Annual report to contract holders for the twelve months ended December 31, 2010

# ANNUAL REPORT

## FOR CONTRACT HOLDERS OF SCUDDER DESTINATIONS℠

**AIM Variable Insurance Funds (Invesco Variable Insurance Funds)**

**The Alger Portfolios (formerly The Alger American Fund)**

**Credit Suisse Trust**

**Dreyfus Investment Portfolios**

**The Dreyfus Socially Responsible Growth Fund, Inc.**

**DWS Investments VIT Funds**

**DWS Variable Series I**

**DWS Variable Series II**

# DWS VARIABLE SERIES II

## SUPPLEMENT TO THE CURRENTLY EFFECTIVE PROSPECTUSES AND SUMMARY PROSPECTUSES OF EACH OF THE LISTED FUNDS:

DWS Mid Cap Growth VIP

DWS Strategic Value VIP

DWS Turner Mid Cap Growth VIP

The Board of each fund noted above has approved a proposal by Deutsche Investment Management Americas Inc. ("DIMA"), the advisor of each fund, to effect the following fund reorganizations or "mergers":

| Acquired Funds | Acquiring Funds |
|---|---|
| DWS Variable Series II — DWS Mid Cap Growth VIP | DWS Variable Series II — DWS Small Cap Growth VIP |
| DWS Variable Series II — DWS Strategic Value VIP | DWS Variable Series II — DWS Large Cap Value VIP |
| DWS Variable Series II — DWS Turner Mid Cap Growth VIP | DWS Variable Series II — DWS Small Cap Growth VIP |

The mergers are expected to occur on or about May 1, 2011 and they are expected to be tax-free reorganizations for federal income tax purposes. Completion of each merger is subject to a number of conditions. On the merger date, an investment in each Acquired Fund will, in effect, be exchanged for an investment with an equal aggregate net asset value in the corresponding Acquiring Fund. Therefore, as a result of the mergers, shareholders of each Acquired Fund will become shareholders of the corresponding Acquiring Fund. You can find information about each Acquiring Fund and its risks, including a prospectus and summary prospectus, online at www.dws-investments.com/vipros. You can also get this information at no cost by e-mailing a request to inquiry.info@dws.com, calling (800) 728-3337 or by contacting your insurance company.

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# DWS VARIABLE SERIES I
# DWS VARIABLE SERIES II

**SUPPLEMENT TO THE CURRENTLY EFFECTIVE PROSPECTUSES AND SUMMARY PROSPECTUSES OF EACH OF THE LISTED FUNDS:**

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DWS Health Care VIP

DWS Technology VIP

The Board of each fund noted above has approved a proposal by Deutsche Investment Management Americas Inc. ("DIMA"), the advisor of each fund, to effect the following fund reorganizations or "mergers":

| Acquired Funds | Acquiring Fund |
|---|---|
| DWS Variable Series I — DWS Health Care VIP | DWS Variable Series I — DWS Capital Growth VIP |
| DWS Variable Series II — DWS Technology VIP | DWS Variable Series I — DWS Capital Growth VIP |

Completion of each merger is subject to a number of conditions, including approval by shareholders of the applicable Acquired Fund at a shareholder meeting expected to be held during the month of April, 2011. Prior to the shareholder meeting, with respect to shares of the Acquired Funds owned as of the record date for the shareholder meeting, each contract owner and their insurance company will receive: (i) a proxy statement/prospectus describing in detail the proposed merger and the Board's considerations in recommending that shareholders approve the merger; and (ii) a prospectus for the Acquiring Fund. Each such contract owner will also receive a voting instruction form and instructions on how to submit their voting instructions to their insurance company. The contract owner's insurance company, as shareholder, will actually vote the shares corresponding to the contract owner's investment (likely by executing a proxy card) once it receives voting instructions.

If shareholder approval is obtained, the mergers are expected to occur on or about May 1, 2011 and are expected to be tax-free reorganizations for federal income tax purposes. On the merger date, an investment in each Acquired Fund will, in effect, be exchanged for an investment with an equal aggregate net asset value in the Acquiring Fund. Therefore, as a result of the mergers, shareholders of each Acquired Fund will become shareholders of the Acquiring Fund. You can find information about the Acquiring Fund and its risks, including a prospectus and summary prospectus, online at www.dws-investments.com/vipros. You can also get this information at no cost by e-mailing a request to inquiry.info@dws.com, calling (800) 728-3337 or by contacting your insurance company.

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# SUPPLEMENT TO THE CURRENTLY EFFECTIVE PROSPECTUSES:

Cash Account Trust
- Government & Agency Securities Portfolio
- Money Market Portfolio
- Tax-Exempt Portfolio

Cash Management Fund Institutional

Cash Reserve Fund, Inc.
- Prime Series

Cash Reserves Fund Institutional

Daily Assets Fund Institutional

DWS Alternative Asset Allocation Plus Fund

DWS Balanced Fund

DWS Blue Chip Fund

DWS California Tax–Free Income Fund

DWS Capital Growth Fund

DWS Climate Change Fund

DWS Communications Fund

DWS Core Fixed Income Fund

DWS Core Plus Income Fund

DWS Disciplined Market Neutral Fund

DWS Diversified International Equity Fund

DWS Dreman International Value Fund

DWS Dreman Mid Cap Value Fund

DWS Dreman Small Cap Value Fund

DWS EAFE® Equity Index Fund

DWS Emerging Markets Equity Fund

DWS Emerging Markets Fixed Income Fund

DWS Enhanced Commodity Strategy Fund

DWS Equity 500 Index Fund

DWS Floating Rate Plus Fund

DWS Global Bond Fund

DWS Global Inflation Plus Fund

DWS Global Small Cap Growth Fund

DWS Global Thematic Fund

DWS GNMA Fund

DWS Gold & Precious Metals Fund

DWS Growth & Income Fund

DWS Health Care Fund

DWS High Income Fund

DWS High Income Plus Fund

DWS Intermediate Tax/AMT Free Fund

DWS International Fund

DWS Large Cap Focus Growth Fund

DWS Large Cap Value Fund

DWS Latin America Equity Fund

DWS LifeCompass 2015 Fund

DWS LifeCompass 2020 Fund

DWS LifeCompass 2030 Fund

DWS LifeCompass 2040 Fund

DWS LifeCompass Retirement Fund

DWS Lifecycle Long Range Fund

DWS Managed Municipal Bond Fund

DWS Massachusetts Tax-Free Fund

DWS Mid Cap Growth Fund

DWS Money Market Prime Series

DWS Money Market Series

DWS New York Tax-Free Income Fund

DWS RREEF Global Infrastructure Fund

DWS RREEF Global Real Estate Securities Fund

DWS RREEF Real Estate Securities Fund

DWS S&P 500 Index Fund

DWS S&P 500 Plus Fund

DWS Select Alternative Allocation Fund

DWS Short Duration Fund

DWS Short Duration Plus Fund

DWS Short-Term Municipal Bond Fund

DWS Small Cap Core Fund

DWS Small Cap Growth Fund

DWS Strategic Government Securities Fund

DWS Strategic High Yield Tax-Free Fund

DWS Strategic Income Fund

DWS Strategic Value Fund

DWS Target 2011 Fund

DWS Target 2012 Fund

DWS Target 2013 Fund

DWS Target 2014 Fund

DWS Technology Fund

DWS U.S. Bond Index Fund

DWS Variable NAV Money Fund

DWS World Dividend Fund

Investors Cash Trust
- Treasury Portfolio

NY Tax Free Money Fund

Tax Free Money Fund Investment

Tax-Exempt California Money Market Fund

**DWS Variable Series I:**

DWS Bond VIP

DWS Capital Growth VIP

DWS Global Opportunities VIP

DWS Growth & Income VIP

DWS Health Care VIP

DWS International VIP

**DWS Variable Series II:**

DWS Alternative Asset Allocation Plus VIP

DWS Balanced VIP

DWS Blue Chip VIP

DWS Core Fixed Income VIP

DWS Diversified International Equity VIP

DWS Dreman Small Mid Cap Value VIP

DWS Global Thematic VIP

DWS Government & Agency Securities VIP

DWS High Income VIP

DWS Large Cap Value VIP

DWS Mid Cap Growth VIP

DWS Money Market VIP

DWS Small Cap Growth VIP

DWS Strategic Income VIP

DWS Strategic Value VIP

DWS Technology VIP

DWS Turner Mid Cap Growth VIP

**DWS Investments VIT Funds:**

DWS Equity 500 Index VIP

DWS Small Cap Index VIP

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DWS INVESTMENTS
Deutsche Bank Group

*The following information replaces the existing disclosure in the "Investing in the Funds-Financial Intermediary Support Payments" or the "How to Exchange or Sell Shares- Financial Intermediary Support Payments" sections of each fund's/portfolio's Prospectuses:*

## FINANCIAL INTERMEDIARY SUPPORT PAYMENTS

The Advisor, DWS Investments Distributors, Inc. (the "Distributor") and/or their affiliates may pay additional compensation, out of their own assets and not as an additional charge to the fund, to selected affiliated and unaffiliated brokers, dealers, participating insurance companies or other financial intermediaries ("financial advisors") in connection with the sale and/or distribution of fund shares or the retention and/or servicing of fund investors and fund shares ("revenue sharing"). Such revenue sharing payments are in addition to any distribution or service fees payable under any Rule 12b-1 or service plan of the fund, any record keeping/sub-transfer agency/networking fees payable by the fund (generally through the Distributor or an affiliate) and/or the Distributor to certain financial advisors for performing such services and any sales charge, commissions, non-cash compensation arrangements expressly permitted under applicable rules of the Financial Industry Regulatory Authority or other concessions described in the fee table or elsewhere in this prospectus or the Statement of Additional Information as payable to all financial advisors. For example, the Advisor, the Distributor and/or their affiliates may compensate financial advisors for providing the fund with "shelf space" or access to a third party platform or fund offering list or other marketing programs, including, without limitation, inclusion of the fund on preferred or recommended sales lists, mutual fund "supermarket" platforms and other formal sales programs; granting the Distributor access to the financial advisor's sales force; granting the Distributor access to the financial advisor's conferences and meetings; assistance in training and educating the financial advisor's personnel; and obtaining other forms of marketing support.

The level of revenue sharing payments made to financial advisors may be a fixed fee or based upon one or more of the following factors: gross sales, current assets and/or number of accounts of the fund attributable to the financial advisor, the particular fund or fund type or other measures as agreed to by the Advisor, the Distributor and/or their affiliates and the financial advisors or any combination thereof. The amount of these revenue sharing payments is determined at the discretion of the Advisor, the Distributor and/or their affiliates from time to time, may be substantial, and may be different for different financial advisors based on, for example, the nature of the services provided by the financial advisor.

The Advisor, the Distributor and/or their affiliates currently make revenue sharing payments from their own assets in connection with the sale and/or distribution of DWS fund shares or the retention and/or servicing of investors and DWS fund shares to financial advisors in amounts that generally range from .01% up to .26% of assets of the fund serviced and maintained by the financial advisor, .05% to .25% of sales of the fund attributable to the financial advisor, a flat fee of $4,000 up to $125,000, or any combination thereof. These amounts are subject to change at the discretion of the Advisor, the Distributor and/or their affiliates. Receipt of, or the prospect of receiving, this additional compensation may influence your financial advisor's recommendation of the fund or of any particular share class of the fund. You should review your financial advisor's compensation disclosure and/or talk to your financial advisor to obtain more information on how this compensation may have influenced your financial advisor's recommendation of the fund. Additional information regarding these revenue sharing payments is included in the fund's Statement of Additional Information, which is available to you on request at no charge (see the back cover of this prospectus for more information on how to request a copy of the Statement of Additional Information).

The Advisor, the Distributor and/or their affiliates may also make such revenue sharing payments to financial advisors under the terms discussed above in connection with the distribution of both DWS funds and non-DWS funds by financial advisors to retirement plans that obtain record keeping services from ADP, Inc. or ExpertPlan Inc. on the DWS Investments branded retirement plan platform (the "Platform") with the level of revenue sharing payments being based upon sales of both the DWS funds and the non-DWS funds by the financial advisor on the Platform or current assets of both the DWS funds and the non-DWS funds serviced and maintained by the financial advisor on the Platform.

It is likely that broker-dealers that execute portfolio transactions for the fund will include firms that also sell shares of the DWS funds to their customers. However, the Advisor will not consider sales of DWS fund shares as a factor in the selection of broker-dealers to execute portfolio transactions for the DWS funds. Accordingly, the Advisor has implemented policies and procedures reasonably designed to prevent its traders from considering sales of DWS fund shares as a factor in the selection of broker-dealers to execute portfolio transactions for the fund. In addition, the Advisor, the Distributor and/or their affiliates will not use fund brokerage to pay for their obligation to provide additional compensation to financial advisors as described above.

*Please Retain This Supplement for Future Reference*

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# DWS VARIABLE SERIES II

## SUPPLEMENT TO THE CURRENTLY EFFECTIVE PROSPECTUS

## DWS Strategic Income VIP

*The following information replaces the existing disclosure contained under the "Portfolio Manager(s)" sub-heading of the "MANAGEMENT" section of the fund's prospectus.*

**Investment Advisor**

Deutsche Investment Management Americas Inc.

**Gary Russell, CFA, Managing Director.** Portfolio Manager of the fund. Joined the fund in 2006.

**William Chepolis, CFA, Managing Director.** Portfolio Manager of the fund. Joined the fund in 2005.

**John D. Ryan, Director**. Portfolio Manager of the fund. Joined the fund in 2010.

**Ohn Choe, CFA, Associate**. Portfolio Manager of the fund. Joined the fund in 2011.

**Darwei Kung, Vice President**. Portfolio Manager of the fund. Joined the fund in 2011.

**Subadvisor**

QS Investors, LLC (QS Investors)

**Portfolio Manager(s)**

**Robert Wang, Head of Portfolio Management and Trading, QS Investors.** Joined the fund in 2007.

**Thomas Picciochi, Head of Global Tactical Asset Allocation Portfolio Management and Trading, QS Investors.** Joined the fund in 2007.

*The following persons are added to the portfolio management team, as reflected under the "MANAGEMENT" sub-heading of the "FUND DETAILS" section of the fund's prospectus.*

**Ohn Choe, CFA, Associate**. Portfolio Manager of the fund. Joined the fund in 2011.

- Portfolio Manager for Retail Fixed Income: New York.
- Joined Deutsche Asset Management in 2005.
- BSBA, Georgetown University.

**Darwei Kung, Vice President**. Portfolio Manager of the fund. Joined the fund in 2011.

- Joined Deutsche Asset Management in 2006; previously has worked as a Director, Engineering and Business Development at Calpoint LLC from 2001-2004.
- Portfolio Manager: New York.
- BS and MS, University of Washington, Seattle; MS and MBA, Carnegie Mellon University.

*The following information replaces similar disclosure, as reflected under the "MANAGEMENT" sub-heading of the "FUND DETAILS" section of the fund's prospectus.*

**Robert Wang, Head of Portfolio Management and Trading, QS Investors.** Joined the fund in 2007.

- Joined QS Investors in 2010 after 28 years of experience of trading fixed income, foreign exchange and derivative products at Deutsche Asset Management and J.P. Morgan.
- BS, The Wharton School, University of Pennsylvania.

**Thomas Picciochi, Head of Global Tactical Asset Allocation Portfolio Management and Trading, QS Investors.** Joined the fund in 2007.

- Joined QS Investors in 2010 after 24 years of experience in portfolio management and various research and analysis positions at Deutsche Asset Management, State Street Global Advisors, FPL Energy, Barnett Bank, Trade Finance Corporation and Reserve Financial Management.
- BA and MBA, University of Miami.

*Please Retain This Supplement for Future Reference.*

February 1, 2011
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DWS INVESTMENTS
Deutsche Bank Group

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# DWS VARIABLE SERIES II

## SUPPLEMENT TO THE CURRENTLY EFFECTIVE PROSPECTUS:

DWS Small Cap Growth VIP

**Effective on or about May 1, 2011, the name of the fund will be changed to DWS Small Mid Cap Growth VIP.**

**Effective on or about May 1, 2011, the following sections of the prospectus are replaced or modified as follows:**

*The section of the fund's prospectus under the heading "INVESTMENT OBJECTIVE" will be replaced in its entirety by the following:*

### INVESTMENT OBJECTIVE

The fund seeks long-term capital appreciation.

*The "Main Investments" section of the fund's prospectus under the heading "PRINCIPAL INVESTMENT STRATEGY" will be replaced in its entirety by the following:*

**Main Investments.** Under normal circumstances, the fund invests at least 80% of net assets, plus the amount of any borrowings for investment purposes, in common stocks and other equity securities of small and mid-sized US companies. The fund defines small companies as those that are similar in market capitalization to those in the Russell 2000® Growth Index. The fund defines mid-sized companies as those that are similar in market capitalization to those in the Russell Midcap® Growth Index. The fund intends to invest primarily in companies whose market capitalizations fall within the normal range of each index. The fund invests primarily in common stocks but may invest in other types of equity securities such as preferred stocks or convertible securities. While the fund invests mainly in US stocks, it could invest up to 25% of total assets in foreign securities. The fund may invest in initial public offerings.

*The following sub-section will be added to the fund's prospectus under the heading "MAIN RISKS":*

**Medium-sized company risk.** Medium-sized company stocks tend to be more volatile than large company stocks. Medium-sized companies are less widely followed by stock analysts and less information about them is available to investors.

*The following supplements the disclosure under the heading "Past Performance" in the fund's prospectus.*

Effective on or about May 1, 2011, the Russell 2500™ Growth Index will replace the Russell 2000® Growth Index as the fund's benchmark index because the Advisor believes that it better reflects the fund's new investment strategy.

*The "Main Investments" sub-section under the sub-heading "ADDITIONAL INFORMATION ABOUT THE FUND — PRINCIPAL INVESTMENT STRATEGY" of the "FUND DETAILS" section of the fund's prospectus will be replaced in its entirety by the following:*

**Main Investments.** Under normal circumstances, the fund invests at least 80% of net assets, plus the amount of any borrowings for investment purposes, in common stocks and other equity securities of small and mid-sized US companies. The fund defines small companies as those that are similar in market capitalization to those in the Russell 2000® Growth Index. The fund defines mid-sized companies as those that are similar in market capitalization to those in the Russell Midcap® Growth Index. The fund intends to invest primarily in companies whose market capitalizations fall within the normal range of each index. The fund invests primarily in common stocks but may invest in other types of equity securities such as preferred stocks or convertible securities. While the fund invests mainly in US stocks, it could invest up to 25% of total assets in foreign securities. The fund may invest in initial public offerings.

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*The following sub-section will be added under the sub-heading "ADDITIONAL INFORMATION ABOUT THE FUND — MAIN RISKS" of the "FUND DETAILS" section of the fund's prospectus:*

**Medium-sized company risk.** Medium-sized company stocks tend to be more volatile than large company stocks. Medium-sized companies are less widely followed by stock analysts and less information about them is available to investors. Industry-wide reversals may have a greater impact on medium-sized companies, since they lack the financial resources of larger companies. Medium-sized company stocks are typically less liquid than large company stocks.

*Please Retain This Supplement for Future Reference*

# IMPORTANT NOTICE REGARDING: A CHANGE TO YOUR FUND'S INVESTMENT POLICY

**SUPPLEMENT TO THE CURRENTLY EFFECTIVE PROSPECTUSES AND SUMMARY PROSPECTUSES**

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## DWS Global Opportunities VIP

**The Board of Trustees has approved changes to the name and investment strategy of DWS Global Opportunities VIP.**

**Effective on or about May 1, 2011, (the "Effective Date"), the name of the fund will change from "DWS Global Opportunities VIP" to "DWS Global Small Cap Growth VIP."**

*On the Effective Date, the first and second paragraphs under the heading "PRINCIPAL INVESTMENT STRATEGY" are deleted in their entirety and replaced with the following:*

**Main Investments.** The fund invests at least 80% of net assets, plus the amount of any borrowings for investment purposes, in common stocks and other equities of small companies throughout the world (companies with market values similar to the smallest 30% of the companies in the S&P Developed Broad Market Index, formerly the S&P/Citigroup Broad Market Index World). As of December 31, 2010, companies in which the fund invests typically have a market capitalization of between $500 million and $5 billion at the time of purchase. As part of the investment process the fund may own stocks even if they are outside this market capitalization range.

The fund may invest up to 20% of total assets in common stocks and other equities of large companies or in debt securities, including up to 5% of net assets in junk bonds (grade BB/Ba and below).

The Board will provide shareholders with at least 60 days notice prior to making any changes to the fund's 80% investment policy as described herein.

*Please Retain This Supplement for Future Reference*

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DWS INVESTMENTS
Deutsche Bank Group

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## SUPPLEMENT TO THE CURRENTLY EFFECTIVE PROSPECTUSES

# DWS International Fund

## DWS VARIABLE SERIES I

# DWS International VIP

*The following information replaces the existing disclosure contained under the "Portfolio Manager(s)" sub-heading of the "MANAGEMENT" section of each fund's prospectus:*

**Nikolaus Poehlmann, CFA, Director.** Lead Portfolio Manager of the fund. Joined the fund in 2009.

**Mark Schumann, Vice President.** Portfolio Manager of the fund. Joined the fund in 2009.

**Andreas Wendelken, Director.** Portfolio Manager of the fund. Joined the fund in 2009.

*The following information replaces the existing disclosure contained under the "MANAGEMENT" sub-heading of the "FUND DETAILS" section of each fund's prospectus:*

**Nikolaus Poehlmann, CFA, Director.** Lead Portfolio Manager of the fund. Joined the fund in 2009.

- Senior portfolio manager for Equities, responsible for European blend as well as dividend funds.
- Joined Deutsche Asset Management in July 1998 in Loan Portfolio Management for Corporate and Investment Bank (CIB) division.
- Managing European diversified funds since 2003, financials funds from 2001-2010, and Italian equity funds from 2002-2010.
- BA from Augsburg University; Master's degree in Economics ("Diplom Volkswirt") from University of Cologne.

**Mark Schumann, Vice President.** Portfolio Manager of the fund. Joined the fund in 2009.

- Joined Deutsche Asset Management in 2003.
- Portfolio Manager for European Large Cap Equity: Frankfurt.
- Masters (Lic oec) from University of St. Gallen (HSG).

**Andreas Wendelken, Director.** Portfolio Manager of the fund. Joined the fund in 2009.

- Joined Deutsche Asset Management in 2001; previously worked for 2 years as a relationship manager for Southeastern Europe at Deutsche Bank's Global Corporates and Institutions division.
- Portfolio manager for emerging markets equity: Frankfurt.
- Master's degree in business administration from Frankfurt School of Finance & Management (previously HfB), Frankfurt; completed bank training program (Bankkaufmann) at Bremer Landesbank, Bremen.

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Deutsche Bank Group

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**SUPPLEMENT TO THE CURRENTLY EFFECTIVE PROSPECTUSES**

# DWS Core Plus Income Fund

**DWS VARIABLE SERIES I**

# DWS Bond VIP

**DWS VARIABLE SERIES II**

# DWS Core Fixed Income VIP

*The following information replaces the existing disclosure contained under the "Portfolio Manager(s)" sub-heading of the "MANAGEMENT" section of each fund's prospectus:*

**Kenneth R. Bowling, CFA, Managing Director.** Portfolio Manager of the fund. Joined the fund in 2008.

**Jamie Guenther, CFA, Managing Director.** Portfolio Manager of the fund. Joined the fund in 2008.

**John Brennan, Director.** Portfolio Manager of the fund. Joined the fund in 2008.

**Bruce Harley, CFA, CEBS, Director.** Portfolio Manager of the fund. Joined the fund in 2008.

**J. Richard Robben, CFA, Director.** Portfolio Manager of the fund. Joined the fund in 2008.

**David Vignolo, CFA,Vice President.** Portfolio Manager of the fund. Joined the fund in 2008.

**J. Kevin Horsley, CFA, CPA, Director.** Portfolio Manager of the fund. Joined the fund in 2008.

**Stephen Willer, CFA,Vice President.** Portfolio Manager of the fund. Joined the fund in 2008.

**William Chepolis, CFA, Managing Director.** Portfolio Manager of the fund. Joined the fund in 2011.

*The following person is added to the portfolio management team, as reflected under the "MANAGEMENT" sub-heading of the "FUND DETAILS" section of each fund's prospectus:*

**William Chepolis, CFA, Managing Director.** Portfolio Manager of the fund. Joined the fund in 2011.

- Joined Deutsche Asset Management in 1998 after 13 years of experience as vice president and portfolio manager for Norwest Bank where he managed the bank's fixed income and foreign exchange portfolios.
- Portfolio Manager for Retail Fixed Income: New York.
- BIS, University of Minnesota.

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**THE ALGER PORTFOLIOS**

**Class I-2 Prospectus**

**Alger Balanced Portfolio**

**Supplement dated January 21, 2011 to the Prospectus dated May 1, 2010**

The following replaces the entry under the heading "Management" on page 29 of the Prospectus:

**Investment Manager:**

Fred Alger Management, Inc.

**Portfolio Managers:**

Andrew Silverberg
Senior Vice President
and Portfolio Manager
Since January 2007

Dan C. Chung, CFA
Chief Executive Officer,
Chief Investment
Officer and Portfolio
Manager
Since January 2011

Steve Thumm
Senior Vice President
Since January 2011

The following replaces the entries for Alger Balanced Portfolio in the chart under the heading "Portfolio Managers Primarily Responsible for Day-to-Day Management of Portfolio Investments" on page 40 of the Prospectus:

| Fund | Portfolio Manager(s) | Since |
|---|---|---|
| Alger Balanced Portfolio | Portfolio Managers: | |
| | Andrew Silverberg | January 2007 |
| | Dan C. Chung, CFA | January 2011 |
| | Steve Thumm | January 2011 |

In addition, the following replaces the paragraph regarding Mr. Curry on page 40 of the Prospectus (Mr. Curry is no longer employed by the Manager):

"Mr. Thumm has been employed by the Manager since 2001 and currently serves as Senior Vice President."

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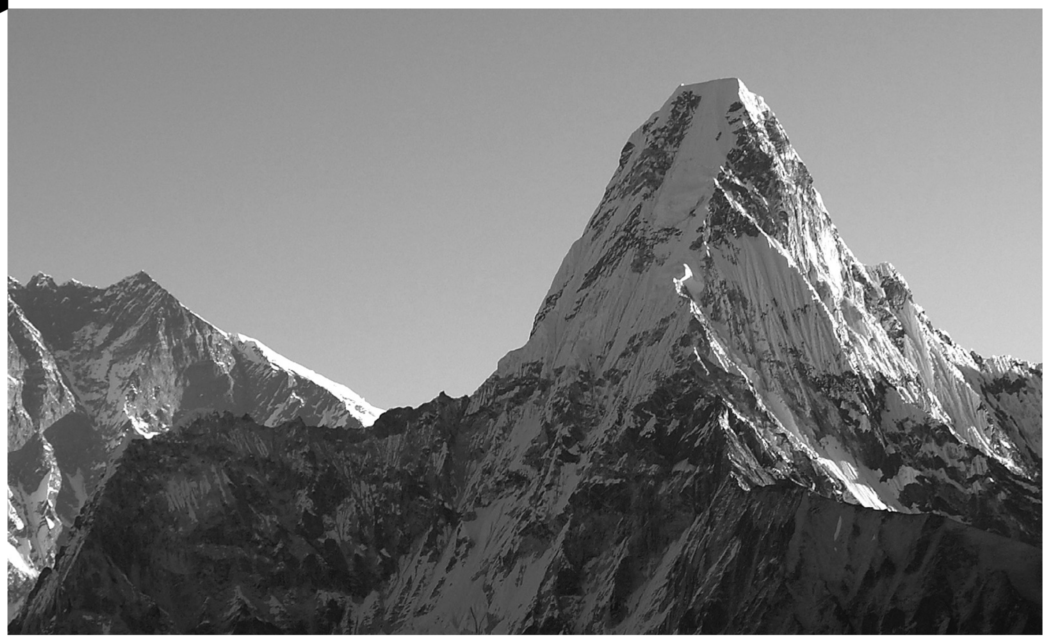
# Invesco V.I. Utilities Fund

Annual Report to Shareholders ■ December 31, 2010



The Fund provides a complete list of its holdings four times in each fiscal year, at the quarter-ends. For the second and fourth quarters, the lists appear in the Fund's semiannual and annual reports to shareholders. For the first and third quarters, the Fund files the lists with the Securities and Exchange Commission (SEC) on Form N-Q. The Fund's Form N-Q filings are available on the SEC website, sec.gov. Copies of the Fund's Forms N-Q may be reviewed and copied at the SEC Public Reference Room in Washington, D.C. You can obtain information on the operation of the Public Reference Room, including information about duplicating fee charges, by calling 202 551 8090 or 800 732 0330, or by electronic request at the following email address: publicinfo@sec.gov. The SEC file numbers for the Fund are 811-07452 and 033-57340. The Fund's most recent portfolio holdings, as filed on Form N-Q, have also been made available to insurance companies issuing variable annuity contracts and variable life insurance policies ("variable products") that invest in the Fund.

A description of the policies and procedures that the Fund uses to determine how to vote proxies relating to portfolio securities is available without charge, upon request, from our Client Services department at 800 959 4246 or on the Invesco website, invesco.com/proxyguidelines. The information is also available on the SEC website, sec.gov.

Information regarding how the Fund voted proxies related to its portfolio securities during the 12 months ended June 30, 2010, is available at our website, invesco.com/proxysearch. The information is also available on the SEC website, sec.gov.

Invesco Advisers, Inc. is an investment adviser; it provides investment advisory services to individual and institutional clients and does not sell securities. Invesco Distributors, Inc. is the U.S. distributor for Invesco Ltd.'s retail mutual funds, exchange-traded funds and institutional money market funds. Both are wholly owned, indirect subsidiaries of Invesco Ltd.

**This report must be accompanied or preceded by a currently effective Fund prospectus and variable product prospectus, which contain more complete information, including sales charges and expenses. Investors should read each carefully before investing.**

Invesco Distributors, Inc.

