ICI MUTUAL **PUBLICATION**

ICI Mutual Then and Now

The Enduring Value of an Industry Mutual Insurer

ICIMutual

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The Enduring Value of an Industry Mutual Insurer

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Introduction

About ICI Mutual:

» formed in 1987 by and for members of the Investment Company Institute (the national trade association of the U.S. fund industry)

» created in response to a liability insurance crisis in the commercial insurance marketplace

» insures more than 100 fund groups, which collectively manage over 60% of the fund industry's assets under management

» Financial Strength Rating of "A" (Excellent) from A.M. Best since first year of eligibility (1993)

ICI Mutual Insurance Company, RRG ("ICI Mutual" or the "Company") is an **"industry mutual"** insurer—i.e., an insurer that is owned and governed by its member-insureds, who themselves operate within a specific industry. In this regard, ICI Mutual differs fundamentally from the commercial insurance companies (generally organized as stock companies) with which it competes. As an industry mutual insurer, ICI Mutual is dedicated solely to serving the insurance and risk management needs of registered investment companies ("funds"), fund directors and officers, and fund advisers and their affiliates, providing them with an expert and reliable long-term alternative to the uncertainties and cyclicality to which commercial insurance markets have historically been subject.

Like similar industry mutual insurers operating in other industries (e.g., legal services, health care, higher education), ICI Mutual is structured to provide enduring value to its member-insureds and to its industry. Indeed, it is precisely because of its structure as an industry mutual insurer that the Company is able to provide its member-insureds, and the fund industry as a whole, with numerous tangible protections and benefits that either are unavailable from commercial insurers, or cannot be counted on to be available from commercial insurers on a consistent, long-term basis.

These protections and benefits include:

- **Coverages:** As an industry mutual insurer, the Company *develops and delivers sustainable insurance coverages tailored to address the fund industry's specialized risks.*
- **Claims Handling:** As an industry mutual insurer, the Company *offers prompt and fair-minded claims handling when these risks generate claims.*
- **Capacity and Pricing:** As an industry mutual insurer, the Company *stands ready to provide insurance capacity* to the fund industry through all stages of the insurance market cycle, *at prices that are rationally related to the fund industry's own risks*.
- **Services:** As an industry mutual insurer, the Company *provides fund industry-focused risk management, loss prevention, and insurance-related services* to its member-insureds and to the fund industry as a whole.
- **Self-Governance:** As an industry mutual insurer, the Company *is overseen and governed by its member-insureds*, thereby ensuring that the Company is operated to serve their interests, along with the broader interests of the fund industry.

As the sole industry mutual insurer serving the fund industry, ICI Mutual has for three decades provided its member-insureds with these protections and benefits. Meanwhile, the Company's longstanding presence and high profile in the fund industry insurance market have spurred commercial insurers to improve their own offerings in order to remain competitive, thereby benefiting even those fund groups that do not insure with ICI Mutual.

Today, as in the past, the risks of shareholder litigation, regulatory investigations and enforcement actions, and operational errors remain inseparable from fund industry operations. Fund groups devote substantial time and attention to constructing liability insurance programs to help them address and manage these risks. Constructing such insurance programs requires fund groups to choose among the various insurers operating in the fund industry insurance

Three Decades of Service to the Fund Industry

2017 marked the thirtieth anniversary of ICI Mutual. Today, ICI Mutual remains the U.S. fund industry's leading provider of directors and officers/errors and omissions liability ("D&O/E&O") insurance, independent directors liability ("IDL") insurance, and investment company blanket ("fidelity") bonds. And today, as in the past, more than 100 fund groups, collectively managing over 60% of the fund industry's assets under management, choose to insure with ICI Mutual.

It is a testament to the foresight of ICI Mutual's founders, to the efforts of the many fund group executives and fund independent directors who have served over time on ICI Mutual's Board of Directors, and to the support and loyalty of ICI Mutual's long-time insured fund groups that the Company has become, and remains, an established and enduring feature in the fund industry insurance landscape.

market, and among the various insurance options that these insurers provide. Further complicating the process is this simple fact: until a significant insurance claim arises and an insurer is called upon to respond, the value of the insurer cannot truly be known.

For fund groups, choosing among insurers and insurance options involves making business judgments. As with any business judgments, those responsible for making such selections find it useful to have access to resources that can assist them to evaluate available choices. ICI Mutual has previously published numerous studies (listed in Appendix C, and available at www.icimutual.com) that may be helpful to fund groups in this regard.

This guide, which complements these previous studies, provides a high-level introduction to ICI Mutual, to the distinctive role of industry mutual insurers, and to the value and benefits that ICI Mutual, as an industry mutual insurer, provides to its member-insureds and to the fund industry as a whole. This guide thus provides a different and broader perspective on fund industry insurance and insurance options than is typically available from commercial insurance brokers or from commercial insurers. As such, fund groups may find this guide to be a useful resource as they evaluate their insurance options and reach business judgments on insurance-related matters.

ICI Mutual vs. Commercial Insurers

Factor	Commercial Markets	ICI Mutual
Coverages	• May be variable, depending on insurance market conditions • Coverages often retrofitted from policies used in the broader corporate insurance arena	• Maintains core coverages through insurance market cycles • Coverages crafted to address the fund industry's specialized risks
Claims Handling	• Carrier reputations differ and may change over time	• Has excellent reputation • Has paid over $1 billion in claims since 1987
Capacity and Pricing	• May be variable, depending on insurance market conditions • Appetite and pricing can be influenced by events beyond the fund industry	• Promotes availability of limits and risk-related pricing through all insurance market conditions • Solely focused on fund industry events
Services	• Few direct services • Contact with insurer is intermediated by brokers	• Provides direct assistance on insurance and risk management-related issues • Direct contact with insureds (will also work with brokers)
Self-Governance	• Typically owned by public shareholders • Insureds are not involved in governance	• Owned by member-insureds • Governed and overseen by member-insureds' representatives

Coverages

As an industry mutual insurer, the Company develops and delivers sustainable insurance coverages tailored to address the fund industry's specialized risks.

Industries within a broad economic sector often have certain risks in common. But structural differences between and among industries, and differences in the laws and regulations to which they are subject, also frequently create specialized risks for specialized industries. Such differences can also heighten the susceptibility of specialized industries to risks that may be faced (to a lesser degree) by other industries in the same broad sector. As a result, insurance coverages developed for use in broader economic sectors do not always respond effectively to the insurance needs of specialized industries, and may have limited relevance to their actual risks and claims.

