FRANKLIN RESOURCES INC
Form 10-Q
January 30, 2015
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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 December 31, 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: 621,826,792 shares of common stock, par value $0.10 per share, of Franklin Resources, Inc. as of January 23, 2015.

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

	Three Months Ended December 31,	
(in millions, except per share data)	2014	2013
Operating Revenues		
Investment management fees	$1,382.4	$1,373.8
Sales and distribution fees	595.0	636.7
Shareholder servicing fees	65.8	76.1
Other	21.1	22.9
Total operating revenues	2,064.3	2,109.5
Operating Expenses		
Sales, distribution and marketing	731.5	776.7
Compensation and benefits	375.5	349.0
Information systems and technology	51.2	50.2
Occupancy	34.3	33.1
General, administrative and other	89.8	87.4
Total operating expenses	1,282.3	1,296.4
Operating Income	782.0	813.1
Other Income (Expenses)		
Investment and other income, net	51.7	48.2
Interest expense	(11.3)	(12.6)
Other income, net	40.4	35.6
Income before taxes	822.4	848.7
Taxes on income	256.1	252.7
Net income	566.3	596.0
Less: Net income (loss) attributable to		
Nonredeemable noncontrolling interests	6.7	(17.2)
Redeemable noncontrolling interests	(6.8)	9.4
Net Income Attributable to Franklin Resources, Inc.	$566.4	$603.8
Earnings per Share		
Basic	$0.91	$0.96
Diluted	0.91	0.96
Dividends per Share	$0.65	$0.12

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 December 31, 2014	2013
Net Income	$566.3	$596.0
Other Comprehensive Income (Loss)		
Net unrealized losses on investments, net of tax	(0.2)	(10.0)
Currency translation adjustments, net of tax	(61.5)	8.1
Net unrealized gains (losses) on defined benefit plans, net of tax	1.0	(1.3)
Total other comprehensive loss	(60.7)	(3.2)
Total comprehensive income	505.6	592.8
Less: Comprehensive income (loss) attributable to		
Nonredeemable noncontrolling interests	6.7	(17.2)
Redeemable noncontrolling interests	(6.8)	9.4
Comprehensive Income Attributable to Franklin Resources, Inc.	$505.7	$600.6

See Notes to Condensed Consolidated Financial Statements.

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FRANKLIN RESOURCES, INC.
Condensed Consolidated Balance Sheets
Unaudited

(in millions, except share and per share data)	December 31, 2014	September 30, 2014
Assets		
Cash and cash equivalents	$7,758.0	$7,476.8
Receivables	926.7	950.0
Investments (including $1,859.4 and $1,845.6 at fair value at December 31, 2014 and September 30, 2014)	2,653.1	2,516.1
Assets of consolidated sponsored investment products		
Cash and cash equivalents	60.6	44.9
Investments, at fair value	996.8	1,373.7
Assets of consolidated variable interest entities		
Cash and cash equivalents	66.6	74.3
Investments, at fair value	754.1	788.4
Deferred taxes, net	77.6	98.1
Property and equipment, net	523.4	530.7
Goodwill and other intangible assets, net	2,307.9	2,325.9
Other	172.0	178.2
Total Assets	$16,296.8	$16,357.1
Liabilities		
Compensation and benefits	$238.9	$465.1
Accounts payable and accrued expenses	194.2	237.5
Dividends	406.7	76.9
Commissions	419.4	440.3
Income taxes	192.6	23.4
Debt	1,198.3	1,198.2
Debt of consolidated sponsored investment products	105.7	122.3
Debt of consolidated variable interest entities (at fair value at September 30, 2014)	795.5	828.5
Deferred taxes	259.7	259.3
Other	257.3	258.4
Total liabilities	4,068.3	3,909.9
Commitments and Contingencies (Note 9)		
Redeemable Noncontrolling Interests	74.0	234.8
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; 622,426,648 and 622,893,090 shares issued and outstanding at December 31, 2014 and September 30, 2014	62.2	62.3
Retained earnings	11,672.0	11,625.6
Appropriated retained earnings of consolidated variable interest entities	—	13.9
Accumulated other comprehensive loss	(178.4)	(117.7)
Total Franklin Resources, Inc. stockholders’ equity	11,555.8	11,584.1
Nonredeemable noncontrolling interests	598.7	628.3
Total stockholders’ equity	12,154.5	12,212.4
Total Liabilities, Redeemable Noncontrolling Interests and Stockholders’ Equity	$16,296.8	$16,357.1

See Notes to Condensed Consolidated Financial Statements.