I-VIUTI-AR-1

# Management's Discussion of Fund Performance

**Performance summary**

For the 12 months ended December 31, 2010, the utilities sector lagged the broad market, as measured by the S&P 500 Index, which posted a double-digit return. Invesco V.I. Utilities Fund had a positive return but lagged the S&P 500 Index for the period. Investment results for the Fund compared favorably to its style-specific benchmark, the S&P 500 Utilities Index. The Fund's positive results relative to the S&P 500 Utilities Index largely were due to our holdings in the gas utilities and oil, gas and consumable fuels industries. Performance drivers were largely stock specific, though the Fund's gas and multiutilities industry holdings had the largest positive impact on the Fund's absolute returns.

Your Fund's long-term performance appears later in this report.

**Fund vs. Indexes**

*Total returns, 12/31/09 to 12/31/10, excluding variable product issuer charges. If variable product issuer charges were included, returns would be lower.*

| | |
|---|---|
| Series I Shares | 6.30% |
| Series II Shares | 6.01 |
| S&P 500 Index▼ (Broad Market Index) | 15.08 |
| S&P 500 Utilities Index▼ (Style-Specific Index) | 5.46 |
| Lipper VUF Utility Funds Category Average▼ (Peer Group) | 10.83 |

▼Lipper Inc.

## How we invest

In selecting investments, we focus on companies within the electric utility, natural gas, water and telecommunications industries. We emphasize companies with solid balance sheets and operational cash flows that support sustained or increasing dividends. Fundamental research and financial statement analysis are the backbone of our bottom-up investment process. Using a variety of valuation techniques, we estimate the potential return of holdings over a two-year investment period. We construct the portfolio to provide the best combination of price appreciation potential, dividend income and risk profile; the Fund typically maintains full sector exposure. We seek to manage risk by maintaining an average of 30 to 50 positions, low turnover and a rigorous sell discipline.

We are committed to providing strategic exposure to a traditionally defensive and income-oriented asset class by using a total return approach to managing the Fund, emphasizing capital appreciation, current income and capital preservation.

## Market conditions and your Fund

Equity markets delivered strong returns but were choppy during the fiscal year as investors weighed the competing issues of solid corporate profitability and soft, albeit improving, macroeconomic data. Corporate earnings improved considerably over the past year as high productivity growth and cost-cutting measures made during the economic downturn led to a rebound in margins and profits. However, high unemployment, weak consumer spending and tepid housing data remained as overhangs to the recovery. The sovereign debt crisis also contributed to market volatility as European countries began implementing austerity programs. Most recently, the market reversed course and rallied again during the last four months of the year on better economic news, ending the fiscal year with double-digit gains.

All 10 sectors within the S&P 500 Index posted gains for the year. More economically sensitive sectors such as consumer discretionary, industrials and materials had the highest returns, while the less economically sensitive sectors such as health care and utilities had some of the lowest returns. The S&P 500 Utilities sector returned 5.46% for the period, as compared with the 15.08% return for the overall S&P 500 Index.

The largest contributor to the Fund's overall return was **CMS Energy** in the multiutilities industry. During the year, the company announced a reduction in the capital investment plan for its Michigan-based coal plant of $800 million over the next five years. The reduced expenditures will minimize future rate increases for its utility customers. The company also announced a 40% increase in its dividend – its second dividend increase during the year. Both of these events were greeted favorably by investors.

Another significant contributor to the Fund's return was **Dominion Resources**. During the year, the company closed the sale of its Appalachian exploration and production (E&P) acreage, effectively exiting the E&P business. The sale was viewed favorably by the market as it reduces the company's need for equity financing to fund infrastructure projects, it reduces the company's commodity sensitivity and it focuses the company on its core regulated businesses.

The largest detractor from results was **E.ON**, a diversified utility provider based in Germany. The company recently sold its U.S. operations to PPL Corporation, which reduced debt and streamlined operations.

**Portfolio Composition**

*By sector*

| | |
|---|---|
| Utilities | 85.8% |
| Telecommunication Services | 6.1 |
| Energy | 3.8 |
| *Money Market Funds Plus Other Assets Less Liabilities* | 4.3 |

**Top 10 Equity Holdings***

| | | |
|---|---|---|
| 1. | Dominion Resources, Inc. | 4.9% |
| 2. | Southern Co. | 4.6 |
| 3. | American Electric Power Co., Inc. | 4.6 |
| 4. | Xcel Energy, Inc. | 4.5 |
| 5. | Portland General Electric Co. | 4.3 |
| 6. | National Grid PLC | 4.3 |
| 7. | Pepco Holdings, Inc. | 4.2 |
| 8. | PPL Corp. | 3.8 |
| 9. | Entergy Corp. | 3.6 |
| 10. | Edison International | 3.6 |

| | |
|---|---|
| Total Net Assets | $65.7 million |
| Total Number of Holdings* | 37 |

The Fund's holdings are subject to change, and there is no assurance that the Fund will continue to hold any particular security.
*Excluding money market fund holdings.

However, weakness in the stock was driven by uncertainty regarding whether the company's nuclear plants in Germany will be granted extensions to operate for timeframes beyond those currently permitted.

Ohio-based power producer **FirstEnergy** was another detractor from returns. In the first quarter of the year, the company announced an acquisition of Allegheny Energy in an all-stock transaction. While the proposed merger is expected to increase FirstEnergy's customer base, as well as its power generation in the region, the company's shares were negatively impacted following the announcement as the market questioned projected synergies of the deal. We trimmed our position in the company during the year.

There were no major positioning changes during the year; however, we increased the number of Fund holdings by initiating new positions in the telecommunications, electric and multiutilities industries. We continue to emphasize regulated over unregulated utilities given their relatively attractive valuations. At the end of the year, the Fund's largest industry allocations were in the electric and multiutilities industries.

As the Fund's fiscal year closed, a dominant issue surrounding the utility sector was the multiyear decline in both consumer and industrial electrical consumption. While investors debate the ultimate trajectory of electrical demand, a tepid recovery could result in further pressure on state utility commissions to deny rate increases or for utilities to file for lower returns on equity (ROEs). An additional overhang is the lack of transparency on timing and content of environmental regulations. Positively, many companies, as a result of the improvement in credit markets, have reduced their debt and generally improved their financial metrics. The volatility and level of commodity prices also has decreased from peak levels, enabling regulated utilities to better manage their input costs. Valuations for the group have improved and remain modestly attractive relative to historical levels.

In closing, we would like to thank you for your continued investment in Invesco V.I. Utilities Fund. We are committed to providing investors strategic exposure to a traditionally defensive and income-oriented asset class through our total return approach.

*The views and opinions expressed in management's discussion of Fund performance are those of Invesco Advisers, Inc. These views and opinions are subject to change at any time based on factors such as market and economic conditions. These views and opinions may not be relied upon as investment advice or recommendations, or as an offer for a particular security. The information is not a complete analysis of every aspect of any market, country, industry, security or the Fund. Statements of fact are from sources considered reliable, but Invesco Advisers, Inc. makes no representation or warranty as to their completeness or accuracy. Although historical performance is no guarantee of future results, these insights may help you understand our investment management philosophy.*

See important Fund and, if applicable, index disclosures later in this report.

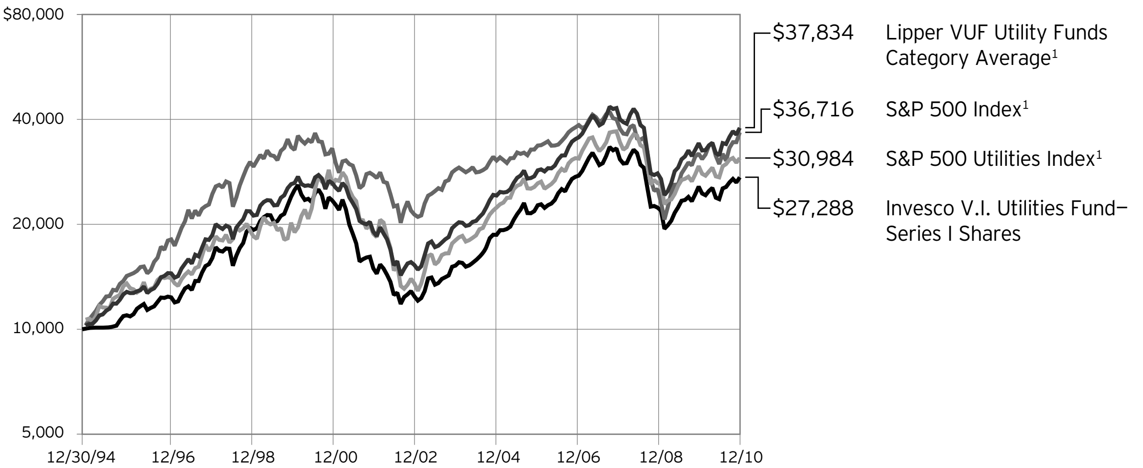
**Meggan Walsh**
Chartered Financial Analyst, portfolio manager, is lead manager of Invesco V.I. Utilities Fund. Ms. Walsh joined Invesco in 1991. She has been in the industry since 1987. Ms. Walsh earned a B.S. in finance from the University of Maryland and an M.B.A. from Loyola University of Maryland.

**Davis Paddock**
Chartered Financial Analyst, portfolio manager, is manager of Invesco V.I. Utilities Fund. Mr. Paddock joined Invesco in 2001. He earned a B.A. and an M.B.A. from The University of Texas at Austin.

# Your Fund's Long-Term Performance

**Results of a $10,000 Investment — Oldest Share Class since Inception**

Fund data from 12/30/94, index data from 12/31/94




1 Lipper Inc.

Past performance cannot guarantee comparable future results.

This chart, which is a logarithmic chart, presents the fluctuations in the value of the Fund and its indexes. We believe that a logarithmic chart is more effective than other types of charts in illustrating changes in value during the early years shown in the chart. The vertical axis, the one that indicates the dollar value of an investment, is constructed with each segment representing a percent change in the value of the investment. In this chart, each segment represents a doubling, or 100% change, in the value of the investment. In other words, the space between $5,000 and $10,000 is the same size as the space between $10,000 and $20,000, and so on.

| **Average Annual Total Returns**<br>*As of 12/31/10* | |
|---|---|
| **Series I Shares** | |
| Inception (12/30/94) | 6.47% |
| 10 Years | 1.34 |
| 5 Years | 4.58 |
| 1 Year | 6.30 |
| **Series II Shares** | |
| 10 Years | 1.09% |
| 5 Years | 4.32 |
| 1 Year | 6.01 |

**Series II shares incepted on April 30, 2004. Performance shown prior to that date is that of Series I shares, restated to reflect the higher 12b-1 fees applicable to Series II. Series I performance reflects any applicable fee waivers or expense reimbursements. The performance of the Fund's Series I and Series II share classes will differ primarily due to different class expenses.**

**The performance data quoted represent past performance and cannot guarantee comparable future results; current performance may be lower or higher. Please contact your variable product issuer or financial adviser for the most recent month-end variable product performance. Performance figures reflect Fund expenses, reinvested distributions and changes in net asset value. Investment return and principal value will fluctuate so that you may have a gain or loss when you sell shares.**

**The net annual Fund operating expense ratio set forth in the most recent Fund prospectus as of the date of this report for Series I and Series II shares was 0.94% and 1.19%, respectively.[1] The total annual Fund operating expense ratio set forth in the most recent Fund prospectus as of the date of this report for Series I and Series II shares was 1.05% and 1.30%, respectively. The expense ratios presented above may vary from the expense ratios presented in other sections of this report that are based on expenses incurred during the period covered by this report.**

**Invesco V.I. Utilities Fund, a series portfolio of AIM Variable Insurance Funds (Invesco Variable Insurance Funds), is currently offered through insurance companies issuing variable products. You cannot purchase shares of the Fund directly. Performance figures given represent the Fund and are not intended to reflect actual variable product values. They do not reflect sales charges, expenses and fees assessed in connection with a variable product. Sales charges, expenses and fees, which are determined by the variable product issuers, will vary and will lower the total return.**

**The most recent month-end performance data at the Fund level, excluding variable product charges, is available at 800 451 4246. As mentioned above, for the most recent month-end performance including variable product charges, please contact your variable product issuer or financial adviser.**

1 Total annual Fund operating expenses after any contractual fee waivers and/or expense reimbursements by the adviser in effect through at least April 30, 2012. See current prospectus for more information.

**Invesco V.I. Utilities Fund's investment objective is long-term growth of capital and, secondarily, current income.**

- Unless otherwise stated, information presented in this report is as of December 31, 2010, and is based on total net assets.
- Unless otherwise noted, all data provided by Invesco.
- To access your Fund's reports/prospectus, visit invesco.com/fundreports.

## Principal risks of investing in the Fund

An investment by the Fund in exchange-traded funds (ETFs) generally presents the same primary risks as an investment in a mutual fund. In addition, ETFs may be subject to the following: a discount of the ETF's shares to its net asset value; failure to develop an active trading market for the ETF's shares; the listing exchange halting trading of the ETF's shares; failure of the ETF's shares to track the referenced index; and holding troubled securities in the referenced index. ETFs may involve duplication of management fees and certain other expenses, as the Fund indirectly bears its proportionate share of any expenses paid by the ETFs in which it invests. Further, certain of the ETFs in which each fund may invest are leveraged. The more a fund invests in such leveraged ETFs, the more this leverage will magnify any losses on those investments.

The Fund's investments are concentrated in a comparatively narrow segment of the economy, which may make the Fund more volatile.

The following factors may affect the Fund's investments in the utilities sector: governmental regulation, economic factors, ability of the issuer to obtain financing, prices of natural resources and risks associated with nuclear power.

The Fund's foreign investments may be affected by changes in the foreign country's exchange rates; political and social instability; changes in economic or taxation policies; difficulties when enforcing obligations; decreased liquidity; and increased volatility. Foreign companies may be subject to less regulation resulting in less publicly available information about the companies.

The Fund may invest a large percentage of its assets in a limited number of securities or other instruments, which could negatively affect the value of the Fund.

The investment techniques and risk analysis used by the Fund's portfolio managers may not produce the desired results.

The prices of and the income generated by the Fund's securities may decline in response to, among other things, investor sentiment; general economic and market conditions; regional or global instability; and currency and interest rate fluctuations.

## About indexes used in this report

The **S&P 500® Index** is an unmanaged index considered representative of the U.S. stock market.

The **S&P 500 Utilities Index** is an unmanaged index considered representative of the utilities market.

The **Lipper VUF Utility Funds Category Average** represents an average of all of the variable insurance underlying funds in the Lipper Utility Funds category.

The Fund is not managed to track the performance of any particular index, including the index(es) defined here, and consequently, the performance of the Fund may deviate significantly from the performance of the index(es).

A direct investment cannot be made in an index. Unless otherwise indicated, index results include reinvested dividends, and they do not reflect sales charges. Performance of the peer group, if applicable, reflects fund expenses; performance of a market index does not.

## Other information

The Chartered Financial Analyst® (CFA®) designation is globally recognized and attests to a charterholder's success in a rigorous and comprehensive study program in the field of investment management and research analysis.

Industry classifications used in this report are generally classified according to the Global Industry Classification Standard, which was developed by and is the exclusive property and a service mark of MSCI Inc. and Standard & Poor's.

The returns shown in management's discussion of Fund performance are based on net asset values calculated for shareholder transactions. Generally accepted accounting principles require adjustments to be made to the net assets of the Fund at period end for financial reporting purposes, and as such, the net asset values for shareholder transactions and the returns based on those net asset values may differ from the net asset values and returns reported in the Financial Highlights. Additionally, the returns and net asset values shown throughout this report are at the Fund level only and do not include variable product issuer charges. If such charges were included, the total returns would be lower.

# Schedule of Investments[a]

*December 31, 2010*

| | Shares | Value |
|---|---|---|
| **Common Stocks–95.66%** | | |
| **Electric Utilities–45.74%** | | |
| American Electric Power Co., Inc. | 83,238 | $ 2,994,903 |
| Duke Energy Corp. | 104,755 | 1,865,687 |
| E.ON AG (Germany) | 53,357 | 1,636,266 |
| Edison International | 60,747 | 2,344,834 |
| Entergy Corp. | 33,384 | 2,364,589 |
| Exelon Corp. | 37,918 | 1,578,906 |
| FirstEnergy Corp. | 53,693 | 1,987,715 |
| NextEra Energy, Inc. | 18,170 | 944,658 |
| Northeast Utilities | 59,859 | 1,908,305 |
| Pepco Holdings, Inc. | 152,313 | 2,779,712 |
| Pinnacle West Capital Corp. | 10,555 | 437,505 |
| Portland General Electric Co. | 129,466 | 2,809,412 |
| PPL Corp. | 95,357 | 2,509,796 |
| Progress Energy, Inc. | 19,382 | 842,729 |
| Southern Co. | 79,108 | 3,024,299 |
| | | 30,029,316 |
| **Gas Utilities–6.74%** | | |
| AGL Resources Inc. | 27,701 | 993,081 |
| Atmos Energy Corp. | 16,927 | 528,122 |
| ONEOK, Inc. | 35,322 | 1,959,311 |
| UGI Corp. | 29,949 | 945,790 |
| | | 4,426,304 |
| **Independent Power Producers & Energy Traders–4.89%** | | |
| Calpine Corp.[b] | 100,072 | 1,334,960 |
| NRG Energy, Inc.[b] | 95,846 | 1,872,831 |
| | | 3,207,791 |
| **Integrated Telecommunication Services–6.05%** | | |
| AT&T Inc. | 39,055 | $ 1,147,436 |
| Qwest Communications International Inc. | 113,728 | 865,470 |
| Verizon Communications, Inc. | 54,675 | 1,956,272 |
| | | 3,969,178 |
| **Multi-Utilities–26.81%** | | |
| CMS Energy Corp. | 41,538 | 772,607 |
| Dominion Resources, Inc. | 75,209 | 3,212,928 |
| DTE Energy Co. | 14,391 | 652,200 |
| National Grid PLC (United Kingdom) | 320,668 | 2,797,076 |
| PG&E Corp. | 37,657 | 1,801,511 |
| Public Service Enterprise Group Inc. | 61,468 | 1,955,297 |
| Sempra Energy | 43,756 | 2,296,315 |
| TECO Energy, Inc. | 26,290 | 467,962 |
| Wisconsin Energy Corp. | 11,231 | 661,057 |
| Xcel Energy, Inc. | 126,774 | 2,985,528 |
| | | 17,602,481 |
| **Oil & Gas Exploration & Production–1.18%** | | |
| EQT Corp. | 17,347 | 777,840 |
| **Oil & Gas Storage & Transportation–4.25%** | | |
| Southern Union Co. | 44,355 | 1,067,625 |
| Williams Cos., Inc. (The) | 69,599 | 1,720,487 |
| | | 2,788,112 |
| Total Common Stocks (Cost $53,504,296) | | 62,801,022 |
| **Money Market Funds–3.98%** | | |
| Liquid Assets Portfolio–Institutional Class[c] | 1,306,377 | 1,306,377 |
| Premier Portfolio–Institutional Class[c] | 1,306,377 | 1,306,377 |
| Total Money Market Funds (Cost $2,612,754) | | 2,612,754 |
| TOTAL INVESTMENTS–99.64% (Cost $56,117,050) | | 65,413,776 |
| OTHER ASSETS LESS LIABILITIES–0.36% | | 236,462 |
| NET ASSETS–100.00% | | $65,650,238 |

Notes to Schedule of Investments:

(a) Industry and/or sector classifications used in this report are generally according to the Global Industry Classification Standard, which was developed by and is the exclusive property and a service mark of MSCI Inc. and Standard & Poor's.
(b) Non-income producing security.
(c) The money market fund and the Fund are affiliated by having the same investment adviser.

See accompanying Notes to Financial Statements which are an integral part of the financial statements.

# Statement of Assets and Liabilities

*December 31, 2010*

| | |
|---|---|
| **Assets:** | |
| Investments, at value (Cost $53,504,296) | $62,801,022 |
| Investments in affiliated money market funds, at value and cost | 2,612,754 |
| Total investments, at value (Cost $56,117,050) | 65,413,776 |
| Receivable for: | |
| Fund shares sold | 71,256 |
| Dividends | 294,278 |
| Investment for trustee deferred compensation and retirement plans | 40,073 |
| Total assets | 65,819,383 |
| **Liabilities:** | |
| Payable for: | |
| Fund shares reacquired | 7,175 |
| Accrued fees to affiliates | 81,453 |
| Accrued other operating expenses | 27,715 |
| Trustee deferred compensation and retirement plans | 52,802 |
| Total liabilities | 169,145 |
| Net assets applicable to shares outstanding | $65,650,238 |
| **Net assets consist of:** | |
| Shares of beneficial interest | $55,921,999 |
| Undistributed net investment income | 2,119,797 |
| Undistributed net realized gain (loss) | (1,691,783) |
| Unrealized appreciation | 9,300,225 |
| | $65,650,238 |
| **Net Assets:** | |
| Series I | $63,944,522 |
| Series II | $ 1,705,716 |
| **Shares outstanding, $0.001 par value per share, unlimited number of shares authorized:** | |
| Series I | 4,301,218 |
| Series II | 115,415 |
| Series I: | |
| Net asset value per share | $ 14.87 |
| Series II: | |
| Net asset value per share | $ 14.78 |

# Statement of Operations

*For the year ended December 31, 2010*

| | |
|---|---|
| **Investment income:** | |
| Dividends (net of foreign withholding taxes of $15,446) | $2,760,250 |
| Dividends from affiliated money market funds (includes securities lending income of $8,139) | 11,649 |
| Total investment income | 2,771,899 |
| **Expenses:** | |
| Advisory fees | 398,396 |
| Administrative services fees | 199,065 |
| Custodian fees | 7,584 |
| Distribution fees — Series II | 4,091 |
| Transfer agent fees | 21,684 |
| Trustees' and officers' fees and benefits | 17,522 |
| Other | 45,992 |
| Total expenses | 694,334 |
| Less: Fees waived | (77,324) |
| Net expenses | 617,010 |
| Net investment income | 2,154,889 |
| **Realized and unrealized gain (loss) from:** | |
| Net realized gain from: | |
| Investment securities | 2,265,663 |
| Foreign currencies | 14,613 |
| | 2,280,276 |
| Change in net unrealized appreciation (depreciation) of: | |
| Investment securities | (672,208) |
| Foreign currencies | (2,357) |
| | (674,565) |
| Net realized and unrealized gain | 1,605,711 |
| Net increase in net assets resulting from operations | $3,760,600 |

See accompanying Notes to Financial Statements which are an integral part of the financial statements.

# Statement of Changes in Net Assets

*For the years ended December 31, 2010 and 2009*

| | 2010 | 2009 |
|---|---|---|
| **Operations:** | | |
| Net investment income | $ 2,154,889 | $ 2,365,392 |
| Net realized gain (loss) | 2,280,276 | (3,566,259) |
| Change in net unrealized appreciation (depreciation) | (674,565) | 9,982,838 |
| Net increase in net assets resulting from operations | 3,760,600 | 8,781,971 |
| **Distributions to shareholders from net investment income:** | | |
| Series I | (2,309,020) | (3,146,581) |
| Series II | (55,316) | (69,727) |
| Total distributions from net investment income | (2,364,336) | (3,216,308) |
| **Distributions to shareholders from net realized gains:** | | |
| Series I | — | (793,124) |
| Series II | — | (19,073) |
| Total distributions from net realized gains | — | (812,197) |
| **Share transactions–net:** | | |
| Series I | (8,086,914) | (14,677,265) |
| Series II | (32,168) | (124,013) |
| Net increase (decrease) in net assets resulting from share transactions | (8,119,082) | (14,801,278) |
| Net increase (decrease) in net assets | (6,722,818) | (10,047,812) |
| **Net assets:** | | |
| Beginning of year | 72,373,056 | 82,420,868 |
| End of year (includes undistributed net investment income of $2,119,797 and $2,314,631, respectively) | $65,650,238 | $ 72,373,056 |

# Notes to Financial Statements

*December 31, 2010*

## NOTE 1—Significant Accounting Policies

Invesco V.I. Utilities Fund (the "Fund") is a series portfolio of AIM Variable Insurance Funds (Invesco Variable Insurance Funds) (the "Trust"). The Trust is a Delaware statutory trust registered under the Investment Company Act of 1940, as amended (the "1940 Act"), as an open-end series management investment company consisting of forty-one separate portfolios, (each constituting a "Fund"). The assets, liabilities and operations of each portfolio are accounted for separately. Information presented in these financial statements pertains only to the Fund. Matters affecting each Fund or class will be voted on exclusively by the shareholders of such Fund or class. Current Securities and Exchange Commission ("SEC") guidance, however, requires participating insurance companies offering separate accounts to vote shares proportionally in accordance with the instructions of the contract owners whose investments are funded by shares of each Fund or class.

The Fund's investment objectives are long-term growth of capital and, secondarily, current income.

The Fund currently offers two classes of shares, Series I and Series II, both of which are offered to insurance company separate accounts funding variable annuity contracts and variable life insurance policies ("variable products").

The following is a summary of the significant accounting policies followed by the Fund in the preparation of its financial statements.

**A. Security Valuations** — Securities, including restricted securities, are valued according to the following policy.

A security listed or traded on an exchange (except convertible bonds) is valued at its last sales price or official closing price as of the close of the customary trading session on the exchange where the security is principally traded, or lacking any sales or official closing price on a particular day, the security may be valued at the closing bid price on that day. Securities traded in the over-the-counter market are valued based on prices furnished by independent pricing services or market makers. When such securities are valued by an independent pricing service they may be considered fair valued. Futures contracts are valued at the final settlement price set by an exchange on which they are principally traded. Listed options are valued at the mean between the last bid and ask prices from the exchange on which they are principally traded. Options not listed on an exchange are valued by an independent source at the mean between the last bid and ask prices. For purposes of determining net asset value per share, futures and option contracts generally are valued 15 minutes after the close of the customary trading session of the New York Stock Exchange ("NYSE").

Investments in open-end and closed-end registered investment companies that do not trade on an exchange are valued at the end of day net asset value per share. Investments in open-end and closed-end registered investment companies that trade on an exchange are valued at the last sales price or official closing price as of the close of the customary trading session on the exchange where the security is principally traded.

Debt obligations (including convertible bonds) and unlisted equities are fair valued using an evaluated quote provided by an independent pricing service. Evaluated quotes provided by the pricing service may be determined without exclusive reliance on quoted prices, and may reflect appropriate factors such as institution-size trading in similar groups of securities, developments related to specific securities, dividend rate, yield, quality, type of issue, coupon rate, maturity, individual trading characteristics and other market data. Short-term obligations, including commercial paper, having 60 days or less to maturity are recorded at amortized cost which approximates value. Debt securities are subject to interest rate and credit risks. In addition, all debt securities involve some risk of default with respect to interest and/or principal payments.

Foreign securities (including foreign exchange contracts) are converted into U.S. dollar amounts using the applicable exchange rates as of the close of the NYSE. If market quotations are available and reliable for foreign exchange traded equity securities, the securities will be valued at the market quotations. Because trading hours for certain foreign securities end before the close of the NYSE, closing market quotations may become unreliable. If between the time trading ends on a particular security and the close of the customary trading session on the NYSE, events occur that are significant and make the closing price unreliable, the Fund may fair value the security. If the event is likely to have affected the closing price of the security, the security will be valued at fair value in good faith using procedures approved by the Board of Trustees. Adjustments to closing prices to reflect fair value may also be based on a screening process of an independent pricing service to indicate the degree of certainty, based on historical data, that the closing price in the principal market where a foreign security trades is not the current value as of the close of the NYSE. Foreign securities meeting the approved degree of certainty that the price is not reflective of current value will be priced at the indication of fair value from the independent pricing service. Multiple factors may be considered by the independent pricing service in determining adjustments to reflect fair value and may include information relating to sector indices, American Depositary Receipts and domestic and foreign index futures. Foreign securities may have additional risks including exchange rate changes, potential for sharply devalued currencies and high inflation, political and economical upheaval, the relative lack of issuer information, relatively low market liquidity and the potential lack of strict financial and accounting controls and standards.

Securities for which market prices are not provided by any of the above methods may be valued based upon quotes furnished by independent sources. The last bid price may be used to value equity securities. The mean between the last bid and asked prices is used to value debt obligations, including Corporate Loans.

Securities for which market quotations are not readily available or are unreliable are valued at fair value as determined in good faith by or under the supervision of the Trust's officers following procedures approved by the Board of Trustees. Issuer specific events, market trends, bid/ask quotes of brokers and information providers and other market data may be reviewed in the course of making a good faith determination of a security's fair value.

Valuations change in response to many factors including the historical and prospective earnings of the issuer, the value of the issuer's assets, general economic conditions, interest rates, investor perceptions and market liquidity. Because of the inherent uncertainties of valuation, the values reflected in the financial statements may materially differ from the value received upon actual sale of those investments.

**B. Securities Transactions and Investment Income** — Securities transactions are accounted for on a trade date basis. Realized gains or losses on sales are computed on the basis of specific identification of the securities sold. Interest income is recorded on the accrual basis from settlement date. Dividend income (net of withholding tax, if any) is recorded on the ex-dividend date.

The Fund may periodically participate in litigation related to Fund investments. As such, the Fund may receive proceeds from litigation settlements. Any proceeds received are included in the Statement of Operations as realized gain (loss) for investments no longer held and as unrealized gain (loss) for investments still held.

Brokerage commissions and mark ups are considered transaction costs and are recorded as an increase to the cost basis of securities purchased and/or a reduction of proceeds on a sale of securities. Such transaction costs are included in the determination of net realized and unrealized gain (loss) from investment securities reported in the Statement of Operations and the Statement of Changes in Net Assets and the net realized and unrealized gains (losses) on securities per share in the Financial Highlights. Transaction costs are included in the calculation of the Fund's net asset value and, accordingly, they reduce the Fund's total returns. These transaction costs are not considered operating expenses and are not reflected in net investment income reported in the Statement of Operations and Statement of Changes in Net Assets, or the net investment income per share and ratios of expenses and net investment income reported in the Financial Highlights, nor are they limited by any expense limitation arrangements between the Fund and the investment adviser.

