

FRANKLIN RESOURCES INC
Form 10-K
November 29, 2007
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

(MARK ONE)

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended September 30, 2007

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, California
(Address of principal executive offices)

94403
(Zip Code)

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

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Common Stock, par value \$.10 per share	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act:

None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

YES NO

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Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.

YES NO

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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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

Large accelerated filer Accelerated filer Non-accelerated filer

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act).

YES NO

The aggregate market value of the voting common equity (common stock) held by non-affiliates of the registrant, as of March 30, 2007 (the last business day of registrant's second quarter of fiscal year 2007), was approximately \$17.9 billion based upon the last sale price reported for such date on the New York Stock Exchange. For purposes of this calculation, shares of common stock held or controlled by executive officers and directors of the registrant and by persons who hold more than 5% of the outstanding shares of common stock have been treated as shares held by affiliates. However, such treatment should not be construed as an admission that any such person is an affiliate of the registrant. The registrant has no non-voting common equity.

Number of shares of the registrant's common stock outstanding at October 31, 2007: 245,015,630.

DOCUMENTS INCORPORATED BY REFERENCE:

Certain portions of the registrant's definitive proxy statement for its annual meeting of stockholders, to be filed with the Securities and Exchange Commission within 120 days after September 30, 2007, are incorporated by reference into Part III of this report.

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PART I

Forward-looking Statements. In addition to historical information, this Annual Report on Form 10-K contains forward-looking statements that involve a number of known and unknown risks, uncertainties and other important factors, including the risks and other factors discussed in Item 1A (Risk Factors), that could cause the actual results and outcomes to differ materially from any future results or outcomes expressed or implied by such forward-looking statements. When used in this report, words or phrases generally written in the future tense and/or preceded by words such as will, may, could, expect, believe, anticipate, intend, or other similar words are forward-looking statements as defined in the Private Securities Litigation Reform Act of 1995. Moreover, statements in Risk Factors, Management's Discussion and Analysis of Financial Condition and Results of Operations (MD&A) and elsewhere in this report that speculate about future events are forward-looking statements. While forward-looking statements are our best prediction at the time that they are made, you should not rely on them. If a circumstance occurs after the date of this Annual Report on Form 10-K that causes any of our forward-looking statements to be inaccurate, we do not have an obligation, and we undertake no obligation, to announce publicly the change to our expectations, or to make any revision to our forward-looking statements, unless required by law.

Item 1. Business.
GENERAL

Franklin Resources, Inc. (Franklin Resources, Inc. or the Company) is an investment management company that is regulated as a bank holding company under the Bank Holding Company Act of 1956, as amended (the BHC Act), and has elected to be a financial holding company under the Gramm-Leach-Bliley Act (the GLB Act). Through our wholly-owned direct and indirect subsidiaries, we provide investment management and fund administration services (investment management services) to open-end and closed-end investment companies (including our own family of retail mutual funds), institutional accounts, high net-worth families, individuals and separate accounts in the United States (U.S.) and internationally. Our sponsored investment products include a broad range of domestic (U.S.) and global/international equity, hybrid, fixed-income and money market mutual funds, as well as other investment products that are sold to the public under the Franklin, Templeton, Mutual Series, Bissett, Fiduciary Trust and Darby brand names. As of September 30, 2007, we had \$645.9 billion in assets under our management with approximately 20.4 million billable shareholder accounts worldwide. In support of our primary business and operating segment, we provide investment management services and other related services, including shareholder services, transfer agency, underwriting, distribution, custodial, trustee and other fiduciary services (collectively investment management and related services). In our secondary business and operating segment, banking/finance, we provide clients with select retail banking, private banking and consumer lending services through our bank subsidiaries. The common stock of the Company is traded on the New York Stock Exchange (NYSE) under the ticker symbol BEN and on the London Stock Exchange under the ticker symbol FRK, and is included in the Standard & Poor's 500 Index. The Franklin Templeton® Investments brand name refers to Franklin Resources, Inc. and its subsidiaries (collectively Franklin Templeton Investments). In this report, words such as we, us, our and similar terms refer to Franklin Resources, Inc. and its subsidiaries collectively.

COMPANY HISTORY AND ACQUISITIONS

Franklin Templeton Investments and its predecessors have been engaged in the investment management and related services business since 1947. Franklin Resources, Inc. was incorporated in Delaware in November 1969. We originated our mutual fund business with the Franklin family of funds, which is now known as the Franklin Funds. We expanded our business, in part, by acquiring companies engaged in the investment management and/or related services business.

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In October 1992, we acquired substantially all of the assets and liabilities of the investment management and related services business of Templeton, Galbraith & Hansberger Ltd. This acquisition added the Templeton family of funds to our organization. The Templeton funds are known for their international and global investment strategies and value style of investing.

In November 1996, we acquired certain assets and liabilities of Heine Securities Corporation, which provided investment management services to various accounts and investment companies, including Mutual Series Fund Inc., now known as Franklin Mutual Series Fund Inc. (Mutual Series). Mutual Series is known for its value-oriented equity funds.

We expanded our business in Korea in July 2000 when we purchased all of the remaining outstanding shares of a Korean asset management company, Ssangyong Templeton Investment Trust Management Co., Ltd. (currently known as Franklin Templeton Investment Trust Management Co., Ltd.), in which we previously held a partial interest. The acquisition has made us one of the larger independent foreign money managers in that country.

We acquired all of the outstanding shares of Bissett & Associates Investment Management Ltd. (Bissett) in October 2000. Bissett now operates as part of our Canadian subsidiary, Franklin Templeton Investments Corp. With the addition of Bissett, we added Bissett's family of mutual funds to our existing Canadian based funds (some of which we previously acquired as part of the Templeton family of funds) and expanded our investment management services throughout Canada to a broad range of clients, including institutional clients such as pension plans, municipalities, universities, charitable foundations and private clients.

In April 2001, we acquired Fiduciary Trust Company International, a bank organized under the New York State Banking Law (Fiduciary Trust). Following the acquisition, Fiduciary Trust became a wholly-owned subsidiary of Franklin Resources, Inc. Fiduciary Trust provides investment management and related services to institutional clients and high net-worth families and individuals. With the acquisition of Fiduciary Trust, we also added Fiduciary Trust's U.S. and non-U.S. mutual funds to our product line.

In July 2002, our subsidiary, Franklin Templeton Asset Management (India) Private Limited (FTAMIPL), acquired all of the outstanding shares of Pioneer ITI AMC Limited (Pioneer). Pioneer was an Indian asset management company that had approximately \$800 million in assets under management as of the purchase date. In April 2007, we completed the purchase of the remaining 25% interest in each of FTAMIPL and Franklin Templeton Trustee Services Private Limited, each located in India, and each of which are now wholly-owned indirect subsidiaries of Franklin Resources, Inc. With these acquisitions, we continue our position as one of the largest private sector asset managers in India.

In October 2003, we acquired all of the remaining outstanding shares of Darby Overseas Investments, Ltd. and all of the remaining outstanding limited partnership interests of Darby Overseas Partners, L.P. (collectively, Darby). Darby, based in Washington, D.C., sponsors and manages funds for institutional investors and high net-worth individuals that invest primarily in emerging markets, private equity, and mezzanine finance transactions, including regional and specialized sector funds.

In July 2006, we completed the purchase of all of the remaining interests in a Brazilian asset management company, Bradesco Templeton Asset Management Ltda., in which we previously held a partial interest. Upon acquisition, the company was renamed Franklin Templeton Investimentos (Brasil) Ltda. and is licensed to manage investment products in Brazil.

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We derive substantially all of our revenues from providing investment management and related services to our retail mutual funds, and to institutional, high net-worth and separately-managed accounts and other investment products. Our revenues depend to a large extent on the amount of assets under management. Underwriting and distribution fees, also a large source of revenue, consist of sales charges and commissions derived from sales of our sponsored investment products and distribution fees. When used in this report, unless the context otherwise makes clear, the term *“funds”* means all of the Franklin, Templeton, Mutual Series, and Bissett mutual funds; similarly, unless the context otherwise makes clear, *“sponsored investment products”* means all of the funds together with closed-end investment companies, non-U.S.-based investment products, and other U.S. and international private, institutional, high net-worth and separate accounts.

A. Assets Under Management (AUM)

Fees for providing investment management and fund administration services (*“investment management fees”*), a large source of our revenue, are generally based upon the monetary value of assets in the accounts that we advise. As of September 30, 2007, the types of assets under management by investment category held by investors on a worldwide basis were:

Type of Asset	Value in Billions	% Total of AUM
Equity		
Growth potential, income potential or various combinations thereof	\$ 387.2	60.0%
Fixed-Income		
Both long-term and short-term	\$ 133.8	20.7%
Hybrid		
Asset allocation, balanced, flexible and income-mixed funds	\$ 117.2	18.1%
Money Market		
Short-term liquid assets	\$ 7.7	1.2%

Broadly speaking, the change in the net assets of the sponsored investment products depends primarily upon two factors: (1) the increase or decrease in the market value of the securities held in the portfolio of investments; and (2) the level of sales (inflows) as compared to the level of redemptions (outflows). We are subject to the risk of asset volatility, resulting from changes in the domestic and global financial and equity markets. In addition, because we generally derive higher revenues and income from our equity assets, a shift in assets from equity to fixed-income or hybrid funds reduces total revenue and, thus, net income. Despite such a risk of volatility, we believe that we are more competitive as a result of the greater diversity of sponsored investment products available to our customers.

B. Types of Investment Management and Related Services

A majority of our revenues are derived from providing investment management and related services to our sponsored investment products. We advise, manage and implement the investment and administrative activities necessary to operate our U.S.-registered open-end and closed-end funds or series, separately-managed accounts and our many non-U.S.-based sponsored investment products.