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

	Three Months Ended December 31,	
(in millions)	2014	2013
Net Income	$566.3	$596.0
Adjustments to reconcile net income to net cash provided by operating activities:		
Amortization of deferred sales commissions	30.2	34.2
Depreciation and other amortization	24.9	25.1
Stock-based compensation	35.4	30.9
Excess tax benefit from stock-based compensation	(1.9)	(2.8)
Gains on sale of assets	(9.5)	(20.2)
Income from investments in equity method investees	(6.7)	(24.9)
Net (gains) losses on other investments of consolidated sponsored investment products	(5.9)	16.2
Net gains of consolidated variable interest entities	(1.6)	(6.6)
Deferred income taxes	23.8	(10.4)
Other	10.5	8.2
Changes in operating assets and liabilities:		
Increase in receivables, prepaid expenses and other	(6.7)	(126.2)
Decrease (increase) in trading securities, net	5.2	(36.8)
Decrease (increase) in trading securities of consolidated sponsored investment products, net	16.0	(230.4)
Decrease in accrued compensation and benefits	(220.6)	(193.9)
Increase (decrease) in commissions payable	(20.9)	16.4
Increase in income taxes payable	171.7	194.5
Increase (decrease) in other liabilities	(37.8)	55.4
Net cash provided by operating activities	572.4	324.7
Purchase of investments	(71.7)	(80.1)
Liquidation of investments	69.4	194.1
Purchase of investments by consolidated sponsored investment products	(51.5)	(95.2)
Liquidation of investments by consolidated sponsored investment products	122.5	32.1
Purchase of investments by consolidated variable interest entities	(88.8)	(45.0)
Liquidation of investments by consolidated variable interest entities	126.8	128.0
Decrease in loans receivable, net	—	30.9
Additions of property and equipment, net	(16.1)	(15.0)
Decrease in cash and cash equivalents from net deconsolidation of sponsored investment products	(0.1)	(34.0)
Net cash provided by investing activities	90.5	115.8
Increase (decrease) in deposits	(0.3)	66.5
Issuance of common stock	—	7.2
Dividends paid on common stock	(75.8)	(64.1)
Repurchase of common stock	(151.2)	(137.1)
Excess tax benefit from stock-based compensation	1.9	2.8
Proceeds from issuance of debt by consolidated sponsored investment products	218.5	190.3
Payments on debt by consolidated sponsored investment products	(234.5)	(176.8)
Payments on debt by consolidated variable interest entities	(44.1)	(60.0)
Payments on contingent consideration liabilities	(7.1)	(2.7)

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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
[Table continued from previous page]

(in millions)	Three Months Ended December 31, 2014	2013
Noncontrolling interests	(35.3)	101.4
Net cash used in financing activities	(327.9)	(72.5)
Effect of exchange rate changes on cash and cash equivalents	(45.8)	8.6
Increase in cash and cash equivalents	289.2	376.6
Cash and cash equivalents, beginning of period	7,596.0	6,323.1
Cash and Cash Equivalents, End of Period	$7,885.2	$6,699.7
Supplemental Disclosure of Cash Flow Information		
Cash paid for income taxes	$57.0	$68.0
Cash paid for interest	12.9	14.2
Cash paid for interest by consolidated variable interest entities and consolidated sponsored investment products	9.0	11.9

See Notes to Condensed Consolidated Financial Statements.

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FRANKLIN RESOURCES, INC.
Notes to Condensed Consolidated Financial Statements
December 31, 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, 2014 ("fiscal year 2014"). Certain amounts for the comparative prior fiscal year period have been reclassified to conform to the financial statement presentation as of and for the period ended December 31, 2014.

Note 2 – New Accounting Guidance

On October 1, 2014, the Company adopted new Financial Accounting Standards Board guidance that provides an entity the election to measure the financial assets and financial liabilities of a consolidated collateralized financing entity using the more observable fair value of either the financial assets or financial liabilities, and elected this measurement alternative for its consolidated collateralized loan obligations ("CLOs"). The adoption resulted in a $14.2 million increase in debt of consolidated variable interest entities ("VIEs"), a $13.9 million reduction in appropriated retained earnings of consolidated VIEs and a $0.3 million reduction in retained earnings as of October 1, 2014. The Company's subsequent earnings from the consolidated CLOs reflect changes in fair value of its own economic interests in the CLOs, and no longer include gains or losses on assets and liabilities of the CLOs, which were primarily attributable to noncontrolling interests.

There were no significant updates to the new accounting guidance not yet adopted by the Company as disclosed in its Form 10-K for fiscal year 2014.

Note 3 – Stockholders' Equity

The changes in total stockholders' equity were as follows:

(in millions) for the three months ended December 31, 2014	Franklin Resources, Inc. Stockholders' Equity	Nonredeemable Noncontrolling Interests	Total Stockholders' Equity
Balance at October 1, 2014	$11,584.1	$ 628.3	$12,212.4
Adjustment for adoption of new accounting guidance	(14.2)		(14.2)
Net income	566.4	6.7	573.1
Other comprehensive loss	(60.7)		(60.7)
Cash dividends on common stock	(405.6)		(405.6)
Repurchase of common stock	(151.2)		(151.2)
Net distributions		(36.3)	(36.3)
Other[1]	37.0		37.0
Balance at December 31, 2014	$11,555.8	$ 598.7	$12,154.5