The fund industry's structure—featuring externalized management, legally distinct investment vehicles (i.e., funds), and the pricing of shares at net asset value (in the case of open-end funds)—differs fundamentally from the structure of other industries within the financial services sector. Similarly, the strict statutory and regulatory oversight regime to which the fund industry is subject differs fundamentally from the regimes governing other financial institutions. Stated simply, the fund industry faces numerous risks that are specific to the industry itself, as well as heightened susceptibility to certain risks that are shared with other financial institutions.

The Benefits of an Industry Mutual Insurer

By definition, an industry mutual insurer focuses solely on the risks and insurance needs of the specific industry it serves. An industry mutual insurer is typically professionally staffed by industry specialists. Its insurance coverages are developed with substantial input and assistance from industry experts (including industry representatives serving on the mutual's board of directors). By reason of its detailed and comprehensive knowledge of its industry's operations and claims, an industry mutual insurer is uniquely positioned to analyze and understand its industry's risks, and to craft insurance coverages that are tailored to address these risks and to remain sustainable over time.

The Value of ICI Mutual

Since its formation, ICI Mutual has continuously provided fund groups with core insurance coverages that respond to the key "real world" risks long faced by funds, fund directors and officers, and fund advisers. Meanwhile, ICI Mutual has developed and introduced

ICI Mutual's Core Insurance Products

- **Directors and Officers / Errors and Omissions (D&O/E&O) Liability Policy**
  Protects individual directors and officers and insured companies against the financial impact of judgments, settlements, and legal defense costs incurred in shareholder lawsuits and regulatory investigations, and the costs of correcting certain operational errors.
- **Independent Directors Liability (IDL) Policy**
  Provides comprehensive coverage tailored to address the concerns, and distinct insurance needs, of fund independent directors.
- **Investment Company Blanket (Fidelity) Bond**
  Protects insureds against specified losses caused by employee theft, third-party fraud, and certain other types of events, and meets the basic fidelity bonding requirement for funds under the Investment Company Act of 1940.

(typically, at no additional premium to its insureds) a host of additional coverages to address the industry's new and emerging risks. In recent years, for example, ICI Mutual has introduced enhanced D&O/E&O and IDL insurance protections for fund independent directors, along with specialized D&O/E&O coverages for expenses incurred by insureds in shareholder derivative demand investigations and in claim-related internal corporate investigations. Most recently, ICI Mutual has introduced new D&O/E&O and IDL policy endorsements that address two of the fund industry's key cyber risks (see box below), and is augmenting its fidelity bond to add social engineering coverage and to expand protections for fraudulent phone/electronic transactions.

As an industry mutual insurer, the Company understands and appreciates that there are numerous important differences between and among the risks faced by fund independent directors, by funds themselves (and their "inside" directors and officers), and by fund advisers and their affiliates. The Company designs its coverages to address and respond to these differences.

ICI Mutual has long focused special attention on ensuring robust insurance protections for **fund independent directors** in recognition of their critical role in protecting fund investors and overseeing fund operations. In addition, as a resource for the independent director community, ICI Mutual assists directors in evaluating their risks and exposures, and in reaching informed decisions regarding the purchase of liability insurance coverages for themselves and the funds they serve. More information about coverages and services for fund independent directors, including FAQs, can be found at www.icimutual.com/independent-directors.

A Case Study: Crafting Coverage for Cyber Risks

Events in recent years—including a number of highly publicized cyber incidents outside the fund industry—have fueled increased attention by regulators, fund boards, and fund advisers to cyber risks within the fund industry, and to the programs in place at fund groups to manage these risks. Not surprisingly, the events and the attention have led many fund groups to seek detailed and reliable guidance as to how their D&O/E&O and IDL insurance policies may respond to key cyber risks.

Commercial market D&O/E&O and IDL policies available to fund groups have typically been silent in this regard, leaving uncertainty among fund groups as to the scope of D&O/E&O and IDL coverage that may be available to their funds, fund directors and officers, and fund advisers for such risks. ICI Mutual takes the view that silence is not an answer. To the contrary, ICI Mutual has long believed that insurance policy language should and must evolve to address and to respond to new and emerging fund industry risks. In accordance with this belief, ICI Mutual has introduced detailed new policy endorsements that address two of the fund industry's key cyber risks:

- **Network Security Event Endorsement –** This endorsement specifies the scope of coverage available under the ICI Mutual D&O/E&O and IDL policies for losses that may be incurred by insureds in connection with network security incidents that result in disruption to, or interference with, the ability of insured entities to conduct advisory, shareholder servicing, or other day-to-day investment management operations.

- **Shareholder Data Breach Event Endorsement –** This endorsement specifies the scope of coverage available under the ICI Mutual D&O/E&O and IDL policies for losses that may be incurred by insureds in connection with data breaches involving the unauthorized disclosure, acquisition, or dissemination of confidential information regarding fund shareholders.

Taken together, these endorsements reflect the leading role played by ICI Mutual in addressing the scope of coverage for cyber-related events under fund D&O/E&O and IDL policies. The endorsements provide certainty and guidance to fund groups with regard to the scope of coverage available for these key cyber risks, reduce the potential for misunderstandings or conflicting expectations as to coverage between insurer and insureds, and assist fund groups in evaluating whether to buttress their cyber risk management programs through the purchase of stand-alone "specialty" cyber insurance products in the commercial insurance market.

More information on these endorsements, including detailed FAQs, can be found at www.icimutual.com.

Claims Handling

As an industry mutual insurer, the Company offers prompt and fair-minded claims handling when fund industry risks generate claims.

An insurance policy is a legal contract under which one party (the insured) pays an agreed-upon sum of money (the premium) to the other party (the insurer); in return, the insurer promises to reimburse the insured for designated types of losses that the insured may sustain over a designated future period. As with any contract, both parties (insured and insurer) are best served when there is "contract clarity"—i.e., when the insurance contract is worded to avoid, insofar as possible, uncertainties or ambiguities regarding the types of losses being covered, the policy conditions and limitations that may affect coverage, and the rights and obligations of each party under the policy.

But future events are inherently uncertain, and fund industry risks are inherently complex. It is unrealistic to expect that contract clarity can ever be absolute. When insureds incur losses and their insurers are presented with associated insurance claims, it is inevitable that differences may arise from time to time between insureds and their insurers over policy coverage issues.