The Fund allocates income and realized and unrealized capital gains and losses to a class based on the relative net assets of each class.

**C. Country Determination** — For the purposes of making investment selection decisions and presentation in the Schedule of Investments, the investment adviser may determine the country in which an issuer is located and/or credit risk exposure based on various factors. These factors include the laws of the country under which the issuer is organized, where the issuer maintains a principal office, the country in which the issuer derives 50% or more of its total revenues and the country that has the primary market for the issuer's securities, as well as other criteria. Among the other criteria that may be evaluated for making this determination are the country in which the issuer maintains 50% or more of its assets, the type of security, financial guarantees and enhancements, the nature of the collateral and the sponsor organization. Country of issuer and/or credit risk exposure has been determined to be the United States of America, unless otherwise noted.

**D. Distributions** — Distributions from income and net realized capital gain, if any, are generally paid to separate accounts of participating insurance companies annually and recorded on ex-dividend date.

**E. Federal Income Taxes** — The Fund intends to comply with the requirements of Subchapter M of the Internal Revenue Code necessary to qualify as a regulated investment company and to distribute substantially all of the Fund's taxable earnings to shareholders. As such, the Fund will not be subject to federal income taxes on otherwise taxable income (including net realized capital gain) that is distributed to shareholders. Therefore, no provision for federal income taxes is recorded in the financial statements.

The Fund files tax returns in the U.S. Federal jurisdiction and certain other jurisdictions. Generally the Fund is subject to examinations by such taxing authorities for up to three years after the filing of the return for the tax period.

**F. Expenses** — Fees provided for under the Rule 12b-1 plan of a particular class of the Fund and which are directly attributable to that class are charged to the operations of such class. All other expenses are allocated among the classes based on relative net assets.

**G. Accounting Estimates** — The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America ("GAAP") requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period including estimates and assumptions related to taxation. Actual results could differ from those estimates by a significant amount. In addition, the Fund monitors for material events or transactions that may occur or become known after the period-end date and before the date the financial statements are released to print.

**H. Indemnifications** — Under the Trust's organizational documents, each Trustee, officer, employee or other agent of the Trust is indemnified against certain liabilities that may arise out of performance of their duties to the Fund. Additionally, in the normal course of business, the Fund enters into contracts, including the Fund's servicing agreements that contain a variety of indemnification clauses. The Fund's maximum exposure under these arrangements is unknown as this would involve future claims that may be made against the Fund that have not yet occurred. The risk of material loss as a result of such indemnification claims is considered remote.

**I. Other Risks** — The Fund's investments are concentrated in a comparatively narrow segment of the economy, which may make the Fund more volatile.

The Fund may invest a large percentage of its assets in a limited number of securities or other instruments, which could negatively affect the value of the Fund.

The following factors may affect the Fund's investments in the utilities sector: governmental regulation, economic factors, ability of the issuer to obtain financing, prices of natural resources and risks associated with nuclear power.

**J. Securities Lending** — The Fund may lend portfolio securities having a market value up to one-third of the Fund's total assets. Such loans are secured by collateral equal to no less than the market value of the loaned securities determined daily by the securities lending provider. Such collateral will be cash or debt securities issued or guaranteed by the U.S. Government or any of its sponsored agencies. Cash collateral received in connection with these loans is invested in short-term money market instruments or affiliated money market funds and is shown as such on the Schedule of Investments. It is the Fund's policy to obtain additional collateral from or return excess collateral to the borrower by the end of the next business day, following the valuation date of the securities loaned. Therefore, the value of the collateral held may be temporarily less than the value of the securities on loan. Lending securities entails a risk of loss to the Fund if and to the extent that the market value of the securities loaned were to increase and the borrower did not increase the collateral accordingly, and the borrower fails to return the securities. Upon the failure of the borrower to return the securities, collateral may be liquidated and the securities may be purchased on the open market to replace the loaned securities. The Fund could experience delays and costs in gaining access to the collateral. The Fund bears the risk of any deficiency in the amount of the collateral available for return to the borrower due to any loss on the collateral invested. Dividends received on cash collateral investments for securities lending transactions, which are net of compensation to counterparties, is included in Dividends from affiliates on the Statement of Operations. The aggregate value of securities out on loan is shown as a footnote on the Statement of Assets and Liabilities, if any.

**K. Foreign Currency Translations** — Foreign currency is valued at the close of the NYSE based on quotations posted by banks and major currency dealers. Portfolio securities and other assets and liabilities denominated in foreign currencies are translated into U.S. dollar amounts at date of valuation. Purchases and sales of portfolio securities (net of foreign taxes withheld on disposition) and income items denominated in foreign currencies are translated into U.S. dollar amounts on the respective dates of such transactions. The Fund does not separately account for the portion of the results of operations resulting from changes in foreign exchange rates on investments and the fluctuations arising from changes in market prices of securities held. The combined results of changes in foreign exchange rates and the fluctuation of market prices on investments (net of estimated foreign tax withholding) are included with the net realized and unrealized gain or loss from investments in the Statement of Operations. Reported net realized foreign currency gains or losses arise from (1) sales of foreign currencies, (2) currency gains or losses realized between the trade and settlement dates on securities transactions, and (3) the difference between the amounts of dividends, interest, and foreign withholding taxes recorded on the Fund's books and the U.S. dollar equivalent of the amounts actually received or paid. Net unrealized foreign currency gains and losses arise from changes in the fair values of assets and liabilities, other than investments in securities at fiscal period end, resulting from changes in exchange rates.

The Fund may invest in foreign securities which may be subject to foreign taxes on income, gains on investments or currency repatriation, a portion of which may be recoverable.

**L. Foreign Currency Contracts** — The Fund may enter into foreign currency contracts to manage or minimize currency or exchange rate risk. The Fund may also enter into foreign currency contracts for the purchase or sale of a security denominated in a foreign currency in order to "lock in" the U.S. dollar price of that security. A foreign currency contract is an obligation to purchase or sell a specific currency for an agreed-upon price at a future date. The use of foreign currency contracts does not eliminate fluctuations in the price of the underlying securities the Fund owns or intends to acquire but establishes a rate of exchange in advance. Fluctuations in the value of these contracts are measured by the difference in the contract date and reporting date exchange rates and are recorded as unrealized appreciation (depreciation) until the contracts are closed. When the contracts are closed, realized gains (losses) are recorded. Realized and unrealized gains (losses) on the contracts are included in the Statement of Operations. The primary risks associated with foreign currency contracts include failure of the counterparty to meet the terms of the contract and the value of the foreign currency changing unfavorably. These risks may be in excess of the amounts reflected in the Statement of Assets and Liabilities.

## NOTE 2—Advisory Fees and Other Fees Paid to Affiliates

The Trust has entered into a master investment advisory agreement with Invesco Advisers, Inc. (the "Adviser" or "Invesco"). Under the terms of the investment advisory agreement, the Fund pays an advisory fee to the Adviser based on the annual rate of 0.60% of the Fund's average daily net assets.

Under the terms of a master sub-advisory agreement between the Adviser and each of Invesco Asset Management Deutschland GmbH, Invesco Asset Management Limited, Invesco Asset Management (Japan) Limited, Invesco Australia Limited, Invesco Hong Kong Limited, Invesco Senior Secured Management, Inc. and Invesco Trimark Ltd. (collectively, the "Affiliated Sub-Advisers") the Adviser, not the Fund, may pay 40% of the fees paid to the Adviser to any such Affiliated Sub-Adviser(s) that provide discretionary investment management services to the Fund based on the percentage of assets allocated to such Sub-Adviser(s).

The Adviser has contractually agreed, through at least April 30, 2012, to waive advisory fees and/or reimburse expenses to the extent necessary to limit total annual fund operating expenses after fee waiver and/or expense reimbursement (excluding certain items discussed below) of Series I shares to 0.93% and Series II shares to 1.18% of average daily net assets. In determining the Adviser's obligation to waive advisory fees and/or reimburse expenses, the following expenses are not taken into account, and could cause the total annual fund operating expenses after fee waiver and/or expense reimbursement to exceed the numbers reflected above: (1) interest; (2) taxes; (3) dividend expense on short sales; (4) extraordinary or non-routine items; and (5) expenses that the Fund has incurred but did not actually pay because of an expense offset arrangement. Unless the Board of the Trustees and Invesco mutually agree to amend or continue the fee waiver agreement, it will terminate on April 30, 2012.

Further, the Adviser has contractually agreed, through at least June 30, 2011, to waive the advisory fee payable by the Fund in an amount equal to 100% of the net advisory fees the Adviser receives from the affiliated money market funds on investments by the Fund of uninvested cash in such affiliated money market funds.

For the year ended December 31, 2010, the Adviser waived advisory fees of $77,324.

At the request of the Trustees of the Trust, Invesco Ltd. agreed to reimburse expenses incurred by the Fund in connection with market timing matters in the Invesco Funds, which may include legal, audit, shareholder reporting, communications and trustee expenses. For the year ended December 31, 2010, Invesco Ltd. did not reimburse any expenses.

The Trust has entered into a master administrative services agreement with Invesco pursuant to which the Fund has agreed to pay Invesco a fee for costs incurred in providing accounting services and fund administrative services to the Fund and to reimburse Invesco for administrative services fees paid to insurance companies that have agreed to provide services to the participants of separate accounts. These administrative services provided by the insurance companies may include, among other things: the printing of prospectuses, financial reports and proxy statements and the delivery of the same to existing participants; the maintenance of master accounts; the facilitation of purchases and redemptions requested by the participants; and the servicing of participants' accounts. Pursuant to such agreement, for the year ended December 31, 2010, Invesco was paid $50,000 for accounting and fund administrative services and reimbursed $149,065 for services provided by insurance companies.

The Trust has entered into a transfer agency and service agreement with Invesco Investment Services, Inc. ("IIS") pursuant to which the Fund has agreed to pay IIS a fee for providing transfer agency and shareholder services to the Fund and reimburse IIS for certain expenses incurred by IIS in the course of providing such services. For the year ended December 31, 2010, expenses incurred under the agreement are shown in the Statement of Operations as transfer agent fees.

The Trust has entered into a master distribution agreement with IDI to serve as the distributor for the Fund. The Trust has adopted a plan pursuant to Rule 12b-1 under the 1940 Act with respect to the Fund's Series II shares (the "Plan"). The Fund, pursuant to the Plan, pays IDI compensation at the annual rate of 0.25% of the Fund's average daily net assets of Series II shares. Of the Plan payments, up to 0.25% of the average daily net assets of the Series II shares may be paid to insurance companies who furnish continuing personal shareholder services to customers who purchase and own Series II shares of the Fund. For the year ended December 31, 2010, expenses incurred under the Plan are detailed in the Statement of Operations as distribution fees.

Certain officers and trustees of the Trust are officers and directors of Invesco, IIS and/or IDI.

## NOTE 3—Additional Valuation Information

GAAP defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date, under current market conditions. GAAP establishes a hierarchy that prioritizes the inputs to valuation methods giving the highest priority to readily available unadjusted quoted prices in an active market for identical assets (Level 1) and the lowest priority to significant unobservable inputs (Level 3) generally when market prices are not readily available or are unreliable. Based on the valuation inputs, the securities or other investments are tiered into one of three levels. Changes in valuation methods may result in transfers in or out of an investment's assigned level:

Level 1 — Prices are determined using quoted prices in an active market for identical assets.

Level 2 — Prices are determined using other significant observable inputs. Observable inputs are inputs that other market participants may use in pricing a security. These may include quoted prices for similar securities, interest rates, prepayment speeds, credit risk, yield curves, loss severities, default rates, discount rates, volatilities and others.

Level 3 — Prices are determined using significant unobservable inputs. In situations where quoted prices or observable inputs are unavailable (for example, when there is little or no market activity for an investment at the end of the period), unobservable inputs may be used. Unobservable inputs reflect the Fund's own assumptions about the factors market participants would use in determining fair value of the securities or instruments and would be based on the best available information.

The following is a summary of the tiered valuation input levels, as of December 31, 2010. The level assigned to the securities valuations may not be an indication of the risk or liquidity associated with investing in those securities. Because of the inherent uncertainties of valuation, the values reflected in the financial statements may materially differ from the value received upon actual sale of those investments.

During the year ended December 31, 2010, there were no significant transfers between investment levels.

| | Level 1 | Level 2 | Level 3 | Total |
|---|---|---|---|---|
| Equity Securities | $62,616,700 | $2,797,076 | $— | $65,413,776 |

## NOTE 4—Trustees' and Officers' Fees and Benefits

"Trustees' and Officers' Fees and Benefits" include amounts accrued by the Fund to pay remuneration to certain Trustees and Officers of the Fund. Trustees have the option to defer compensation payable by the Fund, and "Trustees' and Officers' Fees and Benefits" also include amounts accrued by the Fund to fund such deferred compensation amounts. Those Trustees who defer compensation have the option to select various Invesco Funds in which their deferral accounts shall be deemed to be invested. Finally, certain current Trustees are eligible to participate in a retirement plan that provides for benefits to be paid upon retirement to Trustees over a period of time based on the number of years of service. The Fund may have certain former Trustees who also participate in a retirement plan and receive benefits under such plan. "Trustees' and Officers' Fees and Benefits" include amounts accrued by the Fund to fund such retirement benefits. Obligations under the deferred compensation and retirement plans represent unsecured claims against the general assets of the Fund.

During the year ended December 31, 2010, the Fund paid legal fees of $2,639 for services rendered by Kramer, Levin, Naftalis & Frankel LLP as counsel to the Independent Trustees. A member of that firm is a Trustee of the Trust.

## NOTE 5—Cash Balances

The Fund is permitted to temporarily carry a negative or overdrawn balance in its account with The State Street Bank and Trust Company, the custodian bank. To compensate the custodian bank for such overdrafts, the overdrawn Fund may either (1) leave funds as a compensating balance in the account so the custodian bank can be compensated by earning the additional interest; or (2) compensate by paying the custodian bank at a rate agreed upon by the custodian bank and Invesco, not to exceed the contractually agreed upon rate.

## NOTE 6—Distributions to Shareholders and Tax Components of Net Assets

### Tax Character of Distributions to Shareholders Paid During the Years Ended December 31, 2010 and 2009:

| | 2010 | 2009 |
|---|---|---|
| Ordinary income | $2,364,336 | $3,218,442 |
| Long-term capital gain | — | 810,063 |
| Total distributions | $2,364,336 | $4,028,505 |

### Tax Components of Net Assets at Period-End:

| | 2010 |
|---|---|
| Undistributed ordinary income | $ 2,168,788 |
| Net unrealized appreciation — investments | 9,041,335 |
| Net unrealized appreciation — other investments | 3,499 |
| Temporary book/tax differences | (48,991) |
| Capital loss carryforward | (1,436,392) |
| Shares of beneficial interest | 55,921,999 |
| Total net assets | $65,650,238 |

The difference between book-basis and tax-basis unrealized appreciation (depreciation) is due to differences in the timing of recognition of gains and losses on investments for tax and book purposes. The Fund's net unrealized appreciation difference is attributable primarily to wash sales.

The temporary book/tax differences are a result of timing differences between book and tax recognition of income and/or expenses. The Fund's temporary book/tax differences are the result of the trustee deferral of compensation and retirement plan benefits.

Capital loss carryforward is calculated and reported as of a specific date. Results of transactions and other activity after that date may affect the amount of capital loss carryforward actually available for the Fund to utilize. The ability to utilize capital loss carryforward in the future may be limited under the Internal Revenue Code and related regulations based on the results of future transactions.

The Fund utilized $2,208,857 of capital loss carryforward in the current period to offset net realized capital gain for federal income tax purposes.

The Fund has a capital loss carryforward as of December 31, 2010 which expires as follows:

| Expiration | Capital Loss Carryforward* |
|---|---|
| December 31, 2017 | $1,436,392 |

* Capital loss carryforward as of the date listed above is reduced for limitations, if any, to the extent required by the Internal Revenue Code.

## NOTE 7—Investment Securities

The aggregate amount of investment securities (other than short-term securities, U.S. Treasury obligations and money market funds, if any) purchased and sold by the Fund during the year ended December 31, 2010 was $8,304,719 and $15,568,065, respectively. Cost of investments on a tax basis includes the adjustments for financial reporting purposes as of the most recently completed Federal income tax reporting period-end.

**Unrealized Appreciation (Depreciation) of Investment Securities on a Tax Basis**

| | |
|---|---|
| Aggregate unrealized appreciation of investment securities | $11,048,879 |
| Aggregate unrealized (depreciation) of investment securities | (2,007,544) |
| Net unrealized appreciation of investment securities | $ 9,041,335 |

Cost of investments for tax purposes is $56,372,441.

## NOTE 8—Reclassification of Permanent Differences

Primarily as a result of differing book/tax treatment of foreign currency transactions, on December 31, 2010, undistributed net investment income was increased by $14,613 and undistributed net realized gain (loss) was decreased by $14,613. This reclassification had no effect on the net assets of the Fund.

## NOTE 9—Share Information

**Summary of Share Activity**

| | Year ended December 31, | | | |
|---|---|---|---|---|
| | 2010[a] | | 2009 | |
| | Shares | Amount | Shares | Amount |
| Sold: | | | | |
| Series I | 480,106 | $ 6,843,415 | 609,839 | $ 8,004,977 |
| Series II | 7,837 | 110,711 | 12,671 | 166,300 |
| Issued as reinvestment of dividends: | | | | |
| Series I | 160,460 | 2,309,020 | 276,664 | 3,939,705 |
| Series II | 3,865 | 55,316 | 6,267 | 88,800 |
| Reacquired: | | | | |
| Series I | (1,210,979) | (17,239,349) | (2,046,142) | (26,621,947) |
| Series II | (14,275) | (198,195) | (30,065) | (379,113) |
| Net increase (decrease) in share activity | (572,986) | $ (8,119,082) | (1,170,766) | $(14,801,278) |

[a] There are entities that are record owners of more than 5% of the outstanding shares of the Fund and in the aggregate own 47% of the outstanding shares of the Fund. The Fund and the Fund's principal underwriter or adviser, are parties to participation agreements with these entities whereby these entities sell units of interest in separate accounts funding variable products that are invested in the Fund. The Fund, Invesco and/or Invesco affiliates may make payments to these entities, which are considered to be related to the Fund, for providing services to the Fund, Invesco and/or Invesco affiliates including but not limited to services such as, securities brokerage, third party record keeping and account servicing and administrative services. The Trust has no knowledge as to whether all or any portion of the shares owned of record by these entities are also owned beneficially.

## NOTE 10—Financial Highlights

The following schedule presents financial highlights for a share of the Fund outstanding throughout the periods indicated.

| | Net asset value, beginning of period | Net investment income[a] | Net gains (losses) on securities (both realized and unrealized) | Total from investment operations | Dividends from net investment income | Distributions from net realized gains | Total Distributions | Net asset value, end of period | Total return[b] | Net assets, end of period (000s omitted) | Ratio of expenses to average net assets with fee waivers and/or expenses absorbed | Ratio of expenses to average net assets without fee waivers and/or expenses absorbed | Ratio of net investment income to average net assets | Portfolio turnover[c] |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **Series I** | | | | | | | | | | | | | | |
| Year ended 12/31/10 | $14.51 | $0.47 | $ 0.43 | $ 0.90 | $(0.54) | $ — | $(0.54) | $14.87 | 6.30% | $ 63,945 | 0.92%[d] | 1.04%[d] | 3.25%[d] | 13% |
| Year ended 12/31/09 | 13.38 | 0.45 | 1.53 | 1.98 | (0.68) | (0.17) | (0.85) | 14.51 | 14.93 | 70,671 | 0.93 | 1.04 | 3.35 | 14 |
| Year ended 12/31/08 | 23.97 | 0.52 | (8.36) | (7.84) | (0.59) | (2.16) | (2.75) | 13.38 | (32.35) | 80,704 | 0.93 | 0.96 | 2.53 | 15 |
| Year ended 12/31/07 | 21.23 | 0.47 | 3.94 | 4.41 | (0.47) | (1.20) | (1.67) | 23.97 | 20.64 | 155,748 | 0.93 | 0.94 | 1.97 | 30 |
| Year ended 12/31/06 | 17.83 | 0.47 | 4.06 | 4.53 | (0.70) | (0.43) | (1.13) | 21.23 | 25.46 | 139,080 | 0.93 | 0.96 | 2.40 | 38 |
| **Series II** | | | | | | | | | | | | | | |
| Year ended 12/31/10 | 14.43 | 0.43 | 0.42 | 0.85 | (0.50) | — | (0.50) | 14.78 | 6.01 | 1,706 | 1.17[d] | 1.29[d] | 3.00[d] | 13 |
| Year ended 12/31/09 | 13.30 | 0.41 | 1.52 | 1.93 | (0.63) | (0.17) | (0.80) | 14.43 | 14.61 | 1,702 | 1.18 | 1.29 | 3.10 | 14 |
| Year ended 12/31/08 | 23.80 | 0.46 | (8.28) | (7.82) | (0.52) | (2.16) | (2.68) | 13.30 | (32.51) | 1,717 | 1.18 | 1.21 | 2.28 | 15 |
| Year ended 12/31/07 | 21.12 | 0.41 | 3.91 | 4.32 | (0.44) | (1.20) | (1.64) | 23.80 | 20.32 | 3,293 | 1.18 | 1.19 | 1.72 | 30 |
| Year ended 12/31/06 | 17.76 | 0.42 | 4.06 | 4.48 | (0.69) | (0.43) | (1.12) | 21.12 | 25.25 | 2,462 | 1.18 | 1.21 | 2.15 | 38 |

(a) Calculated using average shares outstanding.

(b) Includes adjustments in accordance with accounting principles generally accepted in the United States of America and as such, the net asset value for financial reporting purposes and the returns based upon those net asset values may differ from the net asset value and returns for shareholder transactions. Total returns do not reflect charges assessed in connection with a variable product, which if included would reduce total returns.

(c) Portfolio turnover is calculated at the fund level and is not annualized for periods less than one year, if applicable.

(d) Ratios are based on average daily net assets (000's) of $64,763 and $1,636 for Series I and Series II shares, respectively.

# Report of Independent Registered Public Accounting Firm

To the Board of Trustees of AIM Variable Insurance Funds (Invesco Variable Insurance Funds)
and Shareholders of Invesco V.I. Utilities Fund:

In our opinion, the accompanying statement of assets and liabilities, including the schedule of investments, and the related statements of operations and of changes in net assets and the financial highlights present fairly, in all material respects, the financial position of Invesco V.I. Utilities Fund (formerly known as AIM V.I. Utilities Fund; one of the funds constituting AIM Variable Insurance Funds (Invesco Variable Insurance Funds), hereafter referred to as the "Fund") at December 31, 2010, the results of its operations for the year then ended, the changes in its net assets for each of the two years in the period then ended and the financial highlights for the each of the five years in the period then ended, in conformity with accounting principles generally accepted in the United States of America. These financial statements and financial highlights (hereafter referred to as "financial statements") are the responsibility of the Fund's management. Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these financial statements in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits, which included confirmation of securities at December 31, 2010 by correspondence with the custodian and brokers, provide a reasonable basis for our opinion.

PRICEWATERHOUSECOOPERS LLP

February 9, 2011
Houston, Texas

# Calculating your ongoing Fund expenses

### Example

As a shareholder of the Fund, you incur ongoing costs, including management fees; distribution and/or service fees (12b-1); and other Fund expenses. This example is intended to help you understand your ongoing costs (in dollars) of investing in the Fund and to compare these costs with ongoing costs of investing in other mutual funds. The example is based on an investment of $1,000 invested at the beginning of the period and held for the entire period July 1, 2010 through December 31, 2010.

The actual and hypothetical expenses in the examples below do not represent the effect of any fees or other expenses assessed in connection with a variable product; if they did, the expenses shown would be higher while the ending account values shown would be lower.

### Actual expenses

The table below provides information about actual account values and actual expenses. You may use the information in this table, together with the amount you invested, to estimate the expenses that you paid over the period. Simply divide your account value by $1,000 (for example, an $8,600 account value divided by $1,000 = 8.6), then multiply the result by the number in the table under the heading entitled "Actual Expenses Paid During Period" to estimate the expenses you paid on your account during this period.

### Hypothetical example for comparison purposes

The table below also provides information about hypothetical account values and hypothetical expenses based on the Fund's actual expense ratio and an assumed rate of return of 5% per year before expenses, which is not the Fund's actual return.

*The hypothetical account values and expenses may not be used to estimate the actual ending account balance or expenses you paid for the period. You may use this information to compare the ongoing costs of investing in the Fund and other funds. To do so, compare this 5% hypothetical example with the 5% hypothetical examples that appear in the shareholder reports of the other funds.*

Please note that the expenses shown in the table are meant to highlight your ongoing costs. Therefore, the hypothetical information is useful in comparing ongoing costs, and will not help you determine the relative total costs of owning different funds.

| | | ACTUAL | | HYPOTHETICAL (5% annual return before expenses) | | |
|---|---|---|---|---|---|---|
| Class | Beginning Account Value (07/01/10) | Ending Account Value (12/31/10)[1] | Expenses Paid During Period[2] | Ending Account Value (12/31/10) | Expenses Paid During Period[2] | Annualized Expense Ratio |
| Series I | $1,000.00 | $1,155.40 | $5.00 | $1,020.57 | $4.69 | 0.92% |
| Series II | 1,000.00 | 1,154.50 | 6.35 | 1,019.31 | 5.96 | 1.17 |

[1] The actual ending account value is based on the actual total return of the Fund for the period July 1, 2010 through December 31, 2010, after actual expenses and will differ from the hypothetical ending account value which is based on the Fund's expense ratio and a hypothetical annual return of 5% before expenses.

[2] Expenses are equal to the Fund's annualized expense ratio as indicated above multiplied by the average account value over the period, multiplied by 184/365 to reflect the most recent fiscal half year.

# Tax Information

Form 1099-DIV, Form 1042-S and other year-end tax information provide shareholders with actual calendar year amounts that should be included in their tax returns. Shareholders should consult their tax advisors.

The following distribution information is being provided as required by the Internal Revenue Code or to meet a specific state's requirement.

The Fund designates the following amounts or, if subsequently determined to be different, the maximum amount allowable for its fiscal year ended December 31, 2010:

| Federal and State Income Tax | |
|---|---|
| Corporate Dividends Received Deduction* | 100% |

* The above percentage is based on ordinary income dividends paid to shareholders during the Fund's fiscal year.

# Trustees and Officers

The address of each trustee and officer is AIM Variable Insurance Funds (Invesco Variable Insurance Funds) (the "Trust"), 11 Greenway Plaza, Suite 2500, Houston, Texas 77046-1173. The trustees serve for the life of the Trust, subject to their earlier death, incapacitation, resignation, retirement or removal as more specifically provided in the Trust's organizational documents. Each officer serves for a one year term or until their successors are elected and qualified. Column two below includes length of time served with predecessor entities, if any.

| Name, Year of Birth and Position(s) Held with the Trust | Trustee and/or Officer Since | Principal Occupation(s) During Past 5 Years | Number of Funds in Fund Complex Overseen by Trustee | Other Directorship(s) Held by Trustee |
|---|---|---|---|---|
| **Interested Persons** | | | | |
| Martin L. Flanagan[1] — 1960<br>Trustee | 2007 | Executive Director, Chief Executive Officer and President, Invesco Ltd. (ultimate parent of Invesco and a global investment management firm); Advisor to the Board, Invesco Advisers, Inc. (formerly known as Invesco Institutional (N.A.), Inc.); Trustee, The Invesco Funds; Vice Chair, Investment Company Institute; and Member of Executive Board, SMU Cox School of Business<br><br>Formerly: Chairman, Invesco Advisers, Inc. (registered investment adviser); Director, Chairman, Chief Executive Officer and President, IVZ Inc. (holding company), INVESCO Group Services, Inc. (service provider) and Invesco North American Holdings, Inc. (holding company); Director, Chief Executive Officer and President, Invesco Holding Company Limited (parent of Invesco and a global investment management firm); Director, Invesco Ltd.; Chairman, Investment Company Institute and President, Co-Chief Executive Officer, Co-President, Chief Operating Officer and Chief Financial Officer, Franklin Resources, Inc. (global investment management organization) | 208 | None |
| Philip A. Taylor[2] — 1954<br>Trustee, President and Principal Executive Officer | 2006 | Head of North American Retail and Senior Managing Director, Invesco Ltd.; Director, Co-Chairman, Co-President and Co-Chief Executive Officer, Invesco Advisers, Inc. (formerly known as Invesco Institutional (N.A.), Inc.) (registered investment adviser); Director, Chief Executive Officer and President, 1371 Preferred Inc. (holding company); Director, Chairman, Chief Executive Officer and President, Invesco Management Group, Inc. (formerly Invesco Aim Management Group, Inc.) (financial services holding company); Director and President, INVESCO Funds Group, Inc. (registered investment adviser and registered transfer agent) and AIM GP Canada Inc. (general partner for limited partnerships); Director and Chairman, Invesco Investment Services, Inc. (formerly known as Invesco Aim Investment Services, Inc.) (registered transfer agent) and IVZ Distributors, Inc. (formerly known as INVESCO Distributors, Inc.) (registered broker dealer); Director, President and Chairman, Invesco Inc. (holding company) and Invesco Canada Holdings Inc. (holding company); Chief Executive Officer, Invesco Trimark Corporate Class Inc. (corporate mutual fund company) and Invesco Trimark Canada Fund Inc. (corporate mutual fund company); Director and Chief Executive Officer, Invesco Trimark Ltd./Invesco Trimark Ltèe (registered investment adviser and registered transfer agent) and Invesco Trimark Dealer Inc. (registered broker dealer); Trustee, President and Principal Executive Officer, The Invesco Funds (other than AIM Treasurer's Series Trust (Invesco Treasurer's Series Trust) and Short-Term Investments Trust); Trustee and Executive Vice President, The Invesco Funds (AIM Treasurer's Series Trust (Invesco Treasurer's Series Trust) and Short-Term Investments Trust only); and Director, Van Kampen Asset Management; Director, Chief Executive Officer and President, Van Kampen Investments Inc. and Van Kampen Exchange Corp.; Director and Chairman, Van Kampen Investor Services Inc. and Director and President, Van Kampen Advisors, Inc.<br><br>Formerly: Director, Invesco Distributors, Inc. (formerly known as Invesco Aim Distributors, Inc.) (registered broker dealer); Manager, Invesco PowerShares Capital Management LLC; Director, Chief Executive Officer and President, Invesco Advisers, Inc.; Director, Chairman, Chief Executive Officer and President, Invesco Aim Capital Management, Inc.; President, Invesco Trimark Dealer Inc. and Invesco Trimark Ltd./Invesco Trimark Ltèe; Director and President, AIM Trimark Corporate Class Inc. and AIM Trimark Canada Fund Inc.; Senior Managing Director, Invesco Holding Company Limited; Trustee and Executive Vice President, Tax-Free Investments Trust; Director and Chairman, Fund Management Company (former registered broker dealer); President and Principal Executive Officer, The Invesco Funds (AIM Treasurer's Series Trust (Invesco Treasurer's Series Trust), Short-Term Investments Trust and Tax-Free Investments Trust only); President, AIM Trimark Global Fund Inc. and AIM Trimark Canada Fund Inc. | 208 | None |
| Wayne M. Whalen[3] – 1939<br>Trustee | 2010 | Of Counsel, and prior to 2010, partner in the law firm of Skadden, Arps, Slate, Meagher & Flom LLP, legal counsel to funds in the Fund Complex | 226 | Director of the Abraham Lincoln Presidential Library Foundation |
| **Independent Trustees** | | | | |
| Bruce L. Crockett – 1944<br>Trustee and Chair | 1993 | Chairman, Crockett Technology Associates (technology consulting company)<br><br>Formerly: Director, Captaris (unified messaging provider); Director, President and Chief Executive Officer COMSAT Corporation; and Chairman, Board of Governors of INTELSAT (international communications company) | 208 | ACE Limited (insurance company); and Investment Company Institute |
| David C. Arch – 1945<br>Trustee | 2010 | Chairman and Chief Executive Officer of Blistex Inc., a consumer health care products manufacturer. | 226 | Member of the Heartland Alliance Advisory Board, a nonprofit organization serving human needs based in Chicago. Board member of the Illinois Manufacturers' Association. Member of the Board of Visitors, Institute for the Humanities, University of Michigan |

[1] Mr. Flanagan is considered an interested person of the Trust because he is an officer of the adviser to the Trust, and an officer and a director of Invesco Ltd., ultimate parent of the adviser to the Trust.
[2] Mr. Taylor is considered an interested person of the Trust because he is an officer and a director of the adviser to, and a director of the principal underwriter of, the Trust.
[3] Mr. Whalen is considered an "interested person" (within the meaning of Section 2(a)(19) of the 1940 Act) of certain Funds in the Fund Complex by reason of he and his firm currently providing legal services as legal counsel to such Funds in the Fund Complex.