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

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(in millions) for the three months ended December 31, 2013	Franklin Resources, Inc. Stockholders' Equity	Nonredeemable Noncontrolling Interests	Total Stockholders' Equity
Balance at October 1, 2013	$10,073.1	$ 612.4	$10,685.5
Net income (loss)	603.8	(17.2)	586.6
Net income reclassified to appropriated retained earnings	4.8	(4.8)	—
Other comprehensive loss	(3.2)		(3.2)
Cash dividends on common stock	(75.9)		(75.9)
Repurchase of common stock	(137.1)		(137.1)
Net distributions		(13.1)	(13.1)
Other[1]	41.6		41.6
Balance at December 31, 2013	$10,507.1	$ 577.3	$11,084.4

———————

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

During the three months ended December 31, 2014 and 2013, the Company repurchased 2.7 million and 2.5 million shares of its common stock at a cost of $151.2 million and $137.1 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 December 31, 2014, 27.1 million shares remained available for repurchase under the program, which is not subject to an expiration date.

Note 4 – Earnings per Share

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

(in millions, except per share data)	Three Months Ended December 31, 2014	2013
Net Income Attributable to Franklin Resources, Inc.	$566.4	$603.8
Less: Allocation of earnings to participating nonvested stock and stock unit awards	3.6	3.5
Net Income Available to Common Stockholders	$562.8	$600.3
Weighted-average shares outstanding – basic	620.1	628.1
Effect of non-participating nonvested stock unit awards and dilutive common stock options	0.1	0.4
Weighted-Average Shares Outstanding – Diluted	620.2	628.5
Earnings per Share		
Basic	$0.91	$0.96
Diluted	0.91	0.96

Non-participating nonvested stock unit awards excluded from the calculation of diluted earnings per share because their effect would have been anti-dilutive were 0.6 million and 0.1 million for the three months ended December 31, 2014 and 2013.

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Note 5 – Investments

The disclosures below include details of the Company's investments, excluding those of consolidated sponsored investment products ("SIPs") and consolidated VIEs. 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)	December 31, 2014	September 30, 2014
Investment securities, trading	$1,270.4	$1,277.5
Investment securities, available-for-sale		
SIPs	541.9	517.6
Securities of U.S. states and political subdivisions	8.7	11.3
Securities of the U.S. Treasury and federal agencies	0.7	0.7
Mortgage-backed securities – agency residential[1]	17.2	17.9
Other equity securities	6.3	6.6
Total investment securities, available-for-sale	574.8	554.1
Investments in equity method investees	652.1	594.9
Other investments	155.8	89.6
Total	$2,653.1	$2,516.1

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

At December 31, 2014 and September 30, 2014, investment securities with aggregate carrying amounts of $5.7 million and $6.1 million were pledged as collateral.

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 December 31, 2014	Cost Basis	Gains	Losses	Fair Value
SIPs	$504.4	$41.9	$(4.4)	$541.9
Securities of U.S. states and political subdivisions	8.5	0.2	—	8.7
Securities of the U.S. Treasury and federal agencies	0.7	—	—	0.7
Mortgage-backed securities – agency residential	17.1	0.1	—	17.2
Other equity securities	5.6	0.7	—	6.3
Total	$536.3	$42.9	$(4.4)	$574.8

(in millions)		Gross Unrealized		
as of September 30, 2014	Cost Basis	Gains	Losses	Fair Value
SIPs	$477.0	$43.5	$(2.9)	$517.6
Securities of U.S. states and political subdivisions	11.0	0.3	—	11.3
Securities of the U.S. Treasury and federal agencies	0.7	—	—	0.7
Mortgage-backed securities – agency residential	18.0	—	(0.1)	17.9
Other equity securities	6.3	0.3	—	6.6
Total	$513.0	$44.1	$(3.0)	$554.1

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)	Less Than 12 Months		12 Months or Greater		Total	
as of December 31, 2014	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses	Fair Value	Gross Unrealized Losses
SIPs	$112.1	$(4.2)	$1.7	$(0.2)	$113.8	$(4.4)

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(in millions) as of September 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	$156.4	$(2.7)	$1.5	$(0.2)	$157.9	$(2.9)
Mortgage-backed securities – agency residential	4.0	—	11.6	(0.1)	15.6	(0.1)
Total	$160.4	$(2.7)	$13.1	$(0.3)	$173.5	$(3.0)

The Company recognized $1.0 million and $0.6 million of other-than-temporary impairment during the three months ended December 31, 2014 and 2013, all of which related to available-for-sale SIPs, except for $0.2 million related to other investments during the 2013 period.