The Benefits of an Industry Mutual Insurer

In commercial (stock) insurance companies, owners (shareholders) and insureds (customers) are separate and distinct. This division creates a potential for conflict between their respective economic interests, and can foster corporate cultures that reward confrontational and adversarial attitudes by insurers towards claims-handling issues. Indeed, in the broader professional liability insurance market, it is not uncommon for commercial insurers to engage in lengthy and expensive litigation with their insureds to resolve such issues.

In mutual insurance companies, owners and insureds are one and the same. The closer alignment of their economic interests tends to foster corporate cultures that promote more cooperative and collaborative postures by mutual insurers towards claims-handling issues. In the case of industry mutual insurers—where insureds tend to present similar risks, to share similar policy wordings, and to know (and communicate with) one another—confrontational and adversarial postures towards claims-handling issues are uncommon. Indeed, for industry mutual insurers, such postures may have noticeable and damaging reputational effects and undercut the industry loyalty and support on which industry mutual insurers rely for their continued existence.

Types of Significant Fund Industry Claims

Regulatory Claims (e.g., by the SEC)

- Formal and informal investigations
- Administrative proceedings/lawsuits

Private (Shareholder) Claims

- Shareholder class action/derivative lawsuits (often initiated by the plaintiffs' bar)
- Institutional investor claims

Costs of Correction Claims

- Operational errors by insured advisers/service providers

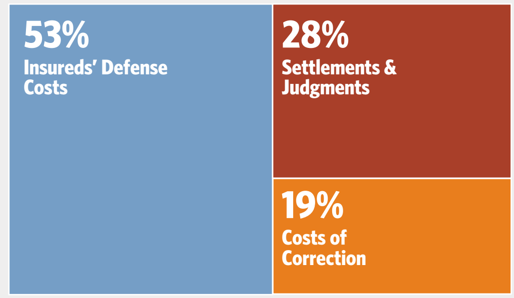
The Value of ICI Mutual

Over the past thirty years, ICI Mutual has paid more than one billion dollars to compensate insured fund groups for losses they have incurred in shareholder litigation, regulatory investigations and enforcement actions, "costs of correction" claims, and other insured matters. Nearly 90% of this total represents payments on matters initiated since 2000, and multimillion dollar insurance claim payments have been common.

ICI Mutual's claims resolutions with its insureds have not always been free of disagreement. But the scores of difficult and complex insurance claims presented to ICI Mutual this century have thus far been amicably resolved, without insurance coverage litigation, and to the satisfaction of all concerned. This is a testament to the Company's emphasis on contract clarity, to its claims handling philosophy and practices, to its long-standing relationships with its insureds and reinsurance partners, and to its deep understanding of its industry. More fundamentally, this is a testament to the value that the Company, as an industry mutual insurer, provides to the fund industry it serves.

ICI Mutual – Over $1 Billion in D&O/E&O Claims Paid

As of December 31, 2017



Payments by ICI Mutual on D&O/E&O Claims

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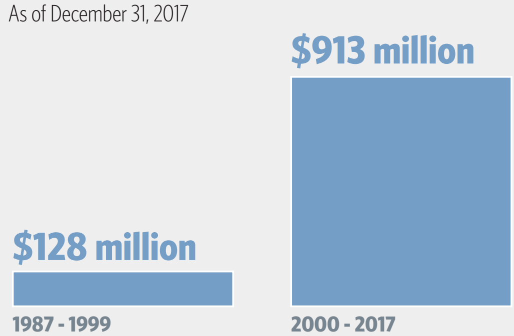
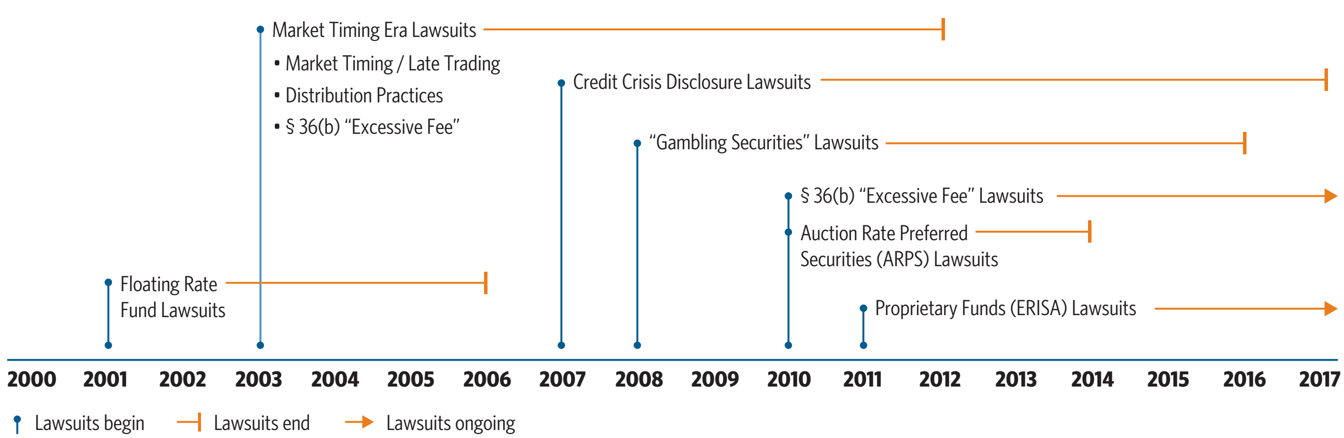


The Plaintiffs' Bar and the Fund Industry

The 21st century has witnessed a series of concerted attacks on the fund industry by the "plaintiffs' bar"—a term commonly used to describe the entrepreneurial cadre of lawyers and law firms who specialize in designing and prosecuting lawsuits against corporate defendants. Since the year 2000, by ICI Mutual's count, the plaintiffs' bar has launched at least seven distinct "waves" of attacks against the fund industry, with each wave marked by substantially similar lawsuits filed against multiple fund groups. These lawsuits have frequently lasted for many years, generating multimillion dollar defense costs for the fund groups involved, and in some cases have resulted in the payment of seven, eight, and even nine-figure settlements.



