return on many bond investments due to lower market valuations of existing bonds. Any decrease in the level of our AUM resulting from price declines, interest rate volatility or uncertainty, increased redemptions or other factors could negatively impact our revenues and income.

We are subject to extensive and complex, overlapping and frequently changing rules, regulations and legal interpretations. There is uncertainty associated with the regulatory environment in which we operate. Our investment management and related services business and our banking/finance business are subject to extensive and complex,

overlapping and frequently changing rules, regulations and legal interpretations in the countries in which we operate, including, among others, securities, banking, accounting, tax, ethics and privacy laws and regulations. The Reform Act enacted in 2010, as well as other legislative and regulatory changes, may impose additional restrictions and limitations on us and will likely result in increased scrutiny and oversight of our financial services and products as the various rules and regulations required for implementation continue to be adopted. Due to the complexity and broad scope of the Reform Act and time required for regulatory implementation, we are not able to predict at this time the specific requirements that will be adopted by regulatory agencies having authority over us pursuant to the Reform Act, or the impact of any changes in regulation.

Financial reporting requirements, and the processes, controls and procedures that have been put in place to address them, are often comprehensive and complex. We may be adversely affected as a result of new or revised legislation or regulations or by changes in the interpretation of existing laws and regulations. While management has focused attention and resources on our compliance policies, procedures and practices, non-compliance with applicable laws or rules or regulations, conflicts of interest requirements or fiduciary principles, or our inability to keep up with, or adapt to, an ever changing, complex regulatory environment, could result in civil liability, criminal liability and/or sanctions against us, including fines and censures, injunctive relief, suspension or expulsion from a particular jurisdiction or market or the revocation of licenses, any of which could adversely affect our reputation, prospects, revenues and income.

We are subject to U.S. federal securities laws, state laws regarding securities fraud, other federal and state laws and rules and regulations of certain regulatory and self-regulatory organizations, including those rules and regulations promulgated by, among others, the SEC, the Financial Industry Regulatory Authority and the New York Stock Exchange. We are also subject to regulation by non-U.S. regulations and regulators, and U.S. regulations and regulators such as the Department of Justice and the SEC with respect to the Foreign Corrupt Practices Act of 1977, with respect to our non-U.S. operations and/or trading in our securities that take place outside the U.S. Certain of our subsidiaries are registered with the SEC under the Investment Advisers Act of 1940 and many of our funds are registered with the SEC under the Investment Company Act, both of which impose numerous obligations, as well as detailed operational requirements, on our subsidiaries which are investment advisers to registered investment companies. Our subsidiaries must comply with a myriad of complex and changing U.S. and/or non-U.S. rules and regulations, some of which may conflict, as well as complex tax regimes. Additionally, as we continue to expand our operations, sometimes rapidly, into more non-U.S. jurisdictions, the rules and regulations of these non-U.S. jurisdictions become applicable, sometimes with short compliance deadlines, and add further regulatory complexity to our ongoing compliance operations.

In addition, we are a bank holding company and a financial holding company subject to the supervision and regulation of the Federal Reserve Board (the “FRB”) and are subject to the restrictions, limitations and prohibitions of the Bank Holding Company Act of 1956 (the “BHC Act”) and the Gramm-Leach-Bliley Act. The provisions of the Reform Act are expected to have an impact on our banking/finance business. Significant aspects of the Reform Act relate to changes in the regulation of banks, thrifts, holding companies and related institutions, including with respect to regulation and supervision in the banking industry, and the imposition of various restrictions and limitations on certain activities of such entities. The Reform Act includes a number of measures that will increase capital and liquidity requirements, impose limits on leverage, and enhance supervisory authority and regulatory oversight of non-banking entities which may apply to our business. The FRB may impose additional limitations or restrictions on our activities, including if the FRB believes that we do not have the appropriate financial and managerial resources to commence or conduct an activity or make an acquisition. Further, our subsidiary, Fiduciary Trust Company International, is subject to extensive regulation, supervision and examination by the Federal Deposit Insurance Corporation and New York State Banking Department, while other subsidiaries are subject to oversight by the Office of the Comptroller of the Currency and various state regulators. The laws and regulations imposed by these regulators generally involve restrictions and requirements in connection with a variety of technical, specialized, and expanding matters and concerns. For example, compliance with anti-money laundering and Know-Your-Customer requirements, both domestically and internationally, and the Bank Secrecy Act has taken on heightened importance with regulators as a result of efforts to, among other things, limit terrorism. At the same time, there has been increased regulation with respect to the protection of customer privacy and the need to secure sensitive customer information. As we continue to address these requirements or focus on meeting new or expanded ones, we may expend a substantial amount of time and resources, even though our banking/finance business does not constitute our dominant business sector. Any inability to meet these requirements, within the timeframes set by regulators, may subject us to sanctions or other restrictions by the regulators that could impact our broader business. Moreover, being subject to banking regulation may put us at a disadvantage compared to our competitors which are not subject to such requirements.