At December 31, 2014, contractual maturities of available-for-sale debt securities were as follows:

(in millions)	Cost Basis	Fair Value
Due in one year or less	$2.6	$2.6
Due after one year through five years	6.6	6.8
Total	$9.2	$9.4

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 SIPs and consolidated VIEs. 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 December 31, 2014	Level 1	Level 2	Level 3	Total
Assets				
Investment securities, trading	$1,189.1	$81.3	$—	$1,270.4
Investment securities, available-for-sale				
SIPs	541.9	—	—	541.9
Securities of U.S. states and political subdivisions	—	8.7	—	8.7
Securities of the U.S. Treasury and federal agencies	—	0.7	—	0.7
Mortgage-backed securities – agency residential	—	17.2	—	17.2
Other equity securities	1.2	5.1	—	6.3
Life settlement contracts	—	—	14.2	14.2
Total Assets Measured at Fair Value	$1,732.2	$113.0	$14.2	$1,859.4
Liabilities				
Contingent consideration liabilities	$—	$—	$100.7	$100.7

(in millions) as of September 30, 2014	Level 1	Level 2	Level 3	Total
Assets				
Investment securities, trading	$1,196.1	$81.4	$—	$1,277.5
Investment securities, available-for-sale				
SIPs	517.6	—	—	517.6
Securities of U.S. states and political subdivisions	—	11.3	—	11.3
Securities of the U.S. Treasury and federal agencies	—	0.7	—	0.7
Mortgage-backed securities – agency residential	—	17.9	—	17.9
Other equity securities	1.7	4.9	—	6.6
Life settlement contracts	—	—	14.0	14.0
Total Assets Measured at Fair Value	$1,715.4	$116.2	$14.0	$1,845.6
Liabilities				
Contingent consideration liabilities	$—	$—	$98.5	$98.5

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 months ended December 31, 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 December 31,	2014 Life Settlement Contracts	2014 Contingent Consideration Liabilities	2013 Life Settlement Contracts	2013 Contingent Consideration Liabilities
Balance at beginning of period	$14.0	$(98.5)	$13.8	$(97.7)
Total realized and unrealized gains (losses)				
Included in investment and other income, net	0.6	—	0.7	—
Included in general, administrative and other expense	—	(9.4)	—	(5.9)
Other	—	(0.1)	—	(0.3)
Purchases	0.1	—	0.1	—
Sales	—	—	(0.7)	—
Settlements	(0.5)	7.1	—	2.7
Effect of exchange rate changes	—	0.2	—	—
Balance at End of Period	$14.2	$(100.7)	$13.9	$(101.2)
Change in unrealized gains (losses) included in net income relating to assets and liabilities held at end of period	$0.3	$(9.5)	$0.3	$(6.2)

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

(in millions) as of December 31, 2014	Fair Value	Valuation Technique	Significant Unobservable Inputs	Range (Weighted Average)
Life settlement contracts	$14.2	Discounted cash flow	Life expectancy Discount rate	22–148 months (71) 3.3%–19.0% (11.7%)
Contingent consideration liabilities	100.7	Discounted cash flow	AUM growth rate EBITDA margin Discount rate	2.9%–19.8% (11.3%) 21.7% - 29.6% (28.0%) 14.0%

(in millions) as of September 30, 2014	Fair Value	Valuation Technique	Significant Unobservable Inputs	Range (Weighted Average)
Life settlement contracts	$14.0	Discounted cash flow	Life expectancy Discount rate	23–150 months (71) 3.3%–21.7% (11.7%)
Contingent consideration liabilities	98.5	Discounted cash flow	AUM growth rate EBITDA margin Discount rate	3.4%–20.2% (12.8%) 21.9%–30.4% (28.2%) 14.0%

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	December 31, 2014 Carrying Value	December 31, 2014 Estimated Fair Value	September 30, 2014 Carrying Value	September 30, 2014 Estimated Fair Value
Financial Assets					
Cash and cash equivalents	1	$7,758.0	$7,758.0	$7,476.8	$7,476.8
Other investments[1]	2 or 3	141.6	150.4	75.6	87.8

Financial Liabilities					
Debt	2	1,198.3	1,239.5	1,198.2	1,235.8

[1] Primarily consist of Level 3 assets.

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Note 7 – Debt

The disclosures below include details of the Company's debt, excluding that of consolidated SIPs and consolidated VIEs. 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)	December 31, 2014	September 30, 2014	Effective Interest Rate	
$250 million 3.125% notes due May 2015	$250.0	$250.0	3.32	%
$300 million 1.375% notes due September 2017	299.1	299.0	1.66	%
$350 million 4.625% notes due May 2020	349.8	349.8	4.74	%
$300 million 2.800% notes due September 2022	299.4	299.4	2.93	%
Total Debt	$1,198.3	$1,198.2		

At December 31, 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 December 31, 2014, the Company was in compliance with the covenants of the notes.

At December 31, 2014, maturities for debt were as follows:

(in millions) for the fiscal years ending September 30,	Amount
2015	$250.0
2016	—
2017	299.1
2018	—
2019	—
Thereafter	649.2
Total	$1,198.3

At December 31, 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.

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.

