FRANKLIN RESOURCES INC
Form 10-Q
July 30, 2014
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q

(MARK ONE)
x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended June 30, 2014
OR
o 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	13-2670991
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
One Franklin Parkway, San Mateo, CA	94403
(Address of principal executive offices)	(Zip Code)

(650) 312-2000
(Registrant's telephone number, including area code)
N/A
(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. x YES o NO
Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). x YES o NO
Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of "large accelerated filer", "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). o YES x NO
Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Outstanding: 625,291,113 shares of common stock, par value $0.10 per share, of Franklin Resources, Inc. as of July 23, 2014.

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PART I – FINANCIAL INFORMATION
Item 1. Financial Statements.
FRANKLIN RESOURCES, INC.
Condensed Consolidated Statements of Income
Unaudited

	Three Months Ended June 30,		Nine Months Ended June 30,	
(in millions, except per share data)	2014	2013	2014	2013
Operating Revenues				
Investment management fees	$1,393.2	$1,318.3	$4,135.0	$3,785.7
Sales and distribution fees	643.7	664.5	1,919.0	1,911.3
Shareholder servicing fees	69.0	77.5	212.8	228.5
Other, net	24.6	24.5	69.1	74.7
Total operating revenues	2,130.5	2,084.8	6,335.9	6,000.2
Operating Expenses				
Sales, distribution and marketing	789.3	812.8	2,332.3	2,324.5
Compensation and benefits	380.7	345.5	1,102.0	1,035.7
Information systems and technology	54.3	44.4	155.5	132.8
Occupancy	34.1	33.9	101.0	99.2
General, administrative and other	85.3	76.5	259.2	221.8
Total operating expenses	1,343.7	1,313.1	3,950.0	3,814.0
Operating Income	786.8	771.7	2,385.9	2,186.2
Other Income (Expenses)				
Investment and other income, net	107.6	10.3	172.8	152.3
Interest expense	(10.9)	(10.0)	(34.9)	(35.4)
Other income, net	96.7	0.3	137.9	116.9
Income before taxes	883.5	772.0	2,523.8	2,303.1
Taxes on income	251.4	209.9	742.9	642.9
Net income	632.1	562.1	1,780.9	1,660.2
Less: Net income attributable to				
Nonredeemable noncontrolling interests	47.4	8.0	23.0	13.1
Redeemable noncontrolling interests	5.8	1.8	14.2	5.9
Net Income Attributable to Franklin Resources, Inc.	$578.9	$552.3	$1,743.7	$1,641.2
Earnings per Share				
Basic	$0.92	$0.87	$2.77	$2.57
Diluted	0.92	0.86	2.77	2.57
Dividends per Share	$0.120	$0.097	$0.36	$1.29

See Notes to Condensed Consolidated Financial Statements.

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FRANKLIN RESOURCES, INC.
Condensed Consolidated Statements of Comprehensive Income
Unaudited

(in millions)	Three Months Ended June 30, 2014	Three Months Ended June 30, 2013	Nine Months Ended June 30, 2014	Nine Months Ended June 30, 2013
Net Income	$632.1	$562.1	$1,780.9	$1,660.2
Other Comprehensive Income (Loss)				
Net unrealized gains (losses) on investments, net of tax	2.5	(9.0)	(6.0)	(28.0)
Currency translation adjustments, net of tax	17.2	(47.7)	25.2	(82.7)
Net unrealized gains (losses) on defined benefit plans, net of tax	0.1	(0.4)	(1.1)	0.3
Total comprehensive income	651.9	505.0	1,799.0	1,549.8
Less: Comprehensive income attributable to				
Nonredeemable noncontrolling interests	47.4	8.0	23.0	13.1
Redeemable noncontrolling interests	5.8	1.8	14.2	5.9
Comprehensive Income Attributable to Franklin Resources, Inc.	$598.7	$495.2	$1,761.8	$1,530.8

See Notes to Condensed Consolidated Financial Statements.

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FRANKLIN RESOURCES, INC.
Condensed Consolidated Balance Sheets
Unaudited

(in millions)	June 30, 2014	September 30, 2013
Assets		
Cash and cash equivalents	$7,604.2	$6,186.0
Receivables	999.1	1,038.9
Investments (including $1,833.9 and $1,892.7 at fair value at June 30, 2014 and September 30, 2013)	2,615.4	2,439.2
Loans receivable, net	3.7	229.7
Assets of consolidated variable interest entities		
Cash and cash equivalents	58.0	44.0
Investments, at fair value	819.4	941.1
Assets of consolidated sponsored investment products		
Cash and cash equivalents	35.4	93.1
Investments, at fair value	1,367.3	1,203.2
Deferred taxes	129.2	112.4
Property and equipment, net	542.1	564.1
Goodwill and other intangible assets, net	2,348.8	2,359.2
Other	169.3	179.4
Total Assets	$16,691.9	$15,390.3
Liabilities		
Compensation and benefits	$435.8	$444.5
Accounts payable and accrued expenses	302.6	273.7
Commissions	458.0	437.7
Deposits	664.2	586.8
Debt	1,198.1	1,197.7
Debt of consolidated variable interest entities, at fair value	853.2	988.5
Debt of consolidated sponsored investment products	138.9	108.9
Deferred taxes	265.0	272.5
Other	271.5	272.7
Total liabilities	4,587.3	4,583.0
Commitments and Contingencies (Note 9)		
Redeemable Noncontrolling Interests	183.7	121.8

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See Notes to Condensed Consolidated Financial Statements.

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FRANKLIN RESOURCES, INC.
Condensed Consolidated Balance Sheets
Unaudited
[Table continued from previous page]

(in millions, except share and per share data)	June 30, 2014	September 30, 2013
Stockholders' Equity		
Preferred stock, $1.00 par value, 1,000,000 shares authorized; none issued	$—	$—
Common stock, $0.10 par value, 1,000,000,000 shares authorized; 625,454,242 and 630,917,532 shares issued and outstanding at June 30, 2014 and September 30, 2013	62.5	63.1
Retained earnings	11,191.5	9,991.2
Appropriated retained earnings of consolidated variable interest entities	17.1	12.7
Accumulated other comprehensive income	24.2	6.1
Total Franklin Resources, Inc. stockholders' equity	11,295.3	10,073.1
Nonredeemable noncontrolling interests	625.6	612.4
Total stockholders' equity	11,920.9	10,685.5
Total Liabilities, Redeemable Noncontrolling Interests and Stockholders' Equity	$16,691.9	$15,390.3

See Notes to Condensed Consolidated Financial Statements.

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

(in millions)	Nine Months Ended June 30, 2014	2013
Net Income	$1,780.9	$1,660.2
Adjustments to reconcile net income to net cash provided by operating activities:		
Amortization of deferred sales commissions	97.2	102.8
Depreciation and other amortization	72.9	70.5
Stock-based compensation	96.9	86.2
Excess tax benefit from stock-based compensation	(8.1)	(16.0)
Gains on sale of assets	(40.0)	(36.8)
Income from investments in equity method investees	(68.2)	(54.3)
Net gains on other investments of consolidated sponsored investment products	(18.2)	(59.7)
Net (gains) losses of consolidated variable interest entities	(8.1)	30.3
Other	(14.4)	15.6
Changes in operating assets and liabilities:		
Increase in receivables, prepaid expenses and other	(133.7)	(188.2)
Increase in trading securities, net	(77.6)	(70.0)
Increase in trading securities of consolidated sponsored investment products, net	(448.9)	(101.9)
Originations of loans held for sale	(38.3)	—
Proceeds from sale of loans originated for resale	38.4	—
Decrease in accrued compensation and benefits	(11.6)	(8.1)
Increase in commissions payable	20.3	50.8
Increase in income taxes payable	3.4	26.7
Increase in other liabilities	168.0	19.5
Net cash provided by operating activities	1,410.9	1,527.6
Purchase of investments	(205.4)	(222.2)
Liquidation of investments	410.4	444.5
Purchase of investments by consolidated sponsored investment products	(261.2)	(177.7)
Liquidation of investments by consolidated sponsored investment products	125.1	129.1
Purchase of investments by consolidated variable interest entities	(162.1)	(488.9)
Liquidation of investments by consolidated variable interest entities	340.2	519.0
Decrease in loans receivable, net	36.8	7.5
Decrease in loans transferred to held for sale	8.2	—
Proceeds from sale of loans transferred to held for sale	181.3	—
Additions of property and equipment, net	(38.2)	(41.6)
Acquisitions of subsidiaries, net of cash acquired	—	3.9
Increase (decrease) in cash from net consolidation (deconsolidation) of sponsored investment products	(150.8)	4.0
Net cash provided by investing activities	284.3	177.6
Increase in deposits	76.3	42.5
Issuance of common stock	20.4	28.8
Dividends paid on common stock	(215.3)	(821.1)
Repurchase of common stock	(444.4)	(226.4)
Excess tax benefit from stock-based compensation	8.1	16.0
Payments on debt	—	(490.9)