Regulatory and legislative actions and reforms have made the regulatory environment in which we operate more costly and future actions and reforms could adversely impact our AUM, increase costs and negatively impact our



profitability and future financial results. Since 2001, the federal securities laws have been augmented substantially and made significantly more complex by, among other measures, the Sarbanes-Oxley Act of 2002, the USA Patriot Act of 2001 and the Reform Act. Moreover, the adoption of new laws or regulations and changes in the interpretation or enforcement of existing laws or regulations have directly affected, and may continue to affect, our business. With new laws and changes in interpretation of existing requirements, the associated time we must dedicate to, and related costs we must incur in, meeting the regulatory complexities of our business have increased. In particular, many provisions of the Reform Act require the adoption of rules to implement the Reform Act and mandate multiple studies, which could result in additional legislative or regulatory action. We may be required to invest significant management time and resources to address the various provisions of the Reform Act and the numerous regulations that are required to be issued under it. In addition, the SEC has proposed changes to Rule 12b-1 promulgated under the Investment Company Act which, if adopted, could limit our ability to recover expenses relating to the distribution of our funds. Outlays associated with meeting regulatory complexities have also increased as we expand our business into new jurisdictions. Compliance activities to meet these and other new legal requirements have required us to expend additional time and resources, and, consequently, we are

incurring increased costs of doing business, which potentially negatively impacts our profitability and future financial results. Moreover, any potential accounting or reporting error, whether financial or otherwise, if material, could damage our reputation, adversely affect our ability to conduct business, and decrease revenues and income. Finally, any regulatory and legislative actions and reforms affecting the mutual fund industry, including compliance initiatives, may negatively impact revenues by increasing our costs of accessing or dealing in the financial markets or by making certain investment offerings less favorable to our clients.

Changes in tax laws or exposure to additional income tax liabilities could have a material impact on our financial condition, results of operations and liquidity. We are subject to income taxes as well as non-income based taxes, in both the U.S. and various non-U.S. jurisdictions and are subject to ongoing tax audits in the U.S. and various non-U.S. jurisdictions. Tax authorities may disagree with certain positions we have taken and assess additional taxes. We regularly assess the likely outcomes of these audits in order to determine the appropriateness of our tax provision. However, there can be no assurance that we will accurately predict the outcomes of these audits, and the actual outcomes of these audits could have a material impact on our net income or financial condition. Changes in tax laws or tax rulings could materially impact our effective tax rate. For example, proposals for fundamental U.S. corporate tax reform, if enacted, could change the amount of taxes we are required to pay and have a significant impact on our future results of operations, profitability and financial condition.

Any significant limitation, failure or security breach of our software applications, technology or other systems that are critical to our operations could constrain our operations. We are highly dependent upon the use of various proprietary and third-party software applications and other technology systems to operate our business. We use our technology to, among other things, obtain securities pricing information, process client transactions, and provide reports and other customer services to the clients of the funds we manage. Any inaccuracies, delays, systems failures or security breaches in these and other processes could subject us to client dissatisfaction and losses. Although we take protective measures, including measures to effectively secure information through system security technology, our technology systems may still be vulnerable to unauthorized access, computer viruses or other events that have a security impact, such as an authorized employee or vendor inadvertently causing us to release confidential information, which could materially damage our operations or cause the disclosure or modification of sensitive or confidential information. Breach of our technology systems could result in the loss of valuable information, liability for stolen assets or information, remediation costs to repair damage caused by the breach, additional security costs to mitigate against future incidents and litigation costs resulting from the incident. Moreover, loss of confidential customer identification information could harm our reputation and subject us to liability under laws that protect confidential personal data, resulting in increased costs or loss of revenues.

Further, although we take precautions to password protect and encrypt our laptops and other mobile electronic hardware, if such hardware is stolen, misplaced or left unattended, it may become vulnerable to hacking or other unauthorized use, creating a possible security risk and resulting in potentially costly actions by us. Most of the software applications that we use in our business are licensed from, and supported, upgraded and maintained by, third-party vendors. A suspension or termination of certain of these licenses or the related support, upgrades and maintenance could cause temporary system delays or interruption. In addition, our failure to properly manage and operate our data centers could have an adverse impact on our business. Although we have in place certain disaster recovery plans, we may experience system delays and interruptions as a result of natural disasters, power failures, acts of war, and third-party failures. Technology is subject to rapid change and we cannot guarantee that our competitors may not implement more advanced technology platforms for their products, which could affect our business. Potential system failures or breaches, or advancements in technology, and the cost necessary to address them, could result in material financial loss or costs, regulatory actions, breach of client contracts, reputational harm or legal claims and liability, which in turn could negatively impact our revenues and income.