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

	December 31, 2014			September 30, 2014		
	Consolidated			Consolidated		
(in millions)	SIPs	VIEs	Total	SIPs	VIEs	Total
Assets						
Cash and cash equivalents	$60.6	$66.6	$127.2	$44.9	$74.3	$119.2
Receivables	14.6	9.0	23.6	16.2	23.0	39.2
Investments, at fair value	996.8	754.1	1,750.9	1,373.7	788.4	2,162.1
Other assets	0.6	—	0.6	0.7	—	0.7
Total Assets	$1,072.6	$829.7	$1,902.3	$1,435.5	$885.7	$2,321.2
Liabilities						
Accounts payable and accrued expenses	$16.2	$22.8	$39.0	$18.5	$35.3	$53.8
Debt (at fair value at September 30, 2014)	—	795.5	795.5	—	828.5	828.5
Debt	105.7	—	105.7	122.3	—	122.3
Other liabilities	12.3	—	12.3	12.4	—	12.4
Total liabilities	134.2	818.3	952.5	153.2	863.8	1,017.0
Redeemable Noncontrolling Interests	74.0	—	74.0	234.8	—	234.8
Stockholders' Equity						
Franklin Resources, Inc.'s interests	285.0	11.4	296.4	436.5	21.9	458.4
Nonredeemable noncontrolling interests	579.4	—	579.4	611.0	—	611.0
Total stockholders' equity	864.4	11.4	875.8	1,047.5	21.9	1,069.4
Total Liabilities, Redeemable Noncontrolling Interests and Stockholders' Equity	$1,072.6	$829.7	$1,902.3	$1,435.5	$885.7	$2,321.2

The consolidated SIPs and consolidated VIEs did not have a significant impact on net income attributable to the Company during the three months ended December 31, 2014 and 2013.

Consolidated SIPs

Consolidated SIPs consist of 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 December 31, 2014, and 30 SIPs as of September 30, 2014. 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.

Consolidated VIEs

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

The assets and liabilities of the CLOs were both carried at fair value through September 30, 2014. The Company adopted new accounting guidance on October 1, 2014 under which the liabilities are measured based on the fair value of the assets. Changes in the fair values of the assets and liabilities prior to the adoption of the new accounting guidance were as follows:

(in millions) for the three months ended December 31, 2013	Amount
Net gains from changes in fair value of assets	$13.4
Net losses from changes in fair value of liabilities	(7.7)
Total Net Gains	$5.7

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During the three months ended December 31, 2014, the Company recognized $5.3 million of net gains related to its own economic interests in the CLOs. There was no net gain or loss resulting from changes in the values of the assets and liabilities of the CLOs as a result of the new accounting guidance.

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

(in millions) as of December 31, 2014	Investments	
Unpaid principal balance	$759.6	
Difference between unpaid principal balance and fair value	(5.5	)
Fair Value	$754.1	

(in millions) as of September 30, 2014	Investments	Debt	
Unpaid principal balance	$787.1	$861.9	
Difference between unpaid principal balance and fair value	1.3	(33.4	)
Fair Value	$788.4	$828.5	

The unpaid principal balance of the debt of the CLOs was $825.5 million at December 31, 2014. There were no investments 90 days or more past due at December 31, 2014 or September 30, 2014.

Investments

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

	December 31, 2014			September 30, 2014		
	Consolidated			Consolidated		
(in millions)	SIPs	VIEs	Total	SIPs	VIEs	Total
Investment securities, trading	$214.5	$—	$214.5	$249.6	$—	$249.6
Other debt securities	151.6	754.1	905.7	205.6	788.4	994.0
Other equity securities	630.7	—	630.7	918.5	—	918.5
Total Investments	$996.8	$754.1	$1,750.9	$1,373.7	$788.4	$2,162.1

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. Investments of consolidated VIEs consist of corporate debt securities.

Debt

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

(in millions)	December 31, 2014	Effective Interest Rate		September 30, 2014	Effective Interest Rate	
Debt of consolidated SIPs due fiscal years 2015-2019	$ 105.7	4.10	%	$ 122.3	3.87	%
Debt of consolidated VIEs due fiscal years 2018-2024	795.5	1.48	%	828.5	1.43	%
Total Debt	$ 901.2			$ 950.8		

The debt of consolidated SIPs had both fixed and floating interest rates ranging from 2.19% to 5.81% at December 31, 2014, and from 2.19% to 5.89% at September 30, 2014. 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.

The debt of consolidated VIEs had floating interest rates ranging from 0.46% to 9.73% at December 31, 2014 and September 30, 2014.

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At December 31, 2014, contractual maturities for debt of consolidated SIPs and consolidated VIEs were as follows:

(in millions) for the fiscal years ending September 30,	Amount
2015	$34.0
2016	—
2017	28.4
2018	224.9
2019	330.6
Thereafter	283.3
Total	$901.2

Fair Value Measurements

The tables below present the balances of assets and liabilities of consolidated SIPs and consolidated VIEs 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 December 31, 2014	Level 1	Level 2	Level 3	Total
Assets				
Cash and cash equivalents of consolidated VIEs	$66.6	$—	$—	$66.6
Receivables of consolidated VIEs	—	9.0	—	9.0
Investments of consolidated VIEs	—	753.7	0.4	754.1
Investments of consolidated SIPs				
Equity securities	131.8	26.2	602.8	760.8
Debt securities	2.4	82.0	151.6	236.0
Total Assets Measured at Fair Value	$200.8	$870.9	$754.8	$1,826.5
Liabilities				
Other liabilities of consolidated SIPs	$4.7	$—	$—	$4.7