Capacity and Pricing

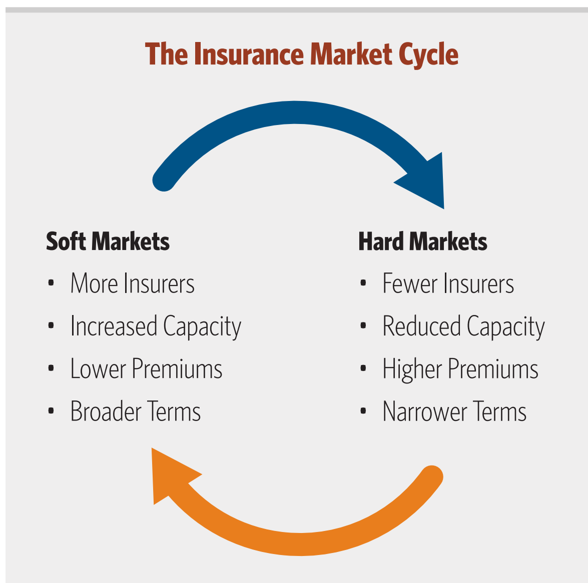
As an industry mutual insurer, the Company stands ready to provide insurance capacity to the fund industry through all stages of the insurance market cycle, at prices that are rationally related to the fund industry's own risks.

Like other lines of commercial insurance, professional liability insurance has long been subject to **the insurance market cycle**—a cycle characterized by swings over time between "soft markets" and "hard markets." Thirty years ago, in the midst of a severe dislocation in this cycle—a dislocation in which the liability insurance market hardened to the point of creating a full-scale insurance crisis—the U.S. fund industry acted collectively to create ICI Mutual. (See Appendix A.) The formation of ICI Mutual represented a direct and forceful response to two fund industry insurance needs that commercial insurers were unable or unwilling to meet: the need for a stable, long-term source of substantial insurance capacity (supply); and the need for insurance pricing that could be counted upon to be reliably and rationally related to the fund industry's own risks.

The Benefits of an Industry Mutual Insurer

An industry mutual insurer, by definition, is dedicated solely to its specific industry and remains committed to insuring its industry continuously and over the long term. Unlike a commercial insurer, an industry mutual insurer has no incentive to reduce (or to terminate) its commitment to its industry in response to changes in the industry's risk profile or to changes in the insurer's own strategic direction. A strong industry mutual insurer thus helps to stabilize the insurance market in which it operates, and to temper the impact on its insureds of the volatility (in insurance capacity and cost) that marks the insurance market cycle.

Indeed, the simple existence of a strong industry mutual insurer—particularly in a relatively small and specialized insurance segment like the fund industry insurance market (See Appendix B)—can affect the behavior of commercial insurers so as to have a stabilizing effect on the availability and pricing of insurance for an industry. An industry mutual insurer can thus benefit even those insureds within an industry who do not insure through the mutual but instead choose to insure through commercial insurers.



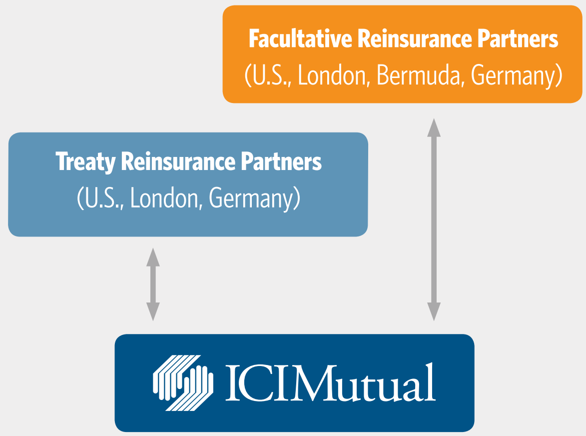
The Value of ICI Mutual

Over the past three decades, ICI Mutual has provided the fund industry with a consistent and readily available source of insurance capacity, at prices reliably and rationally related to the fund industry's own risks. ICI Mutual has remained committed to providing such capacity and pricing even through extraordinary periods—e.g., the market timing/late trading period, the credit crisis period, and the "excessive fee" litigation period—that have generated high frequency/high severity claims for the fund industry and associated high frequency/high severity insurance losses for insurers operating in the fund industry insurance market.

One can only speculate how commercial insurers might have responded during these periods had ICI Mutual never been formed, and to what extent the fund industry insurance market might have been disrupted or otherwise affected. But it is logical to conclude that ICI Mutual, by reason of its existence and its leading role in the fund industry insurance market, has exerted a positive and stabilizing influence on insurance supply and pricing—not only for its own insured fund groups, but for the entire fund industry.

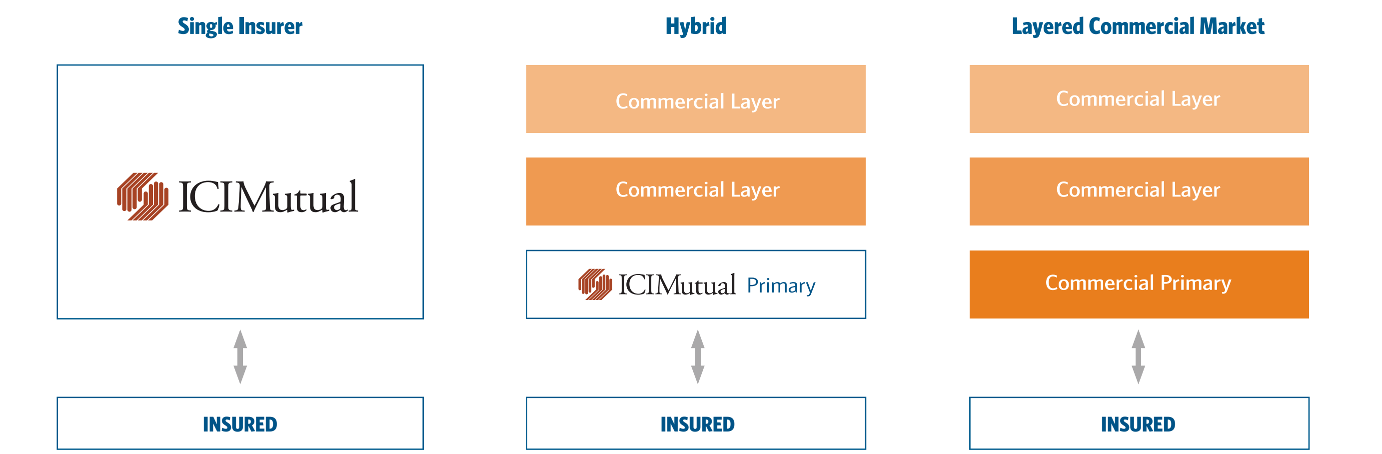
The Role of Reinsurance

Like a number of other industry mutual insurers serving other industries, ICI Mutual utilizes a strong network of highly rated reinsurance partners to manage and diversify its own risk. These reinsurance arrangements enable ICI Mutual to provide the full limits of coverage required by its member-insureds, and to promote relative stability of premium rates and coverage terms for both member-insureds and the fund industry as a whole.