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1. Investment Management Services

We earn investment management fees by providing investment management services pursuant to agreements with each sponsored investment product, including each fund, or, if applicable, each person or legal entity acting on behalf of a sponsored investment product. This business is primarily conducted through our direct and indirect subsidiaries, including, among others, the following:

Fiduciary International, Inc., a registered investment adviser (an Investment Adviser) under the Investment Advisers Act of 1940, as amended (the Advisers Act), provides investment management services to certain of our sponsored investment products, including separate accounts for institutional clients;

Fiduciary Investment Management International, Inc., an Investment Adviser, provides investment management services to separate accounts for institutional and private clients;

Fiduciary Trust, a New York state-chartered bank, provides investment management, custody and related services to high net-worth individuals, families and institutions;

Fiduciary Trust Company of Canada (FTCC), a registered foreign equivalent of an investment adviser with many of the Canadian provincial and territorial securities commissions, provides investment management services to certain Canadian registered retail funds and to separate accounts for private clients primarily in Canada;

Fiduciary Trust International Limited, an Investment Adviser and a registered foreign equivalent investment adviser in the United Kingdom (U.K.), provides investment management services to certain of our funds and separate accounts for institutional and private clients;

Franklin Advisers, Inc., an Investment Adviser, provides investment management services to certain of our funds, non-affiliated entities and institutional and separate accounts;

Franklin Advisory Services, LLC, an Investment Adviser, provides investment management services to certain of our funds and to certain non-affiliated entities;

Franklin Investment Advisory Services, LLC, an Investment Adviser, provides investment management services to fund clients;

Franklin Mutual Advisers, LLC, an Investment Adviser, provides investment management services to the Mutual Series funds and also to certain other funds;

Franklin Templeton Asset Management (India) Private Limited, an Asset Management Company approved by the Securities and Exchange Board of India, provides investment management services to certain of our funds and to institutional and private accounts in India and other jurisdictions;

Franklin Templeton Asset Management S.A., a registered foreign equivalent of an investment adviser in France, provides investment management services to the funds of funds it manages and separate accounts;

Franklin Templeton Institutional, LLC (FTI), an Investment Adviser, provides investment management services to institutional clients and certain of our sponsored investment products;

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Franklin Templeton Investimentos (Brasil) Ltda., a registered foreign equivalent of an investment adviser in Brazil, provides investment management services to certain of our sponsored investment products and separate accounts in Brazil;

Franklin Templeton Investment Management Limited, an Investment Adviser and a registered foreign equivalent of an investment adviser in the U.K., provides investment management services to certain of our investment companies registered in the United States and in non-U.S. jurisdictions, including Europe;

Franklin Templeton Investment Trust Management Co., Ltd., a registered foreign equivalent of an investment adviser in Korea, provides investment management services to equity and fixed income products;

Franklin Templeton Investments (Asia) Limited, an Investment Adviser and a foreign equivalent of an investment adviser in Hong Kong, provides investment management services to certain of our sponsored investment products and to institutional and private accounts in Hong Kong and other jurisdictions;

Franklin Templeton Investments Australia Limited, a registered foreign equivalent of an investment adviser in Australia, provides investment management services to institutional and retail clients in Australia;

Franklin Templeton Investments Corp., a registered foreign equivalent of an investment adviser with many of the Canadian provincial and territorial securities commissions, a registered mutual fund dealer with the Ontario Securities Commission and Alberta Securities Commission and an Investment Adviser, provides investment management and related services to Canadian registered retail funds and investment management services to certain institutional and separate accounts;

Franklin Templeton Investments Japan Limited, an authorized manager in Japan which is a registered foreign equivalent of an investment adviser, provides investment management services to certain of our funds and separate accounts in Japan and manages and sub-advises Japan equity funds that are sold in other regions;

Franklin Templeton Portfolio Advisors, Inc., an Investment Adviser, provides investment management services to separate accounts and in connection with third-party broker/dealer separately-managed accounts or wrap fee programs;

Templeton Asset Management Ltd., an Investment Adviser and a registered foreign equivalent of an investment adviser in Singapore and Hong Kong, provides investment management services to certain of our funds and institutional and separate accounts in Singapore, Hong Kong and other jurisdictions;

Templeton Global Advisors Limited, an Investment Adviser and a registered foreign equivalent of an investment adviser in The Bahamas, provides investment management services to certain of our funds and institutional and separate accounts; and

Templeton Investment Counsel, LLC, an Investment Adviser, provides investment management services to certain of our funds and to institutional and private accounts.

Our subsidiaries conducting investment management services perform investment research for our sponsored investment products and determine which securities the sponsored investment products will purchase, hold or sell under the supervision and oversight of the funds' boards of directors or trustees. In addition, these subsidiaries take all steps necessary to implement such decisions, including selecting brokers and dealers and executing and settling trades in accordance with detailed criteria set forth in the management agreement for each fund, internal policies, and applicable law and practice.

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Generally, the funds themselves have no paid employees. Through our subsidiaries, we provide and pay the salaries of personnel who serve as officers of our U.S.-registered open-end and closed-end funds, including the administrative personnel necessary to conduct such funds day-to-day business operations. Our subsidiaries either provide or arrange for the provision of: office space, telephone, office equipment and supplies; trading desk facilities (unless these facilities are provided by another subsidiary); authorization of expenditures and approval of bills for payment; preparation of annual and semi-annual reports to fund shareholders, notices of dividends, capital gains distributions and tax credits, and other regulatory reports; the daily pricing of fund investment portfolios, including collecting quotations from pricing services; accounting services, including preparing and supervising publication of daily net asset value quotations, periodic earnings reports and other financial data; services to ensure compliance with securities regulations, including recordkeeping requirements; preparation and filing of tax reports; the maintenance of accounting systems and controls; and other administrative services. In some cases our subsidiaries are compensated, based on a percentage of assets under management, under separate administration agreements with the funds. In other cases, our subsidiaries are compensated by our investment management subsidiary from the fees received from our funds and clients. The funds generally pay their own expenses, such as external legal, custody and independent audit fees, regulatory registration fees, and other related expenses. The funds also share in board and shareholder meeting and reporting costs.

Our investment management services include fundamental investment research and valuation analyses, including original economic, political, industry and company research (including the utilization of such sources as company public records and activities, management interviews, company prepared information, and other publicly available information, as well as company visits and inspections), and analyses of suppliers, customers and competitors. In addition, research services provided by brokerage firms are used to support our findings.

Investment management services are provided pursuant to agreements in effect with each of our U.S.-registered open-end and closed-end funds. Agreements are in effect with foreign-registered funds and separate and institutional accounts. In general, the investment management agreements for our U.S.-registered open-end and closed-end funds must be renewed each year (after an initial two-year term), and must be specifically approved at least annually by a vote of each fund's board of directors or trustees as a whole and separately by the directors/trustees that are not interested persons of such fund under the Investment Company Act of 1940, as amended (the '40 Act'), or by a vote of the holders of a majority of such fund's outstanding voting securities. Foreign-registered funds and separate and institutional accounts have various termination rights, and review and renewal provisions.

Under the majority of investment management agreements, the U.S.-registered open-end and closed-end funds pay us a monthly fee in arrears based upon a fund's average daily net assets. Annual fee rates under the various global investment management agreements generally range from 0.15% to a maximum of 2.50% and are often reduced as net assets exceed various threshold levels.

We use a master/feeder fund structure in certain situations. This structure allows an investment adviser to manage a single portfolio of securities at the master fund level and have multiple feeder funds that invest all of their respective assets into the master fund. Individual and institutional shareholders invest in the feeder funds which can offer a variety of service and distribution options. A management fee typically is charged at the master fund level and administrative and shareholder servicing fees are charged at the feeder fund level, although with certain funds, all fees may be charged at the feeder fund level only.

Each U.S. investment management agreement between certain of our subsidiaries and each fund automatically terminates in the event of its assignment, as defined in the '40 Act. In addition, either party may terminate the agreement without penalty after written notice ranging from 30 to 60 days. If agreements

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representing a significant portion of our assets under management were terminated, it would have a material adverse impact on us. To date, none of our agreements with any of our retail funds has been involuntarily terminated.

Our investment management agreements permit us to provide investment management services to more than one fund so long as our ability to render services to each of the funds is not impaired, and so long as purchases and sales of portfolio securities for various advised funds are made on an equitable basis.

Our management personnel and the fund directors or trustees regularly review the investment management services fee structures in light of fund performance, the level and range of services provided, industry conditions and other relevant factors. Investment management services fees are generally waived or voluntarily reduced when a new fund is established and then increased to contractual levels within an established timeline or as net asset values reach certain levels.

2. Underwriting and Distribution

A significant portion of our revenues under the investment management and related services operating segment are generated from providing underwriting and distribution services. Franklin/Templeton Distributors, Inc. (FTDI), a wholly-owned subsidiary of the Company, acts as the principal underwriter and distributor of shares of most of our U.S.-registered open-end funds. Certain of our non-U.S. subsidiaries provide underwriting and distribution services to our non-U.S.-registered funds distributed outside the United States. We earn underwriting and distribution fees primarily by distributing the funds pursuant to distribution agreements between FTDI and the funds. Under each distribution agreement, we offer and sell the fund's shares on a continuous basis and pay certain costs associated with underwriting and distributing the fund's shares, including the costs of developing and producing sales literature and printing prospectuses, which may be then either partially or fully reimbursed by the funds.