# Trustees and Officers – (continued)

| Name, Year of Birth and Position(s) Held with the Trust | Trustee and/or Officer Since | Principal Occupation(s) During Past 5 Years | Number of Funds in Fund Complex Overseen by Trustee | Other Directorship(s) Held by Trustee |
|---|---|---|---|---|
| **Independent Trustees** | | | | |
| Bob R. Baker – 1936<br>Trustee | 2004 | Retired<br><br>Formerly: President and Chief Executive Officer, AMC Cancer Research Center; and Chairman and Chief Executive Officer, First Columbia Financial Corporation | 208 | None |
| Frank S. Bayley – 1939<br>Trustee | 2001 | Retired<br><br>Formerly: Director, Badgley Funds, Inc. (registered investment company) (2 portfolios) and Partner, law firm of Baker & McKenzie | 208 | None |
| James T. Bunch – 1942<br>Trustee | 2004 | Founder, Green, Manning & Bunch Ltd. (investment banking firm)<br><br>Formerly: Executive Committee, United States Golf Association; and Director, Policy Studies, Inc. and Van Gilder Insurance Corporation | 208 | Vice Chairman, Board of Governors, Western Golf Association/Evans Scholars Foundation and Director, Denver Film Society |
| Rodney Dammeyer – 1940<br>Trustee | 2010 | President of CAC, LLC, a private company offering capital investment and management advisory services.<br><br>Formerly: Prior to January 2004, Director of TeleTech Holdings Inc.; Prior to 2002, Director of Arris Group, Inc.; Prior to 2001, Managing Partner at Equity Group Corporate Investments. Prior to 1995, Vice Chairman of Anixter International. Prior to 1985, experience includes Senior Vice President and Chief Financial Officer of Household International, Inc, Executive Vice President and Chief Financial Officer of Northwest Industries, Inc. and Partner of Arthur Andersen & Co. | 226 | Director of Quidel Corporation and Stericycle, Inc. Prior to May 2008, Trustee of The Scripps Research Institute. Prior to February 2008, Director of Ventana Medical Systems, Inc. Prior to April 2007, Director of GATX Corporation. Prior to April 2004, Director of TheraSense, Inc. |
| Albert R. Dowden – 1941<br>Trustee | 2000 | Director of a number of public and private business corporations, including the Boss Group, Ltd. (private investment and management); Reich & Tang Funds (5 portfolios) (registered investment company); and Homeowners of America Holding Corporation/ Homeowners of America Insurance Company (property casualty company)<br><br>Formerly: Director, Continental Energy Services, LLC (oil and gas pipeline service); Director, CompuDyne Corporation (provider of product and services to the public security market) and Director, Annuity and Life Re (Holdings), Ltd. (reinsurance company); Director, President and Chief Executive Officer, Volvo Group North America, Inc.; Senior Vice President, AB Volvo; Director of various public and private corporations; Chairman, DHJ Media, Inc.; Director Magellan Insurance Company; and Director, The Hertz Corporation, Genmar Corporation (boat manufacturer), National Media Corporation; Advisory Board of Rotary Power International (designer, manufacturer, and seller of rotary power engines); and Chairman, Cortland Trust, Inc. (registered investment company) | 208 | Board of Nature's Sunshine Products, Inc. |
| Jack M. Fields – 1952<br>Trustee | 1997 | Chief Executive Officer, Twenty First Century Group, Inc. (government affairs company); and Owner and Chief Executive Officer, Dos Angelos Ranch, L.P. (cattle, hunting, corporate entertainment), Discovery Global Education Fund (non-profit) and Cross Timbers Quail Research Ranch (non-profit)<br><br>Formerly: Chief Executive Officer, Texana Timber LP (sustainable forestry company) and member of the U.S. House of Representatives | 208 | Administaff |
| Carl Frischling – 1937<br>Trustee | 1993 | Partner, law firm of Kramer Levin Naftalis and Frankel LLP | 208 | Director, Reich & Tang Funds (16 portfolios) |
| Prema Mathai-Davis – 1950<br>Trustee | 1998 | Retired<br><br>Formerly: Chief Executive Officer, YWCA of the U.S.A. | 208 | None |
| Lewis F. Pennock – 1942<br>Trustee | 1993 | Partner, law firm of Pennock & Cooper | 208 | None |
| Larry Soll – 1942<br>Trustee | 2004 | Retired<br><br>Formerly, Chairman, Chief Executive Officer and President, Synergen Corp. (a biotechnology company) | 208 | None |
| Hugo F. Sonnenschein – 1940<br>Trustee | 2010 | President Emeritus and Honorary Trustee of the University of Chicago and the Adam Smith Distinguished Service Professor in the Department of Economics at the University of Chicago. Prior to July 2000, President of the University of Chicago. | 226 | Trustee of the University of Rochester and a member of its investment committee. Member of the National Academy of Sciences, the American Philosophical Society and a fellow of the American Academy of Arts and Sciences |
| Raymond Stickel, Jr. – 1944<br>Trustee | 2005 | Retired<br><br>Formerly: Director, Mainstay VP Series Funds, Inc. (25 portfolios) and Partner, Deloitte & Touche | 208 | None |

# Trustees and Officers – (continued)

| Name, Year of Birth and Position(s) Held with the Trust | Trustee and/or Officer Since | Principal Occupation(s) During Past 5 Years | Number of Funds in Fund Complex Overseen by Trustee | Other Directorship(s) Held by Trustee |
|---|---|---|---|---|
| **Other Officers** | | | | |
| Russell C. Burk — 1958<br>Senior Vice President and Senior Officer | 2005 | Senior Vice President and Senior Officer of Invesco Funds | N/A | N/A |
| John M. Zerr — 1962<br>Senior Vice President, Chief Legal Officer and Secretary | 2006 | Director, Senior Vice President, Secretary and General Counsel, Invesco Management Group, Inc. (formerly known as Invesco Aim Management Group, Inc.), Van Kampen Investments Inc. and Van Kampen Exchange Corp., Senior Vice President, Invesco Advisers, Inc. formerly known as Invesco Institutional (N.A.), Inc.) (registered investment adviser); Senior Vice President and Secretary, Invesco Distributors, Inc. (formerly known as Invesco Aim Distributors, Inc.); Director, Vice President and Secretary, Invesco Investment Services, Inc. (formerly known as Invesco Aim Investment Services, Inc.) and IVZ Distributors, Inc. (formerly known as INVESCO Distributors, Inc.); Director and Vice President, INVESCO Funds Group, Inc.; Senior Vice President, Chief Legal Officer and Secretary, The Invesco Funds; Manager, Invesco PowerShares Capital Management LLC; Director, Secretary and General Counsel, Van Kampen Asset Management; Director and Secretary, Van Kampen Advisors Inc.; Secretary and General Counsel, Van Kampen Funds Inc.; and Director, Vice President, Secretary and General Counsel, Van Kampen Investor Services Inc.; and Chief Legal Officer, PowerShares Exchange-Traded Fund Trust, PowerShares Exchange-Traded Fund Trust II, PowerShares India Exchange-Traded Fund Trust and PowerShares Actively Managed Exchange-Traded Fund Trust<br><br>Formerly: Director, Invesco Distributors, Inc. (formerly known as Invesco Aim Distributors, Inc.); Director, Senior Vice President, General Counsel and Secretary, Invesco Advisers, Inc.; Director, Vice President and Secretary, Fund Management Company; Director, Senior Vice President, Secretary, General Counsel and Vice President, Invesco Aim Capital Management, Inc.; Chief Operating Officer and General Counsel, Liberty Ridge Capital, Inc. (an investment adviser); Vice President and Secretary, PBHG Funds (an investment company) and PBHG Insurance Series Fund (an investment company); Chief Operating Officer, General Counsel and Secretary, Old Mutual Investment Partners (a broker-dealer); General Counsel and Secretary, Old Mutual Fund Services (an administrator) and Old Mutual Shareholder Services (a shareholder servicing center); Executive Vice President, General Counsel and Secretary, Old Mutual Capital, Inc. (an investment adviser); and Vice President and Secretary, Old Mutual Advisors Funds (an investment company) | N/A | N/A |
| Lisa O. Brinkley — 1959<br>Vice President | 2004 | Global Compliance Director, Invesco Ltd.; Chief Compliance Officer, Invesco Distributors, Inc. (formerly known as Invesco Aim Distributors, Inc.), Invesco Investment Services, Inc.(formerly known as Invesco Aim Investment Services, Inc.) and Van Kampen Investor Services Inc.; and Vice President, The Invesco Funds<br><br>Formerly: Senior Vice President, Invesco Management Group, Inc.; Senior Vice President and Chief Compliance Officer, Invesco Advisers, Inc. and The Invesco Funds; Vice President and Chief Compliance Officer, Invesco Aim Capital Management, Inc. and Invesco Distributors, Inc.; Vice President, Invesco Investment Services, Inc. and Fund Management Company | N/A | N/A |
| Sheri Morris — 1964<br>Vice President, Treasurer and Principal Financial Officer | 1999 | Vice President, Treasurer and Principal Financial Officer, The Invesco Funds; and Vice President, Invesco Advisers, Inc. (formerly known as Invesco Institutional (N.A.), Inc.) (registered investment adviser)<br><br>Formerly: Vice President, Invesco Advisers, Inc., Invesco Aim Capital Management, Inc. and Invesco Aim Private Asset Management, Inc.; Assistant Vice President and Assistant Treasurer, The Invesco Funds and Assistant Vice President, Invesco Advisers, Inc., Invesco Aim Capital Management, Inc. and Invesco Aim Private Asset Management, Inc. | N/A | N/A |
| Karen Dunn Kelley — 1960<br>Vice President | 1993 | Head of Invesco's World Wide Fixed Income and Cash Management Group; Senior Vice President, Invesco Advisers, Inc. (formerly known as Invesco Institutional (N.A.), Inc.) (registered investment adviser) and Van Kampen Investments Inc.; Executive Vice President, Invesco Distributors, Inc. (formerly known as Invesco Aim Distributors, Inc.); Senior Vice President, Invesco Management Group, Inc. (formerly known as Invesco Aim Management Group, Inc.); and Director, Invesco Mortgage Capital Inc.; Vice President, The Invesco Funds (other than AIM Treasurer's Series Trust (Invesco Treasurer's Series Trust) and Short-Term Investments Trust); President and Principal Executive Officer, The Invesco Funds (AIM Treasurer's Series Trust (Invesco Treasurer's Series Trust) and Short-Term Investments Trust only).<br><br>Formerly: Vice President, Invesco Advisers, Inc. (formerly known as Invesco Institutional (N.A.), Inc.); Director of Cash Management and Senior Vice President, Invesco Advisers, Inc. and Invesco Aim Capital Management, Inc.; President and Principal Executive Officer, Tax-Free Investments Trust; Director and President, Fund Management Company; Chief Cash Management Officer, Director of Cash Management, Senior Vice President, and Managing Director, Invesco Aim Capital Management, Inc.; Director of Cash Management, Senior Vice President, and Vice President, Invesco Advisers, Inc. and The Invesco Funds (AIM Treasurer's Series Trust (Invesco Treasurer's Series Trust), Short-Term Investments Trust and Tax-Free Investments Trust only) | N/A | N/A |

# Trustees and Officers – (continued)

| Name, Year of Birth and Position(s) Held with the Trust | Trustee and/or Officer Since | Principal Occupation(s) During Past 5 Years | Number of Funds in Fund Complex Overseen by Trustee | Other Directorship(s) Held by Trustee |
|---|---|---|---|---|
| **Other Officers** | | | | |
| Lance A. Rejsek — 1967<br>Anti-Money Laundering Compliance Officer | 2005 | Anti-Money Laundering Compliance Officer, Invesco Advisers, Inc. (formerly known as Invesco Institutional (N.A.), Inc.) (registered investment adviser); Invesco Distributors, Inc. (formerly known as Invesco Aim Distributors, Inc.), Invesco Investment Services, Inc. (formerly known as Invesco Aim Investment Services, Inc.), The Invesco Funds, PowerShares Exchange-Traded Fund Trust, PowerShares Exchange-Traded Trust II, PowerShares India Exchange-Traded Fund Trust, PowerShares Actively Managed Exchange-Traded Fund Trust, Van Kampen Asset Management, Van Kampen Investor Services Inc., and Van Kampen Funds Inc.<br><br>Formerly: Anti-Money Laundering Compliance Officer, Fund Management Company, Invesco Advisers, Inc., Invesco Aim Capital Management, Inc. and Invesco Aim Private Asset Management, Inc. | N/A | N/A |
| Todd L. Spillane — 1958<br>Chief Compliance Officer | 2006 | Senior Vice President, Invesco Management Group, Inc. (formerly known as Invesco Aim Management Group, Inc.), Van Kampen Investments Inc. and Van Kampen Exchange Corp.; Senior Vice President and Chief Compliance Officer, Invesco Advisers, Inc. (registered investment adviser) (formerly known as Invesco Institutional (N.A.), Inc.); Chief Compliance Officer, The Invesco Funds, PowerShares Exchange-Traded Fund Trust, PowerShares Exchange-Traded Trust II, PowerShares India Exchange-Traded Fund Trust, PowerShares Actively Managed Exchange-Traded Fund Trust, INVESCO Private Capital Investments, Inc. (holding company), and Invesco Private Capital, Inc. (registered investment adviser); Vice President, Invesco Distributors, Inc. (formerly known as Invesco Aim Distributors, Inc.), Invesco Investment Services, Inc. (formerly known as Invesco Aim Investment Services, Inc.) and Van Kampen Investor Services Inc.<br><br>Formerly: Senior Vice President and Chief Compliance Officer, Invesco Advisers, Inc. and Invesco Aim Capital Management, Inc.; Chief Compliance Officer, Invesco Global Asset Management (N.A.), Inc. and Invesco Senior Secured Management, Inc. (registered investment adviser); Vice President, Invesco Aim Capital Management, Inc. and Fund Management Company | N/A | N/A |

The Statement of Additional Information of the Trust includes additional information about the Fund's Trustees and is available upon request, without charge, by calling 1.800.959.4246. Please refer to the Fund's prospectus for information on the Fund's sub-advisers.

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**Counsel to the Fund**
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**Transfer Agent**
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# The Alger Portfolios

## Alger Balanced Portfolio

**ANNUAL REPORT**

December 31, 2010

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## Dear Shareholders, January 28, 2011

**Year in Review**

The end of 2010 was a fitting conclusion to both an exciting and troubling decade during which change in our country and across the globe was never more evident. I have no doubt that events during the 10-year period will provide much for commentary, study, and entertainment for years to come. It was a decade ushered in by the Internet generating much optimism, which quickly faded, and a time of surprising resilience of the American spirit in our recovery from September 11. Americans embarked on a sobering reassessment of values and fundamentals (of both the financial and principled kind) of the Baby Boomer generation and the American Dream, including its course since World War II. The past year was a fitting way to conclude the decade as volatility and uncertainty dominated investor sentiment. Many investors, as in the past several years, reacted fearfully and continued to retreat from U.S. equities as growing concerns over slowing economic growth, European sovereign debt issues, unresolved government policies, persistently high rates of unemployment, and other challenges dominated all of our thoughts. Investor sentiment over those issues was clearly illustrated by mutual fund asset flows in 2010. During the first 11 months of the year, investors withdrew $29.6 billion from equity funds, according to the Investment Company Institute ("ICI"). In a continuation of the recent past, assets from equity funds and new flows to funds resulted in bond portfolios capturing $266.4 billion in assets.

Such sentiments, while both rational and understandable, were in our view misplaced in 2010. For during the year, like many periods following that of great distress, there was great progress, including adaptation to new realities and, indeed, success in our U.S. economy. In many sectors, leading companies in 2010 achieved not only improvements, but actual record results topping those achieved in 2007's heady economy. While innovation and flexibility to adjust to new realities were key drivers to those kinds of results, the real key is motivation—the determination of employees and managers as well as clients to succeed and to move forward. Investors who focused on the fundamental success of companies, rather than the fear of uncertainty, and who used a disciplined strategy to seek equity opportunities were, broadly speaking, rewarded, as markets generated a 15.06% return as measured by the S&P 500 Index, easily exceeding the 6.54% return of the Barclays Capital U.S. Aggregate Bond Index.

In our opinion, our market outlook for 2010 was very good. For the early part of the year, we expected a consolidation and correction of 2009 gains amidst policy uncertainty on the multiple fronts of healthcare, energy, and reform of financial regulations and fiscal policy. Markets exhibited much volatility: At one point in early July of 2010, the S&P 500 was down 10% for the year to date. We reacted by reiterating in our summer of 2010 Market Commentary that the market would rally strongly on both continued strong corporate earnings and diminishing uncertainty around policy and politics. And so it was: Markets rallied from September 1 to year-end, with the S&P 500 gaining 20.64%, resulting in a year of well-above average performance (historically) and, certainly, achieving performance that was far above expectations of U.S. equity investors.

During the final months of 2010, concerns grew over various economic challenges, including the euro debt crisis, but the year nevertheless ended on an optimistic note. In November, euro-zone leaders rolled out a $113 billion bailout for Ireland, which will address the country's financing needs and help troubled banks. Yet, concerns over the stability of other European countries grew and Moody's Investors Services downgraded its ratings on Spanish government debt while Standard and Poor's lowered its ratings outlook for Belgium. Also troubling, only 39,000 jobs were created in the U.S. in November, considerably below the consensus forecast of 150,000. The unemployment rate, which is determined with a different survey methodology than job creation statistics, also disappointed, increasing 0.2 percentage points to 9.8% in November. On a positive note, strong retail spending helped boost investor optimism. For the three month period through November, year-over-year sales climbed 7.8%. For November, sales climbed 0.8% from October and reached the highest level since 2007. November also saw a 1.9% surge in utility output, while credit card delinquency rates declined. Moreover, the Commerce Department revised the third-quarter GDP growth rate upward twice, first to 2.5% from 2.0% and then to 2.6%. On the policy front, the biggest news was a second round of quantitative easing. Foreshadowed in Federal Reserve Chairman Ben Bernanke's Jackson Hole speech in late August, the central bank's action in early November of authorizing another $600 billion in purchases of fixed-income debt left no doubt among investors that the Fed will be resolute in its effort to stimulate the U.S. economy and to encourage investors to seek "risk assets" like equities, rather than continue to flood into low to "zero" yielding cash and bond investments.

**The Road Ahead**

We believe that strong corporate earnings, an improving outlook for the economy, and much improved sentiment among our holy trinity consisting of U.S. consumers, U.S. businesses, and U.S. investors will result in a good year for U.S. stocks. We think the S&P 500 should see 1500, or be up approximately 20% this year, on this combination of positive factors finally seen in a positive light. We are, however, not calling for the end of volatility and have concerns that the market may struggle to hold such gains, especially during the later portion of 2011. Risks that could derail our view include, especially, policy mistakes by either the U.S. or our global trading partners that result in either strict currency controls or trade restrictions, thus threatening what we at Alger continue to see as a multi-decade expansion of both global trade and, thus, global economic growth. Concerns over a weak real estate market and high rates of unemployment will also support volatility.

The recovery from the depths of the 2008 and 2009 financial crisis could not have happened without the underlying fundamental growth that comes from globalization. In the big picture, globalization is clearly a force that has improved the living standards of billions of people and has played a pivotal part in the recovery of our economy. Regarding the U.S., we believe the following items will support equity gains:

• Retail spending
• Hiring trends
• Corporate earnings from foreign markets
• Capital expenditures by cash rich corporations
• Dividend payments, stock buybacks, and mergers and acquisitions
• Demand for equities by retail investors

**Retail Spending**

With retail spending representing 70% of U.S. GDP, the weakened consumer is a considerable concern. However, in November and December, retail spending was surprisingly strong which, we believe, may indicate the start of a long trend of consumers finally loosening their purse strings. We note, as we have in the past, that publicly traded companies generally represent not the average retailer, but rather highly successful companies able to make some hay even when it's cloudy. Similarly, upper income U.S. consumers are clearly feeling better—luxury goods and bigger ticket consumer purchases (with the exception of real estate) have recovered faster than many expected. A variety of encouraging developments, including increasing family wealth from equity gains and an improving outlook for the job market, may explain this change. The U.S. consumer's balance sheet improved with strong equity gains occurring from July through September helping to offset the impact upon Americans' wealth of declining real estate values. The end result is that Americans' wealth increased 2.2% to approximately $54.9 trillion, according to the Federal Reserve. More importantly, Americans' outlook for the economy has improved, with the Conference Board's Consumer Confidence Index climbing 4.5 points to 54.1 in November, representing a five-month high.

**Reasons for Optimism on the Job Front**

The nation's 9.8% unemployment rate is clearly another concern. According to the Bureau of Labor Statistics (BLS), the number of non-farm jobs in America declined from 137.9 million in January of 2008 to 130.5 million in November of 2010, a 5.37% decline. Moreover, the Construction Sector as defined by the BLS lost 1.85 million jobs, or nearly one out of every four positions, during that timeframe, bringing the current total number of jobs to only 5.6 million. While employment contracted in most sectors during that period, the Goods Producing and Durable Goods sectors were also particularly problematic, losing roughly 17% of their jobs. While Construction job losses continued during 2010, the Goods Producing and Durable Goods sectors started to add jobs, as did most sectors, with private industry creating jobs in each month of the year. Nevertheless, job growth has been painfully slow. According to the BLS, less than a million jobs were created from December of 2009 to November of 2010, which is a very modest improvement when considering that more than seven million jobs were lost over the past three years. Many economists, meanwhile, don't expect hiring to gain steam this year, according to the Federal Reserve Bank of Philadelphia. It recently surveyed 43 economists who on average believe the economy this year will generate only 105,500 jobs per month. Yet, many companies appear to be hiring temporary workers as a stopgap measure while the economy strengthens. Indeed, temporary hiring has increased every month since August of 2009. The hiring trend, fortunately, appears ready to strengthen, with 45% of executives surveyed by the Business Roundtable in the fourth quarter of 2010 saying they expect their companies to hire workers over the next six months. That was the strongest reading since the start of the research in the fourth quarter of 2002. Moreover, the reduction of the Social Security withholding rate by two percentage points to 4.2% for 2011 may double the rate of job creation to 2.6 million this year, lowering the unemployment rate to below 9%, according to estimates by Moody's Analytics.

**Growth from Foreign Markets**
U.S. companies' fast-growing foreign operations have helped S&P 500 constituents increase profits every quarter since September of 2009, a trend which we expect to continue this year. According to S&P 500 estimates, operating earnings per share should reach $25.16 by the fourth quarter of 2011, up from $21.74 in the last quarter of 2010. Regarding non-U.S. revenues, as of April 30 of last year, 38.80% of S&P 500 corporate sales were in foreign markets, a figure which increased slightly to 39.65% as of mid-December. U.S. corporations' access to foreign markets is significant as international growth is expected to outpace that of the U.S. with the International Monetary Fund (IMF) estimating that world GDP will grow 4.3% in 2011, dwarfing the 2.9% GDP growth forecast for America. Perhaps more impressive are expectations that GDP for certain countries, such as Brazil, China, and India, will grow at rates that exceed the global forecasts. Clearly, the U.S. stock market is not just a reflection of the U.S. economy. It is, instead, a gauge of the international marketplace and the success of U.S. companies in it.

**Capital Expenditures**
At the same time, corporate coffers are rich with cash, and businesses have pent up demand for new equipment, such as personal computers, data storage systems, and information networks, after having cut spending during "The Great Recession." At the end of the third quarter, corporations held $1.93 trillion in cash, up from $1.8 trillion at the end of June, according to the Federal Reserve. Corporations now appear to be addressing the demand and we are encouraged to see an increase in corporate spending on technology, which we believe will help further stimulate the economy. On a broader scale, capital expenditures by S&P 500 companies in 2010 increased moderately from $2.99 billion in the first quarter to $3.07 billion in the fourth quarter. We believe this trend will strengthen as 59% of executives surveyed by the Business Roundtable said they expect their companies to increase capital expenditures over the next six months.

**Dividends, Stock Buybacks, and Merger and Acquisitions**
In 2010, nearly 48% of S&P 500 companies either started dividend payments or increased their dividends, according to data from FactSet. The additional income flowing to shareholders will help to stimulate the economy, but perhaps more important, it will help make equities more appealing, especially when considering that the yield on a 10-year bond at the end of 2010 was only 3.30%. In comparison, a typical stock dividend yield is 2% and corporate earnings or free cash flow yields are as high as 8%, 9%, or 10%. The volume of stock buybacks has also increased significantly, helping to support equity valuations while signaling that corporate executives have strong conviction regarding the values of their companies. Stock

buybacks totaling more than $368 billion were announced in 2010, up from $125 billion in 2009, according to equity research firm Birinyi Associates, Inc. Acquisitions and mergers are also gaining steam. In 2010, the total market cap of M&A activity by U.S. companies climbed to $738 billion, which is substantially below the $1.09 trillion in deals completed in 2008, according to Bloomberg. Nevertheless, deal volume last year exceeded the $718 billion of deals completed in 2009. We maintain that increasing levels of M&A activity illustrate that corporate executives believe that acquisition targets are either trading at attractive valuations or are desirable from a strategic point of view.

**Investor Psychology**

Investors' strong preference for bond funds has pushed yields on fixed-income securities to historically low levels. We maintain that even a modest increase in interest rates will create substantial losses in bond funds, which may drive investors to sell fixed-income assets in favor of equities. The process may already have started. Toward the end of 2010, expectations that the economy is strengthening combined with the weakening financial health of municipalities and states sparked a decline in bond values, including those issued by corporations. Impressively, Wal-Mart Stores, Inc. 30-year bonds issued in the fourth quarter of 2010 with a historically low 5% yield dropped 5% in value, underscoring that fixed-income securities entail risk. In comparison, equity markets completed 2010 by recording their second year of solid gains, making stock investments appear attractive. If investors react to fixed-income losses by reallocating assets to equities, the impact on stock valuations could be significant as Americans have approximately $3 trillion invested in fixed-income mutual funds, according to the ICI. Bond investors may have already started to do so, pulling $7.4 billion in assets from fixed-income funds during the one-month period ended December 8. Even though the redemptions are modest, they represent the first period of bond outflows since 2008 and could represent the start of ongoing redemptions from fixed-income funds. One of the big surprises for 2011 could be the re-engagement of investors with U.S. equities, an event that we believe would be quite a fitting reversal of the past decade in which foreign and emerging markets, real estate, commodities and (finally) bonds and cash were favorites at the expense, in particular, of U.S. growth stocks.