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See Notes to Condensed Consolidated Financial Statements.

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FRANKLIN RESOURCES, INC.
Condensed Consolidated Statements of Cash Flows
Unaudited
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	Nine Months Ended June 30,	
(in millions)	2014	2013
Proceeds from issuance of debt by consolidated sponsored investment products	$601.6	$404.8
Payments on debt by consolidated sponsored investment products	(571.9)	(423.1)
Payments on debt by consolidated variable interest entities	(160.6)	(143.3)
Payments on contingent consideration liability	(4.8)	—
Noncontrolling interests	358.3	104.9
Net cash used in financing activities	(332.3)	(1,507.8)
Effect of exchange rate changes on cash and cash equivalents	11.6	(16.7)
Increase in cash and cash equivalents	1,374.5	180.7
Cash and cash equivalents, beginning of period	6,323.1	6,051.4
Cash and Cash Equivalents, End of Period	$7,697.6	$6,232.1
Supplemental Disclosure of Non-Cash Activities		
Contingent consideration liabilities recognized due to acquisitions	$—	$92.0
Increase in noncontrolling interests due to acquisition	—	38.2
Supplemental Disclosure of Cash Flow Information		
Cash paid for income taxes	$767.3	$622.7
Cash paid for interest	33.1	40.1
Cash paid for interest by consolidated sponsored investment products and consolidated variable interest entities	34.3	42.0

See Notes to Condensed Consolidated Financial Statements.

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FRANKLIN RESOURCES, INC.
Notes to Condensed Consolidated Financial Statements
June 30, 2014
(Unaudited)

Note 1 – Basis of Presentation

The unaudited interim financial statements of Franklin Resources, Inc. (“Franklin”) and its consolidated subsidiaries (collectively, the “Company”) included herein have been prepared by the Company in accordance with the instructions to Form 10-Q and the rules and regulations of the U.S. Securities and Exchange Commission (the “SEC”). Under these rules and regulations, some information and footnote disclosures normally included in financial statements prepared under accounting principles generally accepted in the United States of America (“U.S. GAAP”) have been shortened or omitted. Management believes that all adjustments necessary for a fair statement of the financial position and the results of operations for the periods shown have been made. All adjustments are normal and recurring. These financial statements should be read together with the Company’s audited financial statements included in its Form 10-K for the fiscal year ended September 30, 2013 (“fiscal year 2013”). Certain amounts for the comparative prior fiscal year period have been reclassified to conform to the financial statement presentation as of and for the period ended June 30, 2014.

Note 2 – New Accounting Guidance

Recently Adopted Accounting Guidance

On October 1, 2013, the Company adopted new Financial Accounting Standards Board (“FASB”) guidance that requires an entity to report significant reclassifications out of accumulated other comprehensive income by component either on the face of the financial statements or in the notes. See Note 12 – Accumulated Other Comprehensive Income for the expanded disclosures.

New Accounting Guidance Not Yet Adopted

In May 2014, the FASB issued new guidance that requires use of a single principles-based model for recognition of revenue from contracts with customers. The core principle of the model is that revenue is recognized upon the transfer of promised goods or services to customers in an amount that reflects the expected consideration to be received for the goods or services. The guidance allows for either a full retrospective or modified approach at adoption, and is effective for the Company in the first quarter of the fiscal year ending September 30, 2018. The Company is currently evaluating the impact that the adoption of the guidance will have on its consolidated financial statements.

Note 3 – Stockholders’ Equity and Redeemable Noncontrolling Interests

The changes in total stockholders’ equity and redeemable noncontrolling interests were as follows:

(in millions) for the nine months ended June 30, 2014	Franklin Resources, Inc. Stockholders’ Equity	Nonredeemable Noncontrolling Interests	Total Stockholders’ Equity	Redeemable Noncontrolling Interests
Balance at October 1, 2013	$10,073.1	$ 612.4	$10,685.5	$ 121.8
Net income	1,743.7	23.0	1,766.7	14.2
Net income reclassified to appropriated retained earnings	4.4	(4.4)	—	
Other comprehensive income	18.1		18.1	
Cash dividends on common stock	(226.7)		(226.7)	
Repurchase of common stock	(444.4)		(444.4)	
Noncontrolling interests				
Net subscriptions (redemptions/distributions)		(5.4)	(5.4)	363.7
Net deconsolidation of sponsored investment products		—	—	(316.0)
Other[1]	127.1		127.1	
Balance at June 30, 2014	$11,295.3	$ 625.6	$11,920.9	$ 183.7

[1] Primarily relates to stock-based compensation plans.

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(in millions) for the nine months ended June 30, 2013	Franklin Resources, Inc. Stockholders' Equity	Nonredeemable Noncontrolling Interests	Total Stockholders' Equity	Redeemable Noncontrolling Interests
Balance at October 1, 2012	$9,201.3	$ 559.2	$9,760.5	$ 26.7
Net income	1,641.2	13.1	1,654.3	5.9
Net loss reclassified to appropriated retained earnings	(32.3)	32.3	—	
Other comprehensive loss	(110.4)		(110.4)	
Cash dividends on common stock	(825.5)		(825.5)	
Repurchase of common stock	(226.4)		(226.4)	
Noncontrolling interests				
Net subscriptions		65.1	65.1	39.8
Net consolidation (deconsolidation) of sponsored investment products		4.4	4.4	(41.4)
Acquisition		5.4	5.4	32.8
Reclassification		(57.0)	(57.0)	57.0
Other[1]	131.9		131.9	
Balance at June 30, 2013	$9,779.8	$ 622.5	$10,402.3	$ 120.8

[1] Primarily relates to stock-based compensation plans.

The reclassification of $57.0 million of noncontrolling interests from nonredeemable to redeemable during the nine months ended June 30, 2013 relates to a consolidated sponsored investment product ("SIP") which is redeemable on a monthly basis without restriction.

During the three and nine months ended June 30, 2014, the Company repurchased 2.4 million and 8.3 million shares of its common stock at a cost of $128.5 million and $444.4 million under its stock repurchase program. In December 2013, the Company's Board of Directors authorized the repurchase of up to 30.0 million additional shares of its common stock under the stock repurchase program. At June 30, 2014, 33.0 million shares remained available for repurchase under the program, which is not subject to an expiration date. During the three and nine months ended June 30, 2013, the Company repurchased 2.2 million and 4.9 million shares of its common stock at a cost of $105.1 million and $226.4 million.