Most of our U.S. and non-U.S.-registered retail funds are distributed with a multi-class share structure. We adopted this share structure to provide investors with greater sales charge alternatives for their investments. Class A shares represent a traditional fee structure whereby, in most cases, the investor pays a commission at the time of purchase unless minimum investment criteria are met. Class B shares, which are available in some of our non-U.S. funds, have no front-end sales charges, but instead have a declining schedule of sales charges (called contingent deferred sales charges) if the investor redeems within a number of years from the original purchase date. The U.S. funds that had offered Class B shares have ceased offering these shares to both new investors and existing shareholders. Existing Class B shareholders may continue to exchange shares into Class B shares of different funds. Existing Class B shareholders may also continue to reinvest dividends on Class B shares in additional Class B shares. Class C shares have no front-end sales charges, but do have a back-end sales charge for redemptions within 12 months from the date of purchase. Class R shares are available for purchase by certain retirement, college savings and health savings plan accounts in the United States only. Outside of the United States, we offer additional share classes to respond to local needs.

In the United States, we offer Advisor Class shares in many of our funds, and we offer Class Z shares in the Mutual Series funds, both of which have no sales charges. Franklin Global Trust offers eight series of funds, seven of which are sold with no sales charge primarily to high net-worth or institutional investors. Advisor and Class Z shares are offered to institutions and high net-worth clients (both affiliated and unaffiliated) who have assets held in accounts managed by a subsidiary of the Company and are also available to our full-time employees, current and former officers, trustees and directors. In the United States, we also sell money market funds to investors without a sales charge. Under the terms and conditions described in the prospectuses or the statements of additional information for some funds, certain investors

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can purchase shares at net asset value or at reduced sales charges. Outside the United States, we offer share classes similar to the Advisor Class shares to certain types of investors, although depending upon the fund and the country(ies) in which the fund is domiciled, the equivalent share class may be offered on a more restrictive or less restrictive basis than the similar U.S. Advisor Class shares.

Some of our insurance product funds offered for sale in the United States offer a three-class share structure, Class 1, Class 2 and Class 3 shares, which are offered at net asset value without a sales charge directly to insurance company separate accounts.

Internationally, we offer types of share classes based on the local needs of the investors in a particular market. In the majority of cases, investors in any class of shares may exchange their shares for a like class of shares in another fund, subject to certain fees that may apply.

The following table summarizes the sales charges and distribution and service fee structure that generally apply to various share classes of our U.S.-registered retail funds; however, there are exceptions to this schedule for some funds.

Sales Charges and Distribution and Service Fees that Generally Apply to U.S.-Registered Retail Funds

U.S. Retail Funds	Class A Shares	Class B Shares (c)	Class C Shares (d)	Class R Shares
Maximum Sales Charge at Time of Investment				
Equity	5.75%(a)	0.0%	0.0%	0.0%
Fixed-income	4.25%(a)	0.0%	0.0%	0.0%
Contingent Deferred Sales Charge	None.(b)	4% maximum declining to zero after 6 years of each investment.	1% if share-holder sells shares within 12 months of investment.	None.
Maximum Yearly Rule 12b-1 Plan Fees				
Equity	0.35%	1.00%	1.00%	0.50%
Fixed-income				
Taxable	0.25%	0.65%	0.65%	0.50%
Tax-free	0.10%	0.65%	0.65%	0.0%
Types of Investors That May Purchase	Any.	See Note(c) below.	Any.	See Note (f) below.
This Share Class				

U.S. Retail Funds	Advisor Class Shares	Class Z Shares (e)
Sales Charge at Time of Investment	None.	None.
Equity		
Fixed-income		
Contingent Deferred Sales Charge	None.	None.
Yearly Rule 12b-1 Plan Fees	None.	None.
Types of Investors That May Generally	Full-time employees, current and former officers, trustees and directors of Franklin Templeton Investments; institutional and high net-worth clients who have assets held in accounts managed by a subsidiary of the Company.	Full-time employees, current and former officers, trustees and directors of Franklin Templeton Investments; institutional and high net-worth clients who have assets held in accounts managed by a subsidiary of the Company.
Purchase This Share Class		

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- (a) Reductions in the maximum sales charges may be available depending upon the amount invested and the type of investor. In some cases noted in each fund's prospectus or statement of additional information, certain investors may invest in Class A shares at net asset value (with no load). In connection with certain of these no-load purchases, FTDI may make a payment out of its own resources to a broker/dealer involved with that sale.
- (b) For net asset value purchases over \$1 million, a contingent deferred sales charge of 1.00% may apply to shares redeemed within 18 months.
- (c) Class B shares convert to Class A shares after eight years of ownership. In the United States, the U.S. funds that had offered Class B shares have ceased offering these shares to new investors and existing shareholders. Existing Class B shareholders may continue to exchange shares into Class B shares of different funds. Existing Class B shareholders may also continue to reinvest dividends on Class B shares in additional Class B shares.
- (d) FTDI pays a 1.00% broker/dealer commission to broker/dealers of record of Class C shares at the time of purchase. This includes prepaid commission and an advance of the first year's Rule 12b-1 (as defined below) service fee.
- (e) When the Company entered into investment management contracts for the Mutual Series funds, the outstanding shares of Mutual Series funds were reclassified as Class Z shares on October 31, 1996. Current shareholders who held shares of any Mutual Series funds on October 31, 1996 may continue to purchase Class Z shares of any Mutual Series fund. Class Z shareholders may exchange into Class A shares of other funds, which are subject to Rule 12b-1 fees, at net asset value. FTDI may make a payment out of its own resources to a broker/dealer involved in selling Class Z shares.
- (f) The types of investors that may purchase Class R shares include employer sponsored retirement plans, any trust or plan established as part of a qualified tuition program under Section 529 of the Internal Revenue Code of 1986, as amended, and Health Reimbursement Accounts and Health Savings Accounts, either as a direct investment or as a separate or managed account.

Our non-U.S.-registered funds, including Corporate Class shares offered in Canada, have various sales charges and fee structures that are not discussed in this report.

The distribution agreements with the U.S.-registered funds generally provide for FTDI to pay commission expenses for sales of fund shares to broker/dealers. These broker/dealers receive various sales commissions and other fees from FTDI, including fees from the investors in the funds and the funds themselves, for services in matching investors with funds whose investment objectives match such investors' goals and risk profiles. Broker/dealers may also receive fees for their assistance in explaining the operations of the funds, in servicing the investor's account, reporting and various other distribution services. Fund shares are sold primarily through a large network of independent intermediaries, including broker/dealers, banks and other similar financial advisers. We are heavily dependent upon these distribution channels and business relationships. FTDI may make payments to certain broker/dealers who provide marketing support services, which may include business planning assistance, advertising, educating broker/dealer personnel about the funds and shareholder financial planning needs, placement on the broker/dealer's list of offered funds, and access to sales meetings, sales representatives and management representatives of the broker/dealer. There is increasing competition for access to these channels, which has caused our distribution costs to rise and could cause further increases in the future as competition continues and service expectations increase. As of September 30, 2007, over 2,400 local, regional and national securities brokerage firms offered shares of our U.S.-registered funds for sale to the U.S. investing public. In the United States, we have approximately 100 general wholesalers who interface with the broker/dealer community.

Most of the U.S.-registered funds, with the exception of certain of our money market funds, have adopted distribution plans (the "Plans") under Rule 12b-1 promulgated under the '40 Act ("Rule 12b-1"). The Plans are established for an initial term of one year and, thereafter, must be approved annually by each fund's board of directors or trustees and by a majority of its directors or trustees who are not interested persons of the fund under the '40 Act (the "disinterested fund directors/trustees"). All of these Plans are subject to termination at any time by a majority vote of the disinterested fund directors/trustees or by the particular fund shareholders. Fees from the Plans are paid primarily to third-party broker/dealers who provide services to the shareholder accounts and engage in distribution activities. The Plans permit the funds to bear certain expenses relating to the distribution of their shares, such as expenses for marketing,

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advertising, printing and sales promotion. FTDI may also receive reimbursement from the funds for various expenses that FTDI incurs in distributing the funds, such as marketing, advertising, printing and sales promotion, subject to the Plans' limitations on amounts. Each fund has a percentage limit for these types of expenses based on average daily net assets under management.

Similar arrangements exist with the distribution of our international funds and where, generally, the distributor of the funds in the local market arranges for and pays commissions.

Class C shares are generally more costly to us in the year of sale, but they allow us to be competitive by increasing our presence in various distribution channels. Historically, Class B and certain of our Class C deferred commission assets (DCA) arising from our U.S., Canadian and European operations were financed through transfers to or other arrangements with a company in which we hold a 49% ownership interest. The holder of the 51% ownership interest in this company is a subsidiary of an international banking institution that is not affiliated with the Company. Repayments under these financing arrangements are limited to the asset-based distribution fees paid by the funds pursuant to the distribution agreements the funds have with their distributors and to the contingent deferred sales charges collected in connection with early redemptions. The U.S. funds that had offered Class B shares have ceased offering these shares to new investors and existing shareholders. As of December 2005, our DCA have been financed generally by an independent third party.

The sales commissions and payments below, payable to qualifying broker/dealers and other intermediaries, generally apply to our U.S.-registered retail funds; however, there are exceptions to this schedule for some funds. Complete information can be found in each fund's prospectus or statement of additional information.