**Challenges for 2011**

Going forward, fears over a potential worsening of the euro debt crisis will linger, but we believe that the European Financial Stability Facility, which was created in response to the problem, and the IMF will respond diligently if the situation worsens. Domestically, we are concerned that real estate could be a bigger "continuing" problem than perhaps expected. The data suggest that real estate values won't recover any time soon with 9.5 months of inventory available as of November compared to six to seven months of inventory that was typically available prior to "The Great Recession," according to the National Association of Realtors (NAR). Moreover, the S&P/Case-Shiller Home Price Index recorded a 0.8% year-over year decline in October of 2010, the biggest drop since the year-over-year decline recorded in December of 2009. Real estate sales also disappointed. In 2010, 4.85 million homes were expected to have been sold, according to NAR projections. In comparison, the highest number of homes sold during the past 10 years was 7.08 million in 2005.

However, we believe that the large amount of inventory and anemic sales have for the most part been "priced in" by the market. In other words, if the U.S. real estate market remains as it is, figuratively "bumping along the bottom" (without improvement), we believe that will be OK for the stock markets. However, if there is another large price decline, that will change our equities outlook for the 2011-2012 timeframe. Over the longer term, as measured by years, however, the real estate market certainly will improve. Construction of new homes has dropped considerably, limiting the supply of new homes. At present rates, new construction is below the U.S. natural rate of demand driven by household formation, population growth, and the economy. Affordability of homes stands at very attractive levels, so the issue turns on loan availability, employment, and, of course, confidence of the home buyer.

As always, we remain committed to our highly-disciplined and research-driven investment strategy of seeking growth companies with the right strategies, management, business models, and products to succeed in any economy. Similarly, we continue to believe that research is the cornerstone of superior portfolio management, regardless of economic conditions. We believe our proven and disciplined process for identifying companies experiencing Positive Dynamic Change will continue to produce superior long-term investment results for our clients.

**Portfolio Matters**

The Alger Balanced Portfolio returned 10.33% for the one-year period ended December 31, 2010, compared to the Russell 1000 Index, which returned 16.71% and the Barclays Capital U.S. Government/Credit Bond Index, which returned 6.59%.

During the period, the largest sector weightings in the equity portion of the Alger Balanced Portfolio were in the Information Technology and Consumer Staples sectors. The largest sector overweight for the period was in Financials and the largest sector underweight was in Information Technology. Relative outperformance in the Consumer Staples and Utilities sectors was the most important contributor to performance, while Consumer Discretionary and Industrials detracted from results.

Among the most important relative contributors were IAC/InterActiveCorp., Peabody Energy Corp., Cheesecake Factory Inc., BE Aerospace Inc., and Viacom Inc. Conversely, detracting from overall results on a relative basis were Exxon Mobil Corp., Oracle Corp., Bank of America Corp., Boston Scientific Corp., and Transocean Ltd.

Regarding the fixed-income portion of the Fund's portfolio, 52.8% was in corporate securities, 16.5% in U.S. Treasuries, 6.6% was in collateralized mortgage obligations and assets-backed securities, 5.7% in U.S. agency securities, 5.5% in cash, 5.3% in convertible preferred securities, 5.3% in convertible bonds, and 2.3% in preferred stock as of December 31, 2010. After widening in response to sovereign risk exposure in April 2010, the reversal and subsequent tightening of credit spreads has been the major force behind returns. This tightening was not smooth as yields fluctuated in response to uncertain economic growth, U.S. policy uncertainty and European debt issues. With the Fed firmly behind maintaining a low rate environment through the implementation of a second round of quantitative easing, corporations have been aggressively refinancing debt and reducing leverage while increasing cash balances and now generally have strong balance sheets.

Respectfully submitted,

Daniel C. Chung, CFA
Chief Investment Officer

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Investors cannot invest directly in an index. Index performance does not reflect the deduction for fees, expenses, or taxes.

This report and the financial statements contained herein are submitted for the general information of shareholders of The Alger Portfolios. This report is not authorized for distribution to prospective investors in The Alger Portfolios unless proceeded or accompanied by an effective prospectus. Individual Portfolio returns represent the fiscal 12-month period return of Class I-2 shares. Returns include reinvestment of dividends and distributions.

**The performance information quoted in this material represents past performance, which is not an indication or a guarantee of future results.**

Standard performance results can be found on the following pages. The investment return and principal value of an investment in a fund will fluctuate so that an investor's shares, when redeemed, may be worth more or less than their original cost. Current performance may be lower or higher than the performance quoted. For performance data current to the most recent month-end, visit us at www.alger.com, or call us at (800) 992-3863.

The views and opinions of the Portfolio's management in this report are as of the date of the shareholders letter and are subject to change at any time subsequent to this date. There is no guarantee that any of the assumptions that formed the basis for the opinions stated herein are accurate or that they will materialize. Moreover, the information forming the basis for such assumptions is from sources believed to be reliable; however, there is no guarantee that such information is accurate. Any securities mentioned, whether owned in a Portfolio or otherwise, are considered in the context of the construction of an overall portfolio of securities and therefore reference to them should not be construed as a recommendation or offer to purchase or sell any such security. Inclusion of such securities in a fund and transactions in such securities, if any, may be for a variety of reasons, including without limitation, in response to cash flows, inclusion in a benchmark, and risk control. The reference to a specific security should also be understood in such context and not viewed as a statement that the security is a significant holding in a Portfolio. Please refer to the Schedule of Investments for each Portfolio which is included in this report for a complete list of Portfolio holdings as of December 31, 2010. Securities mentioned in the shareholders letter, if not found in the Schedule of Investments, may have been held by the Portfolios during the 12-month fiscal period.

**A Word about Risk**
Growth stocks tend to be more volatile than other stocks as the price of growth stocks tends to be higher in relation to their companies' earnings and may be more sensitive to market, political and economic developments. Investing in the stock market involves gains and losses and may not be suitable for all investors. Stocks of small- and mid-sized companies are subject to greater risk than stocks of larger, more established companies owing to such factors as limited liquidity, inexperienced management, and limited financial resources. Portfolios that invest in fixed-income securities, such as the Alger Balanced Portfolio, are subject to the fixed-income securities' sensitivity to interest rate movements; their market values tend to fall when interest rates rise and to rise when interest rates fall. They are also subject to the risk of a decline in the value of the Portfolio's securities in the event of an issue's falling credit rating or actual default. The Portfolios that invest in mortgage and asset-backed securities are subject to prepayment risk; thus the average life of the security may be less than maturity. Portfolios that participate in leveraging, such as the Alger Capital Appreciation Portfolio and the Alger SMid Cap Growth Portfolio, are subject to the risk that the cost of borrowing money to leverage will exceed the returns for securities purchased or that the securities purchased may actually go down in value; thus, the Portfolio's net asset value can decrease more quickly than if the Portfolio had not borrowed. For a more detailed discussion of the risks associated with a Portfolio, please see the Portfolio's Prospectus.

Before investing, carefully consider a Portfolio's investment objective, risks, charges, and expenses. For a prospectus or a summary prospectus containing this and other information about the Alger Funds call us at (800) 992-3863 or visit us at www.alger.com. Read it carefully before investing.

**Fred Alger & Company, Incorporated, Distributor. Member NYSE Euronext, SIPC.**

**NOT FDIC INSURED. NOT BANK GUARANTEED. MAY LOSE VALUE.**

Definitions:

- Standard & Poor's 500 Index (S&P 500 Index) is an index of 500 leading companies in leading industries in the United States.

- The Russell 3000 Index measures the performance of the 3,000 largest U.S. companies based on the total market capitalization, which represents 99% of the U.S. equity market. The Russell 3000 Growth Index is an unmanaged index designed to measure the performance of those Russell 3000 Index companies with higher price-to-book ratios and higher forecasted growth values.

- The Russell 1000 Index measures the performance of the large-cap segment of the U.S. equity universe. It is a subset of the Russell 3000 Index and includes approximately 1,000 of the largest securities based on a combination of their market cap and current index membership. The Russell 1000 represents approximately 92% of the Russell 3000 Index. The Russell 1000 Growth Index is an unmanaged index designed to measure the performance of the largest 1,000 companies in the Russell 3000 Index with higher price-to-book ratios and higher forecasted growth values.

- The Russell Midcap Growth Index measures the performance of the mid-cap growth segment of the U.S. equity universe. It includes those Russell Midcap Index companies with higher price-to-book ratios and higher forecasted growth values.

- The Russell 2500 Index measures the performance of the small to mid-cap segment of the U.S. equity universe, commonly referred to as "SMid" cap. The Russell 2500 Index is a subset of the Russell 3000 Index. The Russell 2500 Growth Index measures the performance of the small to mid-cap growth segment of the U.S. equity universe. It includes those Russell 2500 companies with higher price-to-book ratios and higher forecasted growth values.

- The Russell 2000 Index measures the performance of the small-cap segment of the U.S. equity universe. The Russell 2000 Index is a subset of the Russell 3000 Index representing approximately 8% of the total market capitalization of that index. The Russell 2000 Growth Index measures the performance of the small cap growth segment of the U.S. equity universe. It includes those Russell 2000 companies with higher price-to-book ratios and higher forecasted growth values.

- The Barclays Capital U.S. Government/Credit Bond Index tracks the performance of government and corporate bonds.

- The Investment Company Institute (ICI) is a national association of U.S. investment companies.

- Moody's Investors Service and Standard & Poor's are credit rating agencies.

- The Business Roundtable is an organization of chief executive officers of leading companies.

- FactSet is a firm that provides market data and analytics to investment firms.

- Birinyi Associates, Inc. is a stock market research firm.

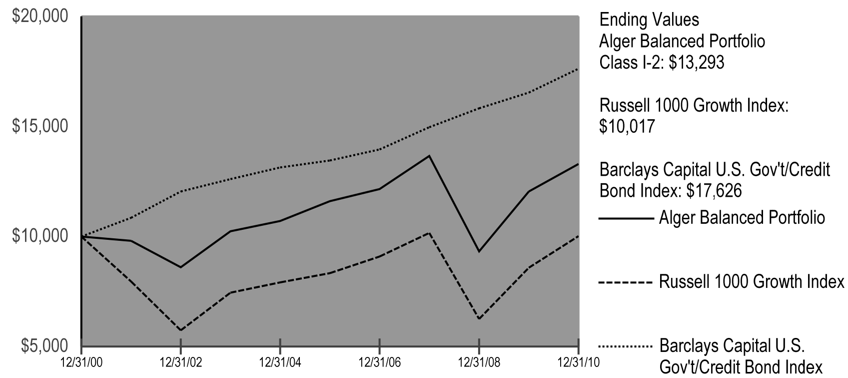
- Bloomberg is a financial publisher and provider of financial data.

- The National Association of Realtors is a trade organization representing members involved in the residential and commercial real estate industries.

- As of December 31, 2010, Wal-Mart Stores Inc. represented 0.43% of firm-wide assets under management.

HYPOTHETICAL $10,000 INVESTMENT IN CLASS I-2 SHARES

*— 10 years ended 12/31/10*




The chart above illustrates the change in value of a hypothetical $10,000 investment made in Alger Balanced Portfolio Class I-2 shares, the Russell 1000 Growth Index (an unmanaged index of common stocks) and the Barclays Capital U.S. Gov't/Credit Bond Index (an unmanaged index of government and corporate bonds) for the ten years ended December 31, 2010. Figures for each of the Alger Balanced Portfolio Class I-2 shares, the Russell 1000 Growth Index and the Barclays Capital U.S. Gov't/Credit Bond Index include reinvestment of dividends and interest. Performance for the Alger Balanced Portfolio Class S shares will be lower from the results shown above due to differences in expenses that class bears.

**PERFORMANCE COMPARISON AS OF 12/31/10**

**AVERAGE ANNUAL TOTAL RETURNS**

| | 1 YEAR | 5 YEARS | 10 YEARS | SINCE INCEPTION |
|---|---|---|---|---|
| **Class I-2 (Inception 9/5/89)** | 10.33% | 2.75% | 2.89% | 7.66% |
| Russell 1000 Growth Index | 16.71% | 3.75% | 0.02% | 7.93% |
| Barclays Capital U.S. Gov't/Credit Bond Index | 6.59% | 5.56% | 5.83% | 7.05% |

*The performance data quoted represents past performance, which is not an indication or a guarantee of future results. Investment return and principal will fluctuate and the Portfolio's shares, when redeemed, may be worth more or less than their original cost. Current performance may be higher or lower than the performance quoted. For performance current to the most recent month end, visit us at www.alger.com or call us at (800) 992-3863.*

*Returns indicated assume reinvestment of all distributions, no transaction costs or taxes, and are net of management fees and fund operating expenses only. Total return does not include deductions at the portfolio or contract level for cost of insurance charges, premium load, administrative charges, mortality and expense risk charges or other charges that may be incurred under the variable annuity contract, variable life insurance plan or retirement plan for which the Portfolio serves as an underlying investment vehicle. If these charges were deducted, the total return figures would be lower. Please refer to the variable insurance product or retirement plan disclosure documents for any additional applicable expenses. Investing in the stock market involves gains and losses and may not be suitable for all investors.*

**THE ALGER PORTFOLIOS | Alger Balanced Portfolio**
**Portfolio Summary†**
**December 31, 2010***(Unaudited)*

| SECTORS/SECURITY TYPES | |
|---|---|
| Consumer Discretionary | 6.7% |
| Consumer Staples | 4.8 |
| Energy | 5.9 |
| Financials | 9.6 |
| Health Care | 5.0 |
| Industrials | 6.3 |
| Information Technology | 12.9 |
| Materials | 2.7 |
| Telecommunication Services | 0.1 |
| Utilities | 0.4 |
| Total Equity Securities | 54.4% |
| Asset Backed Securities | 0.7% |
| Convertible Corporate Bonds | 2.8 |
| Corporate Bonds | 24.8 |
| U.S. Government & Agency Mortgage Backed Obligations | 2.8 |
| U.S. Government & Agency Obligations (excluding Mortgage Backed) | 10.8 |
| Total Debt Securities | 41.9% |
| Short-Term and Net Other Assets | 3.7% |
| | **100.0%** |

† *Based on net assets for the Portfolio*.

| COMMON STOCKS—50.7% | SHARES | VALUE |
|---|---|---|
| **ADVERTISING—0.2%** | | |
| Focus Media Holding Ltd.#* | 12,200 | $ **267,546** |
| **AEROSPACE & DEFENSE—1.6%** | | |
| BE Aerospace Inc. * | 8,300 | 307,349 |
| Boeing Co., /The | 5,100 | 332,826 |
| General Dynamics Corp. | 7,900 | 560,584 |
| ITT Corp. | 6,000 | 312,660 |
| Lockheed Martin Corp. | 3,500 | 244,685 |
| | | **1,758,104** |
| **AIR FREIGHT & LOGISTICS—1.0%** | | |
| FedEx Corp. | 6,500 | 604,565 |
| United Parcel Service Inc., Cl. B | 8,600 | 624,188 |
| | | **1,228,753** |
| **APPLICATION SOFTWARE—0.5%** | | |
| Adobe Systems Inc. * | 8,400 | 258,552 |
| Intuit Inc. * | 6,400 | 315,520 |
| | | **574,072** |
| **ASSET MANAGEMENT & CUSTODY BANKS—0.5%** | | |
| BlackRock Inc. | 1,900 | 362,102 |
| Invesco Ltd. | 10,400 | 250,224 |
| | | **612,326** |
| **AUTO PARTS & EQUIPMENT—0.2%** | | |
| Visteon Corp.* | 3,400 | **252,450** |
| **AUTOMOBILE MANUFACTURERS—0.1%** | | |
| General Motors Co.* | 3,300 | **121,638** |
| **BIOTECHNOLOGY—0.9%** | | |
| Celgene Corp. * | 5,300 | 313,442 |
| Cephalon Inc. * | 6,500 | 401,180 |
| Human Genome Sciences Inc. * | 13,200 | 315,348 |
| | | **1,029,970** |
| **CABLE & SATELLITE—0.4%** | | |
| Comcast Corp., Cl. A | 14,700 | 305,907 |
| Sirius XM Radio Inc. * | 106,600 | 174,824 |
| | | **480,731** |
| **CASINOS & GAMING—0.2%** | | |
| International Game Technology | 15,300 | **270,657** |
| **COAL & CONSUMABLE FUELS—0.4%** | | |
| Peabody Energy Corp. | 7,500 | **479,850** |
| **COMMUNICATIONS EQUIPMENT—1.9%** | | |
| Brocade Communications Systems Inc. * | 45,800 | 242,282 |
| Cisco Systems Inc. * | 54,900 | 1,110,627 |
| Corning Inc. | 12,800 | 247,296 |
| Qualcomm Inc. | 13,500 | 668,115 |
| | | **2,268,320** |
| **COMPUTER & ELECTRONICS RETAIL—0.2%** | | |
| GameStop Corp., Cl. A* | 11,400 | **260,832** |

| COMMON STOCKS—(CONT.) | SHARES | VALUE |
|---|---|---|
| **COMPUTER HARDWARE—3.1%** | | |
| Apple Inc. * | 8,600 | $ 2,774,022 |
| Hewlett-Packard Co. | 24,300 | 1,023,030 |
| | | **3,797,052** |
| **COMPUTER STORAGE & PERIPHERALS—0.9%** | | |
| EMC Corp. * | 34,400 | 787,760 |
| NetApp Inc. * | 4,500 | 247,320 |
| | | **1,035,080** |
| **CONSTRUCTION & ENGINEERING—0.5%** | | |
| Fluor Corp. | 5,900 | 390,934 |
| Foster Wheeler AG * | 7,500 | 258,900 |
| | | **649,834** |
| **CONSTRUCTION & FARM MACHINERY & HEAVY TRUCKS—1.0%** | | |
| Caterpillar Inc. | 5,500 | 515,130 |
| Deere & Co. | 4,000 | 332,200 |
| Joy Global Inc. | 3,900 | 338,325 |
| | | **1,185,655** |
| **DATA PROCESSING & OUTSOURCED SERVICES—0.5%** | | |
| Mastercard Inc. | 2,500 | **560,275** |
| **DISTILLERS & VINTNERS—0.1%** | | |
| Diageo PLC# | 2,000 | **148,660** |
| **DIVERSIFIED BANKS—0.4%** | | |
| Wells Fargo & Co. | 15,700 | **486,543** |
| **DIVERSIFIED CHEMICALS—0.3%** | | |
| EI Du Pont de Nemours & Co. | 7,500 | **374,100** |
| **DIVERSIFIED METALS & MINING—0.3%** | | |
| Cliffs Natural Resources Inc. | 4,200 | **327,642** |
| **DRUG RETAIL—0.5%** | | |
| CVS Caremark Corp. | 15,900 | **552,843** |
| **ENVIRONMENTAL & FACILITIES SERVICES—0.2%** | | |
| Republic Services Inc. | 6,800 | **203,048** |
| **FERTILIZERS & AGRICULTURAL CHEMICALS—0.6%** | | |
| Monsanto Co. | 4,600 | 320,344 |
| Mosaic Co., /The | 1,900 | 145,084 |
| Potash Corporation of Saskatchewan Inc. | 1,900 | 294,177 |
| | | **759,605** |
| **FINANCIALS—1.2%** | | |
| iPATH S&P 500 VIX Short-Term Futures ETN * | 10,682 | 401,536 |
| iShares Barclays 20+ Year Treasury Bond Fund | 1,700 | 160,004 |
| iShares FTSE China 25 Index Fund | 19,969 | 860,465 |
| | | **1,422,005** |
| **FOOTWEAR—0.2%** | | |
| NIKE Inc., Cl. B | 3,400 | **290,428** |
| **GENERAL MERCHANDISE STORES—0.4%** | | |
| Target Corp. | 8,000 | **481,040** |

| COMMON STOCKS—(CONT.) | SHARES | VALUE |
|---|---|---|
| **GOLD—0.5%** | | |
| Goldcorp Inc. | 7,500 | $ 344,850 |
| Yamana Gold Inc. | 23,000 | 294,400 |
| | | **639,250** |
| **HEALTH CARE EQUIPMENT—0.4%** | | |
| Covidien PLC | 4,400 | 200,904 |
| Zimmer Holdings Inc. * | 5,200 | 279,136 |
| | | **480,040** |
| **HEALTH CARE SUPPLIES—0.1%** | | |
| Inverness Medical Innovation* | 4,000 | **146,400** |
| **HOME ENTERTAINMENT SOFTWARE—0.3%** | | |
| Electronic Arts Inc. * | 12,700 | 208,026 |
| Take-Two Interactive Software Inc. * | 11,700 | 143,208 |
| | | **351,234** |
| **HOME IMPROVEMENT RETAIL—0.1%** | | |
| Lowe's Companies, Inc. | 6,500 | **163,020** |
| **HOMEBUILDING—0.5%** | | |
| Toll Brothers Inc.* | 30,800 | **585,200** |
| **HOTELS RESORTS & CRUISE LINES—0.2%** | | |
| Carnival Corp. | 4,200 | **193,662** |
| **HOUSEHOLD PRODUCTS—0.7%** | | |
| Procter & Gamble Co., /The | 12,500 | **804,125** |
| **HYPERMARKETS & SUPER CENTERS—0.8%** | | |
| Costco Wholesale Corp. | 4,200 | 303,282 |
| Wal-Mart Stores Inc. | 12,500 | 674,125 |
| | | **977,407** |
| **INDUSTRIAL CONGLOMERATES—1.3%** | | |
| 3M Co. | 7,000 | 604,100 |
| General Electric Co. | 21,700 | 396,893 |
| McDermott International Inc. * | 12,300 | 254,487 |
| Tyco International Ltd. | 8,700 | 360,528 |
| | | **1,616,008** |
| **INDUSTRIAL GASES—0.2%** | | |
| Praxair Inc. | 2,900 | **276,863** |
| **INTEGRATED OIL & GAS—2.2%** | | |
| Chevron Corp. | 9,500 | 866,875 |
| Exxon Mobil Corp. | 18,900 | 1,381,968 |
| Petroleo Brasileiro SA # | 10,400 | 393,536 |
| | | **2,642,379** |
| **INTERNET RETAIL—1.0%** | | |
| Amazon.com Inc. * | 3,000 | 540,000 |
| Expedia Inc. | 19,600 | 491,764 |
| | | **1,031,764** |
| **INTERNET SOFTWARE & SERVICES—2.2%** | | |
| eBay Inc. * | 20,950 | 583,039 |
| Google Inc., Cl. A * | 1,800 | 1,069,146 |

| COMMON STOCKS—(CONT.) | SHARES | VALUE |
|---|---|---|
| **INTERNET SOFTWARE & SERVICES—(CONT.)** | | |
| IAC/InterActiveCorp. * | 16,150 | $ 463,505 |
| Mixi Inc. *,L2 | 30 | 163,270 |
| Yahoo! Inc. * | 32,200 | 535,486 |
| | | **2,814,446** |
| **INVESTMENT BANKING & BROKERAGE—1.4%** | | |
| Charles Schwab Corp., /The | 20,400 | 349,044 |
| Goldman Sachs Group Inc., /The | 2,200 | 369,952 |
| Lazard Ltd., Cl. A | 11,160 | 440,708 |
| Morgan Stanley | 15,200 | 413,592 |
| | | **1,573,296** |
| **IT CONSULTING & OTHER SERVICES—1.2%** | | |
| Cognizant Technology Solutions Corp., Cl. A * | 4,300 | 315,147 |
| International Business Machines Corp. | 7,500 | 1,100,700 |
| | | **1,415,847** |
| **LEISURE PRODUCTS—0.2%** | | |
| Coach Inc. | 5,200 | **287,612** |
| **LIFE & HEALTH INSURANCE—0.5%** | | |
| MetLife Inc. | 6,100 | 271,084 |
| Prudential Financial Inc. | 6,400 | 375,744 |
| | | **646,828** |
| **LIFE SCIENCES TOOLS & SERVICES—0.5%** | | |
| Charles River Laboratories International Inc. * | 3,500 | 124,390 |
| Thermo Fisher Scientific Inc. * | 9,300 | 514,848 |
| | | **639,238** |
| **MANAGED HEALTH CARE—0.6%** | | |
| Aetna Inc. | 10,100 | 308,151 |
| UnitedHealth Group Inc. | 8,100 | 292,491 |
| WellPoint Inc. * | 2,600 | 147,836 |
| | | **748,478** |
| **METAL & GLASS CONTAINERS—0.2%** | | |
| Owens-Illinois Inc.* | 9,100 | **279,370** |
| **MOVIES & ENTERTAINMENT—1.1%** | | |
| Live Nation Entertainment Inc. * | 13,000 | 148,460 |
| Regal Entertainment Group, Cl. A | 9,500 | 111,530 |
| Time Warner Inc. | 14,300 | 460,031 |
| Viacom Inc., Cl. B | 11,700 | 463,437 |
| | | **1,183,458** |
| **OFFICE REITS—0.2%** | | |
| Digital Realty Trust Inc. | 4,700 | **242,238** |
| **OIL & GAS DRILLING—0.3%** | | |
| Transocean Ltd.* | 4,883 | **339,417** |
| **OIL & GAS EQUIPMENT & SERVICES—1.3%** | | |
| Cameron International Corp. * | 11,400 | 578,322 |
| Schlumberger Ltd. | 9,100 | 759,850 |
| Weatherford International Ltd. * | 8,400 | 191,520 |
| | | **1,529,692** |

| COMMON STOCKS—(CONT.) | SHARES | VALUE |
|---|---|---|
| **OIL & GAS EXPLORATION & PRODUCTION—1.2%** | | |
| Anadarko Petroleum Corp. | 4,800 | $ 365,568 |
| Chesapeake Energy Corp. | 14,000 | 362,740 |
| Devon Energy Corp. | 3,000 | 235,530 |
| Nexen Inc. | 6,100 | 139,690 |
| Plains Exploration & Production Co. * | 10,000 | 321,400 |
| | | **1,424,928** |
| **OIL & GAS STORAGE & TRANSPORTATION—0.5%** | | |
| El Paso Pipeline Partners LP | 9,700 | 324,465 |
| Enterprise Products Partners LP | 6,800 | 282,948 |
| | | **607,413** |
| **OTHER DIVERSIFIED FINANCIAL SERVICES—1.2%** | | |
| Bank of America Corp. | 44,200 | 589,628 |
| Citigroup Inc. * | 32,400 | 153,252 |
| JPMorgan Chase & Co. | 17,700 | 750,834 |
| | | **1,493,714** |
| **PACKAGED FOODS & MEATS—0.4%** | | |
| Kraft Foods Inc., Cl. A | 16,600 | **523,066** |
| **PAPER PRODUCTS—0.3%** | | |
| International Paper Co. | 11,400 | **310,536** |
| **PERSONAL PRODUCTS—0.1%** | | |
| Avon Products Inc. | 3,600 | **104,616** |
| **PHARMACEUTICALS—2.5%** | | |
| Abbott Laboratories | 9,100 | 435,981 |
| Bristol-Myers Squibb Co. | 5,800 | 153,584 |
| Johnson & Johnson | 9,700 | 599,945 |
| Merck & Co., Inc. | 8,600 | 309,944 |
| Mylan Inc. * | 22,400 | 473,312 |
| Pfizer Inc. | 35,720 | 625,457 |
| Shire PLC # | 4,000 | 289,520 |
| | | **2,887,743** |
| **PRECIOUS METALS & MINERALS—0.3%** | | |
| Stillwater Mining Co.* | 15,000 | **320,250** |
| **PROPERTY & CASUALTY INSURANCE—0.2%** | | |
| Travelers Cos., Inc., /The | 5,300 | **295,263** |
| **RAILROADS—0.2%** | | |
| CSX Corp. | 3,500 | **226,135** |
| **RESEARCH & CONSULTING SERVICES—0.2%** | | |
| FTI Consulting Inc.* | 7,100 | **264,688** |
| **RESTAURANTS—0.6%** | | |
| Cheesecake Factory Inc., /The * | 8,600 | 263,676 |
| McDonald's Corp. | 6,700 | 514,292 |
| | | **777,968** |
| **RETAIL REITS—0.3%** | | |
| General Growth Properties Inc. | 6,700 | 103,716 |
| Macerich Co., /The | 4,200 | 198,954 |
| | | **302,670** |

| COMMON STOCKS—(CONT.) | SHARES | VALUE |
|---|---|---|
| **SEMICONDUCTOR EQUIPMENT—0.4%** | | |
| Lam Research Corp. * | 8,300 | $ 429,774 |
| Novellus Systems Inc. * | 3,200 | 103,424 |
| | | **533,198** |
| **SEMICONDUCTORS—0.7%** | | |
| Intel Corp. | 29,600 | 622,488 |
| Micron Technology Inc. * | 23,200 | 186,064 |
| | | **808,552** |
| **SOFT DRINKS—1.4%** | | |
| Coca-Cola Co., /The | 9,900 | 651,123 |
| Hansen Natural Corp. * | 5,500 | 287,540 |
| PepsiCo Inc. | 12,400 | 810,092 |
| | | **1,748,755** |
| **SPECIALIZED FINANCE—0.9%** | | |
| CME Group Inc. | 1,328 | 427,284 |
| Hong Kong Exchanges and Clearing Ltd. [L2] | 18,400 | 417,193 |
| IntercontinentalExchange Inc. * | 1,900 | 226,385 |
| | | **1,070,862** |
| **SPECIALIZED REITS—0.3%** | | |
| Weyerhaeuser Company | 16,659 | **315,355** |
| **SPECIALTY STORES—0.3%** | | |
| Staples Inc. | 16,300 | **371,151** |
| **SYSTEMS SOFTWARE—1.2%** | | |
| Microsoft Corp. | 40,650 | 1,134,948 |
| Oracle Corp. | 10,800 | 338,040 |
| | | **1,472,988** |
| **TOBACCO—0.8%** | | |
| Altria Group Inc. | 11,700 | 288,054 |
| Philip Morris International Inc. | 10,900 | 637,977 |
| | | **926,031** |
| **TRUCKING—0.3%** | | |
| Hertz Global Holdings Inc.* | 26,700 | **386,883** |
| **WIRELESS TELECOMMUNICATION SERVICES—0.1%** | | |
| American Tower Corp., Cl. A* | 3,000 | **154,920** |
| TOTAL COMMON STOCKS (Cost $56,106,774) | | **60,814,016** |