Note 4 – Earnings per Share

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

(in millions, except per share data)	Three Months Ended June 30, 2014	2013	Nine Months Ended June 30, 2014	2013
Net Income Attributable to Franklin Resources, Inc.	$578.9	$552.3	$1,743.7	$1,641.2
Less: Allocation of earnings to participating nonvested stock and stock unit awards	3.9	4.0	11.2	11.2
Net Income Available to Common Stockholders	$575.0	$548.3	$1,732.5	$1,630.0
Weighted-average shares outstanding – basic	623.2	633.6	625.8	634.0
Effect of dilutive common stock options and non-participating nonvested stock unit awards	0.4	0.7	0.5	0.9
Weighted-Average Shares Outstanding – Diluted	623.6	634.3	626.3	634.9
Earnings per Share				
Basic	$0.92	$0.87	$2.77	$2.57
Diluted	0.92	0.86	2.77	2.57

Non-participating nonvested stock unit awards excluded from the calculation of diluted earnings per share because their effect would have been anti-dilutive were 0.1 million for the three and nine months ended June 30, 2014, and nil for the three and nine months ended June 30, 2013.

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Note 5 – Investments

The disclosures below include details of the Company's investments, excluding those of consolidated variable interest entities ("VIEs") and consolidated SIPs. See Note 8 – Variable Interest Entities and Consolidated Sponsored Investment Products for information related to the investments held by these entities.

Investments consisted of the following:

(in millions)	June 30, 2014	September 30, 2013
Investment securities, trading	$1,277.4	$1,196.7
Investment securities, available-for-sale		
SIPs	504.9	534.6
Securities of U.S. states and political subdivisions	11.5	23.1
Securities of the U.S. Treasury and federal agencies	0.7	2.3
Mortgage-backed securities – agency residential[1]	18.8	110.9
Other equity securities	6.8	11.3
Total investment securities, available-for-sale	542.7	682.2
Investments in equity method investees	700.5	485.4
Other investments	94.8	74.9
Total	$2,615.4	$2,439.2

[1] Consist of U.S. government-sponsored enterprise obligations.

At June 30, 2014 and September 30, 2013, investment securities with aggregate carrying amounts of $14.7 million and $28.4 million were pledged as collateral for amounts available in secured Federal Home Loan Bank ("FHLB") short-term borrowing capacity, $6.3 million and $7.1 million were pledged as collateral for the ability to borrow from uncommitted short-term bank lines of credit, and nil and $82.5 million were pledged as collateral for the ability to borrow from the Federal Reserve Bank (see Note 7 - Debt).

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

(in millions)		Gross Unrealized		
as of June 30, 2014	Cost Basis	Gains	Losses	Fair Value
SIPs	$435.5	$70.7	$(1.3)	$504.9
Securities of U.S. states and political subdivisions	11.1	0.4	—	11.5
Securities of the U.S. Treasury and federal agencies	0.7	—	—	0.7
Mortgage-backed securities – agency residential	18.9	—	(0.1)	18.8
Other equity securities	6.6	0.2	—	6.8
Total	$472.8	$71.3	$(1.4)	$542.7

(in millions)		Gross Unrealized		
as of September 30, 2013	Cost Basis	Gains	Losses	Fair Value
SIPs	$465.4	$71.7	$(2.5)	$534.6
Securities of U.S. states and political subdivisions	22.3	0.8	—	23.1
Securities of the U.S. Treasury and federal agencies	2.3	—	—	2.3
Mortgage-backed securities – agency residential	108.9	2.0	—	110.9
Other equity securities	10.9	0.4	—	11.3
Total	$609.8	$74.9	$(2.5)	$682.2

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The following tables show the gross unrealized losses and fair values of available-for-sale securities with unrealized losses aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position:

(in millions) as of June 30, 2014	Less Than 12 Months Fair Value	Less Than 12 Months Gross Unrealized Losses	12 Months or Greater Fair Value	12 Months or Greater Gross Unrealized Losses	Total Fair Value	Total Gross Unrealized Losses
SIPs	$6.8	$(0.1)	$7.4	$(1.2)	$14.2	$(1.3)
Mortgage-backed securities – agency residential	16.4	(0.1)	—	—	16.4	(0.1)
Total	$23.2	$(0.2)	$7.4	$(1.2)	$30.6	$(1.4)

(in millions) as of September 30, 2013	Less Than 12 Months Fair Value	Less Than 12 Months Gross Unrealized Losses	12 Months or Greater Fair Value	12 Months or Greater Gross Unrealized Losses	Total Fair Value	Total Gross Unrealized Losses
SIPs	$50.3	$(2.4)	$1.4	$(0.1)	$51.7	$(2.5)

The Company did not recognize any other-than-temporary impairment of investments during the three months ended June 30, 2014. During the nine months ended June 30, 2014, the Company recognized $0.6 million of other-than-temporary impairment, of which $0.4 million related to available-for-sale SIPs. The Company recognized $0.8 million and $1.8 million of other-than-temporary impairment during the three and nine months ended June 30, 2013, all of which related to available-for-sale SIPs except for $0.7 million during the nine-month period related to other investments.

At June 30, 2014, contractual maturities of available-for-sale debt securities were as follows:

(in millions)	Cost Basis	Fair Value
Due in one year or less	$4.0	$4.0
Due after one year through five years	7.8	8.2
Total	$11.8	$12.2

Mortgage-backed securities are not included in the table above as their actual maturities may differ from contractual maturities because issuers may have the right to call or prepay obligations.

Note 6 – Fair Value Measurements

The disclosures below include details of the Company’s fair value measurements, excluding those of consolidated VIEs and consolidated SIPs. See Note 8 – Variable Interest Entities and Consolidated Sponsored Investment Products for information related to fair value measurements of the assets and liabilities of these entities.

The Company uses a three-level fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value based on whether the inputs to those valuation techniques are observable or unobservable. The three levels of fair value hierarchy are set forth below. The Company’s assessment of the hierarchy level of the assets and liabilities measured at fair value is determined based on the lowest level input that is significant to the fair value measurement in its entirety.

Level 1 Unadjusted quoted prices in active markets for identical assets or liabilities.

Level 2 Observable inputs other than Level 1 quoted prices, such as non-binding quoted prices for similar assets or liabilities in active markets; quoted prices for identical or similar assets or liabilities in markets that are not active; or inputs other than quoted prices that are observable or corroborated by observable market data. Level 2 quoted prices are generally obtained from two independent third-party brokers or dealers, including prices derived from model-based valuation techniques for which the significant assumptions are observable in the market or corroborated by observable market data. Quoted prices are validated through price variance analysis, subsequent sales testing, stale price

	review, price comparison across pricing vendors and due diligence reviews of third-party vendors.
Level 3	Unobservable inputs that are supported by little or no market activity. These inputs require significant management judgment and reflect the Company's estimation of assumptions that market participants would use in pricing the asset or liability.

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Assets and liabilities measured at fair value on a recurring basis were as follows:

(in millions) as of June 30, 2014	Level 1	Level 2	Level 3	Total
Assets				
Investment securities, trading	$1,195.4	$82.0	$—	$1,277.4
Investment securities, available-for-sale				
SIPs	504.9	—	—	504.9
Securities of U.S. states and political subdivisions	—	11.5	—	11.5
Securities of the U.S. Treasury and federal agencies	—	0.7	—	0.7
Mortgage-backed securities – agency residential	—	18.8	—	18.8
Other equity securities	2.0	4.8	—	6.8
Life settlement contracts	—	—	13.8	13.8
Total Assets Measured at Fair Value	$1,702.3	$117.8	$13.8	$1,833.9
Liabilities				
Contingent consideration liabilities	$—	$—	$98.8	$98.8

(in millions) as of September 30, 2013	Level 1	Level 2	Level 3	Total
Assets				
Investment securities, trading	$1,121.5	$75.2	$—	$1,196.7
Investment securities, available-for-sale				
SIPs	534.6	—	—	534.6
Securities of U.S. states and political subdivisions	—	23.1	—	23.1
Securities of the U.S. Treasury and federal agencies	—	2.3	—	2.3
Mortgage-backed securities – agency residential	—	110.9	—	110.9
Other equity securities	11.3	—	—	11.3
Life settlement contracts	—	—	13.8	13.8
Total Assets Measured at Fair Value	$1,667.4	$211.5	$13.8	$1,892.7
Liabilities				
Contingent consideration liabilities	$—	$—	$97.7	$97.7

The fair values of substantially all trading investments, all available-for-sale SIPs and certain other equity securities are determined based on their published net asset values. The fair values of certain trading investments, all available-for-sale debt securities and certain other equity securities are determined using quoted market prices, if available, or independent third-party broker or dealer price quotes, which are evaluated for reasonableness. The fair value of life settlement contracts is determined using a discounted cash flow valuation technique.