Our investment management business operations are complex and a failure to properly perform operational tasks or the misrepresentation of our products and services could have an adverse effect on our revenues and income. Through our subsidiaries, we provide investment management and related services to our sponsored investment products, that consist of investment funds and institutional, high net-worth and separately-managed accounts. Our investment management and related services include fund administration, shareholder services, transfer agency, sales,

distribution, custodial, trustee and other fiduciary services. In order to be competitive, we must properly perform our fund and portfolio administration and related responsibilities, including portfolio recordkeeping and accounting, security pricing, corporate actions, investment restrictions compliance, daily net asset value computations, account reconciliations, and required distributions to fund shareholders. In addition, the intentional or unintentional misrepresentation of our products and services in advertising materials, public relations information, social media or other external communications could adversely affect our reputation and business prospects. Further, certain of our subsidiaries may act as general partner for various investment partnerships, which may subject them to liability for the partnerships' liabilities. If we fail to properly perform and monitor our investment management operations, our business could suffer and our revenues and income could be adversely affected.

We face risks, and corresponding potential costs and expenses, associated with conducting operations and growing our business in numerous countries. We sell mutual funds and offer investment management and related services in many different

regulatory jurisdictions around the world, and intend to continue to expand our operations internationally. As we do so, we will continue to face challenges to the adequacy of our resources, procedures and controls to consistently and effectively operate our business. In order to remain competitive, we must be proactive and prepared to implement necessary resources when growth opportunities present themselves, whether as a result of a business acquisition or rapidly increasing business activities in particular markets or regions. As we grow, we face a heightened risk that the necessary resources and/or personnel will be unavailable to take full advantage of strategic opportunities when they appear or that strategic decisions can be efficiently implemented. Local regulatory environments may vary widely, as may the adequacy and sophistication of each. Similarly, local distributors, and their policies and practices as well as financial viability, may be inconsistent or less developed or mature. Notwithstanding potential long-term cost savings by increasing certain operations, such as transfer agent and other back-office operations, in countries or regions of the world with lower operating costs, growth of our international operations may involve near-term increases in expenses as well as additional capital costs, such as information, systems and technology costs and costs related to compliance with particular regulatory or other local requirements or needs. Local requirements or needs may also place additional demands on sales and compliance personnel and resources, such as meeting local language requirements, while also integrating personnel into an organization with a single operating language. Finding, hiring and retaining additional, well-qualified personnel and crafting and adopting policies, procedures and controls to address local or regional requirements remain a challenge as we expand our operations internationally. Moreover, regulators in non-U.S. jurisdictions could also change their policies or laws in a manner that might restrict or otherwise impede our ability to distribute or register investment products in their respective markets. Any of these local requirements, activities, or needs could increase the costs and expenses we incur in a specific jurisdiction without any corresponding increase in revenues and income from operating in the jurisdiction. In addition, from time to time we enter into international joint ventures in which we may not have control. These investments in joint ventures may involve risks, including the risk that the controlling joint venture partner may have business interests, strategies or goals that are inconsistent with ours, and the risk that business decisions or other actions or omissions of the controlling joint venture partner or the joint venture company may result in harm to our reputation or adversely affect the value of our investment in the joint venture.

We depend on key personnel and our financial performance could be negatively affected by the loss of their services. The success of our business will continue to depend upon our key personnel, including our portfolio and fund managers, investment analysts, investment advisers, sales and management personnel and other professionals as well as our executive officers and business unit heads. Competition for qualified, motivated, and highly skilled executives, professionals and other key personnel in the investment management and banking/finance industries remains significant. Our success depends to a substantial degree upon our ability to find, attract, retain, and motivate qualified individuals, including through competitive compensation packages, and upon the continued contributions of these people. Regulations required to be adopted under the Reform Act as well as regulations under consideration outside the Reform Act, could impose restrictions on compensation paid by financial institutions, which could restrict our ability to compete effectively for qualified professionals. As our business grows, we are likely to need to increase correspondingly the overall number of individuals that we employ. Moreover, in order to retain certain key personnel, we may be required to increase compensation to such individuals, resulting in additional expense without a corresponding increase in potential revenues. We cannot assure you that we will be successful in finding, attracting and retaining qualified individuals, and the departure of key investment personnel, in particular, if not replaced, could cause us to lose clients, which could have a material adverse effect on our financial condition, results of operations and business prospects.

Strong competition from numerous and sometimes larger companies with competing offerings and products could limit or reduce sales of our products, potentially resulting in a decline in our market share, revenues and income. We compete with numerous investment management companies, securities brokerage and investment banking firms, insurance companies, banks and other financial institutions. Our investment products also compete with products offered by these competitors as well as real estate investment trusts, hedge funds and others. The periodic establishment of new investment management companies and other competitors increases the competition that we face. At the same time, consolidation in the financial services industry has created stronger competitors with greater

financial resources and broader distribution channels than our own. Competition is based on various factors, including, among others, business reputation, investment performance, product mix and offerings, service quality and innovation, distribution relationships, and fees charged. Additionally, competing securities broker/dealers whom we rely upon to distribute and sell our mutual funds may also sell their own proprietary funds and investment products, which could limit the distribution of our investment products. To the extent that existing or potential clients, including securities broker/dealers, decide to invest in or distribute the products of our competitors, the sales of our products as well as our market share, revenues and income could decline. Our ability to attract and retain AUM is also dependent on the relative investment performance of our funds and other managed investment portfolios, offering a mix of sponsored investment products that meets investor demand and our ability to maintain our investment management services fees at competitive levels.