Options for Structuring Liability Insurance Programs

Fund groups have three basic options in structuring their liability insurance programs. Some fund groups choose a "single insurer" or "hybrid" structure utilizing ICI Mutual, whereas others choose a "layered commercial market" structure utilizing only commercial insurers. In addition, many fund groups choose to augment their D&O/E&O programs with IDL insurance (also available from ICI Mutual). These choices ultimately involve business judgments. Discussions of factors that fund groups may wish to consider in reaching such judgments are included in ICI Mutual's studies entitled *Mutual Fund D&O/E&O Insurance* and *Independent Director Liability (IDL) Insurance*, both available at www.icimutual.com.



Services

As an industry mutual insurer, the Company provides fund industry-focused risk management, loss prevention, and insurance-related services to its member-insureds and to the fund industry as a whole.

Outside the claims process, commercial insurance companies operating in the financial services sector have little direct contact with their insureds. Instead, the relationships between commercial insurers and their insureds are intermediated. Commercial insurers typically do not advise their insureds directly regarding their insurance options or respond to insurance-related questions. Similarly, commercial insurers do not typically provide direct assistance to their insureds in identifying and managing risks or in preventing or mitigating claims.

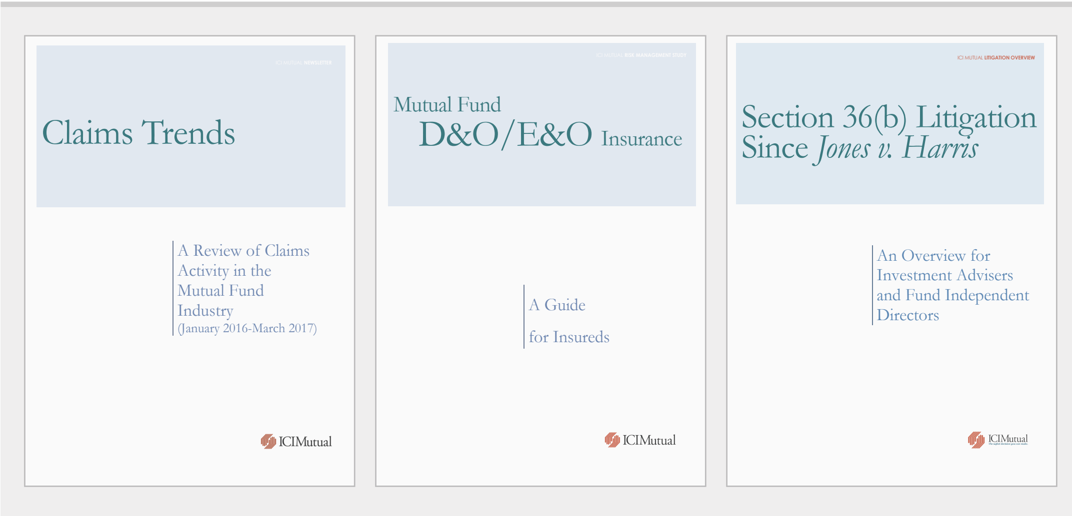
The Benefits of an Industry Mutual Insurer

By definition, an industry mutual insurer is a collective that focuses solely on the risks and associated insurance concerns of a particular industry. As a membership organization, an industry mutual insurer promotes and encourages direct contact between its professional staff and its member-insureds—not only during the underwriting and claims adjustment processes, but throughout the entire period that insurance policies are in force. Member-insureds often develop deep ongoing ties with their industry mutual's management and professional staff, and regularly turn to them for assistance and advice on a broad array of insurance-related needs. By reason of an industry mutual insurer's specialization and detailed understanding of its industry's risks and claims, it is also in a unique position to serve as a provider of—and a clearinghouse for—industry-specific risk management and loss prevention services and advice.

The Value of ICI Mutual

ICI Mutual has long provided its member-insureds and the fund industry with a wide variety of insurance, loss prevention, and risk management-related services. The Company's staff regularly provides individualized assistance to fund groups in reaching business judgments on structuring insurance programs, selecting among insurance options, and establishing appropriate insurance limits. The Company's staff also regularly responds to requests from fund boards, outside counsel, and in-house personnel for presentations, written materials, and informal advice on claims and insurance-related issues and developments.

The Company's staff participates in numerous industry conferences and events (moderating panels and providing an insurer's perspective on fund industry risks and claims), and hosts its own annual conference for industry risk management personnel. The Company also maintains an interactive website (the *Litigation Notebook*) offering real-time information on litigation and enforcement actions affecting the fund industry, and develops and distributes newsletters (including an annual *Claims Trends*) and detailed studies on industry risk management issues. (ICI Mutual's Risk Management Studies are listed in Appendix C.)



These services are provided by ICI Mutual at no cost, and in most instances are made available even to fund groups that do not insure with ICI Mutual. In assisting fund groups to better understand existing, new, and developing risks that may generate claims, and how different types of insurance structures and products may assist in managing these risks, ICI Mutual serves the interests of its member-insureds as well as the broader fund industry.

The Role of Brokers in the Fund Industry Insurance Market

ICI Mutual is the only insurer in the fund industry insurance market that distributes and administers its insurance products directly. D&O/E&O policies, IDL policies, and fidelity bonds issued by commercial insurers are distributed and administered through professional insurance brokers, who serve as third-party intermediaries between commercial insurers and their insureds.

Insurance brokers do not themselves accept or bear any portion of the financial risks that are transferred by fund groups to insurers via the issued insurance products. Rather, broker intermediaries seek to facilitate the process by which these commercial insurance products are made available and sold to fund groups. Brokers are typically compensated through commissions paid by commercial insurers and/or on a "fees for services" basis by their clients. (ICI Mutual does not pay commissions to insurance brokers.)