Sales Commissions and Other Payments Paid to Qualifying Broker/Dealers and Other Intermediaries that Generally Apply to U.S.-Registered Retail Funds

U.S. Retail Funds	Class A Shares	Class C Shares	Class R Shares
Maximum Broker/Dealer Commission at Time of Investment			
Equity	5.00%	1.00%	0.0%
Fixed-income	4.00%	1.00%	0.0%
Maximum Yearly Rule 12b-1 Plan Fees			
Equity	0.25%(a)	1.00%(b)	0.50%
Fixed-income			
Taxable	0.25%(a)	0.65%(c)	0.50%
Tax-free	0.10%	0.65%(c)	0.0%

- (a) The fees referenced above generally apply; however, there are certain individual funds that may apply a different fee structure, such as certain hybrid or taxable fixed-income funds whose Rule 12b-1 fees are 0.15%.
- (b) Rule 12b-1 service fees of 0.25% are paid in advance for the first year and are included within the 1.00% commission payment. FTDI retains the asset-based charge of 0.75% during the first year. Qualifying dealers will earn the full Rule 12b-1 fee (service fee and asset-based charge) beginning in the 13th month.
- (c) Rule 12b-1 service fees of 0.15% are paid in advance for the first year and are included within the 1.00% commission payment. FTDI retains the asset-based charge of 0.50% during the first year. Qualifying dealers will earn the full Rule 12b-1 fee (service fee and asset-based charge) beginning in the 13th month.

Two of the three share classes of our insurance product funds also have adopted a distribution plan under Rule 12b-1. Class 2 and Class 3 shares allow the fund to pay FTDI, the fund's underwriter, the insurance company or others for distribution, including servicing; Class 3 shares, which are offered by three of the insurance funds, may also assess a 1.00% redemption fee when contract owners redeem units of interest from

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an insurance company sub-account held for less than 60 days. The Rule 12b-1 distribution fees are generally assessed quarterly at the current annual rate of 0.25% of the average daily net assets of the class.

Our non-U.S. subsidiaries that provide underwriting and distribution services for our non-U.S.-registered funds pay various sales commissions and other payments to qualifying broker/dealers and other intermediaries that are not discussed in this report.

FTDI and/or its affiliates may make the following additional payments out of FTDI's or its affiliates' own assets to broker/dealers that sell shares of our funds:

Marketing support payments. FTDI may make payments to certain broker/dealers who are holders or dealers of record for accounts in one or more of our funds. A broker/dealer's marketing support services may include business planning assistance, advertising, educating broker/dealer personnel about the funds and shareholder financial planning needs, placement on the broker/dealer's list of offered funds, and access to sales meetings, sales representatives and management representatives of the broker/dealer. FTDI compensates broker/dealers differently depending upon, among other factors, sales and asset levels, redemption rates and the level and/or type of marketing and educational activities provided by the broker/dealer. Such compensation may include financial assistance to broker/dealers that enable FTDI to participate in and/or present at conferences or seminars, sales or training programs for invited registered representatives and other employees, client and investor events and other broker/dealer-sponsored events. These payments may vary depending upon the nature of the event. FTDI periodically reviews its marketing support arrangements to determine whether to continue such payments. In the case of any one broker/dealer, marketing support payments will not exceed the sum of 0.10% of that broker/dealer's current year's total sales of our funds and 0.05% (or 0.03%) of the total assets of equity (or fixed income) funds attributable to that broker/dealer, on an annual basis. The statement of additional information for each retail fund provides a list of broker/dealers that receive such marketing support payments. Marketing support payments made to organizations located outside the United States, with respect to investments in a fund by non-U.S. persons, may exceed the above-stated limitations.

Transaction support payments. FTDI may pay ticket charges of up to \$20 per purchase or exchange order placed by a broker/dealer or one-time payments for ancillary services, such as setting up funds on a broker/dealer's fund trading system.

Other payments. From time to time, FTDI, at its expense, may make additional payments to broker/dealers that sell or arrange for the sale of shares of the funds. FTDI routinely sponsors due diligence meetings for registered representatives during which they receive updates on various funds and are afforded the opportunity to speak with portfolio managers. Invitation to these meetings is not conditioned on selling a specific number of shares. Those who have shown an interest in our funds, however, are more likely to be considered. To the extent permitted by their firm's policies and procedures, registered representatives' expenses in attending these meetings may be covered by FTDI.

Other compensation may be offered to the extent not prohibited by federal or state laws or any self-regulatory agency, such as the Financial Industry Regulatory Authority (FINRA), formerly the National Association of Securities Dealers, Inc. (the NASD). FTDI makes payments for events it deems appropriate, subject to FTDI's guidelines and applicable law.

3. Shareholder and Transfer Agency Services

One of our subsidiaries, Franklin Templeton Investor Services, LLC (FTIS), provides shareholder record keeping services and acts as transfer agent and dividend-paying agent for the U.S.-registered

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open-end funds. FTIS is registered with the SEC as a transfer agent under the Securities Exchange Act of 1934, as amended. Generally, FTIS is compensated under an agreement with each fund on the basis of an annual per account fee that varies with the fund and the type of services being provided. FTIS also is reimbursed for out-of-pocket expenses. In some instances, certain funds compensate FTIS based on assets under management. Other subsidiaries provide the same services to the funds offered for sale in Canada, Europe, Asia and other non-U.S. regions under similar fee arrangements.

FTIS may also pay servicing fees, which are reimbursed by the funds, in varying amounts to certain financial institutions (primarily to help offset costs associated with client account maintenance support, statement preparation and transaction processing) that: (i) maintain omnibus accounts with the fund in the institution's name on behalf of numerous beneficial owners of fund shares; or (ii) provide support for fund shareholder accounts by sharing account data with FTIS through the National Securities Clearing Corporation (NSCC) networking system. FTIS will also receive a fee from the funds for services provided in support of beneficial owners and NSCC networking system accounts.

C. High Net-Worth Investment Management and Related Services

Through Fiduciary Trust (including its trust company and investment adviser subsidiaries), we provide investment management services to, among others, high net-worth individuals and families. Similarly, through our Canadian high net-worth business unit, FTCC, we provide investment management services and offer sponsored investment products to high net-worth individuals and families. Our high net-worth client business seeks to maintain relationships that span generations and help families plan the most appropriate method of intergenerational wealth transfer.

Individual client assets are typically held in accounts separately managed by individual portfolio managers. These portfolio managers determine asset allocation and stock selection for client accounts, taking into consideration each client's specific long-term objectives while utilizing our macroeconomic and individual stock research.

Fiduciary Trust services that focus on managing family wealth from generation to generation include wealth management, estate planning, private banking, tax and custody services. We offer clients personalized attention and estate planning expertise in an integrated package of services known as Family Resource Management® (FRM). Services under FRM provide clients with an integrated strategy to optimize wealth accumulation and maximize after-tax wealth transfer to the next generation. Evaluation of third-party investment management products or services is performed by the Strategic Advisory Group, an investment advisory group within Fiduciary Trust.

D. Institutional Management

We provide a broad array of investment management services to institutional clients, focusing on foundations, endowment funds and government and corporate pension funds. Our subsidiaries offer a wide range of both domestic and international equity, fixed-income and specialty strategies through a variety of investment vehicles, including separate and commingled accounts and open-end and closed-end domestic and offshore funds.

We operate our institutional business under the trade name Franklin Templeton Institutional. Through various legal entities, including FTI, we distribute and market globally the different investment management capabilities of our various investment management subsidiaries under the Franklin, Templeton, Mutual Series, Bissett and Darby brand names. We primarily attract new institutional business through our strong relationships with pension and management consultants and through additional mandates from our existing client relationships.

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Our retirement business is conducted through divisions of FTDI that work closely with sponsors of defined contribution plans, including 401(k) plans, bundled defined contribution plans, variable annuity products and individual retirement accounts (IRAs). This business unit allows us to focus on expanding sales of our asset management capabilities to the U.S. retirement industry by offering a number of investment options, including sub-advised portfolios, funds, education savings plans and variable insurance trusts.

Through our various subsidiaries, we also market and distribute our sponsored investment products to separately-managed accounts. Our subsidiaries, Franklin Templeton Financial Services Corp. and Templeton/Franklin Investment Services, Inc., also serve as direct marketing broker/dealers for institutional investors for certain of our institutional mutual funds and private equity funds.

E. Trust and Custody

Through various trust company subsidiaries, including Fiduciary Trust, we offer a wide range of investment management and related services, including trust services, custody and administration, estate planning, tax planning, and private banking, to high net-worth individuals, families, foundations and institutional clients in the United States and abroad. In addition, we also offer our clients a series of other services, including foreign exchange, performance measurement, securities lending and brokerage services. We provide planned giving administration and related custody services for non-profit organizations, including pooled income funds, charitable remainder trusts, charitable lead trusts and gift annuities, for which we may or may not act as trustee.

Our other subsidiaries involved in the trust business, either as trust companies or companies investing in trust companies, include: Fiduciary Investment Corporation, which is incorporated under the New York State Banking Law and serves as an indirect holding company for several of our trust company subsidiaries; FTCC, a trust company incorporated under the Trust and Loan Companies Act in Canada; Fiduciary Trust International of the South, a Florida state-chartered limited purpose trust company; Fiduciary Trust International of California, a California state-chartered limited purpose trust company; Fiduciary Trust International of Delaware, a Delaware state-chartered limited purpose trust company; FTCI (Cayman) Ltd., an offshore trust company holding an unrestricted trust license in the Cayman Islands; and Franklin Templeton Bank & Trust, F.S.B. (FTB&T), a chartered federal savings bank. All of the trust companies referenced above have full trust powers. FTB&T, among other functions, exercises full trust powers and serves primarily as custodian of IRAs and business retirement plans.

F. Private Equity Investment Management

Darby is primarily engaged in sponsoring and managing funds that invest in private equity and mezzanine finance transactions in emerging markets in Asia, Latin America and Central/Eastern Europe. Darby offers these investment funds through private placements to institutional and high net-worth individual investors.