Changes in the third-party distribution and sales channels on which we depend could reduce our income and hinder our growth. We derive nearly all of our fund sales through third-party broker/dealers and other similar investment advisers. Increasing competition for these distribution channels and regulatory initiatives have caused our distribution costs to rise and could cause further increases in the future or could otherwise negatively impact the distribution of our products. Pursuant to the Reform Act,

the SEC may establish different standards for broker/dealers in their interaction with retail customers, which could have an impact on sales and/or distribution costs. Higher distribution costs lower our income; consolidations in the broker/dealer industry could also adversely impact our income. Moreover, if several of the major financial advisers who distribute our products were to cease operations or limit or otherwise end the distribution of our products, it could have a significant adverse impact on our income. There is no assurance we will continue to have access to the third-party broker/dealers and similar investment advisers that currently distribute our products, or continue to have the opportunity to offer all or some of our existing products through them. A failure to maintain strong business relationships with the major investment advisers who currently distribute our products may also impair our distribution and sales operations. Because we use broker/dealers and other similar investment advisers to sell our products, we do not control the ultimate investment recommendations given to clients. Any inability to access and successfully sell our products to clients through third-party distribution channels could have a negative effect on our level of AUM, income and overall business and financial condition.

Our increasing focus on international markets as a source of investments and sales of investment products subjects us to increased exchange rate and other risks in connection with our revenues and income generated overseas. While we maintain a significant portion of our operations in the U.S., we also provide services and earn revenues in The Bahamas, Asia-Pacific, Europe, Canada, Latin America, the Middle East and Africa. As a result, we are subject to foreign exchange risk through our non-U.S. operations. Fluctuations in the exchange rates to the U.S. dollar may affect our financial results from one period to the next. While we have taken steps to reduce our exposure to foreign exchange risk, for example, by denominating a significant amount of our transactions in U.S. dollars, the situation may change in the future as our business continues to grow outside the U.S. Appreciation of the U.S. dollar could moderate revenues from managing investment products internationally or could affect relative investment performance of certain funds invested in non-U.S. securities. In addition, we have risk associated with the foreign exchange revaluation of U.S. dollar balances held by certain non-U.S. subsidiaries for which the local currency is the functional currency. Separately, management fees that we earn tend to be higher in connection with international AUM than with U.S. AUM. Consequently, a downturn in international markets could have a significant effect on our revenues and income. Moreover, as our business continues to grow in non-U.S. markets, any ongoing and future business, economic, social or political unrest affecting these markets, in addition to any direct consequences such as unrest may have on our personnel and facilities located in the affected area, may also have a more lasting impact on the long-term investment climate in these and other areas and, as a result, our AUM and the corresponding revenues and income that we generate from them may be negatively affected.

Poor investment performance of our products could affect our sales or reduce the level of AUM, potentially negatively impacting our revenues and income. Our investment performance, along with achieving and maintaining superior distribution and client services, is critical to the success of our investment management and related services business. Strong investment performance often stimulates sales of our investment products. Poor investment performance as compared to third-party benchmarks or competitive products could lead to a decrease in sales of investment products we manage and stimulate redemptions from existing products, generally lowering the overall level of AUM and reducing the management fees we earn. We cannot assure you that past or present investment performance in the investment products we manage will be indicative of future performance. Any poor investment performance may negatively impact our revenues and income.

We could suffer losses in our revenues and income if our reputation is harmed. Our reputation is important to the success of our business. We believe that our Franklin Templeton Investments brand has been, and continues to be, well received both in our industry and with our clients, reflecting the fact that our brand, like our business, is based in part on trust and confidence. If our reputation is harmed, existing clients may reduce amounts held in, or withdraw entirely from, funds that we advise or funds may terminate their management agreements with us, which could reduce the amount of AUM and cause us to suffer a corresponding loss in our revenues and income. Moreover, reputational harm may cause us to lose current employees and we may be unable to continue to attract new ones with similar qualifications, motivations, or skills. If we fail to address, or appear to fail to address, successfully and promptly the underlying causes of any reputational harm, we may be unsuccessful in repairing any existing harm to our reputation and our future business prospects would likely be affected.

Our future results are dependent upon maintaining an appropriate level of expenses, which is subject to fluctuation. The level of our expenses is subject to fluctuation and may increase for the following or other reasons: changes in the level and scope of our advertising expenses in response to market conditions; variations in the level of total compensation expense due to, among other things, bonuses, changes in our employee count and mix, and competitive factors; changes in expenses and capital costs, including costs incurred to maintain and enhance our administrative and operating services infrastructure or to cover uninsured losses and an increase in insurance expenses including through the assumption of higher deductibles and/or co-insurance liability.