(in millions) as of September 30, 2014	Level 1	Level 2	Level 3	Total
Assets				
Cash and cash equivalents of consolidated VIEs	$74.3	$—	$—	$74.3
Receivables of consolidated VIEs	—	23.0	—	23.0
Investments of consolidated VIEs	—	787.9	0.5	788.4
Investments of consolidated SIPs				
Equity securities	149.9	304.0	614.3	1,068.2
Debt securities	2.4	96.8	206.3	305.5
Total Assets Measured at Fair Value	$226.6	$1,211.7	$821.1	$2,259.4
Liabilities				
Accounts payable and accrued expenses of consolidated VIEs	$—	$35.3	$—	$35.3
Debt of consolidated VIEs	—	781.3	47.2	828.5
Other liabilities of consolidated SIPs	4.0	0.6	—	4.6
Total Liabilities Measured at Fair Value	$4.0	$817.2	$47.2	$868.4

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The investments in fund products for which fair value was estimated using reported net asset value ("NAV") as a practical expedient consisted of the following:

(in millions)	Redemption Frequency	Fair Value Level	December 31, 2014	September 30, 2014
Global fixed-income fund	Monthly	2	$ —	$ 275.1
Hedge funds	Monthly or quarterly	2	26.1	27.2
Real estate and private equity funds	Nonredeemable	3	409.6	392.3
Hedge funds	Triennially	3	1.1	1.2
Total			$ 436.8	$ 695.8

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 3.6 years and 3.9 years at December 31, 2014 and September 30, 2014. The consolidated SIPs' unfunded commitments to these funds totaled $128.0 million and $139.2 million at December 31, 2014 and September 30, 2014, of which the Company was contractually obligated to fund $2.8 million and $3.1 million based on its ownership percentage in the SIPs.

There were no transfers between Level 1 and Level 2 during the three months ended December 31, 2014. There were no transfers into Level 2 from Level 1, and transfers into Level 1 from Level 2 were $0.1 million during the three months ended December 31, 2013.

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

(in millions)	Investments of Consolidated SIPs		Investments of Consolidated VIEs	Total Level 3 Assets	Debt of Consolidated VIEs
for the three months ended December 31, 2014	Equity	Debt			
Balance at October 1, 2014	$614.3	$206.3	$0.5	$821.1	$(47.2)
Adjustment for adoption of new accounting guidance	—	—	—	—	47.2
Realized and unrealized gains (losses) included in investment and other income, net	8.3	3.9	(0.1)	12.1	—
Purchases	47.3	1.7	—	49.0	—
Sales	(65.1)	(57.2)	—	(122.3)	—
Settlements	—	(0.6)	—	(0.6)	—
Effect of exchange rate changes	(2.0)	(2.5)	—	(4.5)	—
Balance at December 31, 2014	$602.8	$151.6	$0.4	$754.8	$—
Change in unrealized gains (losses) included in net income relating to assets and liabilities held at December 31, 2014	$2.6	$3.6	$(0.1)	$6.1	$—

(in millions)	Investments of Consolidated SIPs		Investments of Consolidated VIEs	Total Level 3 Assets	Debt of Consolidated VIEs
for the three months ended December 31, 2013	Equity	Debt			
Balance at October 1, 2013	$470.9	$272.3	$0.5	$743.7	$(59.7)
Realized and unrealized gains (losses) included in investment and other income, net	(3.7)	(27.7)	—	(31.4)	7.5
Purchases	50.2	22.2	—	72.4	—
Sales	(15.6)	(13.9)	—	(29.5)	—
Effect of exchange rate changes	0.8	1.5	—	2.3	—
Balance at December 31, 2013	$502.6	$254.4	$0.5	$757.5	$(52.2)
	$(3.3)	$(28.8)	$—	$(32.1)	$7.5

Change in unrealized gains (losses) included
in net income relating to assets and liabilities
held at December 31, 2013

There were no transfers into or out of Level 3 during the three months ended December 31, 2014 and 2013.

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

(in millions) as of December 31, 2014	Fair Value	Valuation Technique	Significant Unobservable Inputs	Range (Weighted Average)
Debt securities	$151.6	Discounted cash flow	Discount rate	3.6%–18.0% (10.1%)
			Risk premium	0.0%–8.0% (2.4%)
Equity securities	150.4	Market comparable companies	EBITDA multiple	3.1–11.0 (8.0)
			Discount for lack of marketability	25.0%–50.0% (33.2%)
	22.0	Discounted cash flow	Discount rate	6.3%–20.0% (13.4%)
	19.7	Market pricing	Price to book value ratio	1.8-2.8 (2.3)

(in millions) as of September 30, 2014	Fair Value	Valuation Technique	Significant Unobservable Inputs	Range (Weighted Average)
Debt securities	$206.3	Discounted cash flow	Discount rate	3.6%–18.0% (11.9%)
			Risk premium	0.0%–8.0% (1.9%)
Equity securities	152.9	Market comparable companies	EBITDA multiple	3.1–11.0 (8.0)
			Discount for lack of marketability	25.0%–50.0% (33.2%)
	38.1	Discounted cash flow	Discount rate	6.0%–20.0% (16.9%)
	29.8	Market pricing	Price to book value ratio	1.8–2.8 (2.1)

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 December 31, 2014 and September 30, 2014.