G. Summary of Our Sponsored Investment Products

Our sponsored investment products are offered to retail, institutional, high net-worth and separate account clients, which include individual investors, qualified groups, trustees, tax-deferred (such as IRAs in the United States and retirement saving plans, or RSPs, in Canada) or money purchase plans, employee benefit and profit sharing plans, trust companies, bank trust departments and institutional investors. Clients in our sponsored investment products were located in approximately 170 countries at September 30, 2007.

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1. Investment Objectives

The sponsored investment products that we offer accommodate a variety of investment goals, spanning the spectrum of our clients' risk tolerance from capital appreciation (with our more growth-oriented products) to capital preservation (with our fixed-income offerings). In seeking to achieve such objectives, each portfolio emphasizes different strategies and invests in different types of securities.

Our equity investment products include some that are considered value-oriented, others that are considered growth-oriented, and some that use a combination of growth and value characteristics, generally identified as blend or core products. Value investing focuses on identifying companies that our research analysts and portfolio managers believe are undervalued based on a number of different factors, usually put in the context of historical ratios such as price-to-earnings or price-to-book value; however, we also consider the future earnings potential of each individual company on a multi-year basis. Our growth portfolios maintain a philosophy of identifying future drivers of growth that are not reflected in a company's current stock price, as determined by our research analysts and portfolio managers. Paramount to all of our different equity products is the incorporation of independent, fundamental research through our own in-house investment professionals. Our approach, across the variety of equity products we manage, emphasizes bottom-up stock selection within a disciplined portfolio construction process, and is complemented by our ongoing assessment of risk at both the security and portfolio levels.

Portfolios seeking income generally focus on one or more of the following securities: taxable and tax-exempt money market instruments; tax-exempt municipal bonds; global fixed-income securities; and fixed-income debt securities of corporations, of the U.S. government and its sponsored agencies and instrumentalities, such as the Government National Mortgage Association, the Federal National Mortgage Association and the Federal Home Loan Mortgage Corporation, or of the various states in the United States. Still others focus on investments in particular countries and regions.

2. Types of Sponsored Investment Products

As of September 30, 2007 we had \$645.9 billion in assets under management. Our U.S.-registered open-end funds (excluding our insurance products trust) accounted for \$334.0 billion of our assets under management. As of September 30, 2007, the net assets under management of our five largest funds were Franklin Income Fund (\$62.3 billion), Templeton Growth Fund (\$39.4 billion), Mutual Shares Fund (\$25.9 billion), Mutual Discovery Fund (\$17.1 billion) and Templeton Foreign Fund (\$15.2 billion). These five funds represented, in the aggregate, approximately 25% of all sponsored investment product assets under management.

Franklin Templeton Variable Insurance Products Trust, our insurance products trust, offers 23 funds to U.S. investors, with assets of \$37.0 billion as of September 30, 2007. Our insurance products funds are available as investment options through variable insurance contracts and are also sold to certain funds of funds. Most of the insurance products funds have been fashioned after some of our more popular U.S. retail funds offered to the general public and are managed, in most cases, by the same investment advisors.

We also provide investment management and related services to a number of closed-end investment companies whose shares are traded on various major U.S. stock exchanges. Our U.S. closed-end funds accounted for \$5.6 billion of our assets under management. On a company-wide basis, institutional, separate, high net-worth and other accounts accounted for \$150.0 billion of assets under management.

In addition, \$119.3 billion of our assets under management were held in open-end and closed-end funds and other accounts that are sold outside of the United States, and whose investment objectives vary, but are primarily international and global equity-oriented. We provide investment management, marketing

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and distribution services to SICAV (Société d Investissement à Capital Variable) funds, contract-type funds and umbrella unit trusts organized in Luxembourg and Ireland, respectively, which are distributed in non-U.S. market places, as well as to locally organized funds in various countries outside the United States. In some countries, we offer products for the particular local market. For example, Franklin Templeton Asset Management (India) Private Limited, one of our subsidiaries in India, manages various local open-ended and closed-ended funds offered to investors in India, with assets under management of \$7.7 billion as of September 30, 2007.

Our sponsored investment products include portfolios managed for some of the world's largest corporations, endowments, charitable foundations, pension funds, wealthy individuals and other institutions. We use various investment techniques to focus on specific client objectives for these specialized portfolios.

The following table shows the various types of our U.S.-registered open-end funds and dedicated insurance product funds as of September 30, 2007, and is categorized using the investment classifications set forth below:

U.S.-REGISTERED OPEN-END FUNDS**CATEGORY**

(and approximate amount of assets under
management, as of September 30, 2007)

In Billions	INVESTMENT CLASSIFICATION	NO. OF MUTUAL FUNDS	NO. OF INSURANCE PRODUCT FUNDS
<i>I. EQUITY FUNDS (\$214.0)</i>			
<i>A. Capital Appreciation Funds (\$31.6)</i>			
	Seek capital appreciation; dividends are not a primary consideration.		
1. Aggressive Growth Funds	Invest primarily in common stocks of small, growth companies.	5	1
2. Growth Funds	Invest primarily in common stocks of well-established companies.	11	2
3. Sector Funds	Invest primarily in companies in related fields.	8	2
<i>B. World Equity Funds (\$121.9)</i>			
1. Emerging Market Funds	Invest primarily in companies based in developing regions of the world.	3	1
2. Global Equity Funds	Invest primarily in equity securities traded worldwide, including those of U.S. companies.	11	2
3. International Equity Funds	Invest primarily in equity securities of companies located outside the United States.	4	1
4. Regional Equity Funds	Invest in companies based in a specific part of the world.	3	0
<i>C. Total Return Funds (\$60.5)</i>			
	Seek a combination of current income and capital appreciation.		

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(and approximate amount of assets under
management, as of September 30, 2007)

In Billions	INVESTMENT CLASSIFICATION	NO. OF MUTUAL FUNDS	NO. OF INSURANCE PRODUCT FUNDS
1. Growth and Income Funds	Invest primarily in common stocks of established companies with the potential for growth and a consistent record of dividend payments.	9	5
2. Income Equity Funds	Invest primarily in equity securities of companies with good dividend-paying records.	1	0
<i>II. HYBRID FUNDS (\$71.1)</i>	Invest in a mix of equities, fixed-income securities, and derivative instruments.		
<i>A. Asset Allocation Funds (\$0.2)</i>	Invest in various asset classes including, but not limited to, equities, fixed-income securities, and money market instruments.	17	2
<i>B. Income-Mixed Funds (\$70.9)</i>	Invest in a variety of income-producing securities, including equities and fixed-income instruments.	6	1
<i>C. Balanced (\$0.04)</i>	Invest in a specific mix of equity securities and bonds with the three-part objective of conserving principal, providing income, and achieving long-term growth of both principal and income.	1	0
<i>III. TAXABLE BOND FUNDS (\$25.3)</i>			
<i>A. High Yield Funds (\$3.0)</i>	Invest two-thirds or more of their portfolios in lower-rated U.S. corporate bonds (Baa or lower by Moody's and BBB or lower by Standard & Poor's rating services).	2	1
<i>B. World Bond Funds (\$8.6)</i>	Invest in debt securities offered by non-U.S. companies and governments.		
1. Global Bond Funds:			
General	Invest in debt securities worldwide with no stated average maturity or an average maturity of five years or more.	1	2
2. Global Bond Funds:			
Short-Term	Invest in debt securities worldwide with an average maturity of one to five years.	1	0
3. Other World Bond Funds	Invest in international bond and emerging market debt securities, such as non-U.S. government and corporate debt instruments.	1	0

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(and approximate amount of assets under
management, as of September 30, 2007)

In Billions	INVESTMENT CLASSIFICATION	NO. OF MUTUAL FUNDS	NO. OF INSURANCE PRODUCT FUNDS
<i>C. Government Bond Funds (\$7.8)</i>			
1. Government Bond Funds:	Invest in U.S. government bonds of varying maturities.		
Intermediate Term	Invest two-thirds or more of their portfolios in U.S. government securities with an average maturity of five to ten years.	0	1
2. Government Bond Funds:	Invest two-thirds or more of their portfolios in U.S. government securities with an average maturity of one to five years.	1	0
Short-Term			
3. Mortgage-Backed Funds	Invest two-thirds or more of their portfolios in pooled mortgage-backed securities.	3	0
<i>D. Strategic Income Funds (\$3.9)</i>			
<i>E. Corporate Bond Funds (\$2.0)</i>			
1. Corporate Bond Funds:	Seek current income by investing in high-quality debt securities issued by U.S. corporations.		
Short-Term	Invest two-thirds or more of their portfolios in U.S. corporate bonds with an average maturity of one to five years.	1	0
<i>IV. TAX-FREE BOND FUNDS (\$55.5)</i>			
<i>A. State Municipal Bond Funds (\$38.9)</i>			
1. State Municipal Bond Funds:	Invest primarily in municipal bonds issued by a particular state.		
General	Invest primarily in single-state municipal bonds with an average maturity of greater than five years or no specific stated maturity. The income from these funds is largely exempt from federal as well as state income tax for residents of the state.	29	0
2. State Municipal Bond Funds:	Invest primarily in single-state municipal bonds with an average maturity of one to five years. The income from these funds is largely exempt from federal as well as state income tax for residents of the state.	2	0
Short-Term			
<i>B. National Municipal Bond Funds (\$16.6)</i>			
	Invest primarily in bonds of various municipal issuers in the United States.		