In the fund industry insurance market, broker intermediaries are also often called upon to assist where fund groups require overall insurance limits in excess of amounts available from their primary (first-level) insurance carriers; in such cases, the broker intermediaries assist the fund groups in constructing "towers" of professional liability or fidelity bond coverage on which multiple insurers participate. In addition, brokers frequently assist fund groups in understanding the range of pricing and coverage available from commercial insurers, and may provide advice on other client-specific insurance issues.

The individual insurance brokers who assist fund groups are typically employed by brokerage firms. In today's fund industry insurance market, a handful of brokerage firms serve the great majority of fund groups. The fund industry-specific experience and expertise of the individual brokers employed by these brokerage firms, and of the brokerage firms themselves, varies. In many cases, however, these firms have considerable institutional experience in assessing and placing professional liability and bond insurance for financial institutions generally, if not always in the more specialized and arcane area of assessing and placing D&O/E&O, IDL, and fidelity bond insurance for fund groups.

Self-Governance

As an industry mutual insurer, the Company is overseen and governed by its member-insureds, thereby ensuring that the Company is operated to serve their interests, along with the broader interests of the fund industry.

In commercial (stock) insurance companies, there can be a conflict—or at least a strong tension—between the shorter-term economic interests of company owners (shareholders) and the longer-term economic interests of company insureds (policyholders). The fact that shares of commercial insurance companies are frequently traded on stock exchanges may add to the tension, by increasing the pressure on such companies to achieve short-term profit targets. The boards of directors and professional managers of commercial insurance companies face this tension in governing their companies, and in seeking to strike an appropriate balance between the respective economic interests of owners and insureds.

The Benefits of an Industry Mutual Insurer

In an industry mutual insurance company, owners and insureds are one and the same. This "mutual" structure reduces the potential for a conflict between the economic interests of owners and insureds. An industry mutual insurer is also self-governed. Its member-insureds exercise voting rights in corporate governance matters, including in the election of the industry mutual insurer's directors (who themselves are typically representatives of member-insureds or otherwise associated with the member-insureds' industry).

To assure quality of service and to preserve appropriate confidentiality for member-insureds, an industry mutual insurer's board of directors often delegates day-to-day responsibilities for

Mutual vs. Stock Insurers

Most insurance companies take one of two basic organizational forms. **Mutual insurance companies** are owned by their insureds (policyholders). This defining organizational feature differentiates mutuals from **stock insurance companies**, which are typically owned by public investors (shareholders). Both forms of insurance company—mutual and stock—date back hundreds of years in America. (In 1752, Benjamin Franklin helped found a Philadelphia-based mutual insurer that continues in operation today.) Both forms remain common in today's property and casualty insurance market.

Policyholders of an insurance company tend to be primarily concerned with the nature, quality, and cost of the company's insurance products, its claims-handling reputation, and its services. In contrast, **shareholders** of an insurance company tend to be primarily concerned with the financial return on their investment (profits and dividends). As a result, and as explored in a number of academic and economic studies, there can be a conflict—or at the very least, a strong tension—in stock insurance companies between the short-term financial demands of company shareholders and the long-term interests of company policyholders. This potential for conflict between the economic interests of owners (shareholders) and insureds (policyholders) is reduced in mutual insurance companies, given their merger of owner and insured. For this reason, among others, mutuals are often viewed as more oriented towards their insureds, more focused on long-term over short-term results, and more committed to their lines of business than are stock insurance companies.

underwriting and claims decisions to a professional staff with experience and expertise in its industry's particular risks and claims. But the board sets strategic direction for its industry mutual insurer, and provides oversight and advice on development of new coverages and other important company initiatives. This self-governance feature helps to ensure that an industry mutual insurer is operated to serve the interests (short and long-term) of its member-insureds, along with the broader interests of its industry.

The Value of ICI Mutual

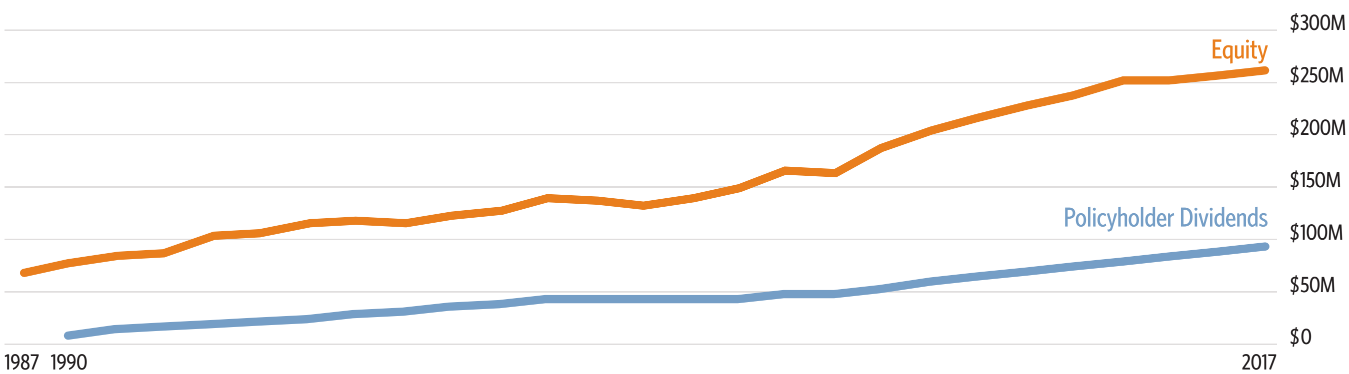
ICI Mutual was formed in 1987 under the auspices of the Investment Company Institute, the national trade association of the U.S. fund industry. Both classes of ICI Mutual's members—i.e., "Participating" and "Non-Participating" members—enjoy voting rights on governance matters, including rights to elect ICI Mutual's Board of Directors. ICI Mutual's Board comprises up to 25 directors at any given time, the great majority of whom serve simultaneously as senior executives or fund independent directors with ICI Mutual's insured fund groups.

The Board has long provided ICI Mutual with an invaluable source of fund industry expertise and experience; over the years, more than 120 individuals, associated with five dozen different member fund groups (including some fund groups that have since combined with others), have served on the ICI Mutual Board. The dedication and involvement of ICI Mutual's directors have been critical to its success, and to its ability to adhere to the mission envisioned by its founders—i.e., to provide funds, their directors and officers, and advisers with an expert and reliable alternative to the uncertainties and historical cyclicality of the commercial insurance markets.