The fair values of Level 3 assets and liabilities that were determined based on NAV or third-party pricing information are excluded from the above two tables. At December 31, 2014 and September 30, 2014, the asset exclusions consisted of $410.7 million and $393.5 million of investments in various funds held by consolidated SIPs for which fair value was estimated using NAV as a practical expedient. At September 30, 2014, $47.2 million of debt of consolidated VIEs that was valued using third-party broker or dealer price quotes was also excluded.

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.

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.

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

(in millions)	Fair Value Level	December 31, 2014 Carrying Value	December 31, 2014 Estimated Fair Value	September 30, 2014 Carrying Value	September 30, 2014 Estimated Fair Value
Financial Assets					
Cash and cash equivalents of consolidated SIPs	1	$60.6	$60.6	$44.9	$44.9
Financial Liabilities					
Debt of consolidated VIEs[1]	2 or 3	795.5	783.3	—	—
Debt of consolidated SIPs	3	105.7	104.1	122.3	122.0

[1] Substantially all is Level 2.

Redeemable Noncontrolling Interests

Changes in redeemable noncontrolling interests of consolidated SIPs were as follows:

(in millions) for the three months ended December 31,	2014	2013
Balance at beginning of period	$234.8	$121.8
Net (loss) income	(6.8)	9.4
Net subscriptions	1.0	114.5
Net deconsolidations	(155.0)	(91.9)
Balance at End of Period	$74.0	$153.8

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)	December 31, 2014	September 30, 2014
Receivables	$48.3	$49.8
Investments	196.4	202.0
Total	$244.7	$251.8

The Company's total AUM of non-consolidated VIEs was $40.6 billion at December 31, 2014 and $42.4 billion at September 30, 2014.

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 2014 or the three months ended December 31, 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 December 31, 2014 to provide for any probable losses that may arise from such matters for which the Company could reasonably estimate an amount.

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Other Commitments and Contingencies

At December 31, 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 2014.

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.

Stock and stock unit award activity was as follows:

(shares in thousands)	Shares	Weighted-Average Grant-Date Fair Value
Nonvested balance at October 1, 2014	3,473	$ 48.55
Granted	2,636	55.69
Vested	(525)	41.88
Forfeited/canceled	(123)	41.60
Nonvested Balance at December 31, 2014	5,461	$ 52.80

Total unrecognized compensation cost related to nonvested stock and stock unit awards, net of estimated forfeitures, was $233.7 million at December 31, 2014. This cost is expected to be recognized over a remaining weighted-average vesting period of 2.1 years.

Note 11 – Other Income (Expenses)

Other income (expenses) consisted of the following:

	Three Months Ended December 31,	
(in millions)	2014	2013
Investment and Other Income, Net		
Dividend income	$2.2	$3.1
Interest income	2.0	2.3
Gains (losses) on trading investment securities, net	(3.0)	3.4
Realized gains on sale of investment securities, available-for-sale	4.8	19.6
Realized losses on sale of investment securities, available-for-sale	(0.3)	(0.6)
Income from investments in equity method investees	6.7	24.9
Other-than-temporary impairment of investments	(1.0)	(0.6)
Gains (losses) on investments of consolidated SIPs, net	2.9	(5.3)
Gains from consolidated VIEs, net	5.3	5.7
Foreign currency exchange gains (losses), net	23.3	(10.5)
Other, net	8.8	6.2
Total	51.7	48.2
Interest Expense	(11.3)	(12.6)
Other Income, Net	$40.4	$35.6

Substantially all of the Company's dividend income and realized gains and losses on sale of available-for-sale securities were generated by investments in its non-consolidated SIPs. Interest income was primarily generated by trading investment securities and cash equivalents. Proceeds from the sale of available-for-sale securities were $36.5 million and $125.6 million for the three months ended December 31, 2014 and 2013.

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Net gains (losses) recognized on the Company's trading investment securities that were held at December 31, 2014 and 2013 were $(3.0) million and $1.9 million. Net gains (losses) recognized on trading investment securities of consolidated SIPs that were held at December 31, 2014 and 2013 were $(5.9) million and $10.0 million.