The fair value of contingent consideration liabilities is determined using an income-based method which considers the net present value of anticipated future cash flows. Substantially all of the balance relates to the Company’s commitment to acquire the remaining interests in K2 Advisors Holdings, LLC. There were no transfers between Level 1 and Level 2, or into or out of Level 3, during the three and nine months ended June 30, 2014 and 2013.

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The changes in Level 3 assets and liabilities measured at fair value on a recurring basis were as follows:

(in millions) for the three months ended June 30,	2014 Investments	2014 Contingent Consideration Liabilities	2013 Investments	2013 Contingent Consideration Liabilities
Balance at beginning of period	$13.6	$(104.2)	$13.4	$(90.0)
Acquisition	—	—	—	(1.4)
Total realized and unrealized gains (losses)				
Included in investment and other income, net	0.7	—	0.7	—
Included in general, administrative and other expense	—	3.3	—	(5.1)
Other	—	0.1	—	(0.3)
Purchases	—	—	0.4	—
Settlements	(0.5)	2.0	(0.8)	—
Balance at End of Period	$13.8	$(98.8)	$13.7	$(96.8)
Change in unrealized gains (losses) included in net income relating to assets and liabilities held at end of period	$0.3	$3.4	$0.3	$(5.4)

(in millions) for the nine months ended June 30,	2014 Investments	2014 Contingent Consideration Liabilities	2013 Investments	2013 Contingent Consideration Liabilities
Balance at beginning of period	$13.8	$(97.7)	$14.8	$—
Acquisitions	—	—	—	(92.0)
Total realized and unrealized gains (losses)				
Included in investment and other income, net	2.4	—	1.6	—
Included in general, administrative and other expense	—	(5.6)	—	(7.3)
Other	—	(0.3)	—	(0.5)
Purchases	0.1	—	1.1	—
Sales	(0.7)	—	(1.6)	—
Settlements	(1.8)	4.8	(2.2)	3.0
Balance at End of Period	$13.8	$(98.8)	$13.7	$(96.8)
Change in unrealized gains (losses) included in net income relating to assets and liabilities held at end of period	$0.9	$(5.9)	$1.0	$(7.8)

The valuation techniques and significant unobservable inputs used in recurring Level 3 fair value measurements were as follows:

(in millions)

as of June 30, 2014	Fair Value	Valuation Technique	Significant Unobservable Inputs	Range (Weighted Average)
Life settlement contracts	$13.8	Discounted cash flow	Life expectancy Discount rate	24–153 months (73) 3.3%–21.7% (11.7%)
Contingent consideration liabilities	98.8	Discounted cash flow	AUM growth rate EBITDA margin Discount rate	5.4%–23.0% (12.0%) 23.7% - 34.4% (30.5%) 14.0%

(in millions)

as of September 30, 2013	Fair Value	Valuation Technique	Significant Unobservable Inputs	Range (Weighted Average)
Life settlement contracts	$13.8	Discounted cash flow	Life expectancy Discount rate	25–160 months (76) 3.3%–21.7% (11.7%)

Contingent consideration liabilities	97.7	Discounted cash flow	AUM growth rate EBITDA margin Discount rate	6.0%–25.0% (14.6%) 26.4% - 38.9% (34.4%) 14.0%

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For life settlement contracts, a significant increase (decrease) in the life expectancy or the discount rate in isolation would result in a significantly lower (higher) fair value measurement.

For contingent consideration liabilities, a significant increase (decrease) in the AUM growth rate or EBITDA margin, or decrease (increase) in the discount rate, in isolation would result in a significantly higher (lower) fair value measurement.

Financial instruments that were not measured at fair value were as follows:

(in millions)	Fair Value Level	June 30, 2014 Carrying Value	June 30, 2014 Estimated Fair Value	September 30, 2013 Carrying Value	September 30, 2013 Estimated Fair Value
Financial Assets					
Cash and cash equivalents	1	$7,604.2	$7,604.2	$6,186.0	$6,186.0
Other investments[1]	2 or 3	81.0	92.4	61.1	69.2
Loans receivable, net	2	3.7	3.9	229.7	230.1
Financial Liabilities					
Deposits	2	$664.2	$664.2	$586.8	$587.2
Debt	2	1,198.1	1,244.4	1,197.7	1,221.5

[1] Primarily consist of Level 3 assets.

Note 7 – Debt

The disclosures below include details of the Company's debt, excluding that of consolidated VIEs and consolidated SIPs. See Note 8 – Variable Interest Entities and Consolidated Sponsored Investment Products for information related to the debt of these entities.

Debt consisted of the following:

(in millions)	June 30, 2014	September 30, 2013	Effective Interest Rate
$250 million 3.125% notes due May 2015	$250.0	$249.9	3.32 %
$300 million 1.375% notes due September 2017	298.9	298.7	1.66 %
$350 million 4.625% notes due May 2020	349.8	349.7	4.74 %
$300 million 2.800% notes due September 2022	299.4	299.4	2.93 %
Total Debt	$1,198.1	$1,197.7	

At June 30, 2014, the Company's outstanding senior unsecured and unsubordinated notes had an aggregate face value of $1.2 billion. The notes have fixed interest rates with interest payable semi-annually and contain an optional redemption feature that allows the Company to redeem each series of notes prior to maturity in whole or in part at any time, at a make-whole redemption price. The indentures governing the notes contain limitations on the Company's ability and the ability of its subsidiaries to pledge voting stock or profit participating equity interests in its subsidiaries to secure other debt without similarly securing the notes equally and ratably. The indentures also include requirements that must be met if the Company consolidates or merges with, or sells all or substantially all of its assets to, another entity. At June 30, 2014, the Company was in compliance with the covenants of the notes.

At June 30, 2014, maturities for debt were as follows:

(in millions) for the fiscal years ending September 30,	Amount
2014	$—
2015	250.0
2016	—
2017	298.9
2018	—
Thereafter	649.2
Total	$1,198.1

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At June 30, 2014, the Company had $500.0 million of short-term commercial paper available for issuance under an uncommitted private placement program which has been inactive since April 2012, $260.0 million available in uncommitted short-term bank lines of credit under the Federal Reserve System, $14.1 million available in an uncommitted short-term bank line of credit and $14.0 million available in secured FHLB short-term borrowing capacity. On July 11, 2014, the Company closed its account at the Federal Reserve Bank of New York resulting in the termination of its bank lines of credit under the Federal Reserve System and its ability to borrow through the secured Federal Reserve Bank short-term discount window.

Note 8 – Variable Interest Entities and Consolidated Sponsored Investment Products

The Company sponsors and manages various types of investment products, which consist of both VIEs and non-VIEs. The Company consolidates the VIE products for which it is the primary beneficiary and the non-VIE products which it controls. The Company has no right to the consolidated products' assets, other than its direct equity investment in them, and/or investment management fees earned from them. The debt holders of these consolidated entities have no recourse to the Company's assets beyond the level of its direct investment, therefore the Company bears no other risks associated with the entities' liabilities.