Financial-Related Benefits of Membership in an Industry Mutual Insurer

In addition to the long-term insurance-related benefits that their memberships provide (e.g., stable coverages and pricing, prompt and fair-minded claims handling), members of industry mutual insurers can (and often do) receive certain financial-related benefits. Most tangibly, members may receive policyholder dividends, which serve to lower their total cost of insurance.

Participating members of ICI Mutual are eligible to receive policyholder dividends. Such dividends (totaling nearly $100 million over the life of the Company) have been declared in each of the past nine years and in 23 of the Company's 30 years of existence. Meanwhile, as a mark of the Company's financial strength and stability, equity has grown to over $250 million.



Appendix A

A Short History of ICI Mutual

The 1970s

By the 1970s, the fund industry's need for, and reliance on, financial institution (fidelity) bonds and D&O/E&O insurance was firmly established. At the same time, however, the fund industry was facing problems in meeting its bond and D&O/E&O insurance needs through commercial insurance markets. In 1970 and again in 1979-80, the Investment Company Institute ("ICI"), the national trade association for the U.S. fund industry, conducted studies of the industry's insurance problems. The results of the two ICI studies were consistent: investment companies were paying high premiums, were experiencing relatively few losses, and were frequently unable to obtain appropriate or sufficient insurance coverage from commercial insurers.

The Mid-1980s

The fund industry's insurance problems intensified in the 1980s. A nationwide liability insurance crisis in the mid-1980s—a crisis which has been described as "the most extreme event in the U.S. liability insurance market since industry wide data have been collected"—led to (1) a dramatic increase in premiums charged by commercial insurance companies for numerous types of liability insurance products, (2) reductions by these companies in insurance limits and scope of coverage, and (3) a refusal by some of these companies to provide coverage for certain risks at any price.

The causes of the crisis remain a subject of debate. But even at the time, the impact on the fund industry was all too clear. Many funds experienced premium rate increases from commercial markets of 300 to 500 percent. (In one instance, a 1000 percent increase was reported.) Certain funds saw their coverage canceled, notwithstanding that they had never reported an insurance claim. In 1985-86, the ICI again studied the insurance problems facing the fund industry. The results were consistent with those of the ICI's earlier studies: high premiums, relatively few losses, and a frequent inability of funds to obtain appropriate or sufficient insurance coverage from commercial insurers.

The Late 1980s

The insurance crisis in the 1980s vividly illustrated the threat to the fund industry of relying solely on the uncertainties of commercial insurance markets to meet the bonding and professional liability insurance needs of funds, their directors and officers, and their investment advisers. In response to the crisis and to the ongoing refusal of the commercial insurance markets to respond to the industry's specialized needs, the ICI's Board of Governors and its Executive Committee in 1987 authorized the establishment of ICI Mutual Insurance Company as a fund-industry owned and operated insurer that would be dedicated solely to serving the interests of the fund industry. After appropriate regulatory relief was secured from the U.S. Securities and Exchange Commission and sufficient commitments of financial support were obtained from prospective insured fund groups, ICI Mutual issued its first bonds and policies in 1988.

By 1989, ICI Mutual, operating under the oversight of its own Board of Directors (comprising representatives selected from among ICI Mutual's member-insured fund groups), was issuing bonds and policies to more than 100 fund groups. That same year, ICI Mutual entered into a reinsurance arrangement with one of the world's leading reinsurance markets, Lloyd's of London. This initial reinsurance arrangement proved to be the first of many such arrangements that ICI Mutual would enter into over the following decades with a large number of highly rated reinsurers. These arrangements have permitted ICI Mutual to prudently diversify its own risk and to make "one-stop insurance purchasing" a reality for its insured fund groups and for the fund industry at large.

The 1990s

The seven-fold growth in the fund industry's assets under management during the 1990s spurred a dramatic increase in the insurance limits required by individual fund groups. At the same time, the increasing reliance by the fund industry on computers and the Internet was creating new fraud-related risks, and by the end of the decade, the plaintiffs' bar was beginning to emerge as a significant threat to the industry. In response to these developments, ICI Mutual greatly expanded the dollar amount of D&O/E&O and bond limits available to its member-insureds (while continuing to diversify its own risk through entry into reinsurance arrangements with an array of highly rated reinsurance partners), and crafted various industry-specific coverages to address the industry's rapidly evolving fraud and litigation-related risks (including enhanced liability insurance protections for fund independent directors).

Meanwhile, under the oversight of its Board of Directors, ICI Mutual adhered to a philosophy of conservative financial management. In 1993, in its first year of eligibility, ICI Mutual secured an "A" (Excellent) Financial Strength Rating from A.M. Best (which rating has been continuously retained over the years since). ICI Mutual's financial strength—surplus (equity) tripled during the decade—positioned the Company to institute a series of annual dividends for qualifying member-insureds (i.e., "Participating" members). (See "Financial-Related Benefits of Membership in an Industry Mutual Insurer," at p. 13.)

The 2000s

The 2000s proved to be an extraordinary decade for fund industry claims. Severe scrutiny of the industry by state and federal regulators and by the plaintiffs' bar—scrutiny ignited by the market timing scandal and refueled by the credit crisis—spawned scores of regulatory investigations, regulatory enforcement actions, and shareholder lawsuits involving fund industry entities and individuals. (See "The Plaintiffs' Bar and the Fund Industry," at p. 7.) Claims initiated during the ten-year period ultimately resulted in over $600 million in insurance payments being made by ICI Mutual to more than fifty insured fund groups; more than $400 million of this total represented payments made by ICI Mutual to reimburse fund advisers, fund directors, and funds themselves for their legal defense costs. ICI Mutual's steadfast support of these defense efforts assisted not only its affected member-insureds, but also the fund industry as a whole. The many positive, industry-specific judicial decisions issued by both trial and appellate courts over the course of the decade will likely help guide courts in adjudicating claims against the fund industry for many years to come, and should thereby continue to contribute to a more predictable claims environment for the fund industry going forward.

Whether measured by frequency or severity, the fund industry's claims activity in the 2000s had no historical precedent. ICI Mutual's emergence from the decade with a (then) record level of surplus, with its A.M. Best "A" rating intact, and with continued strong support from its many reinsurance partners, evidenced the resiliency of ICI Mutual's "industry mutual insurer" model, and underscored ICI Mutual's leadership role among fund industry insurers.