Note 12 – Accumulated Other Comprehensive Income (Loss)

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

(in millions) for the three months ended December 31, 2014	Unrealized Gains (Losses) on Investments	Currency Translation Adjustments	Unrealized Gains (Losses) on Defined Benefit Plans	Total
Balance at October 1, 2014	$31.0	$(143.6)	$(5.1)	$(117.7)
Other comprehensive income (loss) before reclassifications, net of tax	3.0	(61.5)	1.0	(57.5)
Reclassifications to net investment and other income, net of tax	(3.2)	—	—	(3.2)
Total other comprehensive income (loss)	(0.2)	(61.5)	1.0	(60.7)
Balance at December 31, 2014	$30.8	$(205.1)	$(4.1)	$(178.4)

(in millions) for the three months ended December 31, 2013	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	0.9	8.1	(1.3)	7.7
Reclassifications to net investment and other income, net of tax	(10.9)	—	—	(10.9)
Total other comprehensive income (loss)	(10.0)	8.1	(1.3)	(3.2)
Balance at December 31, 2013	$61.9	$(55.1)	$(3.9)	$2.9

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, 2014 (“fiscal year 2014”) 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.

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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, marketing, shareholder servicing, trustee, custody and other fiduciary services. Our SIPs and investment management and related services are distributed or marketed to the public globally under eight 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 three months ended December 31, 2014, the global equity markets experienced volatility but provided positive returns, evidenced by increases of 1% in the MSCI World Index and 5% in the S&P 500 Index. The overall market performance benefited from a continued rally in the U.S. equity markets, but was tempered by ongoing economic growth concerns in Europe and emerging markets, including political uncertainty in Greece. The global bond markets had mixed results during the quarter, with the Barclays Global Aggregate Index decreasing 1% as the Federal Reserve Bank ended its quantitative easing program while interest rates remained low and other central banks continued their accommodative monetary policies. The U.S. dollar continued to strengthen during the quarter, while a sharp decline in oil prices had a negative impact on the energy sector.

Our total AUM at December 31, 2014 was $880.1 billion, 2% lower than at September 30, 2014 and essentially the same as at December 31, 2013. Simple monthly average AUM ("average AUM") for the three months ended December 31, 2014 increased 3% from the same period in the prior fiscal year.

The business and regulatory environments in which we operate globally remain complex, uncertain and subject to change. We are subject to various laws, rules and regulations globally that impose restrictions, limitations and registration, reporting and disclosure requirements on our business and add complexity to our global compliance operations.

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 December 31, 2014	Three Months Ended December 31, 2013	Percent Change
Operating revenues	$2,064.3	$2,109.5	(2)%
Operating income	782.0	813.1	(4)%
Net income attributable to Franklin Resources, Inc.	566.4	603.8	(6)%
Diluted earnings per share	$0.91	$0.96	(5)%
Operating margin[1]	37.9%	38.5%	

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

Operating income decreased $31.1 million for the three months ended December 31, 2014, as compared to the same period in the prior fiscal year, as revenues decreased 2% and operating expenses decreased 1%. AUM was relatively flat year over year, however lower sales resulted in decreases in both revenues and expenses. The expense decrease was largely offset by higher compensation and benefits.

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Net income attributable to Franklin Resources, Inc. decreased $37.4 million for the three months ended December 31, 2014, primarily due to the decrease in operating income.
Diluted earnings per share decreased consistent with the decrease in net income, partially offset by the impact of a 1% decrease in diluted average common shares outstanding primarily resulting from repurchases of shares of our common stock during the twelve-month period ended December 31, 2014.
ASSETS UNDER MANAGEMENT
AUM by investment objective was as follows:

(in billions)	December 31, 2014	December 31, 2013	Percent Change
Equity			
Global/international	$248.5	$260.4	(5)%
United States	113.1	105.3	7%
Total equity	361.6	365.7	(1)%
Hybrid	157.1	147.8	6%
Fixed-Income			
Tax-free	73.2	69.0	6%
Taxable			
Global/international	219.1	231.3	(5)%
United States	62.2	58.7	6%
Total fixed-income	354.5	359.0	(1)%
Cash Management	6.9	6.6	5%
Total	$880.1	$879.1	0%
Average for the Three-Month Period	$894.1	$865.9	3%

AUM at December 31, 2014 was essentially unchanged from December 31, 2013. During the twelve-month period AUM increased by $24.6 billion of market appreciation, which was offset by a $10.3 billion decrease due to the impact of foreign exchange revaluation, $8.1 billion of net new outflows and $5.2 billion of net distributions.
Average AUM increased 3% during the three months ended December 31, 2014 from the same period in the prior fiscal year, as the current-year period began with a higher level of AUM. Average AUM is generally more indicative of trends in revenue for providing investment management and fund administration services than the year-over-year change in ending AUM.
Average AUM and the mix of average AUM by investment objective are shown below.

(in billions)	Average AUM		Percent	Mix of Average AUM	
for the three months ended December 31,	2014	2013	Change	2014	2013
Equity					
Global/international	$255.7	$254.6	0%	29%	29%
United States	112.0	101.8	10%	12%	12%
Total equity	367.7	356.4	3%	41%	41%
Hybrid	158.7	143.1	11%	18%	16%
Fixed-Income					