| CONVERTIBLE PREFERRED STOCK—1.8% | SHARES | VALUE |
|---|---|---|
| **AUTOMOBILE MANUFACTURERS—0.8%** | | |
| General Motors Co., 4.75%, 12/1/13* | 17,500 | **946,925** |
| **ELECTRIC UTILITIES—0.4%** | | |
| PPL Corp., 9.50%, 07/1/13 | 8,000 | **439,760** |
| **MULTI-LINE INSURANCE—0.6%** | | |
| Hartford Financial Services Group Inc., 7.25%, 04/1/13 | 28,000 | **717,080** |
| TOTAL CONVERTIBLE PREFERRED STOCK (Cost $2,000,900) | | **2,103,765** |

| MANDATORY CONVERTIBLE PREFERRED STOCK—0.8% | SHARES | VALUE |
|---|---|---|
| **OTHER DIVERSIFIED FINANCIAL SERVICES—0.8%** | | |
| Citigroup Inc., 7.50%, 12/15/12(a) | 7,000 | $ **956,830** |
| (Cost $715,925) | | |

| PREFERRED STOCKS—1.1% | SHARES | VALUE |
|---|---|---|
| **DIVERSIFIED BANKS—0.9%** | | |
| HSBC Holdings PLC, 8.00%, 12/15/15 | 40,000 | **1,066,000** |
| **OTHER DIVERSIFIED FINANCIAL SERVICES—0.2%** | | |
| Citigroup Capital XIII, 7.88%, 10/30/40* | 8,100 | **217,971** |
| **TOTAL PREFERRED STOCKS** | | |
| (Cost $1,202,500) | | **1,283,971** |

| CONVERTIBLE CORPORATE BONDS—2.8% | PRINCIPAL AMOUNT | VALUE |
|---|---|---|
| **COMPUTER STORAGE & PERIPHERALS—0.3%** | | |
| SanDisk Corp., 1.50%, 8/15/17L2 | 300,000 | **340,125** |
| **GOLD—0.7%** | | |
| AngloGold Ashanti Holdings Finance PLC, 3.50%, 5/22/14L2(b) | 650,000 | **812,500** |
| **MULTI-UTILITIES—0.6%** | | |
| CMS Energy Corp., 5.50%, 6/15/29L2 | 500,000 | **703,750** |
| **OFFICE REITS—0.4%** | | |
| SL Green Operating Partnership LP, 3.00%, 10/15/17L2(b) | 500,000 | **513,125** |
| **SEMICONDUCTORS—0.4%** | | |
| Intel Corp., 3.25%, 8/1/39L2(b) | 425,000 | **511,594** |
| **WIRELESS TELECOMMUNICATION SERVICES—0.4%** | | |
| SBA Communications Corp., 4.00%, 10/1/14L2 | 350,000 | **521,500** |
| **TOTAL CONVERTIBLE CORPORATE BONDS** | | |
| (Cost $2,761,094) | | **3,402,594** |

| CORPORATE BONDS—24.8% | PRINCIPAL AMOUNT | VALUE |
|---|---|---|
| **AEROSPACE & DEFENSE—1.2%** | | |
| Bombardier Inc., 7.75%, 3/15/20L2(b) | 650,000 | 703,626 |
| L-3 Communications Corp., 4.75%, 7/15/20L2 | 350,000 | 344,519 |
| Northrop Grumman Corp., 1.85%, 11/15/15L2 | 350,000 | 335,970 |
| | | **1,384,115** |
| **APPLICATION SOFTWARE—0.6%** | | |
| Adobe Systems Inc., 4.75%, 2/1/20L2 | 650,000 | **666,109** |
| **AUTOMOBILE MANUFACTURERS—0.5%** | | |
| Toyota Motor Credit Corp., 1.38%, 8/12/13L2 | 650,000 | **653,081** |
| **CABLE & SATELLITE—0.7%** | | |
| Cablevision Systems Corp., 7.75%, 4/15/18L2 | 150,000 | 157,875 |
| Comcast Corp., 5.70%, 7/1/19L2 | 625,000 | 684,446 |
| | | **842,321** |
| **COMMUNICATIONS EQUIPMENT—0.6%** | | |
| Cisco Systems Inc., 4.95%, 2/15/19L2 | 350,000 | 382,059 |

| CORPORATE BONDS—(CONT.) | PRINCIPAL AMOUNT | VALUE |
|---|---|---|
| **COMMUNICATIONS EQUIPMENT—(CONT.)** | | |
| Harris Corp., 4.40%, 12/15/20L2 | $ 350,000 | $ 350,681 |
| | | **732,740** |
| **COMPUTER HARDWARE—1.0%** | | |
| Hewlett-Packard Co., 3.75%, 12/1/20L2 | 650,000 | 637,062 |
| Hewlett-Packard Co., 6.13%, 3/1/14L2 | 600,000 | 679,948 |
| | | **1,317,010** |
| **CONSUMER FINANCE—1.7%** | | |
| American Express Credit Corp., 7.30%, 8/20/13L2 | 600,000 | 676,524 |
| Capital One Capital V, 10.25%, 8/15/39L2 | 1,300,000 | 1,399,124 |
| | | **2,075,648** |
| **DIVERSIFIED BANKS—0.5%** | | |
| National Australia Bank Ltd., 1.70%, 12/10/13L2(b) | 650,000 | **644,840** |
| **DIVERSIFIED CHEMICALS—0.7%** | | |
| Dow Chemical Co., /The, 4.25%, 11/15/20L2 | 925,000 | **889,574** |
| **DIVERSIFIED METALS & MINING—0.4%** | | |
| Anglo American Capital PLC, 9.38%, 4/8/14L2(b) | 350,000 | **421,695** |
| **ELECTRIC UTILITIES—0.6%** | | |
| Florida Power Corp., 5.80%, 9/15/17L2 | 600,000 | **682,534** |
| **ELECTRONIC MANUFACTURING SERVICES—0.7%** | | |
| Jabil Circuit Inc., 5.63%, 12/15/20L2 | 825,000 | **814,687** |
| **FERTILIZERS & AGRICULTURAL CHEMICALS—0.5%** | | |
| Potash Corp of Saskatchewan Inc., 3.25%, 12/1/17L2 | 650,000 | **630,836** |
| **HEALTH CARE DISTRIBUTORS—0.6%** | | |
| AmerisourceBergen Corp., 4.88%, 11/15/19L2 | 650,000 | **664,035** |
| **HEALTH CARE EQUIPMENT—0.3%** | | |
| St Jude Medical Inc., 2.50%, 1/15/16L2 | 350,000 | **345,896** |
| **HEALTH CARE SERVICES—0.6%** | | |
| HCA Inc., 7.25%, 9/15/20L2 | 650,000 | **682,500** |
| **HOMEBUILDING—0.7%** | | |
| Lennar Corp., 12.25%, 6/1/17L2 | 650,000 | **786,500** |
| **HOTELS RESORTS & CRUISE LINES—0.2%** | | |
| Wyndham Worldwide Corp., 7.38%, 3/1/20L2 | 175,000 | **192,710** |
| **INDUSTRIAL CONGLOMERATES—0.3%** | | |
| Tyco International Finance SA, 8.50%, 1/15/19L2 | 320,000 | **410,221** |
| **INTEGRATED TELECOMMUNICATION SERVICES—0.6%** | | |
| Cellco Partnership / Verizon Wireless Capital LLC, 7.38%, 11/15/13L2 | 600,000 | **695,593** |
| **IT CONSULTING & OTHER SERVICES—0.4%** | | |
| SAIC Inc., 4.45%, 12/1/20L2(b) | 475,000 | **476,702** |
| **LIFE & HEALTH INSURANCE—0.7%** | | |
| Lincoln National Corp., 8.75%, 7/1/19L2 | 350,000 | 438,485 |
| Prudential Financial Inc., 8.88%, 6/15/38L2 | 350,000 | 410,375 |
| | | **848,860** |

| CORPORATE BONDS—(CONT.) | PRINCIPAL AMOUNT | VALUE |
|---|---|---|
| **LIFE SCIENCES TOOLS & SERVICES—0.3%** | | |
| Life Technologies Corp., 4.40%, 3/1/15L2 | $ 350,000 | **$ 364,055** |
| **METAL & GLASS CONTAINERS—0.2%** | | |
| Ball Corp., 5.75%, 5/15/21L2 | 200,000 | **194,000** |
| **MOVIES & ENTERTAINMENT—0.2%** | | |
| Time Warner Cable Inc., 8.25%, 2/14/14L2 | 125,000 | 145,196 |
| Time Warner Inc., 3.15%, 7/15/15L2 | 150,000 | 152,563 |
| | | **297,759** |
| **MULTI-LINE INSURANCE—0.2%** | | |
| International Lease Finance Corp., 6.50%, 9/1/14L2(b) | 175,000 | **186,375** |
| **MULTI-UTILITIES—0.8%** | | |
| Consolidated Edison Co., of New York Inc., 5.30%, 12/1/16L2 | 875,000 | **983,855** |
| **OIL & GAS DRILLING—0.6%** | | |
| Transocean Inc., 6.50%, 11/15/20L2 | 650,000 | **691,379** |
| **OIL & GAS EXPLORATION & PRODUCTION—1.1%** | | |
| Anadarko Petroleum Corp., 6.38%, 9/15/17L2 | 650,000 | 709,020 |
| Plains Exploration & Production Co., 7.63%, 4/1/20L2 | 650,000 | 688,188 |
| | | **1,397,208** |
| **OIL & GAS STORAGE & TRANSPORTATION—0.5%** | | |
| Inergy LP/Inergy Finance Corp., 7.00%, 10/1/18L2(b) | 175,000 | 177,188 |
| Williams Cos Inc., /The, 8.75%, 1/15/20L2 | 350,000 | 425,121 |
| | | **602,309** |
| **OTHER DIVERSIFIED FINANCIAL SERVICES—1.6%** | | |
| Citigroup Inc., 8.50%, 5/22/19L2 | 600,000 | 746,029 |
| JPMorgan Chase & Co., 7.90%, 4/30/49L2 | 1,000,000 | 1,066,570 |
| | | **1,812,599** |
| **PACKAGED FOODS & MEATS—0.1%** | | |
| Kraft Foods Inc., 6.75%, 2/19/14L2 | 125,000 | **142,594** |
| **PHARMACEUTICALS—1.6%** | | |
| AstraZeneca PLC, 5.40%, 6/1/14L2 | 600,000 | 667,748 |
| Mylan Inc., 6.00%, 11/15/18L2(b) | 650,000 | 640,250 |
| Roche Holdings Inc., 5.00%, 3/1/14L2(b) | 600,000 | 657,527 |
| | | **1,965,525** |
| **PROPERTY & CASUALTY INSURANCE—0.6%** | | |
| Liberty Mutual Group Inc., 7.80%, 3/15/37L2(b) | 700,000 | **696,500** |
| **REGIONAL BANKS—0.9%** | | |
| SouthTrust Bank, 6.57%, 12/15/27L2 | 1,000,000 | **1,050,308** |
| **SEMICONDUCTORS—0.6%** | | |
| Analog Devices Inc., 5.00%, 7/1/14L2 | 350,000 | 377,523 |
| Broadcom Corp., 1.50%, 11/1/13L2(b) | 350,000 | 347,855 |
| | | **725,378** |
| **SPECIALIZED REITS—0.2%** | | |
| Host Hotels & Resorts LP, 7.13%, 11/1/13L2 | 224,000 | **228,480** |

| CORPORATE BONDS—(CONT.) | PRINCIPAL AMOUNT | VALUE |
|---|---|---|
| **SPECIALTY CHEMICALS—0.5%** | | |
| Sigma-Aldrich Corp., 3.38%, 11/1/20[L2] | $ 650,000 | **$ 610,936** |
| **SYSTEMS SOFTWARE—0.3%** | | |
| Microsoft Corp., 3.00%, 10/1/20[L2] | 350,000 | **328,877** |
| **WIRELESS TELECOMMUNICATION SERVICES—0.4%** | | |
| American Tower Corp., 4.50%, 1/15/18[L2] | 350,000 | 347,460 |
| MetroPCS Wireless Inc., 7.88%, 9/1/18[L2] | 175,000 | 182,438 |
| | | **529,898** |
| **TOTAL CORPORATE BONDS** (Cost $27,981,929) | | **29,666,242** |

| ASSET BACKED SECURITIES—0.7% | PRINCIPAL AMOUNT | VALUE |
|---|---|---|
| **MULTI-UTILITIES—0.3%** | | |
| CenterPoint Energy Transition Bond Co., LLC, 2005A, 4.97%, 8/1/14[L2] | 368,533 | **379,172** |
| **OTHER DIVERSIFIED FINANCIAL SERVICES—0.4%** | | |
| Nissan Auto Receivables Owner Trust, 2005A, 3.20%, 2/15/13[L2] | 518,588 | **525,719** |
| **TOTAL ASSET BACKED SECURITIES** (Cost $887,609) | | **904,891** |

| U.S. GOVERNMENT & AGENCY MORTGAGE BACKED OBLIGATIONS—2.8% (c) | PRINCIPAL AMOUNT | VALUE |
|---|---|---|
| **COLLATERALIZED MORTGAGE BACKED OBLIGATIONS—2.4%** | | |
| Federal National Mortgage Association, REMICS, 6.00%, 4/25/35 [+,L2] | 1,800,000 | **1,989,800** |
| Federal Home Loan Mortgage Corp., REMICS, 6.00%, 8/15/29 [+,L2] | 749,078 | **753,301** |
| Government National Mortgage Association, REMICS, 5.00%, 5/16/29 [+,L2] | 169,889 | **170,736** |
| | | **2,913,837** |
| **FEDERAL NATIONAL MORTGAGE ASSOCIATION—0.4%** | | |
| Federal National Mortgage Association, 5.00%, 4/01/18 [L2] | 493,711 | **527,573** |
| **TOTAL U.S. GOVERNMENT & AGENCY MORTGAGE BACKED OBLIGATIONS** (Cost $3,220,014) | | **3,441,410** |

| U.S. GOVERNMENT & AGENCY OBLIGATIONS (EXCLUDING MORTGAGE-BACKED)—10.8% (c) | PRINCIPAL AMOUNT | VALUE |
|---|---|---|
| **FEDERAL HOME LOAN BANK—0.2%** | | |
| Federal Home Loan Banks, 5.38%, 6/08/12 [L2] | 200,000 | **213,913** |

| U.S. GOVERNMENT & AGENCY OBLIGATIONS (EXCLUDING MORTGAGE-BACKED)—(CONT.) | PRINCIPAL AMOUNT | VALUE |
|---|---|---|
| **FEDERAL NATIONAL MORTGAGE ASSOCIATION—2.6%** | | |
| Federal National Mortgage Association, | | |
| 4.63%, 5/01/13 L2 | $ 1,400,000 | $ 1,505,868 |
| 5.00%, 2/13/17 L2 | 1,400,000 | 1,581,824 |
| | | **3,087,692** |
| **U.S. GOVERNMENT NOTE/BOND—8.0%** | | |
| U.S. Treasury Bonds L2 | | |
| 5.25%, 11/15/28 L2 | 1,000,000 | **1,146,250** |
| U.S. Treasury Notes | | |
| 5.00%, 8/15/11 L2 | 1,285,000 | 1,322,947 |
| 1.13%, 1/15/12 L2 | 1,400,000 | 1,411,430 |
| 1.50%, 12/31/13 L2 | 1,400,000 | 1,420,343 |
| 4.50%, 2/15/16 L2 | 640,000 | 716,750 |
| 4.75%, 8/15/17 L2 | 640,000 | 725,850 |
| 3.50%, 2/15/18 L2 | 150,000 | 157,817 |
| 3.38%, 11/15/19 L2 | 1,650,000 | 1,684,677 |
| 2.63%, 11/15/20 L2 | 1,000,000 | 943,438 |
| | | **8,383,252** |
| **TOTAL U.S. GOVERNMENT & AGENCY OBLIGATIONS (EXCLUDING MORTGAGE-BACKED)** (Cost $12,342,890) | | **12,831,107** |

| | | |
|---|---|---|
| Total Investments (Cost $107,219,635)(d) | 96.3% | 115,404,826 |
| Other Assets in Excess of Liabilities | 3.7 | 4,398,842 |
| **NET ASSETS** | 100.0% | **$ 119,803,668** |

‡ *Securities classified as Level 1 for ASC 820 disclosure purposes based on valuation inputs unless otherwise noted. See Notes 2 and 8 to the Financial Statements.*

\+ *Real Estate Mortgage Investment Conduit*
* *Non-income producing security.*
\# *American Depository Receipts.*
(a) *These securities are required to be converted on the date listed; they generally may be converted prior to this date at the option of the holder.*
(b) *Pursuant to Securities and Exchange Commission Rule 144A, these securities may be sold prior to their maturity only to qualified institutional buyers. These securities are deemed to be liquid and represent 5.7% of the net assets of the Fund.*
(c) *Securities issued by these agencies, except for United States Treasury Notes and Bonds, are neither guaranteed nor issued by the United States Government.*
(d) *At December 31, 2010, the net unrealized appreciation on investments, based on cost for federal income tax purposes of $107,312,056 amounted to $8,092,770 which consisted of aggregate gross unrealized appreciation of $13,447,414 and aggregate gross unrealized depreciation of $5,354,644.*
L2 *Security classified as Level 2 for ASC 820 disclosure purposes based on valuation inputs.*

***Industry classifications are unaudited.***
***See Notes to Financial Statements.***

| | | |
|---|---|---|
| ASSETS: | | |
| Investments in securities, at value (Identified cost)* see accompanying schedule of investments | $ | 115,404,826 |
| Cash and cash equivalents | | 2,761,466 |
| Receivable for investment securities sold | | 1,801,582 |
| Receivable for shares of beneficial interest sold | | 48,326 |
| Dividends and interest receivable | | 629,945 |
| Prepaid expenses | | 37,071 |
| Total Assets | | 120,683,216 |
| LIABILITIES: | | |
| Payable for investment securities purchased | | 604,581 |
| Payable for shares of beneficial interest redeemed | | 152,543 |
| Accrued investment advisory fees | | 68,039 |
| Accrued transfer agent fees | | 4,572 |
| Accrued administrative fees | | 2,793 |
| Accrued shareholder servicing fees | | 1,015 |
| Accrued other expenses | | 46,005 |
| Total Liabilities | | 879,548 |
| **NET ASSETS** | **$** | **119,803,668** |
| **Net Assets Consist of:** | | |
| Paid in capital | | 136,469,810 |
| Undistributed net investment income | | 3,099,954 |
| Accumulated net realized loss | | (27,951,291) |
| Net unrealized appreciation on investments | | 8,185,195 |
| **NET ASSETS** | **$** | **119,803,668** |
| **Net Asset Value Per Share** | | |
| Class I-2 | | $11.61 |
| **Net Assets By Class** | | |
| Class I-2 | | 119,803,668 |
| Class S | | — |
| **Shares of Benefical Interest Outstanding— Note 6 (Par Value $.001)** | | |
| Class I-2 | | 10,323,288 |
| *Identified Cost | $ | 107,219,635 |

**Statement of Operations**

*For the year ended December 31, 2010*

| | | |
|---|---|---|
| INCOME: | | |
| Dividends (net of foreign withholding taxes*) | $ | 1,292,831 |
| Interest | | 2,900,228 |
| Other | | 40,549 |
| Total Income | | 4,233,608 |
| EXPENSES | | |
| Advisory fees—Note 3 | | 866,232 |
| Distribution fees Class S—Note 3 | | 601 |
| Administrative fees—Note 3 | | 33,551 |
| Custodian fees | | 31,800 |
| Interest expenses | | 383 |
| Transfer agent fees and expenses—Note 3 | | 34,465 |
| Printing fees | | 33,775 |
| Professional fees | | 35,212 |
| Registration fees | | 43,936 |
| Trustee fees—Note 3 | | 18,257 |
| Miscellaneous | | 26,146 |
| Total Expenses | | 1,124,358 |
| Less, expense reimbursements/waivers—Note 3 | | (48,802) |
| Net Expenses | | 1,075,556 |
| NET INVESTMENT INCOME | | 3,158,052 |
| REALIZED AND UNREALIZED GAIN (LOSS) ON INVESTMENTS, OPTIONS AND FOREIGN CURRENCY TRANSACTIONS: | | |
| Net realized gain on investments and purchased options | | 1,897,794 |
| Net realized loss on foreign currency transactions | | (193) |
| Net change in unrealized appreciation (depreciation) on investments and foreign currency | | 6,662,845 |
| Net realized and unrealized gain on investments, options and foreign currency | | 8,560,446 |
| **NET INCREASE IN NET ASSETS RESULTING FROM OPERATIONS** | **$** | **11,718,498** |
| *Foreign withholding taxes | $ | 2,498 |

*See Notes to Financial Statements.*

| | For the Year Ended December 31, 2010 | For the Year Ended December 31, 2009 |
|---|---|---|
| Net investment income | $ 3,158,052 | $ 3,121,265 |
| Net realized gain (loss) on investments, options and foreign currency transactions | 1,897,601 | (12,805,562) |
| Net change in unrealized appreciation on investments, options and foreign currency | 6,662,845 | 40,357,012 |
| Net increase in net assets resulting from operations | 11,718,498 | 30,672,715 |
| Dividends and distributions to shareholders from: | | |
| Net investment income | | |
| Class I-2 | (3,115,203) | (3,885,030) |
| Class S | (5,390) | (7,319) |
| Net realized gains | | |
| Class I-2 | — | — |
| Class S | — | — |
| Total dividends and distributions to shareholders | (3,120,593) | (3,892,349) |
| Increase (decrease) from shares of beneficial interest transactions: | | |
| Class I-2 | (16,551,023) | (17,726,993) |
| Class S | (276,098) | 22,064 |
| Net decrease from shares of beneficial interest transactions—Note 6 | (16,827,121) | (17,704,929) |
| Total increase (decrease) | (8,229,216) | 9,075,437 |
| Net Assets: | | |
| Beginning of period | 128,032,884 | 118,957,447 |
| **END OF PERIOD** | **$ 119,803,668** | **$ 128,032,884** |
| Undistributed net investment income | $ 3,099,954 | $ 3,051,230 |

Alger Balanced Portfolio

| | Class I-2 | | | | |
|---|---|---|---|---|---|
| | Year ended 12/31/2010 | Year ended 12/31/2009 | Year ended 12/31/2008 | Year ended 12/31/2007 | Year ended 12/31/2006 |
| Net asset value, beginning of period | $ 10.79 | $ 8.64 | $ 14.61 | $ 14.11 | $ 14.44 |
| INCOME FROM INVESTMENT OPERATIONS: | | | | | |
| Net investment income(i) | 0.28 | 0.25 | 0.26 | 0.26 | 0.24 |
| Net realized and unrealized gain (loss) on investments | 0.82 | 2.21 | (4.35) | 1.41 | 0.39 |
| Total from investment operations | 1.10 | 2.46 | (4.09) | 1.67 | 0.63 |
| Dividends from net investment income | (0.28) | (0.31) | (0.33) | (0.31) | (0.22) |
| Distributions from net realized gains | — | — | (1.55) | (0.86) | (0.74) |
| Net asset value, end of period | $ 11.61 | $ 10.79 | $ 8.64 | $ 14.61 | $ 14.11 |
| Total return | 10.33% | 29.25% | (31.76)% | 12.37% | 4.72% |
| RATIOS/SUPPLEMENTAL DATA: | | | | | |
| Net assets, end of period (000's omitted) | $ 119,804 | $ 127,756 | $ 118,759 | $ 224,090 | $ 254,579 |
| Ratio of gross expenses to average net assets | 0.91% | 0.89% | 0.85% | 0.84% | 0.86% |
| Ratio of expense reimbursements to average net assets | (0.04)% | (0.04)% | (0.04)% | (0.04)% | 0.00% |
| Ratio of net expenses to average net assets | 0.87% | 0.85% | 0.81% | 0.80% | 0.86% |
| Ratio of net investment income to average net assets | 2.60% | 2.60% | 2.19% | 1.79% | 1.71% |
| Portfolio turnover rate | 69.30% | 104.04% | 76.32% | 103.77% | 288.73% |

(i) *Amount was computed based on average shares outstanding during the period.*

***See Notes to Financial Statements.***

## NOTE 1 — General:

The Alger Portfolios (the "Fund") is a diversified, open-end registered investment company organized as a business trust under the laws of the Commonwealth of Massachusetts. The Fund operates as a series company currently issuing seven series of shares of beneficial interest: the Alger Capital Appreciation Portfolio, Alger Large Cap Growth Portfolio, Alger Mid Cap Growth Portfolio, Alger SMid Cap Growth Portfolio, Alger Small Cap Growth Portfolio, Alger Growth & Income Portfolio, and Alger Balanced Portfolio (collectively the "Portfolios"). These financial statements include only the Alger Balanced Portfolio (the "Portfolio"). The Portfolio's investment objective is current income and long-term capital appreciation which it seeks to achieve through investing in equity and fixed income securities. Shares of the Portfolio are available and are being marketed exclusively as a pooled funding vehicle for qualified retirement plans and for life insurance companies writing all types of variable annuity contracts and variable life insurance policies.

The Portfolio offers Class I-2 shares. The Portfolio discontinued offering Class S shares on October 1, 2010 and the Class was liquidated on November 23, 2010.

## NOTE 2 — Significant Accounting Policies:

*(a) Investment Valuation:* The Portfolio values its financial instruments at fair value using independent dealers or pricing services under policies approved by the Board. Investments of the Portfolio are valued on each day the New York Stock Exchange (the "NYSE") is open, as of the close of the NYSE (normally 4:00 p.m. Eastern time).

Equity securities and option contracts for which such information is readily available are valued at the last reported sales price or official closing price as reported by an independent pricing service on the primary market or exchange on which they are traded. In the absence of reported sales, securities are valued at a price within the bid and ask price or, in the absence of a recent bid or ask price, the equivalent as obtained from one or more of the major market makers for the securities to be valued.

Debt securities generally trade in the over-the-counter market. Securities with remaining maturities of more than sixty days at the time of acquisition are valued on the basis of last available bid prices or current market quotations provided by dealers or pricing services. In determining the value of a particular investment, pricing services may use certain information with respect to transactions in such investments, quotations from dealers, pricing matrixes, market transactions in comparable investments, various relationships observed in the market between investments and calculated yield measures based on valuation technology commonly employed in the market for such investments. Asset-backed and mortgage-backed securities are valued by independent pricing services using models that consider estimated cash flows of each tranche of the security, establish a benchmark yield and develop an estimated tranche specific spread to the benchmark yield based on the unique attributes of the tranche.

Securities for which market quotations are not readily available are valued at fair value, as determined in good faith pursuant to procedures established by the Board of Trustees.

Securities in which the Portfolio invests may be traded in foreign markets that close before the close of the NYSE. Developments that occur between the close of the foreign markets and the close of the NYSE may result in adjustments to the closing prices to reflect what the investment adviser, pursuant to policies established by the Board of Trustees, believes to be the fair value of these securities as of the close of the NYSE. The Portfolio may also fair value securities in other situations, for example, when a particular foreign market is closed but the Portfolio is open.

Financial Accounting Standards Board Accounting Standards Codification 820 – Fair Value Measurements and Disclosures ("ASC 820") defines fair value as the price that the Portfolio would receive upon selling an investment in a timely transaction to an independent buyer in the principal or most advantageous market of the investment. ASC 820 established a three-tier hierarchy to maximize the use of observable market data and minimize the use of unobservable inputs and to establish classification of fair value measurements for disclosure purposes. "Inputs" refer broadly to the assumptions that market participants would use in pricing the asset or liability and may be observable or unobservable. Observable inputs are based on market data obtained from sources independent of the Portfolio. Unobservable inputs are inputs that reflect the Portfolio's, own assumptions based on the best information available in the circumstances. The three-tier hierarchy of inputs is summarized in the three broad Levels listed below.

- Level 1 – quoted prices in active markets for identical investments
- Level 2 – significant other observable inputs (including quoted prices for similar investments, interest rates, prepayment speeds, credit risk, etc.)
- Level 3 – significant unobservable inputs (including the Portfolio's, own assumptions in determining the fair value of investments)

The Portfolio's valuation techniques are consistent with the market approach whereby prices and other relevant information generated by market transactions involving identical or comparable assets are used to measure fair value. Inputs for Level 1 include exchange listed prices and broker quotes in an active market. Inputs for Level 2 include the last trade price in the case of a halted security, a broker quote in an inactive market, an exchange listed price which has been adjusted for fair value factors, and prices of closely related securities. Additional Level 2 inputs include an evaluated price which is based upon on a compilation of observable market information such as spreads for fixed income and preferred securities. Inputs for Level 3 include derived prices from unobservable market information which can include cash flows and other information obtained from a company's financial statements, or from market indicators such as benchmarks and indices.

*(b) Cash and Cash Equivalents:* Cash and cash equivalents include U.S. dollars and short-term securities maturing in sixty days or less. Such short-term securities are valued at amortized cost which approximates market value.

*(c) Security Transactions and Investment Income*: Security transactions are recorded on a trade date basis. Realized gains and losses from security transactions are recorded on the identified cost basis. Dividend income is recognized on the ex-dividend date and interest

income is recognized on the accrual basis.

Premiums and discounts on debt securities purchased are amortized or accreted over the lives of the respective securities.

*(d) Foreign Currency Transactions:* The books and records of the Portfolio are maintained in U.S. dollars. Foreign currencies, investments and other assets and liabilities are translated into U.S. dollars at the prevailing rates of exchange on the valuation date. Purchases and sales of investment securities and income and expenses are translated into U.S. dollars at the prevailing exchange rates on the respective dates of such transactions.

Net realized gains and losses on foreign currency transactions represent net gains and losses from the disposition of foreign currencies, currency gains and losses realized between the trade dates and settlement dates of security transactions, and the difference between the amount of net investment income accrued and the U.S. dollar amount actually received. The effects of changes in foreign currency exchange rates on investments in securities are included in realized and unrealized gain or loss on investments in the Statement of Operations.