Our ability to successfully integrate widely varied business lines can be impeded by systems and other technological limitations. Our continued success in effectively managing and growing our business depends on our ability to integrate the varied accounting, financial, information, and operational systems of our various businesses on a global basis. Moreover, adapting or developing our existing technology systems to meet our internal needs, as well as client needs, industry demands and new regulatory requirements, is also critical for our business. The constant introduction of new technologies presents new challenges to us. We

have an ongoing need to continually upgrade and improve our various technology systems, including our data processing, financial, accounting, and trading systems. Further, we also must be proactive and prepared to implement technology systems when growth opportunities present themselves, whether as a result of a business acquisition or rapidly increasing business activities in particular markets or regions. These needs could present operational issues or require, from time to time, significant capital spending. It also may require us to reevaluate the current value and/or expected useful lives of our technology systems, which could negatively impact our results of operations.

Our inability to successfully recover should we experience a disaster or other business continuity problem could cause material financial loss, loss of human capital, regulatory actions, reputational harm, or legal liability. Should we experience a local or regional disaster or other business continuity problem, such as an earthquake, tsunami, terrorist attack, pandemic or other natural or man-made disaster, our continued success will depend, in part, on the safety and availability of our personnel, our office facilities, and the proper functioning of our computer, telecommunication and other related systems and operations. While our operational size, the diversity of locations from which we operate, and our redundant back-up systems provide us with a strong advantage should we experience a local or regional disaster or other business continuity event, we could still experience near-term operational challenges, in particular depending upon how a local or regional event may affect our human capital across our operations or with regard to particular segments of our operations, such as key executive officers or personnel in our technology group. Moreover, as we grow our operations in new geographic regions, the potential for particular types of natural or man-made disasters, political, economic or infrastructure instabilities, or other country- or region-specific business continuity risks increases. Past disaster recovery efforts have demonstrated that even seemingly localized events may require broader disaster recovery efforts throughout our operations and, consequently, we regularly assess and take steps to improve upon our existing business continuity plans and key management succession. However, a disaster on a significant scale or affecting certain of our key operating areas within or across regions, or our inability to successfully recover should we experience a disaster or other business continuity problem, could materially interrupt our business operations and cause material financial loss, loss of human capital, regulatory actions, reputational harm, or legal liability.

Certain of the portfolios we manage, including our emerging market portfolios, are vulnerable to significant market-specific political, economic or other risks, any of which may negatively impact our revenues and income. Our emerging market portfolios and revenues derived from managing these portfolios are subject to significant risks of loss from political, economic, and diplomatic developments, currency fluctuations, social instability, changes in governmental policies, expropriation, nationalization, asset confiscation and changes in legislation related to non-U.S. ownership. International trading markets, particularly in some emerging market countries, are often smaller, less liquid, less regulated and significantly more volatile than those in the U.S.

Our revenues and income could be adversely affected if the terms of our management agreements are significantly altered or these agreements are terminated by the funds and other sponsored investment products we advise. Our revenues are dependent on fees earned under investment management and related services agreements that we have with the funds and other sponsored investment products we advise. These revenues could be adversely affected if these agreements are altered significantly or terminated. The decline in revenues that might result from alteration or termination of our investment management services agreements could have a material adverse impact on our revenues and income.

Regulatory and governmental examinations and/or investigations, litigation and the legal risks associated with our business, could adversely impact our AUM, increase costs and negatively impact our profitability and/or our future financial results. From time to time we may receive requests for documents or other information from governmental authorities or regulatory bodies or we also may become the subject of governmental or regulatory investigations and/or examinations, and governmental or regulatory investigations and/or examinations that have been inactive could become active. In addition, we may be named in litigation. We may be obligated, and under our certificate of incorporation and by-laws and our standard form of indemnification agreement with certain directors in some instances, we are obligated, or we may choose, to indemnify directors, officers or employees against liabilities and expenses they may incur in connection with such matters to the extent permitted under applicable law. Even if claims made against us are without merit, litigation typically is an expensive process. Risks associated with legal liability



often are difficult to assess or quantify and their existence and magnitude can remain unknown for significant periods of time. Moreover, settlements or judgments against us have the potential of being substantial if we are unsuccessful in settling or otherwise resolving matters early in the process and/or on favorable terms. Eventual exposures from and expenses incurred relating to current and future litigation, investigations, examinations and settlements could adversely impact our AUM, increase costs and negatively impact our profitability and/or our future financial results. Judgments or findings of wrongdoing by regulatory or governmental authorities or in litigation against us could affect our reputation, increase our costs of doing business and/or negatively impact our revenues, any of which could have a material negative impact on our financial results.