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CATEGORY

(and approximate amount of assets under management, as of September 30, 2007)

In Billions	INVESTMENT CLASSIFICATION	NO. OF MUTUAL FUNDS	NO. OF INSURANCE PRODUCT FUNDS
1. National Municipal Bond Funds: General	Invest primarily in municipal bonds with an average maturity of more than five years or no specific stated maturity.	4	0
2. National Municipal Bond Funds: Short-Term	Invest primarily in municipal bonds with an average maturity of one to five years.	1	0
<i>V. MONEY MARKET FUNDS (\$5.1)</i>			
<i>A. Taxable Money Market Funds (\$4.2)</i>			
1. Taxable Money Market Funds: Non-Government	Invest in short-term, high-grade money market securities with average maturities of 90 days or less.	6	1
<i>B. Tax-Exempt Money Market Funds (\$0.9)</i>			
1. National Tax-Exempt Money Market Funds	Invest in short-term securities of various U.S. municipal issuers.	1	0
2. State Tax-Exempt Money Market Funds	Invest primarily in short-term securities of municipal issuers in a single state to achieve tax-free income for residents of the state.	2	0

The following table sets forth the types of our non-U.S. open-end funds as of September 30, 2007 categorized by investment classification and sales region.

NON-U.S. OPEN-END FUNDS (a)

CATEGORY

(and approximate amount of assets under management, as of September 30, 2007)

In Billions	INVESTMENT CLASSIFICATION	NO. OF MUTUAL FUNDS BY SALES REGION	
<i>I. EQUITY FUNDS (\$76.8)</i>			
A. Global/International Equity Funds (\$73.7)	Invest in securities of companies traded world-wide, including U.S. and non-U.S. companies.	Asia-Pacific:	45
		Canada:	20
		Europe:	41
			2

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B. Domestic (U.S.) Equity Funds (\$3.1) Invest in equity securities of U.S. companies.

Latin America:	
Asia-Pacific:	1
	5
Canada:	11
Europe:	

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CATEGORY (and approximate amount of assets under management, as of September 30, 2007)		NO. OF MUTUAL FUNDS BY SALES REGION
In Billions	INVESTMENT CLASSIFICATION	
II. FIXED-INCOME FUNDS (\$28.8)		
A. Global/International Fixed- Income Funds (\$21.6)	Invest world-wide in debt securities offered by non-U.S. companies and governments. These funds may also invest assets in debt securities offered by companies located in the United States.	Asia-Pacific: 35 7 Canada: 19 Europe:
B. Domestic (U.S.) Fixed-Income Funds (\$7.2)	Invest in debt securities offered by U.S. companies and the U.S. government and/or municipalities located in the United States.	Asia-Pacific: 2 2 Canada: 4 Europe:
III. HYBRID FUNDS (\$4.3)		
	Invest in a mix of global equity, fixed-income securities and derivative instruments.	Asia-Pacific: 19 6 Canada: 11 Europe:
IV. TAXABLE MONEY FUNDS (\$2.5)		
	Invest in securities issued or guaranteed by U.S. or non-U.S. governments or agencies.	Asia-Pacific: 4 4 Canada: 2 Europe:

(a) Does not include the Franklin Templeton Global Fund, the Fiduciary Emerging Markets Bond Fund plc, and fund-of-funds. For purposes of this table, we consider the sales region to be where a fund is based and primarily sold and not necessarily the region where a particular fund is invested. Many funds are also distributed across different sales regions (e.g., SICAV funds are based, primarily sold in, and, therefore, considered to be within the Europe sales region, although also distributed in the Asia-Pacific and Latin America sales regions), but are only designated a single sales region in the table.

3. Fund Introductions, Mergers and Liquidations

In an effort to address changing market conditions and evolving investor needs, we periodically introduce new funds, merge existing funds or liquidate existing funds. During the fiscal year ended September 30, 2007 (fiscal year 2007), we introduced a number of funds within the United States, Canada, Europe and other regions.

In the United States, we added three funds to our retail product line during fiscal year 2007. To support our clients' interests in investing in emerging countries, we added the Templeton Emerging Markets Small Cap Fund. Additionally, to further round out our value equity offering, we launched the Franklin All Cap Value Fund to provide our clients with an additional multi-cap value investment option. We also launched the Founding Funds investment strategy in our insurance product line for insurance investors looking for a similar product to our retail Franklin Templeton Founding Fund.

In Canada, we launched the Bissett Canadian Core Plus Bond Fund, the Franklin Templeton Global Aggregate Bond Fund and the Bissett Corporate Bond Fund to strengthen our strategic focus on fixed income. We also enhanced our balanced and equity line-ups by launching the Quotential Global Balanced Portfolio and Quotential Global Balanced Corporate Class Portfolio, the Franklin US Core Equity Fund and the Bissett Energy Corporate Class, as well as a Corporate Class version of the Bissett Canadian Balanced Fund.

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In Europe, we launched new core funds and investment products that address the unique needs of local markets. We continued to expand our international cross-border product offering through the introduction of several new share classes and seven new SICAV funds, the majority of which are designed to respond to increased investor interest in fixed income products. We further expanded our SICAV funds of funds

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product range to include three additional funds of funds targeting investors wishing to invest in dollar denominated products. We launched a part II SICAV currently with one underlying sub-fund which will be promoted on a private placement basis.

In India, we introduced several new closed-end fixed income funds, an open-end India High Growth Companies fund and three quarterly interval plans to provide investors with choices in their asset allocations. In Korea, we launched seven internationally invested master funds as well as two domestic master funds to respond to changing market dynamics. From these master funds, we also developed feeder funds to tailor our products towards meeting our clients' varied investment needs. In Japan, we launched two new global equity and Japanese core active funds. We initiated new products in other country specific markets, including Brazil and Singapore.

Darby's private equity funds generally are structured as partnerships with a limited life, including most commonly a five-year investment period and a five-year divestment period. Darby launches new funds, as well as invests, divests, and liquidates existing funds as these periods expire, primarily in Asia, Latin America and Central/Eastern Europe.

During fiscal year 2007, the following fund mergers and liquidations, among others, occurred: three U.S.-registered open-end funds were merged into other U.S.-registered open-end funds; two U.S.-registered institutional open-end funds were liquidated; six non-U.S.-registered open-end funds were merged into other non-U.S.-registered open-end funds; and 20 funds around the world were liquidated.

II. Banking/Finance

Our secondary business segment is banking/finance, which offers select retail banking, private banking and consumer lending services.

One of our subsidiaries, Fiduciary Trust, a New York state-chartered bank, is insured by the Federal Deposit Insurance Corporation (FDIC), and provides private banking services primarily to high net-worth clients who maintain trust, custody and/or management accounts with Fiduciary Trust in the United States. Fiduciary Trust's private banking and credit products include, among others, loans secured by marketable securities, deposit accounts and other banking services. Fiduciary Trust also offers investment management, custody and related services to institutional accounts and high net-worth individuals and families.

Another of our subsidiaries, Franklin Capital Corporation (FCC), engages primarily in the purchase, securitization and servicing of retail installment sales contracts (automobile contracts) originated by independent automobile dealerships. FCC is incorporated and headquartered in Utah and conducts its business primarily in the Western region of the United States. As of September 30, 2007, FCC's total assets included \$370.5 million of outstanding automobile contracts and \$0.7 million in other fixed term assets. During fiscal year 2007, FCC securitized approximately \$676.9 million of automobile contract receivables for which it maintains servicing rights. As of September 30, 2007, FCC was servicing \$749.8 million of receivables that had been securitized to date. See Note 9 Securitization of Loans Held for Sale in the Notes to Consolidated Financial Statements in Item 8 of Part II of this Form 10-K.

Our securitized automobile contracts business is subject to marketplace fluctuation and competes with businesses with significantly larger portfolios. Automobile loan portfolio losses can be influenced significantly by trends in the economy and credit markets, which reduce borrowers' ability to repay loans. A more detailed analysis of loan losses and delinquency rates in our consumer lending and dealer automobile loan business is contained in Note 9 Securitization of Loans Held for Sale in the Notes to Consolidated Financial Statements in Item 8 of Part II of this Form 10-K. See also Risk Factors in Item 1A of Part I of this Form 10-K.

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Our subsidiary FTB&T, with total assets of \$118.8 million, as of September 30, 2007, provides deposit accounts insured by the FDIC and general consumer loan products, such as credit card loans, unsecured loans, loans secured by marketable securities, mortgage loans, debit card products and automobile loans. It also provides Advisor Director Trust[®], a directed trust service. FTB&T (formerly known as Franklin Bank) became chartered as a federal savings bank on May 1, 2000 when the Office of Thrift Supervision (the OTS) approved FTB&T's application to convert from a California state banking charter to a federal thrift charter. Immediately following the conversion of FTB&T's state charter to a federal thrift charter, Franklin Templeton Trust Company, a California chartered trust company, was merged into FTB&T and continues to perform its prior activities as a division of FTB&T.

Our other banking subsidiaries include, among others, FTCI (Cayman) Ltd., which is an offshore trust company that holds an unrestricted trust license in the Cayman Islands.

FINANCIAL INFORMATION ABOUT SEGMENTS AND GEOGRAPHIC AREAS

Certain financial information by business segment and geographic area is contained in Note 18 Segment Information in the Notes to Consolidated Financial Statements in Item 8 of Part II of this Form 10-K, which is incorporated herein by reference.