The 2010s

The 2010s have witnessed, among other things, increased concerns in the fund industry over potential regulatory and legal exposures faced by fund independent directors in fund-related proceedings, as well as over renewed efforts by the plaintiffs' bar to utilize a unique provision of the Investment Company Act of 1940 to attack advisory fees charged by fund advisers. ICI Mutual has responded quickly and forcefully to these concerns, by introducing (at no extra cost) special insurance policy enhancements for fund independent directors (see p. 5); by publishing relevant litigation and insurance-related studies; by presenting on these issues to fund boards and advisers, and at industry conferences and events; and most importantly, by continuing to encourage and pay for thorough and aggressive defense efforts by member-insureds targeted in such matters.

Meanwhile, ICI Mutual has remained committed to developing innovative and sustainable insurance coverage enhancements to address other new and evolving industry risks, including those that are cyber-related (see p. 5). As it enters its fourth decade of service as an industry mutual insurer to the fund industry, ICI Mutual is well positioned to utilize its specialized focus and unmatched industry knowledge and expertise to meet the challenges that lie ahead.

Appendix B

Today's Fund Industry Insurance Market

A Small and Specialized Market

Notwithstanding the fund industry's exponential growth in assets under management since the 1980s, the market for fund industry insurance remains relatively small by insurance standards. Business insurance products are commonly secured on a fund group-wide basis, rather than by individual funds; today, perhaps 250 fund groups generate the vast majority of annual D&O/E&O, IDL, and fidelity bond insurance premiums in the fund industry. Even so, the collective annual premiums generated by these 250 fund groups represent less than 1% of the annual insurance premiums generated in the broader professional liability and fidelity bond insurance markets, respectively, and a far smaller percentage of the annual premiums generated within the U.S. property and casualty insurance market as a whole.

The fund industry insurance market also remains highly specialized. There are numerous fundamental differences (structural, regulatory, and operational) between fund groups, on the one hand, and other types of companies (including other types of financial institutions), on the other. Given these differences, it follows that there are likewise numerous fundamental differences between the insurable risks, insurance needs, and insurance claims of fund groups and those of other types of companies. Most fund groups have grown to expect that their insurers—and especially the insurers who provide them with "primary" (i.e., first level) professional liability insurance coverage—will demonstrate a sophisticated understanding of these differences in evaluating (i.e., underwriting) the risks presented by individual fund groups, in developing policy wordings for fund industry insurance products, and in responding to the fund industry's insurance claims.

Given the limited size and high degree of sophistication of the fund industry insurance market, it is not surprising that a relatively small number of insurers—ICI Mutual and four or five commercial insurers—write the overwhelming majority of the primary D&O/E&O policies, IDL policies, and fidelity bonds that are purchased by the top 250 fund groups. ICI Mutual and commercial insurers in this market seek to differentiate themselves in various areas, including (1) scope and sophistication of their coverages, (2) claims-handling reputation and expertise, (3) fund industry knowledge and expertise, (4) long-term commitment to the fund industry insurance market, (5) product pricing, (6) nature and scope of non-claims services provided, and (7) timeliness of product issuance and general responsiveness to requests by insureds. Different fund groups find these different criteria to be of greater or lesser importance in their selection of insurers, depending on their individual risk management needs, overall risk tolerance, sensitivity to cost, and other factors.

Over the past three decades, new insurers have from time to time sought to enter the market for primary fund industry insurance, even as others have left. The insurers who have competed most effectively in the market for primary fund industry insurance are those, like ICI Mutual, who have recognized the market's distinctive nature, who have demonstrated their commitment to remaining in the market over the long term, and who have developed the expertise and resources to understand and address—through their insurance product language, claims handling, and other services—the specific interests and specialized insurance needs of fund industry insureds.

Meanwhile, many more insurers are involved in providing fund groups with "excess" insurance (i.e., insurance limits that supplement the limits provided by, and that mirror the terms and conditions of, underlying primary policies and bonds). It is not uncommon for new insurers to seek to enter the market for excess fund industry insurance, particularly during periods of abundant insurance capacity (i.e., insurance supply available to meet demand). Because excess insurance is sometimes viewed as a commodity by both insureds and insurers (as well as by insurance brokers), and because the market for excess insurance has relatively low barriers to entry, periods of abundant insurance capacity can attract excess insurers with little or no institutional experience or expertise in the area of fund industry risks or claims, who compete primarily on price (i.e., premium).

Appendix C

ICI Mutual’s Risk Management Studies

2016	Section 36(b) Litigation Since *Jones v. Harris*
2015	Shareholder Authentication
2014	Trends in Fee Litigation
2013	Independent Directors Liability (IDL) Insurance
2012	Risk Management in the Digital Age
2011	Managing Operational Risks of Private Accounts
2010	ERISA Liability
2010	Mutual Fund Prospectus Liability
2009	Mutual Fund D&O/E&O Insurance
2008	Outsourcing by Advisers and Affiliated Service Providers
2008	Managing Risks in Trade Allocation
2007	What to Expect in the Claims Process
2007	Preparing for a Pandemic
2006	The Two Faces of Identity Theft
2006	Independent Director Litigation Risk
2006	Fair Valuation Study – The Role of the Board (with ICI/IDC)
2005	Fair Valuation Study – An Introduction (with ICI/IDC)
2004	Managing Defense Costs
2003	Computer Security Lite
2002	Understanding Bond Fund Risks
2002	Investment Management Compliance Risks
2001	Managing Risk in Processing Corporate Actions

Copies of ICI Mutual’s Risk Management Studies are available at ICI Mutual’s website (www.icimutual.com).

ICI Mutual

ICI Mutual is the predominant provider of D&O/E&O liability insurance and fidelity bonding for the U.S. fund industry. Its insureds represent more than 60% of the industry's managed assets. As the fund industry's dedicated insurance company, ICI Mutual is owned and operated by and for its insureds. ICI Mutual's services assist insureds with identifying and managing risk and defending regulatory enforcement proceedings and civil litigation.

ICI Mutual also serves as a primary source of industry information regarding fund industry insurance coverage, claims, risk management issues, and litigation developments. Publications include an extensive library of risk management studies, the online *Litigation Notebook*, and the annual *Claims Trends* newsletter. Additional services include peer group profiles, coverage analyses, and assistance to insureds and their counsel in litigation defense.

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