Our ability to meet cash needs depends upon certain factors, including the market value of our assets, operating cash flows and our perceived creditworthiness. Our ability to meet anticipated cash needs depends upon factors such as the market value of our assets, our operating cash flows and our creditworthiness as perceived by lenders. If we are unable to obtain funds and financing, we may be forced to incur unanticipated costs or revise our business plans. Further, our access to the capital markets depends

significantly on our credit ratings. A reduction in our long- or short-term credit ratings could increase our borrowing costs and limit our access to the capital markets. Volatility in the global financing markets may also impact our ability to access the capital markets should we seek to do so, and have an adverse effect on investors' willingness to purchase our securities, interest rates, credit spreads and the valuation levels of equity markets. If we are unable to obtain funds and financing, or access the capital markets in a timely manner, we may be forced to incur unanticipated costs or revise our business plans, and our business could be adversely impacted.

Diverse and strong competition limits the interest rates that we can charge on consumer loans. We compete with many types of institutions for consumer loans, certain of which can provide loans at significantly below-market interest rates. Our inability to compete effectively against these companies could limit the growth of our consumer loan business. Economic and credit market downturns could reduce the ability of our customers to repay loans, which could cause losses to our consumer loan portfolio.

Our business could be negatively affected if we or our banking subsidiaries fail to remain well capitalized, and liquidity needs could affect our banking business. Our bank and thrift subsidiaries are subject to significant regulation and supervision, which includes minimum regulatory capital standards. Franklin is also subject to minimum regulatory capital standards because it is a bank holding company and financial holding company registered with the FRB under the BHC Act. Franklin and its bank and thrift subsidiaries are currently well capitalized under applicable guidelines. However, our business could be negatively affected if Franklin or its bank or thrift subsidiaries failed to remain well capitalized. For example, because our bank and thrift subsidiaries are well capitalized and we otherwise qualify as a financial holding company, we are permitted to engage in a broader range of activities than are permitted to a bank holding company. Loss of financial holding company status would require that we either cease these broader activities or divest our banking subsidiaries if we desire to continue such activities. The banking regulators are authorized (and sometimes required) to impose a wide range of requirements, conditions, and restrictions on banks, thrifts, and bank holding companies that fail to maintain adequate capital levels. The Reform Act imposes more stringent capital, liquidity and leverage ratio requirements on bank holding companies. In addition, liquidity needs could affect our banking business, which may be subject to an unanticipated large number of withdrawals as a result of a number of factors, such as changed or unstable economic conditions, adverse trends or events, business closings and lay-offs, rates paid by competitors, general interest rate levels, and returns available to clients on alternative investments. Our banking subsidiaries may be required from time to time to rely on secondary sources of liquidity, such as the sale of investment securities, FHLB advances and federal funds lines to enable them to meet such withdrawal demands. These secondary sources may not be sufficient to meet liquidity needs.

We are dependent on the earnings of our subsidiaries. Substantially all of our operations are conducted through our subsidiaries. As a result, our cash flow and our ability to fund operations are dependent upon the earnings of our subsidiaries and the distribution of earnings, loans or other payments by our subsidiaries. Our subsidiaries are separate and distinct legal entities and have no obligation to provide us with funds for our payment obligations, whether by dividends, distributions, loans or other payments. Any payments to us by our subsidiaries could be subject to statutory or contractual restrictions and are contingent upon our subsidiaries' earnings and business considerations.

### Item 3. Quantitative and Qualitative Disclosures About Market Risk.

In the normal course of business, our financial position is subject to market risk, including, but not limited to, potential loss due to changes in the value of financial instruments including those resulting from adverse changes in interest rates, foreign currency exchange rates and market valuation. Financial instruments include, but are not limited to, investment securities, loans, deposits and debt obligations. Management is responsible for managing market risk. Our Enterprise Risk Management Committee is responsible for providing a framework to assist management to identify, assess, and manage market and other risks.

We are also exposed to market risk through our investment management and distribution fees, which are generally calculated as a percentage of the market value of AUM. Changes in equity market prices, interest rates, credit spreads, foreign exchange rates, or a combination of these factors could cause the value of AUM to decline, which would result in lower investment management and distribution fees.

We are exposed to changes in interest rates, primarily through our loans, investments in debt securities, and outstanding debt. We minimize the impact of changes in interest rates related to our investments in debt securities by

managing the maturities of these securities, and through diversification. We minimize the impact of changes in interest rates related to our outstanding debt by entering into financing transactions that ensure an appropriate mix of debt at fixed and variable interest rates. In addition, our banking/finance segment monitors the net interest rate margin and the average maturity of interest earning assets, as well as funding sources. From time to time, we may enter into interest-rate swap agreements to mitigate interest rate exposure arising from the loans receivable portfolio.

As of December 31, 2011, we have considered the potential impact of a 200 basis point movement in market interest rates on our interest-earning assets, net of interest-bearing liabilities, total debt outstanding and our portfolio of debt securities. Based on our analysis, we do not expect that such a change would have a material impact on our operating revenues or results of operations in the next twelve months, for each of these categories or in the aggregate.