The balances of consolidated VIEs and consolidated SIPs included in the Company's condensed consolidated balance sheets were as follows:

	June 30, 2014			September 30, 2013		
	Consolidated			Consolidated		
(in millions)	VIEs	SIPs	Total	VIEs	SIPs	Total
Assets						
Cash and cash equivalents	$58.0	$35.4	$93.4	$44.0	$93.1	$137.1
Receivables	21.5	19.1	40.6	37.7	19.1	56.8
Investments, at fair value	819.4	1,367.3	2,186.7	941.1	1,203.2	2,144.3
Other assets	—	0.7	0.7	—	0.7	0.7
Total Assets	$898.9	$1,422.5	$2,321.4	$1,022.8	$1,316.1	$2,338.9
Liabilities						
Accounts payable and accrued expenses	$21.2	$25.4	$46.6	$10.9	$25.2	$36.1
Debt, at fair value	853.2	—	853.2	988.5	—	988.5
Debt	—	138.9	138.9	—	108.9	108.9
Other liabilities	—	11.3	11.3	—	8.5	8.5
Total liabilities	874.4	175.6	1,050.0	999.4	142.6	1,142.0
Redeemable Noncontrolling Interests	—	183.7	183.7	—	121.8	121.8
Stockholders' Equity						
Franklin Resources, Inc.'s interests	24.5	454.1	478.6	23.4	454.8	478.2
Nonredeemable noncontrolling interests	—	609.1	609.1	—	596.9	596.9
Total stockholders' equity	24.5	1,063.2	1,087.7	23.4	1,051.7	1,075.1
Total Liabilities, Redeemable Noncontrolling Interests and Stockholders' Equity	$898.9	$1,422.5	$2,321.4	$1,022.8	$1,316.1	$2,338.9

The consolidated VIEs and consolidated SIPs did not have a significant impact on net income attributable to the Company during the three and nine months ended June 30, 2014 and 2013.

Consolidated VIEs

Consolidated VIEs consist of sponsored collateralized loan obligations ("CLOs"), which are asset-backed financing entities collateralized by a pool of corporate debt securities.

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The assets and liabilities of the CLOs are carried at fair value. Changes in the fair values were as follows:

(in millions)	Three Months Ended June 30, 2014	Three Months Ended June 30, 2013	Nine Months Ended June 30, 2014	Nine Months Ended June 30, 2013
Net gains from changes in fair value of assets	$7.1	$17.2	$31.5	$58.3
Net losses from changes in fair value of liabilities	(7.6)	(18.1)	(24.1)	(86.0)
Total Net Gains (Losses)	$(0.5)	$(0.9)	$7.4	$(27.7)

The following tables present information on the investments and debt of the CLOs:

(in millions) as of June 30, 2014	Total Investments	Debt
Unpaid principal balance	$ 816.3	$887.7
Difference between unpaid principal balance and fair value	3.1	(34.5)
Fair Value	$ 819.4	$853.2

There were no investments 90 days or more past due at June 30, 2014.

(in millions) as of September 30, 2013	Total Investments	Investments 90 Days or More Past Due	Debt
Unpaid principal balance	$ 943.6	$7.9	$1,017.8
Difference between unpaid principal balance and fair value	(2.5)	(7.7)	(29.3)
Fair Value	$ 941.1	$0.2	$988.5

Consolidated SIPs

Consolidated SIPs consist of non-VIE limited partnerships and similar structures that the Company controls and other fund products in which the Company has a controlling financial interest. The Company consolidated 29 SIPs as of June 30, 2014, and 36 SIPs as of September 30, 2013. SIPs are typically consolidated when the Company makes an initial investment in a newly launched fund or limited partnership entity. They are deconsolidated when the Company redeems its investment in the SIP or its voting interests decrease to a minority percentage. The Company's investments in SIPs subsequent to deconsolidation are accounted for as trading or available-for-sale investment securities, or equity method or cost method investments depending on the nature of the SIP and the Company's level of ownership.

Investments

Investments of consolidated VIEs and consolidated SIPs consisted of the following:

(in millions)	June 30, 2014 Consolidated VIEs	June 30, 2014 Consolidated SIPs	June 30, 2014 Total	September 30, 2013 Consolidated VIEs	September 30, 2013 Consolidated SIPs	September 30, 2013 Total
Investment securities, trading	$—	$241.0	$241.0	$—	$244.1	$244.1
Other debt securities	819.4	219.3	1,038.7	941.1	272.3	1,213.4
Other equity securities	—	907.0	907.0	—	686.8	686.8
Total Investments	$819.4	$1,367.3	$2,186.7	$941.1	$1,203.2	$2,144.3

Investments of consolidated VIEs consist of corporate debt securities. Investment securities, trading held by consolidated SIPs consist of debt and equity securities that are traded in active markets. Other debt and equity securities held by consolidated SIPs primarily consist of direct investments in secured and unsecured debt securities and equity securities of entities in emerging markets, which are generally not traded in active markets. Other equity securities also include investments in funds that are not traded in active markets.

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Debt

Debt of consolidated VIEs and consolidated SIPs consisted of the following:

(in millions)	June 30, 2014	Effective Interest Rate		September 30, 2013	Effective Interest Rate	
Debt of consolidated VIEs, at fair value, due fiscal years 2018-2024	$853.2	1.40	%	$ 988.5	1.32	%
Debt of consolidated SIPs due fiscal years 2014-2019	138.9	3.70	%	108.9	4.08	%
Total Debt	$992.1			$ 1,097.4		

The debt of consolidated VIEs had floating interest rates ranging from 0.45% to 9.73% at June 30, 2014, and from 0.50% to 9.77% at September 30, 2013.

The debt of consolidated SIPs had both fixed and floating interest rates ranging from 2.19% to 5.89% at June 30, 2014, and from 2.45% to 5.83% at September 30, 2013. The repayment of amounts outstanding under the debt agreements is secured by the assets of the consolidated SIPs or a pledge of the right to call capital.

At June 30, 2014, contractual maturities for debt of consolidated VIEs and consolidated SIPs were as follows:

(in millions) for the fiscal years ending September 30,	
2014	$65.6
2015	—
2016	—
2017	28.1
2018	276.4
Thereafter	622.0
Total	$992.1

Fair Value Measurements

The tables below present the balances of assets and liabilities of consolidated VIEs and consolidated SIPs measured at fair value on a recurring basis. See Note 6 – Fair Value Measurements for information related to the three levels of fair value hierarchy.

(in millions) as of June 30, 2014	Level 1	Level 2	Level 3	Total
Assets				
Cash and cash equivalents of consolidated VIEs	$58.0	$—	$—	$58.0
Receivables of consolidated VIEs	—	21.5	—	21.5
Investments of consolidated VIEs	—	818.9	0.5	819.4
Investments of consolidated SIPs				
Debt securities	0.9	96.8	219.9	317.6
Equity securities	144.1	276.7	628.9	1,049.7
Total Assets Measured at Fair Value	$203.0	$1,213.9	$849.3	$2,266.2
Liabilities				
Accounts payable and accrued expenses of consolidated VIEs	$—	$21.2	$—	$21.2
Debt of consolidated VIEs	—	805.2	48.0	853.2
Other liabilities of consolidated SIPs	3.7	—	—	3.7
Total Liabilities Measured at Fair Value	$3.7	$826.4	$48.0	$878.1

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(in millions) as of September 30, 2013	Level 1	Level 2	Level 3	Total
Assets				
Cash and cash equivalents of consolidated VIEs	$44.0	$—	$—	$44.0
Receivables of consolidated VIEs	—	37.7	—	37.7
Investments of consolidated VIEs	—	940.6	0.5	941.1
Investments of consolidated SIPs				
Debt securities	4.5	83.8	272.3	360.6
Equity securities	158.1	213.6	470.9	842.6
Total Assets Measured at Fair Value	$206.6	$1,275.7	$743.7	$2,226.0
Liabilities				
Accounts payable and accrued expenses of consolidated VIEs	$—	$10.9	$—	$10.9
Debt of consolidated VIEs	—	928.8	59.7	988.5
Total Liabilities Measured at Fair Value	$—	$939.7	$59.7	$999.4

The fair value of cash and cash equivalents of consolidated VIEs is based on quoted market prices. The fair values of the other assets and liabilities of consolidated VIEs are primarily obtained from independent third-party broker or dealer price quotes. The fair value of a portion of the debt of consolidated VIEs is determined using significant unobservable inputs in a market-based approach.