*(e) Option Contracts:* When a Portfolio writes an option, an amount equal to the premium received by the Portfolio is recorded as a liability and is subsequently adjusted to the current fair value of the option written. Premiums received from writing options that expire unexercised are treated by the Portfolio on the expiration date as realized gains from investments. The difference between the premium and the amount paid on effecting a closing purchase transaction, including brokerage commissions, is also treated as a realized gain, or, if the premium is less than the amount paid for the closing purchase transaction, as a realized loss. If a written call option is exercised, the premium is added to the proceeds from the sale of the underlying security in determining whether the Portfolio has realized a gain or loss. If a written put option is exercised, the premium reduces the cost basis of the securities purchased by the Portfolio. The Portfolio as writer of an option bears the market risk of an unfavorable change in the price of the security underlying the written option.

The Portfolio may also purchase put and call options. The Portfolio pays a premium which is included in the Portfolio's Statement of Assets and Liabilities as an investment and subsequently marked to market to reflect the current value of the option. Premiums paid for purchasing options which expire are treated as realized losses. The risk of loss associated with purchasing put and call options is limited to the premium paid. Premiums paid for purchasing options which are exercised or closed are added to the amounts paid or offset against the proceeds on the underlying security to determine the realized gain or loss.

*(f) Lending of Portfolio Securities*: The Portfolio may lend its securities to financial institutions, provided that the market value of the securities loaned will not at any time exceed one third of the Portfolio's total assets. The Portfolio earns fees on the securities loaned. In order to protect against the risk of failure by the borrower to return the securities loaned or any delay in the delivery of such securities, the loan is collateralized by cash, letters of credit or U.S. Government securities that are maintained in an amount

equal to at least 100 percent of the current market value of the loaned securities. The "current market value" of the loaned securities is determined at the close of business of the Portfolio and any required additional collateral is delivered to the Portfolio on the next business day. There were no securities on loan during the year ended December 31, 2010.

*(g) Dividends to Shareholders:* Dividends and distributions payable to shareholders are recorded by the Portfolio on the ex-dividend date.

Dividends from net investment income are declared and paid annually. Dividends from net realized gains, offset by any loss carryforward, are declared and paid annually after the end of the fiscal year in which earned. Each class is treated separately in determining the amounts of dividends from net investment income payable to holders of its shares.

The characterization of distributions to shareholders for financial reporting purposes is determined in accordance with federal income tax rules. Therefore, the source of the Portfolio's distributions may be shown in the accompanying financial statements as either from, or in excess of, net investment income or net realized gain on investment transactions, or return of capital, depending on the type of book/tax differences that may exist. Capital accounts within the financial statements are adjusted for permanent book/tax differences. Reclassifications result primarily from the difference in tax treatment of net operating losses, premium/discount of debt securities, realized gain or loss from foreign currency transactions, and realized gains from redemptions in kind, if any. The reclassifications have no impact on the net asset values of the Portfolio and were designed to present the Portfolio's capital accounts on a tax basis.

*(h) Federal Income Taxes:* It is the Portfolio's policy to comply with the requirements of the Internal Revenue Code Subchapter M applicable to regulated investment companies and to distribute all of the taxable income, including net realized capital gains, of the Portfolio to its respective shareholders. Therefore, no federal income tax provision is required. The Portfolio is treated as a separate entity for the purpose of determining such compliance.

Financial Accounting Standards Board Accounting Standards Codification 740 – Income Taxes ("ASC 740") requires the Portfolio to measure and recognize in its financial statements the benefit of a tax position taken (or expected to be taken) on an income tax return if such position will more likely than not be sustained upon examination based on the technical merits of the position. No tax years are currently under investigation. The Portfolio files income tax returns in the U.S. Federal jurisdiction, as well as the New York State and New York City jurisdictions. Based upon their review of tax positions for the Portfolio's open tax years of 2007-2010 in these jurisdictions, the Portfolio has determined that ASC 740 did not have a material impact on the Portfolio's financial statements for the year ended December 31, 2010.

*(i) Allocation Methods:* The Fund accounts separately for the assets, liabilities and operations of each Portfolio. Expenses directly attributable to each Portfolio are charged to that Portfolio's operations; expenses which are applicable to all Portfolios are allocated among them based on net assets. Income, realized and unrealized gains and losses, and expenses of each Portfolio are allocated among the Portfolio's classes based on relative net assets, with the exception of distribution fees and transfer agency fees.

*(j) Estimates:* These financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America, which require using estimates and assumptions that affect the reported amounts therein. Actual results may differ from those estimates.

## NOTE 3 — Investment Advisory Fees and Other Transactions with Affiliates:

*(a) Investment Advisory and Administration Fees*: Fees incurred by the Portfolio, pursuant to the provisions of the Fund's Investment Advisory Agreement and Administration Agreement with Fred Alger Management, Inc. ("Alger Management"), are payable monthly and computed based on the average daily net assets of the Portfolio at the following annual rate:

| | Advisory Fee | Administration Fee |
|---|---|---|
| Alger Balanced Portfolio | .710% | .0275% |

As part of a settlement with the New York State Attorney General dated October 11, 2006, Alger Management has agreed to reduce its advisory fee listed above to 0.67% for the Portfolio, for the period from December 1, 2006 through November 30, 2011.

*(b) Distribution Fees*: Class S shares—The Fund has adopted a Distribution Plan pursuant to which Class S shares of each Portfolio pay Fred Alger & Company, Incorporated, the Fund's distributor (the "Distributor" or "Alger Inc."), a fee at the annual rate of .25% of the respective average daily net assets of the Class S shares of the designated Portfolio to compensate the Alger Inc. for its activities and expenses incurred in distributing the Class S shares. The fees paid may be more or less than the expenses incurred by Alger Inc. The Portfolio liquidated the Class S shares on November 23, 2010.

*(c) Brokerage Commissions*: During the year ended December 31, 2010, the Portfolio paid Alger Inc. $18,872, in connection with securities transactions.

*(d) Shareholder Administrative Fees*: The Fund has entered into a shareholder administrative services agreement with Alger Management to compensate Alger Management on a per account basis for its liaison and administrative oversight of Boston Financial Data Services, Inc. ("BFDS") the transfer agent, and other related services. Effective June 1, 2010 the Fund compensates Alger Management at the annual rate of 0.01% of the average daily net assets for these services. From January 1, 2010 through December 31, 2010, the Portfolio incurred fees of $6,989, for these services, which are included in transfer agent fees and expenses in the Statements of Operations.

*(e) Trustee Fees:* From January 1, 2010 through February 8, 2010, the Portfolio paid each Trustee who is not affiliated with Alger Management or its affiliates $500 for each meeting attended, to a maximum of $2,000 per annum. The Chairman of the Board of Trustees received an additional annual fee of $10,000 which is paid, pro rata, by all portfolios managed by Alger Management. Additionally, each member of the audit committee received an additional $50 from the Portfolio for each audit committee meeting attended, to a maximum of $200 per annum.

Effective February 9, 2010 the Portfolio pays each trustee who is not affiliated with Alger Management or its affiliates $750 for each meeting attended, to a maximum of $3,000 per annum, plus travel expenses incurred for attending the meeting. The chairman of the Board of Trustees receives an additional annual fee of $15,000 which is paid, pro rata, by all funds managed by Alger Management. Additionally, each member of the audit committee receives an additional $75 for each audit committee meeting attended, to a maximum of $300 per annum.

*(f) Interfund Loans:* The Portfolio, along with other funds advised by Alger Management, may borrow money from and lend money to each other for temporary or emergency purposes. To the extent permitted under its investment restrictions, the Portfolio may lend uninvested cash in an amount up to 15% of its net assets to other Portfolios, and the Portfolio may borrow in an amount up to 10% of its net assets from other Portfolios. If the Portfolio has borrowed from other Portfolios and has aggregate borrowings from all sources that exceed 10% of the Portfolio's total assets, the Portfolio will secure all of its loans from other Portfolios. The interest rate charged on interfund loans is equal to the average of the overnight time deposit rate and bank loan rate available to the Portfolios.

During the year ended December 31, 2010, the Portfolio incurred interest expense of $67, in connection with interfund loans.

*(g) Other Transactions With Affiliates:* Certain trustees and officers of the Trust are directors and officers of Alger Management and the Distributor.

## NOTE 4 — Securities Transactions:

Purchases and sales of securities, other than U.S. Government and short-term securities, for the year ended December 31, were as follows:

| | PURCHASES | SALES |
|---|---|---|
| Alger Balanced Portfolio | $82,347,206 | $96,434,910 |

## NOTE 5 — Borrowing:

The Portfolio may borrow from its custodian on an uncommitted basis. The Portfolio pays the custodian a market rate of interest, generally based upon the London Inter-Bank Offer Rate. The Portfolio may also borrow from other portfolios advised by Alger Management, as discussed in Note 3 (f). For the year ended December 31, the Portfolio had the following borrowings:

| | AVERAGE DAILY BORROWING | WEIGHTED AVERAGE INTEREST RATE |
|---|---|---|
| Alger Balanced Portfolio | $ 16,951 | 1.88% |

The highest amount borrowed during the year ended December 31, 2010 for the Portfolio was as follows:

| | HIGHEST BORROWING |
|---|---|
| Alger Balanced Portfolio | $841,353 |

## NOTE 6 — Share Capital:

The Fund has an unlimited number of authorized shares of beneficial interest of $.001 par value for each share class. During the year ended December 31, 2010 and the year ended December 31, 2009, transactions of shares of beneficial interest were as follows:

| | FOR THE YEAR ENDED DECEMBER 31, 2010 | | FOR THE YEAR ENDED DECEMBER 31, 2009 | |
|---|---|---|---|---|
| | SHARES | AMOUNT | SHARES | AMOUNT |
| **Alger Balanced Portfolio** | | | | |
| **Class I-2:** | | | | |
| Shares sold | 594,492 | $ 6,504,085 | 843,697 | $ 8,050,600 |
| Dividends reinvested | 285,275 | 3,115,203 | 438,986 | 3,885,030 |
| Shares redeemed | (2,397,137) | (26,170,311) | (3,183,478) | (29,662,623) |
| **Net decrease** | **(1,517,370)** | **$ (16,551,023)** | **(1,900,795)** | **$ (17,726,993)** |
| **Class S:** | | | | |
| Shares sold | 56 | $ 698 | 4,947 | $ 46,643 |
| Dividends reinvested | 454 | 5,390 | 760 | 7,319 |
| Shares redeemed | (24,051) | (282,186) | (3,249) | (31,898) |
| **Net increase (decrease)** | **(23,541)** | **$ (276,098)** | **2,458** | **$ 22,064** |

## NOTE 7 — Income Tax Information:

The tax character of distributions paid during the year ended December 31, 2010 and the year ended December 31, 2009 was as follows:

| | YEAR ENDED DECEMBER 31, 2010 | YEAR ENDED DECEMBER 31, 2009 |
|---|---|---|
| **Alger Balanced Portfolio** | | |
| Distributions paid from: | | |
| Ordinary Income | $ 3,120,593 | $ 3,892,349 |
| Long-term capital gain | — | — |
| **Total distributions paid** | $ 3,120,593 | $ 3,892,349 |

As of December 31, 2010, the components of accumulated gains and losses on a tax basis were as follows:

| **Alger Balanced Portfolio** | |
|---|---|
| Undistributed ordinary income | $ 3,162,400 |
| Undistributed long-term gains | — |
| Net accumulated earnings | 3,162,400 |
| Capital loss carryforwards | (27,921,312) |
| Net unrealized appreciation | 8,092,770 |
| Total accumulated losses | $ (16,666,142) |

At December 31, 2010, the Portfolio, for federal income tax purposes, had capital loss carryforwards which expire as set forth in the table below. These amounts may be applied against future net realized gains until the earlier of their utilization or expiration.

| Expiration Dates | Alger Balanced Portfolio |
|---|---|
| 2016 | $ 4,137,651 |
| 2017 | 23,783,661 |
| Total | 27,921,312 |

Net capital losses incurred after October 31 and within the taxable year are deemed to arise on the first business day of the portfolio's next taxable year.

The difference between book-basis and tax-basis unrealized appreciation (depreciation) is determined annually and is attributable primarily to the tax deferral of losses on wash sales, the tax treatment of premium/discount on debt securities, and the tax treatment of partnership investments.

Permanent differences, primarily from the tax treatment of premium/discount on debt securities, and partnership investments sold by the Portfolio, resulted in the following reclassifications among the Portfolio's components of net assets at December 31, 2010:

| Alger Balanced Portfolio | |
|---|---|
| Undistributed net investment income | $ 11,265 |
| Accumulated net realized loss | $ 36,275 |
| Paid in capital | $ (47,540) |

## NOTE 8 — Fair Value Measurements:

The major categories of securities and their respective fair value inputs are detailed in each Portfolio's Schedule of Investments. The following is a summary of the inputs used as of December 31, 2010 in valuing the Portfolios' investments carried at fair value. There were no significant transfers of investment assets between Levels 1 and 2 as of December 31, 2010.

| Alger Balanced Portfolio | TOTAL FUND | LEVEL 1 | LEVEL 2 | LEVEL 3 |
|---|---|---|---|---|
| **COMMON STOCKS** | | | | |
| Consumer Discretionary | $ 7,019,157 | $ 7,019,157 | — | — |
| Consumer Staples | 5,785,503 | 5,785,503 | — | — |
| Energy | 7,023,679 | 7,023,679 | — | — |
| Financials | 8,461,100 | 8,043,907 | 417,193 | — |
| Health Care | 5,931,869 | 5,931,869 | — | — |
| Industrials | 7,519,108 | 7,519,108 | — | — |
| Information Technology | 15,631,064 | 15,467,794 | 163,270 | — |
| Materials | 3,287,616 | 3,287,616 | — | — |
| Telecommunication Services | 154,920 | 154,920 | — | — |
| **TOTAL COMMON STOCKS** | **$ 60,814,016** | **$ 60,233,553** | **$ 580,463** | **—** |

| | | | | |
|---|---|---|---|---|
| **CONVERTIBLE CORPORATE BONDS** | | | | |
| Financials | $ 513,125 | — | $ 513,125 | — |
| Information Technology | 851,719 | — | 851,719 | — |
| Materials | 812,500 | — | 812,500 | — |
| Telecommunication Services | 521,500 | — | 521,500 | — |
| Utilities | 703,750 | — | 703,750 | — |
| **TOTAL CONVERTIBLE CORPORATE BONDS** | **$ 3,402,594** | **—** | **$ 3,402,594** | **—** |
| **CONVERTIBLE PREFERRED STOCK** | | | | |
| Consumer Discretionary | $ 946,925 | $ 946,925 | — | — |
| Financials | 717,080 | 717,080 | — | — |
| Utilities | 439,760 | 439,760 | — | — |
| **TOTAL CONVERTIBLE PREFERRED STOCK** | **$ 2,103,765** | **$ 2,103,765** | **—** | **—** |
| **CORPORATE BONDS** | | | | |
| Consumer Discretionary | $ 2,772,371 | — | $ 2,772,371 | — |
| Consumer Staples | 142,594 | — | 142,594 | — |
| Energy | 2,690,896 | — | 2,690,896 | — |
| Financials | 7,543,610 | — | 7,543,610 | — |
| Health Care | 4,022,011 | — | 4,022,011 | — |
| Industrials | 1,794,336 | — | 1,794,336 | — |
| Information Technology | 5,061,503 | — | 5,061,503 | — |
| Materials | 2,747,041 | — | 2,747,041 | — |
| Telecommunication Services | 1,225,491 | — | 1,225,491 | — |
| Utilities | 1,666,389 | — | 1,666,389 | — |
| **TOTAL CORPORATE BONDS** | **$ 29,666,242** | **—** | **$ 29,666,242** | **—** |
| **MANDATORY CONVERTIBLE PREFERRED STOCK** | | | | |
| Financials | $ 956,830 | $ 956,830 | — | — |
| **PREFERRED STOCKS** | | | | |
| Financials | $ 1,283,971 | $ 1,283,971 | — | — |
| **ASSET BACKED SECURITIES** | | | | |
| Financials | $ 525,719 | — | $ 525,719 | — |
| Utilities | 379,172 | — | 379,172 | — |
| **TOTAL ASSET BACKED SECURITIES** | **$ 904,891** | **—** | **$ 904,891** | **—** |
| **U.S. GOVERNMENT & AGENCY MORTGAGE BACKED OBLIGATIONS** | | | | |
| Collateralized Mortgage Backed Obligations | $ 2,913,837 | — | $ 2,913,837 | — |
| Federal National Mortgage Association | 527,573 | — | 527,573 | — |
| **TOTAL U.S. GOVERNMENT & AGENCY MORTGAGE BACKED OBLIGATIONS** | **$ 3,441,410** | **—** | **$ 3,441,410** | **—** |
| **U.S. GOVERNMENT & AGENCY OBLIGATIONS (EXCLUDING MORTGAGE-BACKED)** | | | | |
| Federal Home Loan Bank | $ 213,913 | — | $ 213,913 | — |
| Federal National Mortgage Association | 3,087,692 | — | 3,087,692 | — |
| U.S. Treasury Bonds | 1,146,250 | — | 1,146,250 | — |
| U.S. Treasury Notes | 8,383,252 | — | 8,383,252 | — |
| **TOTAL U.S. GOVERNMENT & AGENCY OBLIGATIONS (EXCLUDING MORTGAGE-BACKED)** | **$ 12,831,107** | **—** | **$ 12,831,107** | **—** |
| **TOTAL INVESTMENTS IN SECURITIES** | **$ 115,404,826** | **$ 64,578,119** | **$ 50,826,707** | **—** |

## NOTE 9 — Derivatives:

Financial Accounting Standards Board Accounting Standards Codification 815 – Derivatives and Hedging ("ASC 815") requires qualitative disclosures about objectives and strategies for using derivatives, quantitative disclosures about fair value amounts of and gains and losses on derivative instruments, and disclosures about credit-risk-related contingent features in derivative agreements.

Forward currency contracts—In connection with portfolio purchases and sales of securities denominated in foreign currencies, the Portfolio may enter into forward currency contracts. Additionally, the Portfolio may enter into such contracts to economically hedge certain other foreign currency denominated investments. These contracts are valued at the current cost of covering or offsetting such contracts, and the related realized and unrealized foreign exchange gains and losses are included in the statement of operations. In the event that counterparties fail to settle these currency contracts or the related foreign security trades, the Portfolio could be exposed to foreign currency fluctuations.

Options—The Portfolio seek to capture the majority of the returns associated with equity market investments. To meet this investment goal, the Portfolio invests in a broadly diversified portfolio of common stocks, while also buying and selling call and put options on equities and equity indices. The Portfolio purchases call options to increase its exposure to stock market risk and also provide diversification of risk. The Portfolio purchases put options in order to protect from significant market declines that may occur over a short period of time. The Portfolio will write covered call and cash secured put options to generate cash flows while reducing the volatility of the portfolio. The cash flows may be an important source of the Portfolio's return, although written call options may reduce the Portfolio's ability to profit from increases in the value of the underlying security or equity portfolio. The value of a call option generally increases as the price of the underlying stock increases and decreases as the stock decreases in price. Conversely, the value of a put option generally increases as the price of the underlying stock decreases and decreases as the stock increases in price. The combination of the diversified stock portfolio and the purchase and sale of options is intended to provide the Portfolio with the majority of the returns associated with equity market investments but with reduced volatility and returns that are augmented with the cash flows from the sale of options. During the year ended December 31, 2010, written equity and index put options were used in accordance with this objective.

During the year ended December 31, 2010, the Portfolio had no derivative instruments.

## NOTE 10 — Litigation:

On August 31, 2005, the West Virginia Securities Commissioner (the "WVSC"), in an ex parte Summary Order to Cease and Desist and Notice of Right to Hearing, concluded that the Manager and the Distributor had violated the West Virginia Uniform Securities Act (the "WVUSA"), and ordered the Manager and the Distributor to cease and desist from further violations of the WVUSA by engaging in the market-timing-related conduct described in the order. The ex parte order provided notice of their right to a hearing with respect to the violations of law asserted by the WVSC. Other firms unaffiliated with the

Manager were served with similar orders. The Manager and the Distributor intend to request a hearing for the purpose of seeking to vacate or modify the order.

In addition, in 2003 and 2004 several purported class actions and shareholder derivative suits were filed against various parties in the mutual fund industry, including the Manager, certain mutual funds managed by the Manager (the "Alger Mutual Funds"), and certain current and former Alger Mutual Fund trustees and officers, alleging wrongful conduct related to market-timing and late-trading by mutual fund shareholders. These cases were transferred to the U.S. District Court of Maryland by the Judicial Panel on Multidistrict Litigation for consolidated pre-trial proceedings under the caption number 1:04-MD-15863 (JFM). After a number of the claims in the Alger lawsuits, including all claims against Alger Mutual Funds and their independent trustees, were dismissed by the court, the Alger-related class and derivative suits were settled. A Final Judgment and Order approving the settlement was entered on October 25, 2010. No appeals from the Final Judgment and Order were filed within the allotted time limit. The settlement was paid by insurance, and had no financial impact on the Alger Mutual Funds.

## NOTE 11 — Subsequent Event:

Each Portfolio has evaluated events that have occurred after December 31, 2010. No events have been identified which require recognition as of December 31, 2010.

## REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Shareholders and Board of Trustees of The Alger Portfolios:

We have audited the accompanying statement of assets and liabilities, including the schedule of investments, of the Alger Balanced Portfolio, one of the portfolios constituting The Alger Portfolios (the "Fund") as of December 31, 2010, and the related statement of operations for the year then ended, the statements of changes in net assets for each of the two years in the period then ended, and the financial highlights for each of the two years in the period then ended. These financial statements and financial highlights are the responsibility of the Fund's management. Our responsibility is to express an opinion on these financial statements and financial highlights based on our audits. The Fund's financial highlights for the respective periods ended December 31, 2008 were audited by other auditors, whose report dated February 10, 2009, expressed an unqualified opinion on such financial highlights.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements and financial highlights are free of material misstatement. The Fund is not required to have, nor were we engaged to perform, an audit of their internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Fund's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. Our procedures included confirmation of securities owned as of December 31, 2010, by correspondence with the custodian and brokers; where replies were not received from brokers, we performed other auditing procedures. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements and financial highlights referred to above, present fairly, in all material respects, the financial position of the Alger Balanced Portfolio of The Alger Portfolios as of December 31, 2010, the results of its operations for the year then ended, the changes in its net assets for each of the two years in the period then ended, and the financial highlights for each of the two years in the period then ended, in conformity with accounting principles generally accepted in the United States of America.

Deloitte & Touche LLP
New York, New York
February 17, 2011

## Shareholder Expense Example

As a shareholder of a Portfolio, you incur two types of costs: transaction costs, if applicable; and ongoing costs, including management fees, distribution (12b-1) fees, if applicable, and other fund expenses. This example is intended to help you understand your ongoing costs (in dollars) of investing in a Portfolio and to compare these costs with the ongoing costs of investing in other mutual funds.

The example below is based on an investment of $1,000 invested at the beginning of the six-month period starting July 1, 2010 and ending December 31, 2010.

## Actual Expenses

The first line for each class of shares in the table below provides information about actual account values and actual expenses. You may use the information in this line, together with the amount you invested, to estimate the expenses that you would have paid over the period. Simply divide your account value by $1,000 (for example, an $8,600 account value divided by $1,000 = 8.6), then multiply the result by the number in the first line under the heading entitled "Expenses Paid During the Period" to estimate the expenses you paid on your account during this period.

## Hypothetical Example for Comparison Purposes

The second line for each class of shares in the table below provides information about hypothetical account values and hypothetical expenses based on the Portfolio's actual expense ratios for each class of shares and an assumed rate of return of 5% per year before expenses, which is not the Portfolio's actual return. The hypothetical account values and expenses may not be used to estimate the actual ending account balance or expenses you paid for the period. You may use this information to compare the ongoing costs of investing in a Portfolio and other funds. To do so, compare this 5% hypothetical example with the 5% hypothetical examples that appear in the shareholder reports of other funds.

Please note that the expenses shown in the table are meant to highlight your ongoing costs only and do not reflect any transaction costs or deduction of insurance charges against assets or annuities. Therefore, the second line under each class of shares in the table is useful in comparing ongoing costs only, and will not help you determine the relative total costs of owning different funds. In addition, if these transactional costs were included, your costs would have been higher.

| | | Beginning Account Value July 1, 2010 | Ending Account Value December 31, 2010 | Expenses Paid During the Six Months Ended December 31, 2010(a) | Ratio of Expenses to Average Net Assets For the Six Months Ended December 31, 2010(b) |
|---|---|---|---|---|---|
| **Alger Balanced Portfolio** | | | | | |
| **Class I-2** | Actual | $ 1,000.00 | $ 1,137.12 | $ 4.69 | 0.87% |
| | Hypothetical(c) | 1,000.00 | 1,020.82 | 4.43 | 0.87 |

*(a) Expenses are equal to the annualized expense ratio of the respective share class, multiplied by the average account value over the period, multiplied by 184/365 (to reflect the one-half year period).*
*(b) Annualized.*
*(c) 5% annual return before expenses.*

## Trustees and Officers of the Fund

Information about the trustees and officers of the Fund is set forth below. In the table the term "Alger Fund Complex" refers to the Fund, The Alger Funds, The Alger Institutional Funds, Alger China-U.S. Growth Fund and The Alger Funds II, each of which is a registered investment company managed by Fred Alger Management, Inc. ("Alger Management"). Each Trustee serves until an event of termination, such as death or resignation, or until his successor is duly elected; each officer's term of office is one year. Unless otherwise noted, the address of each person named below is 111 Fifth Avenue, New York, NY 10003.

| Name, Age, Position with the Fund | Principal Occupations | Trustee and/or Officer Since | Number of Funds in the Alger Fund Complex which are Overseen by Trustee |
|---|---|---|---|
| **INTERESTED TRUSTEE** | | | |
| Hilary M. Alger (49) | Director of Development, Pennsylvania Ballet since 2004; Associate Director of Development, College of Arts and Sciences and Graduate School, University of Virginia 1999-2003. | 2003 | 27 |
| **NON-INTERESTED TRUSTEE** | | | |
| Charles F. Baird, Jr. (57) | Managing Partner of North Castle Partners, a private equity securities group; Chairman of Leiner Health Products, Enzymatic Therapy and Caleel & Hayden (skincare business); former Chairman of Elizabeth Arden Day Spas, Naked Juice, Equinox (fitness company) and EAS (manufacturer of nutritional products). Formerly Managing Director of AEA Investors, Inc. | 2000 | 27 |
| Roger P. Cheever (65) | Associate Vice President for Principal Gifts, and Senior Associate Dean for Development in the Faculty of Arts and Sciences at Harvard University; Formerly Deputy Director of the Harvard College Fund. | 2000 | 27 |
| Lester L. Colbert Jr. (76) | Private investor since 1988; Formerly Chairman of the Board, President and Chief Executive Officer of Xidex Corporation (manufacturer of computer information media). | 2000 | 27 |
| Stephen E. O'Neil (78) | Attorney. Private Investor since 1981. Formerly of Counsel to the law firm of Kohler & Barnes. | 1986 | 27 |
| David Rosenberg (48) | Associate Professor of Law since January 2006 (Assistant Professor 2000-2005), Zicklin School of Business, Baruch College, City University of New York. | 2007 | 27 |
| Nathan E. Saint-Amand M.D. (73) | Medical doctor in private practice; Member of the Board of the Manhattan Institute (non-profit policy research) since 1988; Formerly Co-Chairman, Special Projects Committee, Memorial Sloan Kettering. | 1986 | 27 |

| Name, Age, Position with the Fund | Principal Occupations | Trustee and/or Officer Since | Number of Funds in the Alger Fund Complex which are Overseen by Trustee |
|---|---|---|---|
| **OFFICERS** | | | |
| Dan C. Chung (48)<br>President | Chief Investment Officer and Director since 2001, and Chief Executive Officer since 2006, of Alger Management; President since 2003 of Alger Associates, Inc. ("Associates"); President and Director since 2003 of Fred Alger International Advisory S.A. ("International"); President since 2003 and Director since 2003 of Analysts Resources, Inc. ("Resources"); Formerly Trustee of the Trust from 2001 to 2007. | 2001 | N/A |
| Michael D. Martins (45)<br>Treasurer | Senior Vice President of Alger Management; Assistant Treasurer since 2004. | 2005 | N/A |
| Hal Liebes (46)<br>Secretary | Executive Vice President, Chief Legal Officer, Chief Operating Officer and Secretary of Alger Management; Director since 2006 of International and Resources. | 2005 | N/A |
| Lisa A. Moss (45)<br>Assistant Secretary | Senior Vice President since 2009, and Vice President and Assistant General Counsel of Alger Management since June 2006. Formerly Director of Merrill Lynch Investment Managers, L.P. from 2005-2006. | 2006 | N/A |
| Anthony S. Caputo (55)<br>Assistant Treasurer | Employed by Alger Management since 1986, currently serving as Vice President. | 2007 | N/A |
| Sergio M. Pavone (49)<br>Assistant Treasurer | Employed by Alger Management since 2002, currently serving as Vice President. | 2007 | N/A |
| Barry J. Mullen (57)<br>Chief Compliance Officer | Senior Vice President and Chief Compliance officer for Alger Management since May 2006. Formerly Director of BlackRock, Inc. from 2004-2006. | 2006 | N/A |

Ms. Alger is an "interested person" (as defined in the Investment Company Act) of the Fund because of her affiliations with Alger Management. No Trustee is a director of any public company except as indicated under "Principal Occupations".

The Statement of Additional Information contains additional information about the Fund's Trustees and is available without charge upon request by calling (800) 992-3863.

## Investment Management Agreement Renewal

At an in-person meeting held on September 14, 2010, the Trustees, including the Independent Trustees, unanimously approved renewal of the Investment Advisory Agreement (the "Agreement") between the Fund and Fred Alger Management, Inc. ("Alger Management"). The Independent Trustees were assisted in their review by independent legal counsel and met with such counsel in executive session separate from representatives of Alger Management.