REGULATORY CONSIDERATIONS

Virtually all aspects of our business, including those conducted through our various subsidiaries, are subject to various federal, state, and international regulation and supervision. In the U.S., we are subject to regulation and supervision by, among others, the SEC, FINRA, the Federal Reserve Board (the FRB), the FDIC, the OTS and the New York State Banking Department (NYSBD). Globally, we are subject to regulation and supervision by, among others, the Office of the Superintendent of Financial Institutions Canada as well as provincial and territorial regulators of financial services and securities in Canada and the Mutual Fund Dealers Association of Canada, the Monetary Authority of Singapore, the Securities Commission of The Bahamas, the Financial Services Authority in the U.K., the Irish Financial Services Regulatory Authority, the Commission de Surveillance du Secteur Financier in Luxembourg, the Autorité des Marchés Financiers in France, the Federal Financial Supervisory Authority in Germany, the Commissione Nazionale per le Società e la Borsa in Italy, the Comisión Nacional del Mercado de Valores in Spain, the Autoriteit Financiële Markten in The Netherlands, the Finansinspektionen in Sweden, the Swiss Federal Banking Commission, the Dubai Financial Services Authority, the Securities and Futures Commission of Hong Kong, the Korean Ministry of Finance and Economy, the Financial Supervisory Commission and the Financial Supervisory Services in Korea, the Securities and Exchange Board of India, the China Securities Regulatory Commission, the Taiwan Securities and Futures Bureau, the Ministry of Finance, and the Commerce Department, Ministry of Economic Affairs in Taiwan, the Financial Services Agency in Japan, the Australian Securities and Investment Commission in Australia, the Brazilian Securities and Exchange Commission in Brazil, and the Comisión Nacional Bancaria y de Valores in Mexico. The Advisers Act imposes numerous obligations on our subsidiaries, which are registered in the United States as investment advisers, including record keeping, operating and marketing requirements, disclosure obligations and prohibitions on fraudulent activities. The 40 Act imposes similar obligations on the investment companies that are advised by our subsidiaries. The SEC is authorized to institute proceedings and impose sanctions for violations of the Advisers Act and the 40 Act, ranging from fines and censure to termination of an investment adviser's registration.

The Company and many of the investment companies advised by our various subsidiaries are subject to federal securities laws and state securities and corporate laws, including those affecting corporate governance, such as the Sarbanes-Oxley Act of 2002 and rules adopted by the SEC. As an NYSE-listed

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company, we are also subject to the rules of the NYSE, including its corporate governance standards. The federal securities laws have also been augmented by other measures, including the USA Patriot Act of 2001.

Since 1993, the NASD Conduct Rules (under FINRA) have limited the amount of aggregate sales charges that may be paid in connection with the purchase and holding of investment company shares sold through broker/dealers. The effect of the rule is to limit the amount of fees that could be paid pursuant to a fund's Rule 12b-1 Plan to FTDI, our principal underwriting and distribution subsidiary in the United States, which earns underwriting commissions on the distribution of fund shares in the United States.

Following the acquisition of Fiduciary Trust in April 2001, the Company registered as a bank holding company under the BHC Act and became subject to supervision, regulation and examination by the FRB. The Company also has elected to be a financial holding company. Under FRB policy, a bank holding company, including a financial holding company, is expected to act as a source of financial strength to each of its banking subsidiaries. In addition, bank holding companies should pay cash dividends on common stock only out of income available from the previous fiscal year and only if prospective earnings retention is consistent with anticipated future needs and financial condition.

The FRB also has adopted a system of risk-based capital guidelines to evaluate the capital adequacy of most bank holding companies, including the Company. Under these guidelines, the Company currently is well capitalized. In addition, each of Fiduciary Trust and FTB&T was well capitalized as of September 30, 2007, as such term is defined by the FDIC and OTS, respectively. A depository institution generally is prohibited from making capital distributions, including paying dividends, or paying management fees to a holding company if the institution would thereafter be undercapitalized. Moreover, undercapitalized institutions may not accept, renew or roll over brokered deposits. Bank regulators are required to take prompt corrective action to resolve any problems associated with insured depository institutions, including Fiduciary Trust and FTB&T, which become undercapitalized. The GLB Act, however, generally prohibits the FRB from imposing similar capital requirements on regulated non-bank subsidiaries of a financial holding company.

Pursuant to the GLB Act, a bank holding company may also elect to become a financial holding company to engage in a broader range of activities that are financial in nature, including securities underwriting, dealing and market making, securitizing assets, sponsoring mutual funds and investment companies, engaging in insurance underwriting and brokerage activities and investing (without providing routine management) in companies engaged in non-financial activities. To qualify as a financial holding company, each of a bank holding company's domestic subsidiary banks and other depository institution subsidiaries, which are not subject to an exemption, must be and remain at all times well capitalized and well managed. In addition, each such subsidiary must have achieved at least a satisfactory rating under the Community Reinvestment Act (CRA) in the evaluation preceding the financial holding company election. We elected to become a financial holding company in 2001, and, accordingly, FTB&T is subject to CRA requirements, although Fiduciary Trust is exempt from such requirements because it qualifies as a special purpose bank. If, however, we do not continue to meet all of the requirements for status as a financial holding company, we would, depending on which requirement is not met, be required to (i) cause Fiduciary Trust or FTB&T to meet such requirement and, in the meantime, seek prior FRB approval to undertake certain new activities or certain banking and non-banking acquisitions, or (ii) either discontinue our banking (but not our thrift) business, or discontinue those activities not generally permissible for bank holding companies.

The BHC Act generally requires that a bank holding company obtain prior approval of the FRB before acquiring control of any bank. In addition, the FRB may impose limitations, restrictions, or prohibitions on the activities or acquisitions of a financial holding company if the FRB believes that the financial holding

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company does not have appropriate financial and managerial resources. The GLB Act establishes the FRB as the umbrella supervisor for financial holding companies and adopts an administrative approach to regulation that generally requires the FRB to defer to the actions and requirements of the U.S. functional regulators of subsidiary broker/dealers, investment advisers, investment companies, insurance companies, and other regulated non-depository institutions. The FRB, however, retains broad authority to prohibit activities of bank holding companies and their non-banking subsidiaries that represent unsafe and unsound banking practices or that constitute violations of law or regulation. Civil money penalties may be imposed for certain activities conducted on a knowing or reckless basis if those activities caused a substantial loss to the bank holding company.

Each of our banking subsidiaries is subject to restrictions under federal law that limit transactions with the Company and its non-bank subsidiaries, including loans and other extensions of credit, investments, or asset purchases. These and various other transactions, including any payment of money to the Company and its non-bank subsidiaries, must be on terms and conditions that are, or in good faith would be, offered to companies that are not affiliated with these entities. In addition, these laws and related regulations may limit our ability to obtain funds from subsidiary banks or affiliates.

The operations and activities of Fiduciary Trust are subject to extensive regulation, supervision and examination by the FDIC and NYSBD while the operations and activities of our other subsidiaries, including FTB&T, are subject to oversight by the OTS and various state regulators. The laws and regulations of these regulators generally impose restrictions and requirements, with which we must comply, on capital adequacy, management practices, liquidity, branching, earnings, loans, dividends, investments, reserves against deposits and the provision of services.

The federal banking agencies and the NYSBD have broad enforcement powers, including the power to terminate deposit insurance, impose substantial fines and other civil and criminal penalties and appoint a conservator or receiver. Failure to comply with applicable laws, regulations and supervisory agreements could subject the Company, our thrift and banking subsidiaries, as well as officers, directors and other so-called institution-affiliated parties of these organizations to administrative sanctions and potentially substantial civil money penalties. In addition, the appropriate federal banking agency may appoint the FDIC as conservator or receiver for a banking institution, or the FDIC may appoint itself if certain circumstances exist.

COMPETITION

The financial services industry is highly competitive and has increasingly become a global industry. There are approximately 8,900 open-end investment companies of varying sizes, and with varying investment policies and objectives, whose shares are being offered to the public in the United States. Due to our international presence and varied product mix, it is difficult to assess our market position relative to other asset managers on a worldwide basis, but we believe that we are one of the more widely diversified asset managers in the United States. We believe that our equity and fixed-income asset mix coupled with our global presence will serve our competitive needs well over the long term. We continue to focus on the performance of our investment products, service to customers and extensive marketing activities through our strong broker/dealer and other financial institution distribution network as well as with high net-worth and institutional customers. We believe that performance, diversity of products and customer service, along with fees and costs, are the primary methods of competition in the asset management industry.

We face strong competition from numerous asset management companies, mutual fund, stock brokerage and investment banking firms, insurance companies, banks, savings and loan associations and other financial institutions, which offer a wide range of financial and investment management services to

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the same institutional accounts, separate accounts, retail investors and high net-worth customers that we are seeking to attract. Over the past decade, a significant number of new asset management firms and investment products have been established, increasing competition. Many of our competitors have long-standing and established relationships with broker/dealers and investment adviser customers. Others have focused on, offer and market specific product lines, which are able to provide strong competition to certain of our asset classes, since we have a broad range of products. In recent years, there also has been a trend of consolidation in the financial services industry, resulting in stronger competitors, some with greater financial resources and broader distribution channels than our own.

We rely largely on intermediaries to distribute and sell our fund shares. We have and continue to pursue sales relationships with all types of intermediaries to broaden our distribution network. We have experienced increased costs related to maintaining our distribution channels and we anticipate that this trend will continue. A failure to maintain strong business relationships with the major intermediaries who currently distribute our products may also impair our distribution and sales operations. 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 assets under management, related revenues and overall business and financial condition.

We maintain a sophisticated Internet platform to compete with the rapidly developing and evolving capabilities being offered with this technology. However, technology is subject to rapid change and we cannot guarantee that our competitors may not implement more advanced Internet platforms for their products, which could affect our business.

We believe that we are well positioned to deal with changes in marketing trends as a result of our already extensive advertising activities and broad based marketplace recognition. We conduct significant advertising and promotional campaigns through various media sources to promote brand recognition. We advertise in major financial publications, as well as on radio, television and the Internet to promote brand name recognition and to assist our distribution network. Such activities include purchasing network and cable programming, sponsorship of sporting events, and extensive newspaper and magazine advertising.