Investments of consolidated SIPs consist of trading securities and other investments that are not generally traded in active markets. The fair value of the trading securities is determined using quoted market prices, or independent third-party broker or dealer price quotes if quoted market prices are not available. The fair value of debt and equity securities not traded in active markets, other than fund products, is determined using significant unobservable inputs in either a market-based or income-based approach. The fair value of fund products not traded in active markets is determined using net asset value (“NAV”) as a practical expedient.

Other liabilities of consolidated SIPs consist of short positions in debt and equity securities. The fair value of the liabilities is determined based on the fair value of the underlying securities using quoted market prices, or independent third-party broker or dealer price quotes if quoted market prices securities are not available.

The investments in fund products for which fair value was estimated using NAV as a practical expedient consisted of the following:

(in millions)	Redemption Frequency	Fair Value Level	June 30, 2014	September 30, 2013
Global fixed-income fund	Monthly	2	$250.6	$ 191.8
Hedge funds	Monthly or quarterly	2	25.8	6.6
Real estate and private equity funds	Nonredeemable	3	383.7	242.1
Hedge funds	Annually or triennially	3	1.7	1.5
Total			$661.8	$ 442.0

The investments in real estate and private equity funds are expected to be returned through distributions as a result of liquidations of the funds’ underlying assets over a weighted-average period of 4.3 years and 4.7 years at June 30, 2014 and September 30, 2013. The consolidated SIPs’ unfunded commitments to these funds totaled $206.3 million and $135.5 million at June 30, 2014 and September 30, 2013, of which the Company was contractually obligated to fund $4.1 million and $2.8 million based on its ownership percentage in the SIPs.

Transfers into Level 2 from Level 1 were nil and $0.1 million during the three and nine months ended June 30, 2014, and transfers into Level 1 from Level 2 were $0.1 million and $0.2 million during the same periods. Transfers into Level 2 from Level 1 were $0.4 million and $47.4 million during the three and nine months ended June 30, 2013, and transfers into Level 1 from Level 2 were $0.1 million and $53.9 million during the same periods. The transfers into Level 2 from Level 1 during the prior year included $47.0 million of securities for which the quoted market prices were adjusted as of December 31, 2012 due to significant price changes in U.S.-traded market proxies resulting from the resolution of U.S. fiscal cliff negotiations. The impacted securities trade in 16 different countries in Europe, Asia and Latin America. The adjustments were made after the close of the foreign markets and were based on third-party factors derived from model-based valuation techniques for which the significant assumptions were observable in the market. The transfers into Level 1 from Level 2 were securities that were valued using

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unadjusted quoted market prices.

The changes in Level 3 assets and liabilities measured at fair value on a recurring basis were as follows:

(in millions)	Investments of Consolidated VIEs	Investments of Consolidated SIPs		Total Level 3 Assets	Debt of Consolidated VIEs
for the three months ended June 30, 2014		Debt	Equity		
Balance at April 1, 2014	$0.5	$268.5	$552.1	$821.1	$(51.1)
Realized and unrealized gains (losses) included in investment and other income, net	—	(1.3)	51.6	50.3	3.1
Purchases	—	10.8	36.7	47.5	—
Sales	—	(58.3)	(10.6)	(68.9)	—
Transfers into Level 3	—	0.6	—	0.6	—
Transfers out of Level 3	—	—	(0.6)	(0.6)	—
Effect of exchange rate changes	—	(0.4)	(0.3)	(0.7)	—
Balance at June 30, 2014	$0.5	$219.9	$628.9	$849.3	$(48.0)
Change in unrealized gains (losses) included in net income relating to assets and liabilities held at June 30, 2014	$—	$(1.5)	$51.8	$50.3	$3.1

(in millions)	Investments of Consolidated VIEs	Investments of Consolidated SIPs		Total Level 3 Assets	Debt of Consolidated VIEs
for the nine months ended June 30, 2014		Debt	Equity		
Balance at October 1, 2013	$0.5	$272.3	$470.9	$743.7	$(59.7)
Realized and unrealized gains (losses) included in investment and other income, net	—	(22.7)	32.1	9.4	11.7
Purchases	—	49.5	163.2	212.7	—
Sales	—	(80.9)	(37.3)	(118.2)	—
Transfers into Level 3	—	0.6	—	0.6	—
Transfers out of Level 3	—	—	(0.6)	(0.6)	—
Effect of exchange rate changes	—	1.1	0.6	1.7	—
Balance at June 30, 2014	$0.5	$219.9	$628.9	$849.3	$(48.0)
Change in unrealized gains (losses) included in net income relating to assets and liabilities held at June 30, 2014	$—	$(23.8)	$32.3	$8.5	$11.7

(in millions)	Investments of Consolidated SIPs		Total Level 3 Assets	Debt of Consolidated VIEs
for the three months ended June 30, 2013	Debt	Equity		
Balance at April 1, 2013	$330.2	$624.5	$954.7	$(75.8)
Realized and unrealized gains included in investment and other income, net	3.2	6.9	10.1	8.8
Purchases	4.0	28.2	32.2	—
Sales	(5.5)	(7.0)	(12.5)	—
Reclassification to Level 2	—	(205.4)	(205.4)	—
Effect of exchange rate changes	2.1	0.9	3.0	—
Balance at June 30, 2013	$334.0	$448.1	$782.1	$(67.0)
Change in unrealized gains (losses) included in net income relating to assets and liabilities held at June 30, 2013	$3.2	$6.9	$10.1	$(6.0)

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(in millions)	Investments of Consolidated SIPs		Total Level 3	Debt of Consolidated
for the nine months ended June 30, 2013	Debt	Equity	Assets	VIEs
Balance at October 1, 2012	$317.5	$527.0	$844.5	$(67.9)
Realized and unrealized gains included in investment and other income, net	9.0	56.9	65.9	0.9
Purchases	57.4	114.1	171.5	—
Sales	(51.5)	(46.1)	(97.6)	—
Acquisition	—	0.8	0.8	—
Reclassification to Level 2	—	(205.4)	(205.4)	—
Effect of exchange rate changes	1.6	0.8	2.4	—
Balance at June 30, 2013	$334.0	$448.1	$782.1	$(67.0)
Change in unrealized gains included in net income relating to assets and liabilities held at June 30, 2013	$37.0	$22.2	$59.2	$1.9

There were no transfers into or out of Level 3 during the three and nine months ended June 30, 2013. The reclassification out of Level 3 to Level 2 during the three and nine months ended June 30, 2013 relates to an investment in a global fixed-income fund which is redeemable on a monthly basis without restriction and was originally misclassified as Level 3.