We are subject to foreign currency exchange risk through our international operations. While we operate primarily in the U.S., we also provide services and earn revenues in The Bahamas, Asia-Pacific, Europe, Canada, Latin America, the Middle East and Africa. Our exposure to foreign currency exchange risk is minimized in relation to our results of operations since a significant portion of these revenues are denominated in U.S. dollars. This situation may change in the future as our business continues to grow outside the U.S. and expenses incurred denominated in foreign currencies increase. Our exposure to foreign currency exchange risk in relation to our condensed consolidated balance sheet mostly relates to cash and cash equivalents and investments that are denominated in foreign currencies, primarily in Euro, Indian Rupee, Pound Sterling, and Canadian Dollar. These assets accounted for approximately 11% of the total cash and cash equivalents and investments at December 31, 2011. We also have exposure to foreign exchange revaluation of U.S. dollar balances held by certain non-U.S. subsidiaries for which their local currency is the functional currency. These assets accounted for approximately 5% of the total cash and cash equivalents and investments at December 31, 2011. We generally do not use derivative financial instruments to manage foreign currency exchange risk exposure. As a result, both positive and negative currency fluctuations against the U.S. dollar may affect our results of operations and accumulated other comprehensive income.

We are exposed to market valuation risks related to securities we hold that are carried at fair value and securities held by sponsored investment products that we consolidate, which are also carried at fair value. To mitigate the risks we maintain a diversified investment portfolio and, from time to time, we may enter into derivative agreements. Our exposure to these risks is also minimized as we sponsor a broad range of investment products in various global jurisdictions, which allows us to mitigate the impact of changes in any particular market(s) or region(s).

The following is a summary of the effect of a 10% increase or decrease in the carrying values of our financial instruments subject to market valuation risks at December 31, 2011.

(in thousands)	Carrying Value	Carrying Value Assuming a 10% Increase	Carrying Value Assuming a 10% Decrease
<b>Assets</b>			
<b>Current Assets</b>			
Investment securities, trading	\$ 1,056,668	\$ 1,162,335	\$ 951,001
Investment securities, available-for-sale	756,165	831,782	680,549
Investments of consolidated VIEs, at fair value	10,561	11,617	9,505
Total current assets	1,823,394	2,005,734	1,641,055
<b>Banking/Finance Assets</b>			
Investment securities, available-for-sale	331,621	364,783	298,459
<b>Non-Current Assets</b>			
Investments of consolidated sponsored investment products	623,326	685,659	560,993
Investments of consolidated VIEs, at fair value	826,632	909,295	743,969
Total non-current assets	1,449,958	1,594,954	1,304,962
Total Assets	\$ 3,604,973	\$ 3,965,471	\$ 3,244,476
<b>Liabilities</b>			
<b>Current Liabilities</b>			
Current maturities of long-term debt of consolidated VIEs, at fair value	\$ 24,924	\$ 27,416	\$ 22,432
<b>Non-Current Liabilities</b>			
Long-term debt of consolidated VIEs, at fair value	823,741	906,115	741,367
Total Liabilities	\$ 848,665	\$ 933,531	\$ 763,799



Our cash, cash equivalents and investments portfolio by investment objective at December 31, 2011 was as follows:

(dollar amounts in thousands)	Total Portfolio	Percent of Total Portfolio	Trading Securities Included in Portfolio	Percent of Total Trading Securities		
Cash and Cash Equivalents	\$4,911,858	54	% \$—	0		%
Investment Securities						
Equity						
Global/international	509,857	6	% 162,174	15		%
United States	26,005	0	% 308	0		%
Total equity	535,862	6	% 162,482	15		%
Hybrid	139,233	1	% 56,667	6		%
Fixed-Income						
Tax-free	89,798	1	% —	0		%
Taxable						
Global/international	1,051,984	12	% 305,626	29		%
United States	1,788,096	20	% 531,893	50		%
Total fixed-income	2,929,878	33	% 837,519	79		%
Total Investment Securities	3,604,973	40	% 1,056,668	100		%
Other Investments	579,313	6	% —	0		%
Total Cash and Cash Equivalents and Investments	\$9,096,144	100	% \$1,056,668	100		%

Investments categorized as investment securities, trading in our condensed consolidated balance sheets include securities held by consolidated sponsored investment products. These securities, which amounted to \$443.2 million at December 31, 2011, are generally assigned a classification in the table above based on the investment objective of the consolidated sponsored investment products holding the trading securities. In addition, \$411.2 million of non-current investments held by consolidated sponsored investment products were included in global/international fixed-income, \$207.1 million were included in global/international equity, and \$5.0 million were included in hybrid.

Investments of consolidated VIEs, at fair value are included in the table above in the United States taxable fixed-income investment objective.

Investments categorized as other investments in the table above include \$484.6 million of investments in equity method investees and other that hold securities which primarily have a global/international equity investment objective, are subject to market valuation risks and are readily marketable.

#### Item 4. Controls and Procedures.

The Company's management evaluated, with the participation of the Company's principal executive and principal financial officers, the effectiveness of the Company's disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the "Exchange Act")) as of December 31, 2011. Based on their evaluation, the Company's principal executive and principal financial officers concluded that the Company's disclosure controls and procedures as of December 31, 2011 were designed and are functioning effectively to provide reasonable assurance that the information required to be disclosed by the Company in reports filed under the Exchange Act is (i) recorded, processed, summarized, and reported within the time periods specified in the SEC's rules and forms, and (ii) accumulated and communicated to management, including the principal executive and principal financial officers, as appropriate, to allow timely decisions regarding required disclosure.