Diverse and strong competition affects the banking/finance segment of our business as well, and limits the fees that can be charged for our services. For example, in our banking/finance segment we compete with many types of institutions for consumer loans, including the finance subsidiaries of large automobile manufacturers, which offer special incentives from time to time to stimulate automobile sales, including no-interest loans. These product offerings by our competitors limit the interest rates that we can charge on consumer loans.

INTELLECTUAL PROPERTY

We have used, registered, and/or applied to register certain trademarks, service marks and trade names to distinguish our sponsored investment products and services from those of our competitors in the United States and in other countries and jurisdictions, including, but not limited to, Franklin[®], Templeton[®], Bissett[®], Mutual Series[®], Fiduciary and Darby[®]. Our trademarks, service marks and trade names are important to us and, accordingly, we enforce our trademark, service mark and trade name rights in the United States and abroad. The Franklin Templeton Investments brand has been, and continues to be, extremely 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 brand is harmed, our future business prospects may be affected.

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EMPLOYEES

As of September 30, 2007, we employed approximately 8,700 employees and operated offices in 29 countries. We consider our relations with our employees to be satisfactory.

AVAILABLE INFORMATION

The Company files reports with the SEC, including current and periodic reports, proxy statements and other information filed with or furnished to the SEC from time to time. The public may read and copy any of these filings at the SEC's Public Reference Room at 100 F Street, N.E., Washington, D.C. 20549. Information on the operation of the Public Reference Room can be obtained by calling the SEC at 1-800-SEC-0330.

The SEC also maintains an Internet site that contains reports, proxy and information statements, and other information regarding issuers, including the Company, who file electronically with the SEC, at <http://www.sec.gov>. Additional information about the Company can also be obtained at our website at www.franklinresources.com under Investor Relations on the Our Company page. We make available free of charge on our website our Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended, as soon as reasonably practicable after we electronically file such material with, or furnish it to, the SEC.

Corporate Governance Guidelines. The Company has adopted Corporate Governance Guidelines. The Corporate Governance Guidelines are posted on the Company's website under Corporate Governance on the Our Company page and are available in print to any stockholder who requests a copy.

Committee Charters. The Company's Board of Directors has an Audit Committee, Compensation Committee and Corporate Governance Committee. The Board of Directors has adopted written charters for each such committee, which are posted on the Company's website under Corporate Governance on the Our Company page and are available in print to any stockholder who requests a copy.

Item 1A. Risk Factors.

We are subject to extensive and often complex, overlapping and frequently changing rules, regulations and legal interpretations in the United States and abroad. Our investment management and related services business and our banking/finance business are subject to extensive and often complex, overlapping and frequently changing rules, regulations and legal interpretations in the United States and abroad, including, among others, securities, banking, accounting and tax laws and regulations. Moreover, financial reporting requirements, and the processes, controls and procedures that have been put in place to address them, are often comprehensive and complex. 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, either in the United States or abroad, or our inability to keep up with, or adapt to, an often ever changing, complex regulatory environment could result in 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 also adversely affect our reputation, prospects, revenues, and earnings.

We are subject to 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, FINRA and the NYSE, and to the extent operations or trading in our securities take place outside the United States, by non-U.S. regulations and

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regulators, such as the U.K. Listing Authority. Certain of our subsidiaries are registered with the SEC under the Investment Advisers Act of 1940, as amended, and many of our funds are registered with the SEC under the Investment Company Act of 1940, as amended, 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, both in the United States and abroad, must comply with a myriad of complex and often changing U.S. and/or non-U.S. rules and regulations, some of which may conflict, including complex U.S. and non-U.S. tax regimes. Additionally, as we expand our operations, sometimes rapidly, into 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, or FRB, and are subject to the restrictions, limitations, or prohibitions of the Bank Holding Company Act of 1956, as amended, and the Gramm-Leach-Bliley Act. 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, is subject to extensive regulation, supervision and examination by the Federal Deposit Insurance Corporation (the FDIC) and New York State Banking Department, while other subsidiaries are subject to oversight by the Office of Thrift Supervision 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 recently 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. Moreover, any inability to meet these requirements, within the timeframes set by regulators, may subject us to sanctions or other restrictions by the regulators that impact our broader business.

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 assets under management, 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 and the USA Patriot Act of 2001. Moreover, changes in the interpretation or enforcement of existing laws or regulations have directly affected our business. With new laws and changes in interpretation and enforcement 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. These outlays have also increased as we expand our business into various non-U.S. jurisdictions. For example, in the past few years following the enactment of the Sarbanes-Oxley Act of 2002, new rules of the SEC, NYSE and FINRA were promulgated and other rules revised. Among other things, these new requirements have necessitated us to make changes to our corporate governance and public disclosure policies, procedures and practices and our registered investment companies and investment advisers have been required to make similar changes. In addition, complex accounting and financial reporting requirements have been implemented in the past several years pursuant to the Sarbanes-Oxley Act of 2002 and the rules of the SEC and the Public Company Accounting Oversight Board, which apply across different legal entities within our corporate structure and varied geographical and/or jurisdictional areas in which we operate. Compliance activities to meet these new requirements have required us to expend additional time and resources, including without limitation substantial efforts to conduct evaluations

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required to ensure compliance with the management certification and attestation requirements under the Sarbanes-Oxley Act of 2002, 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 revenue and net 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.

Our ability to maintain the beneficial tax treatment we anticipate with respect to non-U.S. earnings we have repatriated is based on current interpretations of the American Jobs Creation Act of 2004 (the Jobs Act) and timely and permitted use of such amounts in accordance with our domestic reinvestment plan and the Jobs Act. In September 2006, we completed our planned repatriation into the United States of approximately \$2.1 billion of undistributed earnings of our non-U.S. subsidiaries in accordance with our domestic reinvestment plan and the Jobs Act. However, our ability to maintain the anticipated beneficial tax treatment with respect to these non-U.S. earnings is subject to current interpretations and compliance with the Jobs Act (including Internal Revenue Code Section 965), as well as the rules and regulations promulgated by, among others, the Internal Revenue Service and the United States Treasury Department. Moreover, changes in the interpretation of these rules and regulations may have an effect on our ability to maintain the beneficial tax treatment with respect to our repatriated non-U.S. earnings. Our inability to timely complete, to appropriately use repatriated amounts for permitted purposes or to otherwise satisfy the requirements of our planned repatriation could also have a negative impact on the scope and breadth of our anticipated tax treatment with respect to such amounts.

Any significant limitation or failure of our software applications and other technology 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 or systems failures 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. 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 revenue.

Further, although we take precautions to password protect 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, we have outsourced to a single vendor the operation of our U.S. data centers, which includes responsibility for processing data and managing the centers. This vendor is also responsible for the vast majority of our disaster recovery systems. A failure by this vendor to continue to manage our U.S. data centers and our disaster recovery systems adequately in the future could have a material adverse impact on our business. Moreover, 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

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is subject to rapid change and we cannot guarantee that our competitors may not implement more advanced Internet 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.

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 various ongoing challenges to ensure that we have sufficient resources, procedures and controls in place to address and ensure that our operations abroad operate consistently and effectively. 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 and hiring 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. In a tightening labor market, competition for qualified, motivated and highly skilled executives, professionals and other key personnel in the asset management and banking/finance industries remains significant. Our success depends to a substantial degree upon our ability to attract, retain and motivate qualified individuals, including through competitive compensation packages, and upon the continued contributions of these people. 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 revenue. We cannot assure you that we will be successful in attracting and retaining qualified individuals, and the

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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 net income. We compete with numerous asset management companies, mutual fund, stock brokerage and investment banking firms, insurance companies, banks, savings and loan associations 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. Over the past decade, a significant number of new asset management firms and mutual funds have been established, increasing competition. 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 customers, 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 net income could decline. Our ability to attract and retain assets under our management 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 distribution and sales channels on which we depend could reduce our revenues and hinder our growth. We derive nearly all of our fund sales through broker/dealers and other similar investment advisers. Increasing competition for these distribution channels and recent 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. Higher distribution costs lower our net revenues and earnings. Additionally, if one or more 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 revenues and earnings. 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 assets under management, related revenues and overall business and financial condition.

The amount or mix of our assets under management are subject to significant fluctuations and could negatively impact our revenues and income. We have become subject to an increased risk of asset volatility from changes in the domestic and global financial and equity markets. Individual financial and equity markets may be adversely affected by 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 or other business, social or political crises. Declines in these markets have caused in the past, and would cause in the future, a decline in our revenues and income. Global economic conditions, exacerbated by war or terrorism or financial crises, changes in the equity market place, currency exchange rates, interest rates, inflation rates, the yield curve and other factors that are difficult to predict affect the mix, market values and levels of our assets under management. Our investment management services

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revenues are derived primarily from fees based on a percentage of the value of assets under management 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 assets under management 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 revenue and income depending upon the nature of our assets under management 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 revenue 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 assets under management resulting from price declines, interest rate volatility or uncertainty or other factors could negatively impact our revenues and income.

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 earnings and income generated overseas. While we operate primarily in the United States, we also provide services and earn revenues in The Bahamas, Asia, Canada, Europe, Latin America, Africa and Australia. As a result, we are subject to foreign exchange risk through our non-U.S. operations. 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 United States. Stabilization or appreciation of the U.S. dollar could moderate revenues from sales of investment products internationally or could affect relative investment performance of certain funds invested in non-U.S. securities. Separately, management fees that we earn tend to be higher in connection with international assets under management than with U.S. assets under management. Consequently, a downturn in international markets could have a significant effect on our revenues and income. Moreover, as our business grows in non-U.S. markets, any business, social and 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 assets under management 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 assets under management, 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 assets under management 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 future performance may negatively impact our revenues and income.

We could suffer losses in earnings or revenue 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 con