The valuation techniques and significant unobservable inputs used in recurring Level 3 fair value measurements were as follows:

(in millions)

as of June 30, 2014	Fair Value	Valuation Technique	Significant Unobservable Inputs	Range (Weighted Average)
Debt securities	$219.9	Discounted cash flow	Discount rate Risk premium	3.6%–18.0% (11.3%) 0.0%–18.0% (3.3%)
Equity securities	182.8	Market comparable companies	EBITDA multiple	1.0–14.0 (7.4)
			Discount for lack of marketability	20.0%-50.0% (41.5%)
	30.9	Discounted cash flow	Discount rate	6.0%–18.0% (16.4%)
	29.8	Market pricing	Price to book value ratio	1.8–2.8 (2.1)

(in millions)

as of September 30, 2013	Fair Value	Valuation Technique	Significant Unobservable Inputs	Range (Weighted Average)
Debt securities	$272.3	Discounted cash flow	Discount rate Risk premium	5.7%–25.6% (8.3%) 0.0%–19.3% (2.2%)
Equity securities	137.4	Market comparable companies	EBITDA multiple	5.0–10.2 (8.0)
			Discount for lack of marketability	20.0%–30.0% (23.7%)
	70.8	Discounted cash flow	Discount rate Discount for lack of marketability	12.0%–18.0% (16.2%) 0.0%–50.0% (20.6%)
	19.1	Market pricing	Price to book value ratio	1.7

Level 3 debt securities held by consolidated SIPs consisted of corporate loans and notes, mezzanine loans and convertible debentures, and equity securities consisted primarily of common and preferred shares at June 30, 2014 and September 30, 2013.

The fair values of Level 3 assets and liabilities that were determined based on third-party pricing information or NAV are excluded from the above two tables. At June 30, 2014 and September 30, 2013, the exclusions consisted of $48.0

million and $59.7 million of debt of consolidated VIEs that was valued using third-party broker or dealer price quotes and $385.4 million and $243.6 million of investments in various funds held by consolidated SIPs for which fair value was estimated using NAV as a practical expedient.

Following are descriptions of the sensitivity of the Level 3 recurring fair value measurements to changes in the significant unobservable inputs presented in the above tables.

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For securities utilizing the discounted cash flow valuation technique, a significant increase (decrease) in the discount rate, risk premium or discount for lack of marketability in isolation would result in a significantly lower (higher) fair value measurement. The discount for lack of marketability used to determine fair value may include other factors such as liquidity or credit risk. Generally, a change in the discount rate is accompanied by a directionally similar change in the risk premium and discount for lack of marketability.

For securities utilizing the market comparable companies valuation technique, a significant increase (decrease) in the EBITDA multiple in isolation would result in a significantly higher (lower) fair value measurement. A significant increase (decrease) in the discount for lack of marketability in isolation would result in a significantly lower (higher) fair value measurement. The discount for lack of marketability used to determine fair value may include other factors such as liquidity or credit risk.

For securities utilizing a market pricing valuation technique, a significant increase (decrease) in the price to book value ratio would result in a significantly higher (lower) fair value measurement.

Financial instruments of consolidated SIPs that were not measured at fair value were as follows:

		June 30, 2014		September 30, 2013	
(in millions)	Fair Value Level	Carrying Value	Estimated Fair Value	Carrying Value	Estimated Fair Value
Financial Assets					
Cash and cash equivalents of consolidated SIPs	1	$35.4	$35.4	$93.1	$93.1
Financial Liabilities					
Debt of consolidated SIPs	3	138.9	140.9	108.9	110.4

Non-consolidated VIEs

VIEs for which the Company is not the primary beneficiary consist of sponsored and other investment products from which the Company earns investment management fees and/or in which it has an equity ownership interest.

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

(in millions)	June 30, 2014	September 30, 2013
Receivables	$57.5	$46.3
Investments	239.7	198.5
Total	$297.2	$244.8

The Company's total AUM of non-consolidated VIEs was $43.0 billion at June 30, 2014 and $37.3 billion at September 30, 2013.

While the Company has no contractual obligation to do so, it routinely makes cash investments in the course of launching SIPs. The Company also may voluntarily elect to provide its SIPs with additional direct or indirect financial support based on its business objectives. The Company did not provide financial or other support to its SIPs during fiscal year 2013 or the nine months ended June 30, 2014.

Note 9 – Commitments and Contingencies

Legal Proceedings

The Company is from time to time involved in litigation relating to claims arising in the normal course of business. Management is of the opinion that the ultimate resolution of such claims will not materially affect the Company's business, financial position, results of operations or liquidity. In management's opinion, an adequate accrual has been made as of June 30, 2014 to provide for any probable losses that may arise from such matters for which the Company could reasonably estimate an amount.

Other Commitments and Contingencies

The Company, in its role as agent or trustee, facilitates the settlement of investor share purchase, redemption and other transactions with affiliated mutual funds. The Company is appointed by the affiliated mutual funds as agent or trustee to manage, on their behalf, bank deposit accounts that contain only (i) cash remitted by investors to the affiliated mutual funds for the direct purchase of fund shares, or (ii) cash remitted by the affiliated mutual funds for direct delivery to the investors for either the proceeds

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of fund shares liquidated at the investors' direction, or dividends and capital gains earned on fund shares. At June 30, 2014 and September 30, 2013, the Company held cash of $174.6 million and $236.4 million off-balance sheet in agency or trust for investors and the affiliated mutual funds.

At June 30, 2014, there were no changes that would have a material effect on the other commitments and contingencies reported in the Company's Form 10-K for fiscal year 2013.

Note 10 – Stock-Based Compensation

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

Total unrecognized compensation cost related to nonvested stock and stock unit awards, net of estimated forfeitures, was $157.1 million at June 30, 2014. This cost is expected to be recognized over a remaining weighted-average vesting period of 1.8 years.

Nonvested stock and stock unit award activity was as follows:

(shares in thousands)	Shares	Weighted-Average Grant-Date Fair Value
Nonvested balance at September 30, 2013	3,732	$ 40.61
Granted	2,624	53.87
Vested	(542)	40.35
Forfeited/canceled	(152)	45.55
Nonvested Balance at June 30, 2014	5,662	$ 46.65

Note 11 – Other Income (Expenses)

Other income (expenses) consisted of the following:

(in millions)	Three Months Ended June 30, 2014	Three Months Ended June 30, 2013	Nine Months Ended June 30, 2014	Nine Months Ended June 30, 2013
Investment and Other Income, Net				
Dividend income	$2.5	$2.1	$7.8	$7.6
Interest income	2.1	2.4	6.8	7.9
Gains (losses) on trading investment securities, net	2.6	(11.1)	9.7	2.5
Realized gains on sale of investment securities, available-for-sale	7.8	9.0	38.4	36.8
Realized losses on sale of investment securities, available-for-sale	—	(0.3)	(0.8)	(0.3)
Income from investments in equity method investees	33.6	12.1	68.2	54.3
Other-than-temporary impairment of investments	—	(0.8)	(0.6)	(1.8)
Gains on investments of consolidated SIPs, net	59.4	3.8	38.7	66.2
Gains (losses) on assets and liabilities of consolidated VIEs, net	(0.5)	(0.9)	7.4	(27.7)
Foreign currency exchange gains (losses), net	0.3	(8.5)	(12.3)	(1.2)
Other, net	(0.2)	2.5	9.5	8.0
Total	107.6	10.3	172.8	152.3
Interest Expense	(10.9)	(10.0)	(34.9)	(35.4)
Other Income, Net	$96.7	$0.3	$137.9	$116.9

Substantially all of the dividend income and realized gains and losses on sale of available-for-sale securities were generated by investments in non-consolidated SIPs. Interest income was primarily generated by cash equivalents and investments in trading securities. Proceeds from the sale of available-for-sale securities were $95.6 million and $284.2 million for the three and nine months ended June 30, 2014, and $54.0 million and $254.0 million for the three and nine months ended June 30, 2013.

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The Company recognized net gains (losses) on trading investment securities that were held at June 30, 2014 and 2013 of $2.0 million and $7.2 million during the three and nine months ended June 30, 2014, and $(12.1) million and $(2.7) million during the three and nine months ended June 30, 2013. Net gains (losses) on trading investment securities of consolidated SIPs that were held at June 30, 2014 and 2013 were $4.2 million and $10.3 million during the three and nine months ended June 30, 2014, and $(6.9) million and $6.8 million during the three and nine months ended June 30, 2013.