There has been no change in the Company's internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) that occurred during the Company's fiscal quarter ended December 31, 2011, that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.



## PART II – OTHER INFORMATION

## Item 1. Legal Proceedings.

For a description of our legal proceedings, please see the description set forth in the “Legal Proceedings” section in Note 9 – Commitments and Contingencies in the notes to the condensed consolidated financial statements in Item 1 of Part I of this Form 10-Q, which is incorporated herein by reference.

## Item 1A. Risk Factors.

Our Form 10-K for the fiscal year ended September 30, 2011 filed with the SEC includes a detailed discussion of the Risk Factors applicable to us, which are also set forth under the heading “Risk Factors” in Item 2 of Part I of this Form 10-Q. There are no material changes from the Risk Factors as previously disclosed in our Form 10-K for the fiscal year ended September 30, 2011.

## Item 2. Unregistered Sales of Equity Securities and Use of Proceeds.

The following table provides information with respect to the shares of Franklin’s common stock we repurchased during the three months ended December 31, 2011.

Month	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number of Shares that May Yet Be Purchased Under the Plans or Programs
October 2011	416,000	\$ 93.64	416,000	4,328,976
November 2011	1,328,800	\$ 99.68	1,328,800	3,000,176
December 2011	1,244,477	\$ 95.98	1,244,477	11,755,699
Total	2,989,277		2,989,277	

Under our stock repurchase program, we can repurchase shares of Franklin’s common stock from time to time in the open market and in private transactions in accordance with applicable laws and regulations, including without limitation applicable federal securities laws. From time to time we have announced the existence of and updates to the Company’s continuing policy of repurchasing shares of its common stock. In December 2011, our Board of Directors authorized the repurchase of up to 10.0 million additional shares of our common stock under our stock repurchase program. At December 31, 2011, approximately 11.8 million shares of our common stock remained available for repurchase under our stock repurchase program. Our stock repurchase program is not subject to an expiration date. There were no unregistered sales of equity securities during the period covered by this report.



Item 6. Exhibits.

Exhibit No.	Description
Exhibit 3(i)(a)	Registrant's Certificate of Incorporation, as filed November 28, 1969, incorporated by reference to Exhibit (3)(i) to the Registrant's Annual Report on Form 10-K for the fiscal year ended September 30, 1994 (File No. 001-09318) (the "1994 Annual Report").
Exhibit 3(i)(b)	Registrant's Certificate of Amendment of Certificate of Incorporation, as filed March 1, 1985, incorporated by reference to Exhibit (3)(ii) to the 1994 Annual Report.
Exhibit 3(i)(c)	Registrant's Certificate of Amendment of Certificate of Incorporation, as filed April 1, 1987, incorporated by reference to Exhibit (3)(iii) to the 1994 Annual Report.
Exhibit 3(i)(d)	Registrant's Certificate of Amendment of Certificate of Incorporation, as filed February 2, 1994, incorporated by reference to Exhibit (3)(iv) to the 1994 Annual Report.
Exhibit 3(i)(e)	Registrant's Certificate of Amendment of Certificate of Incorporation, as filed on February 4, 2005, incorporated by reference to Exhibit (3)(i)(e) to the Registrant's Quarterly Report on Form 10-Q for the period ended December 31, 2004 (File No. 001-09318).
Exhibit 3(ii)	Registrant's Amended and Restated Bylaws (as adopted and effective September 15, 2011), incorporated by reference to Exhibit 3.1 to the Registrant's Form 8-K filed with the SEC on September 16, 2011 (File No. 001-09318).
Exhibit 10.1	Registrant's 1998 Employee Stock Investment Plan (as amended and restated effective as of February 1, 2012) (filed herewith).*
Exhibit 31.1	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith).
Exhibit 31.2	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith).
Exhibit 32.1	Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (furnished herewith).
Exhibit 32.2	Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (furnished herewith).
Exhibit 101	The following materials from the Registrant's Quarterly Report on Form 10-Q for the quarter ended December 31, 2011, formatted in Extensible Business Reporting Language (XBRL), include: (i) the Condensed Consolidated Statements of Income, (ii) the Condensed Consolidated Balance Sheets, (iii) the Condensed Consolidated Statements of Cash Flows, and (iv) related notes (furnished herewith).

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\* Management/Employment Contract or Compensatory Plan or Arrangement



SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

FRANKLIN RESOURCES, INC.  
(Registrant)

Date: February 1, 2012

By: /S/ KENNETH A. LEWIS  
Kenneth A. Lewis  
Executive Vice President and Chief Financial Officer  
(Duly Authorized Officer and Principal Financial Officer)

EXHIBIT INDEX

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