Note 12 – Accumulated Other Comprehensive Income

Changes in accumulated other comprehensive income by component were as follows:

(in millions) for the three months ended June 30, 2014	Unrealized Gains (Losses) on Investments	Currency Translation Adjustments	Unrealized Gains (Losses) on Defined Benefit Plans	Total
Balance at April 1, 2014	$63.4	$(55.2)	$(3.8)	$4.4
Other comprehensive income before reclassifications, net of tax	17.9	17.2	0.1	35.2
Reclassifications to net investment and other income, net of tax	(15.4)	—	—	(15.4)
Total other comprehensive income	2.5	17.2	0.1	19.8
Balance at June 30, 2014	$65.9	$(38.0)	$(3.7)	$24.2

(in millions) for the nine months ended June 30, 2014	Unrealized Gains (Losses) on Investments	Currency Translation Adjustments	Unrealized Losses on Defined Benefit Plans	Total
Balance at October 1, 2013	$71.9	$(63.2)	$(2.6)	$6.1
Other comprehensive income (loss) before reclassifications, net of tax	22.9	25.2	(1.1)	47.0
Reclassifications to net investment and other income, net of tax	(28.9)	—	—	(28.9)
Total other comprehensive income (loss)	(6.0)	25.2	(1.1)	18.1
Balance at June 30, 2014	$65.9	$(38.0)	$(3.7)	$24.2

Note 13 – Banking Regulatory Ratios

As of June 30, 2014, Franklin was a bank holding company and a financial holding company subject to various U.S. regulatory capital requirements. Based on the Company’s calculations, it exceeded the applicable capital adequacy requirements as listed below.

(in millions)	June 30, 2014	September 30, 2013	Capital Adequacy Minimum
Tier 1 capital	$8,671.2	$7,449.2	N/A
Total risk-based capital	8,711.5	7,482.6	N/A
Tier 1 leverage ratio	63%	58%	4%
Tier 1 risk-based capital ratio	61%	58%	4%
Total risk-based capital ratio	61%	58%	8%

Note 14 – Subsequent Events

On July 14, 2014, the Company closed all of its outstanding client deposit accounts. The Company has ceased accepting deposits and originating loans, and believes that it is no longer a bank holding company. On July 16, 2014, the Company submitted a letter to the Board of Governors of the Federal Reserve System to withdraw its registration as a bank holding company.

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

Forward-Looking Statements

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

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

The following discussion should be read in conjunction with our Form 10-K for the fiscal year ended September 30, 2013 (“fiscal year 2013”) filed with the U.S. Securities and Exchange Commission (the “SEC”), and the condensed consolidated financial statements and notes thereto included elsewhere in this Form 10-Q.

Overview

We are a global investment management organization and derive our operating revenues and net income from providing investment management and related services to investors in jurisdictions worldwide through products that include investment funds and institutional, high net-worth and separately-managed accounts (collectively, our “sponsored investment products” or “SIPs”). In addition to investment management, our services include fund administration, sales, distribution, shareholder services, transfer agency, trustee, custodial and other fiduciary services. Our SIPs and investment management and related services are distributed or marketed to the public globally under the following distinct brand names: Franklin®, Templeton®, Mutual Series®, Bissett®, Fiduciary Trust™, Darby®, Balanced Equity Management® and K2®. We offer a broad range of SIPs under equity, hybrid, fixed-income and cash management funds and accounts, including alternative investment products, that meet a wide variety of specific investment needs of individual and institutional investors. We also provide sub-advisory services to certain investment products sponsored by other companies which may be sold to the public under the brand names of those other companies or on a co-branded basis.

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

During the first nine months of our fiscal year, the global equity markets provided strong gains, evidenced by increases of 15% in the MSCI World Index and 18% in the S&P 500 Index. Easing of geopolitical concerns about the crisis in Ukraine and the economic slowdown in China, along with an improving global economic outlook and ongoing accommodative monetary policy from central banks, resulted in increases of 5% in both the MSCI World and S&P 500 indexes during our third fiscal quarter. The global bond markets continued to show signs of stabilization during the quarter, and the Barclays Global Aggregate Index increased 2% for the period. The overall market improvement benefited our assets under management, fee revenues and operating income, all of which increased from the first nine months of fiscal year 2013.

Our total AUM at June 30, 2014 was $920.5 billion, 9% higher than at September 30, 2013 and 13% higher than at June 30, 2013. Simple monthly average AUM (“average AUM”) for the three and nine months ended June 30, 2014 increased 8% and 10% from the same periods in the prior fiscal year, primarily driven by $116.9 billion of market appreciation during the previous twelve months.

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The business and regulatory environments in which we operate remain complex, uncertain and subject to change. In the U.S., the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, regulatory changes adopted by the Commodity Futures Trading Commission in 2012 and the Foreign Account Tax Compliance Act impose additional restrictions, limitations and registration and reporting requirements on our business. We are also subject to numerous regulations by U.S. and non-U.S. regulators that add further complexity to our ongoing global compliance operations. We expect that such regulatory requirements and developments will cause us to incur additional administrative and compliance costs.

Uncertainties regarding economic stabilization and improvement remain for the foreseeable future. As we continue to confront the challenges of the current economic and regulatory environments, we remain focused on the investment performance of our SIPs and on providing high quality customer service to our clients. While we are focused on expense management, we will also seek to attract, retain and develop employees and invest strategically in systems and technology that will provide a secure and stable environment. We will continue to seek to protect and further our brand recognition while developing and maintaining broker/dealer and client relationships. The success of these and other strategies may be influenced by the factors discussed in the “Risk Factors” section set forth below.

RESULTS OF OPERATIONS

(in millions, except per share data)	Three Months Ended June 30, 2014	Three Months Ended June 30, 2013	Percent Change	Nine Months Ended June 30, 2014	Nine Months Ended June 30, 2013	Percent Change
Operating revenues	$2,130.5	$2,084.8	2 %	$6,335.9	$6,000.2	6 %
Operating income	786.8	771.7	2 %	2,385.9	2,186.2	9 %
Net income attributable to Franklin Resources, Inc.	578.9	552.3	5 %	1,743.7	1,641.2	6 %
Diluted earnings per share	$0.92	$0.86	7 %	$2.77	$2.57	8 %
Operating margin[1]	36.9 %	37.0 %		37.7 %	36.4 %	

[1] Defined as operating income divided by total operating revenues.

Operating income increased $15.1 million and $199.7 million for the three and nine months ended June 30, 2014, as compared to the same periods in the prior fiscal year, primarily due to 6% and 9% increases in investment management fees, which were driven by 8% and 10% increases in average AUM, partially offset by 2% and 4% increases in operating expenses.

Net income attributable to Franklin Resources, Inc. increased $26.6 million and $102.5 million for the three and nine months ended June 30, 2014, primarily due to the increases in operating income. The increase for the three-month period was also impacted by higher investment and other income, net, less the portion attributable to noncontrolling interests.

The increases in diluted earnings per share for the three and nine months ended June 30, 2014 were consistent with the changes in net income and the impacts of 2% and 1% decreases in diluted average common shares outstanding primarily resulting from repurchases of shares of our common stock during the twelve-month period ended June 30, 2014.

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ASSETS UNDER MANAGEMENT

AUM by investment objective was as follows:

(in billions)	June 30, 2014	June 30, 2013	Percent Change	
Equity				
Global/international	$273.8	$224.0	22	%
United States	114.5	89.5	28	%
Total equity	388.3	313.5	24	%
Hybrid	162.5	129.4	26	%
Fixed-Income				
Tax-free	71.6	79.1	(9	)%
Taxable				
Global/international	230.6	229.1	1	%
United States	61.1	57.5	6	%
Total fixed-income	363.3	365.7	(1	