In evaluating the Agreement, the Trustees drew on materials that they had requested and which were provided to them in advance of the meeting by Alger Management and by counsel. The materials covered, among other matters, (i) the nature, extent and quality of the services provided by Alger Management under the Agreement, (ii) the investment performance of the Fund's portfolios (each a "Portfolio"), (iii) the costs to Alger Management of its services and the profits realized by Alger Management and Alger Inc. from their relationship with the Fund, and (iv) the extent to which economies of scale would be realized if and as the Portfolios grow and whether the fee levels in the Agreement reflect these economies of scale. These materials included an analysis of the Portfolios and Alger Management's services by FUSE Research Network LLC ("FUSE"), an independent consulting firm whose specialties include assistance to fund trustees and directors in their review of advisory contracts pursuant to section 15(c) of the Investment Company Act of 1940. At the meeting, senior FUSE personnel provided a presentation to the Trustees based on the FUSE materials.

In deciding whether to approve renewal of the Agreement, the Trustees considered various factors, including those enumerated above. They also considered other direct and indirect benefits to Alger Management and its affiliates from their relationship with the Fund.

**Nature, Extent and Quality of Services.** In considering the nature, extent and quality of the services provided by Alger Management pursuant to the Agreement, the Trustees relied on their prior experience as Trustees of the Fund, their familiarity with the personnel and resources of Alger Management and its affiliates, and the materials provided at the meeting. They noted that under the Agreement Alger Management is responsible for managing the investment operations of the Portfolios. They also noted that administrative, compliance, reporting and accounting services necessary for the conduct of the Fund's affairs are provided by Alger Management under the separate Administration Agreement. The Trustees reviewed the background and experience of Alger Management's senior investment management personnel, including the individuals currently responsible for the investment operations of the Portfolios. They also considered the resources, operational structures and practices of Alger Management in managing each Portfolio, as well as Alger Management's overall investment management business. They noted especially Alger Management's history of expertise in managing portfolios of "growth" stocks and that, according to an analysis provided by FUSE, the characteristics of each equity Portfolio had been consistent with those of a fund that holds itself out to investors as growth-oriented. They also took notice of the ability of the manager of the fixed-income portion of the Balanced Portfolio to manage fixed-income instruments across the credit and credit quality spectra. The Trustees concluded that Alger Management's experience, resources and strength in the areas of importance to the Fund are considerable. The Trustees considered the level and depth of Alger Management's ability to execute portfolio transactions to effect investment decisions, including those through Alger Inc. The Trustees also considered the ongoing enhancements to the control and compliance environment at Alger Management and within the Fund.

**Investment Performance of the Funds.** Drawing upon information provided at the meeting by Alger Management as well as FUSE and upon reports provided to the Trustees by Alger Management throughout the preceding year, the Trustees reviewed each Portfolio's returns for the year-to-date (at 6/30/10), second-quarter, and 1-, 3-, 5-, and 10-year periods to the extent available (and its year-by-year returns), together with supplemental data through 8/31/10, and compared them with benchmark and peer-group data for the same periods. They noted that for the year to date through 6/30/10 each of the Portfolios had underperformed both its benchmark and the median for its peers, except that the Large Cap Portfolio, Class I-2 of the Balanced Portfolio and the Small Cap Portfolio had surpassed their respective peer medians and the Small Cap Portfolio had also outperformed its benchmark. The performance of the Portfolios for the 1-, 3- and 5-year periods through 6/30/10 had been generally consistent with the shorter-term data, except that the Large Cap Portfolio had significantly outperformed both its benchmark and its peer median for the 1-year period, the Growth & Income Portfolio had surpassed both measures for the 3-year period, and the Capital Appreciation Portfolio had outperformed both measures for all three periods.

**Fund Fees and Expense Ratios; Profitability to Alger Management and its Affiliates.** The Trustees considered the profitability of the Investment Advisory Agreement to Alger Management and its affiliates, and the methodology used by Alger Management in determining such profitability. The Trustees reviewed previously-provided data on each Portfolio's profitability to Alger Management and its affiliates for the year ended June 30, 2010. In addition, the Trustees reviewed each Portfolio's management fee and expense ratio and compared them with a group of comparable funds. In order to assist the Trustees in this comparison, FUSE had provided the Trustees with comparative information with respect to fees paid, and expense ratios incurred, by similar funds. That information indicated that all of the fees and expense ratios were above the median for the applicable FUSE reference groups except that the fees of the Mid Cap and Growth & Income Portfolio, the expense ratio of Class I-2 of the Balanced Portfolio and the fee and expense ratios of the Small Cap Portfolio were below the applicable median. The Trustees determined that such information should be taken into account in weighing the size of the fee against the nature, extent and quality of the services provided. The Trustees also considered fees paid to Alger Management by other types of clients, specifically mutual funds for which Alger Management was sub-adviser and Alger Management's institutional clients. The Trustees determined that in both cases the fees were of doubtful relevance for purposes of comparison with those of the Portfolios because of the significant differences in services provided by Alger Management to those types of clients as opposed to the Portfolios, but that to the extent that meaningful comparison was practicable, the differences in services adequately explained the differences in the fees. After discussing with representatives of the Adviser and FUSE the methodologies used in computing the costs that formed the bases of the profitability calculations, the Trustees turned to the profitability data provided. After analysis and discussion, they concluded that, to the extent that Alger Management's and its affiliates' relationships with the Portfolios had been profitable to either or both of those entities in the case of one or more Portfolios, the profit margin in each case was not unacceptable.

**Economies of Scale.** On the basis of their discussions with management and their analysis of information provided at the meeting, the Trustees determined that the nature of the Portfolios and their operations is such that Alger Management is likely to realize economies of scale in the management of each Portfolio at some point as (and if) it grows in size, but that adoption of breakpoints in one or more of the advisory fees, while possibly appropriate at a later date, could await further analysis of the sources and potential scale of the economies and the fee structure that would best reflect them. Accordingly, the Trustees requested that Alger Management address this topic with the Trustees at future meetings.

**Other Benefits to Alger Management.** The Trustees considered whether Alger Management benefits in other ways from its relationship with the Fund. They noted that Alger Management maintains soft-dollar arrangements in connection with the equity Portfolios' brokerage transactions, reports on which are regularly supplied to the Trustees at their quarterly meetings and summaries of which, listing soft-dollar commissions by Portfolio for the twelve months through June 30, 2010, had been included in the materials supplied prior to the meeting. The Trustees also noted that Alger Management receives fees from the Portfolios under the Administration Agreement, that Alger, Inc. provides a substantial portion of the Portfolios' equity brokerage and that Alger Management also receives fees from the Fund under a shareholder services agreement. The Trustees had been provided with information regarding, and had considered, the administration fee, brokerage and shareholder services fee benefits in connection with their review of the profitability to Alger Management and its affiliates of their relationships with the Fund. As to other benefits received, the Trustees decided that none were so significant as to render Alger Management's fees excessive.

**Conclusions and Determinations.** At the conclusion of these discussions, each of the Independent Trustees expressed the opinion that he had been furnished with sufficient information to make an informed business decision with respect to renewal of the Investment Advisory Agreement. Based on its discussions and considerations as described above, the Board made the following conclusions and determinations:

- The Board concluded that the nature, extent and quality of the services provided to each Portfolio by Alger Management are adequate and appropriate.
- The performance of the Portfolios was acceptable to the Board.

- The Board concluded that each advisory fee paid to Alger Management was reasonable in light of comparative performance and expense and advisory fee information, costs of the services provided and profits to be realized and benefits derived or to be derived by Alger Management and its affiliates from the relationship with the Portfolio.
- The Board determined that there were not at this time significant economies of scale to be realized by Alger Management in managing the Portfolios' assets but that, to the extent that material economies of scale should be realized in the future, the Board would seek to ensure that they were shared with the applicable Portfolio.

The Board considered these conclusions and determinations and, without any one factor being dispositive, determined with respect to each Portfolio that renewal of the Investment Advisory Agreement was in the best interests of the Portfolio and its shareholders.

## Privacy Policy

**Your Privacy Is Our Priority**
At Fred Alger & Company, Incorporated ("Alger") we value the confidence you have placed in us. In trusting us with your assets, you provide us with personal and financial data. Alger is committed to maintaining the confidentiality of the personal nonpublic information ("personal information") entrusted to us by our customers. Your privacy is very important to us, and we are dedicated to safeguarding your personal information as we serve your financial needs.

**Our Privacy Policy**
We believe you should know about Alger's Privacy Policy and how we collect and protect your personal information. This Privacy Policy ("Policy") describes our practices and policy for collecting, sharing and protecting the personal information of our prospective, current and former customers. The Policy is applicable to Alger and its affiliate, Fred Alger Management, Inc., as well as the following funds: The Alger Funds, The Alger Institutional Funds, The Alger Portfolios, Alger China-U.S. Growth Fund and The Alger Funds II. We are proud of our Policy and hope you will take a moment to read about it.

**Information We Collect**
The type of personal information we collect and use varies depending on the Alger products or services you select.

We collect personal information that enables us to serve your financial needs, develop and offer new products and services, and fulfill legal and regulatory requirements. Depending on the products or services you request, we obtain personal information about you from the following sources:

- Information, such as your name, address and social security number, provided on applications and other forms we receive from you or your representative;

- Information from your communications with Alger employees or from your representative, which may be provided to us by telephone, in writing or through Internet transactions; and
- Information about your transactions, such as the purchase and redemption of fund shares, account balances and parties to the transactions, which we receive from our affiliates or other third parties.

**Sharing of Personal Information**

We may share your personal information with our affiliates so that they may process and service your transactions.

However, Alger never sells customer lists to any third party. Further, we do not disclose personal information to nonaffiliated third parties, except as required by law or as permitted by law to service your account, such as follows:

- To third-party service providers that assist us in servicing your accounts (e.g. securities clearinghouses);
- To governmental agencies and law enforcement officials (e.g. valid subpoenas, court orders); and
- To financial institutions that perform marketing services on our behalf or with whom we have joint marketing agreements that provide for the confidentiality of personal information.

**Our Security Practices**

We protect your personal information by maintaining physical, electronic and procedural safeguards. When you visit Alger's Internet sites your information is protected by our systems that utilize 128-bit data encryption, Secure Socket Layer (SSL) protocol, user names, passwords and other precautions. We have implemented safeguards to ensure that access to customer information is limited to employees, such as customer service representatives, who require such information to carry out their job responsibilities. Our employees are aware of their strict responsibility to respect the confidentiality of your personal information.

Thank you for choosing to invest with Alger. We value your relationship with us and assure you we will abide by our policy to protect your information.

## Proxy Voting Policies

A description of the policies and procedures the Fund uses to determine how to vote proxies relating to portfolio securities and the proxy voting record is available, without charge, by calling (800) 992-3863 or online on the Fund’s website at http://www.alger.com or on the SEC’s website at http://www.sec.gov

## Fund Holdings

The Portfolio’s most recent month end portfolio holdings are available approximately sixty days after month end on the Fund’s website at www.alger.com. The Portfolio also files its complete schedule of portfolio holdings with the SEC for the first and third quarter of each fiscal year on Form N-Q. Forms N-Q are available online on the SEC's website at www.sec.gov or may be reviewed and copied at the SEC's Public Reference Room in Washington, D.C. Information regarding the operation of the SEC's Public Reference Room may be obtained by calling 1-800-SEC-0330. A copy of the most recent quarterly holdings may also be obtained from the Fund by calling (800) 992-3863.

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## THE ALGER PORTFOLIOS

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New York, NY 10003
(800) 992-3862
www.alger.com

### Investment Advisor

Fred Alger Management, Inc.
111 Fifth Avenue
New York, NY 10003

### Distributor

Fred Alger & Company, Incorporated
111 Fifth Avenue
New York, NY 10003

### Transfer Agent and Dividend Disbursing Agent

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# The Alger Portfolios

## Alger Capital Appreciation Portfolio

**ANNUAL REPORT**

December 31, 2010

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## Dear Shareholders,

January 28, 2011

**Year in Review**

The end of 2010 was a fitting conclusion to both an exciting and troubling decade during which change in our country and across the globe was never more evident. I have no doubt that events during the 10-year period will provide much for commentary, study, and entertainment for years to come. It was a decade ushered in by the Internet generating much optimism, which quickly faded, and a time of surprising resilience of the American spirit in our recovery from September 11. Americans embarked on a sobering reassessment of values and fundamentals (of both the financial and principled kind) of the Baby Boomer generation and the American Dream, including its course since World War II. The past year was a fitting way to conclude the decade as volatility and uncertainty dominated investor sentiment. Many investors, as in the past several years, reacted fearfully and continued to retreat from U.S. equities as growing concerns over slowing economic growth, European sovereign debt issues, unresolved government policies, persistently high rates of unemployment, and other challenges dominated all of our thoughts. Investor sentiment over those issues was clearly illustrated by mutual fund asset flows in 2010. During the first 11 months of the year, investors withdrew $29.6 billion from equity funds, according to the Investment Company Institute ("ICI"). In a continuation of the recent past, assets from equity funds and new flows to funds resulted in bond portfolios capturing $266.4 billion in assets.

Such sentiments, while both rational and understandable, were in our view misplaced in 2010. For during the year, like many periods following that of great distress, there was great progress, including adaptation to new realities and, indeed, success in our U.S. economy. In many sectors, leading companies in 2010 achieved not only improvements, but actual record results topping those achieved in 2007's heady economy. While innovation and flexibility to adjust to new realities were key drivers to those kinds of results, the real key is motivation—the determination of employees and managers as well as clients to succeed and to move forward. Investors who focused on the fundamental success of companies, rather than the fear of uncertainty, and who used a disciplined strategy to seek equity opportunities were, broadly speaking, rewarded, as markets generated a 15.06% return as measured by the S&P 500 Index, easily exceeding the 6.54% return of the Barclays Capital U.S. Aggregate Bond Index.

In our opinion, our market outlook for 2010 was very good. For the early part of the year, we expected a consolidation and correction of 2009 gains amidst policy uncertainty on the multiple fronts of healthcare, energy, and reform of financial regulations and fiscal policy. Markets exhibited much volatility: At one point in early July of 2010, the S&P 500 was down 10% for the year to date. We reacted by reiterating in our summer of 2010 Market Commentary that the market would rally strongly on both continued strong corporate earnings and diminishing uncertainty around policy and politics. And so it was: Markets rallied from September 1 to year-end, with the S&P 500 gaining 20.64%, resulting in a year of well-above average performance (historically) and, certainly, achieving performance that was far above expectations of U.S. equity investors.

During the final months of 2010, concerns grew over various economic challenges, including the euro debt crisis, but the year nevertheless ended on an optimistic note. In November, euro-zone leaders rolled out a $113 billion bailout for Ireland, which will address the country's financing needs and help troubled banks. Yet, concerns over the stability of other European countries grew and Moody's Investors Services downgraded its ratings on Spanish government debt while Standard and Poor's lowered its ratings outlook for Belgium. Also troubling, only 39,000 jobs were created in the U.S. in November, considerably below the consensus forecast of 150,000. The unemployment rate, which is determined with a different survey methodology than job creation statistics, also disappointed, increasing 0.2 percentage points to 9.8% in November. On a positive note, strong retail spending helped boost investor optimism. For the three month period through November, year-over-year sales climbed 7.8%. For November, sales climbed 0.8% from October and reached the highest level since 2007. November also saw a 1.9% surge in utility output, while credit card delinquency rates declined. Moreover, the Commerce Department revised the third-quarter GDP growth rate upward twice, first to 2.5% from 2.0% and then to 2.6%. On the policy front, the biggest news was a second round of quantitative easing. Foreshadowed in Federal Reserve Chairman Ben Bernanke's Jackson Hole speech in late August, the central bank's action in early November of authorizing another $600 billion in purchases of fixed-income debt left no doubt among investors that the Fed will be resolute in its effort to stimulate the U.S. economy and to encourage investors to seek "risk assets" like equities, rather than continue to flood into low to "zero" yielding cash and bond investments.

**The Road Ahead**

We believe that strong corporate earnings, an improving outlook for the economy, and much improved sentiment among our holy trinity consisting of U.S. consumers, U.S. businesses, and U.S. investors will result in a good year for U.S. stocks. We think the S&P 500 should see 1500, or be up approximately 20% this year, on this combination of positive factors finally seen in a positive light. We are, however, not calling for the end of volatility and have concerns that the market may struggle to hold such gains, especially during the later portion of 2011. Risks that could derail our view include, especially, policy mistakes by either the U.S. or our global trading partners that result in either strict currency controls or trade restrictions, thus threatening what we at Alger continue to see as a multi-decade expansion of both global trade and, thus, global economic growth. Concerns over a weak real estate market and high rates of unemployment will also support volatility.

The recovery from the depths of the 2008 and 2009 financial crisis could not have happened without the underlying fundamental growth that comes from globalization. In the big picture, globalization is clearly a force that has improved the living standards of billions of people and has played a pivotal part in the recovery of our economy. Regarding the U.S., we believe the following items will support equity gains:

• Retail spending
• Hiring trends
• Corporate earnings from foreign markets
• Capital expenditures by cash rich corporations
• Dividend payments, stock buybacks, and mergers and acquisitions
• Demand for equities by retail investors

**Retail Spending**

With retail spending representing 70% of U.S. GDP, the weakened consumer is a considerable concern. However, in November and December, retail spending was surprisingly strong which, we believe, may indicate the start of a long trend of consumers finally loosening their purse strings. We note, as we have in the past, that publicly traded companies generally represent not the average retailer, but rather highly successful companies able to make some hay even when it's cloudy. Similarly, upper income U.S. consumers are clearly feeling better—luxury goods and bigger ticket consumer purchases (with the exception of real estate) have recovered faster than many expected. A variety of encouraging developments, including increasing family wealth from equity gains and an improving outlook for the job market, may explain this change. The U.S. consumer's balance sheet improved with strong equity gains occurring from July through September helping to offset the impact upon Americans' wealth of declining real estate values. The end result is that Americans' wealth increased 2.2% to approximately $54.9 trillion, according to the Federal Reserve. More importantly, Americans' outlook for the economy has improved, with the Conference Board's Consumer Confidence Index climbing 4.5 points to 54.1 in November, representing a five-month high.

**Reasons for Optimism on the Job Front**

The nation's 9.8% unemployment rate is clearly another concern. According to the Bureau of Labor Statistics (BLS), the number of non-farm jobs in America declined from 137.9 million in January of 2008 to 130.5 million in November of 2010, a 5.37% decline. Moreover, the Construction Sector as defined by the BLS lost 1.85 million jobs, or nearly one out of every four positions, during that timeframe, bringing the current total number of jobs to only 5.6 million. While employment contracted in most sectors during that period, the Goods Producing and Durable Goods sectors were also particularly problematic, losing roughly 17% of their jobs. While Construction job losses continued during 2010, the Goods Producing and Durable Goods sectors started to add jobs, as did most sectors, with private industry creating jobs in each month of the year. Nevertheless, job growth has been painfully slow. According to the BLS, less than a million jobs were created from December of 2009 to November of 2010, which is a very modest improvement when considering that more than seven million jobs were lost over the past three years. Many economists, meanwhile, don't expect hiring to gain steam this year, according to the Federal Reserve Bank of Philadelphia. It recently surveyed 43 economists who on average believe the economy this year will generate only 105,500 jobs per month. Yet, many companies appear to be hiring temporary workers as a stopgap measure while the economy strengthens. Indeed, temporary hiring has increased every month since August of 2009. The hiring trend, fortunately, appears ready to strengthen, with 45% of executives surveyed by the Business Roundtable in the fourth quarter of 2010 saying they expect their companies to hire workers over the next six months. That was the strongest reading since the start of the research in the fourth quarter of 2002. Moreover, the reduction of the Social Security withholding rate by two percentage points to 4.2% for 2011 may double the rate of job creation to 2.6 million this year, lowering the unemployment rate to below 9%, according to estimates by Moody's Analytics.

**Growth from Foreign Markets**
U.S. companies' fast-growing foreign operations have helped S&P 500 constituents increase profits every quarter since September of 2009, a trend which we expect to continue this year. According to S&P 500 estimates, operating earnings per share should reach $25.16 by the fourth quarter of 2011, up from $21.74 in the last quarter of 2010. Regarding non-U.S. revenues, as of April 30 of last year, 38.80% of S&P 500 corporate sales were in foreign markets, a figure which increased slightly to 39.65% as of mid-December. U.S. corporations' access to foreign markets is significant as international growth is expected to outpace that of the U.S. with the International Monetary Fund (IMF) estimating that world GDP will grow 4.3% in 2011, dwarfing the 2.9% GDP growth forecast for America. Perhaps more impressive are expectations that GDP for certain countries, such as Brazil, China, and India, will grow at rates that exceed the global forecasts. Clearly, the U.S. stock market is not just a reflection of the U.S. economy. It is, instead, a gauge of the international marketplace and the success of U.S. companies in it.

**Capital Expenditures**
At the same time, corporate coffers are rich with cash, and businesses have pent up demand for new equipment, such as personal computers, data storage systems, and information networks, after having cut spending during "The Great Recession." At the end of the third quarter, corporations held $1.93 trillion in cash, up from $1.8 trillion at the end of June, according to the Federal Reserve. Corporations now appear to be addressing the demand and we are encouraged to see an increase in corporate spending on technology, which we believe will help further stimulate the economy. On a broader scale, capital expenditures by S&P 500 companies in 2010 increased moderately from $2.99 billion in the first quarter to $3.07 billion in the fourth quarter. We believe this trend will strengthen as 59% of executives surveyed by the Business Roundtable said they expect their companies to increase capital expenditures over the next six months.

**Dividends, Stock Buybacks, and Merger and Acquisitions**
In 2010, nearly 48% of S&P 500 companies either started dividend payments or increased their dividends, according to data from FactSet. The additional income flowing to shareholders will help to stimulate the economy, but perhaps more important, it will help make equities more appealing, especially when considering that the yield on a 10-year bond at the end of 2010 was only 3.30%. In comparison, a typical stock dividend yield is 2% and corporate earnings or free cash flow yields are as high as 8%, 9%, or 10%. The volume of stock buybacks has also increased significantly, helping to support equity valuations while signaling that corporate executives have strong conviction regarding the values of their companies. Stock

buybacks totaling more than $368 billion were announced in 2010, up from $125 billion in 2009, according to equity research firm Birinyi Associates, Inc. Acquisitions and mergers are also gaining steam. In 2010, the total market cap of M&A activity by U.S. companies climbed to $738 billion, which is substantially below the $1.09 trillion in deals completed in 2008, according to Bloomberg. Nevertheless, deal volume last year exceeded the $718 billion of deals completed in 2009. We maintain that increasing levels of M&A activity illustrate that corporate executives believe that acquisition targets are either trading at attractive valuations or are desirable from a strategic point of view.

**Investor Psychology**

Investors' strong preference for bond funds has pushed yields on fixed-income securities to historically low levels. We maintain that even a modest increase in interest rates will create substantial losses in bond funds, which may drive investors to sell fixed-income assets in favor of equities. The process may already have started. Toward the end of 2010, expectations that the economy is strengthening combined with the weakening financial health of municipalities and states sparked a decline in bond values, including those issued by corporations. Impressively, Wal-Mart Stores, Inc. 30-year bonds issued in the fourth quarter of 2010 with a historically low 5% yield dropped 5% in value, underscoring that fixed-income securities entail risk. In comparison, equity markets completed 2010 by recording their second year of solid gains, making stock investments appear attractive. If investors react to fixed-income losses by reallocating assets to equities, the impact on stock valuations could be significant as Americans have approximately $3 trillion invested in fixed-income mutual funds, according to the ICI. Bond investors may have already started to do so, pulling $7.4 billion in assets from fixed-income funds during the one-month period ended December 8. Even though the redemptions are modest, they represent the first period of bond outflows since 2008 and could represent the start of ongoing redemptions from fixed-income funds. One of the big surprises for 2011 could be the re-engagement of investors with U.S. equities, an event that we believe would be quite a fitting reversal of the past decade in which foreign and emerging markets, real estate, commodities and (finally) bonds and cash were favorites at the expense, in particular, of U.S. growth stocks.

**Challenges for 2011**

Going forward, fears over a potential worsening of the euro debt crisis will linger, but we believe that the European Financial Stability Facility, which was created in response to the problem, and the IMF will respond diligently if the situation worsens. Domestically, we are concerned that real estate could be a bigger "continuing" problem than perhaps expected. The data suggest that real estate values won't recover any time soon with 9.5 months of inventory available as of November compared to six to seven months of inventory that was typically available prior to "The Great Recession," according to the National Association of Realtors (NAR). Moreover, the S&P/Case-Shiller Home Price Index recorded a 0.8% year-over year decline in October of 2010, the biggest drop since the year-over-year decline recorded in December of 2009. Real estate sales also disappointed. In 2010, 4.85 million homes were expected to have been sold, according to NAR projections. In comparison, the highest number of homes sold during the past 10 years was 7.08 million in 2005.

However, we believe that the large amount of inventory and anemic sales have for the most part been "priced in" by the market. In other words, if the U.S. real estate market remains as it is, figuratively "bumping along the bottom" (without improvement), we believe that will be OK for the stock markets. However, if there is another large price decline, that will change our equities outlook for the 2011-2012 timeframe. Over the longer term, as measured by years, however, the real estate market certainly will improve. Construction of new homes has dropped considerably, limiting the supply of new homes. At present rates, new construction is below the U.S. natural rate of demand driven by household formation, population growth, and the economy. Affordability of homes stands at very attractive levels, so the issue turns on loan availability, employment, and, of course, confidence of the home buyer.

As always, we remain committed to our highly-disciplined and research-driven investment strategy of seeking growth companies with the right strategies, management, business models, and products to succeed in any economy. Similarly, we continue to believe that research is the cornerstone of superior portfolio management, regardless of economic conditions. We believe our proven and disciplined process for identifying companies experiencing Positive Dynamic Change will continue to produce superior long-term investment results for our clients.

**Portfolio Matters**

The Alger Capital Appreciation Portfolio returned 14.03% for the one-year period ended December 31, 2010, compared to the 17.64% return of its benchmark, the Russell 3000 Growth Index.

During the period, the largest sector weightings in the Alger Capital Appreciation Portfolio were in the Information Technology and Health Care sectors. The largest sector overweight for the period was in Information Technology and the largest sector underweight for the period was in Consumer Staples. Relative outperformance in the Materials and Energy sectors was the most important contributor to performance, while sectors that detracted from performance included Consumer Discretionary and Health Care.

Among the most important contributors to relative performance were Skyworks Solutions Inc., Cliffs Natural Resources Inc., Peabody Energy Corp., Apple Inc., and IAC/InterActiveCorp. Conversely, detracting from relative performance were Hewlett-Packard Co., Marvell Technology Group Ltd., Baxter International Inc., Expedia Inc., and International Business Machines Corp.

Respectfully submitted,

Daniel C. Chung, CFA
Chief Investment Officer

Investors cannot invest directly in an index. Index performance does not reflect the deduction for fees, expenses, or taxes.

This report and the financial statements contained herein are submitted for the general information of shareholders of The Alger Portfolios. This report is not authorized for distribution to prospective investors in The Alger Portfolios unless proceeded or accompanied by an effective prospectus. Individual Portfolio returns represent the fiscal 12-month period return of Class I-2 shares. Returns include reinvestment of dividends and distributions.

**The performance information quoted in this material represents past performance, which is not an indication or a guarantee of future results.**

Standard performance results can be found on the following pages. The investment return and principal value of an investment in a fund will fluctuate so that an investor's shares, when redeemed, may be worth more or less than their original cost. Current performance may be lower or higher than the performance quoted. For performance data current to the most recent month-end, visit us at www.alger.com, or call us at (800) 992-3863.

The views and opinions of the Portfolio's management in this report are as of the date of the shareholders letter and are subject to change at any time subsequent to this date. There is no guarantee that any of the assumptions that formed the basis for the opinions stated herein are accurate or that they will materialize. Moreover, the information forming the basis for such assumptions is from sources believed to be reliable; however, there is no guarantee that such information is accurate. Any securities mentioned, whether owned in a Portfolio or otherwise, are considered in the context of the construction of an overall portfolio of securities and therefore reference to them should not be construed as a recommendation or offer to purchase or sell any such security. Inclusion of such securities in a fund and transactions in such securities, if any, may be for a variety of reasons, including without limitation, in response to cash flows, inclusion in a benchmark, and risk control. The reference to a specific security should also be understood in such context and not viewed as a statement that the security is a significant holding in a Portfolio. Please refer to the Schedule of Investments for each Portfolio which is included in this report for a complete list of Portfolio holdings as of December 31, 2010. Securities mentioned in the shareholders letter, if not found in the Schedule of Investments, may have been held by the Portfolios during the 12-month fiscal period.

**A Word about Risk**

Growth stocks tend to be more volatile than other stocks as the price of growth stocks tends to be higher in relation to their companies' earnings and may be more sensitive to market, political and economic developments. Investing in the stock market involves gains and losses and may not be suitable for all investors. Stocks of small- and mid-sized companies are subject to greater risk than stocks of larger, more established companies owing to such factors as limited liquidity, inexperienced management, and limited financial resources. Portfolios that invest in fixed-income securities, such as the Alger Balanced Portfolio, are subject to the fixed-income securities' sensitivity to interest rate movements; their market values tend to fall when interest rates rise and to rise when interest rates fall. They are also subject to the risk of a decline in the value of the Portfolio's securities in the event of an issue's falling credit rating or actual default. The Portfolios that invest in mortgage and asset-backed securities are subject to prepayment risk; thus the average life of the security may be less than maturity. Portfolios that participate in leveraging, such as the Alger Capital Appreciation Portfolio and the Alger SMid Cap Growth Portfolio, are subject to the risk that the cost of borrowing money to leverage will exceed the returns for securities purchased or that the securities purchased may actually go down in value; thus, the Portfolio's net asset value can decrease more quickly than if the Portfolio had not borrowed. For a more detailed discussion of the risks associated with a Portfolio, please see the Portfolio's Prospectus.

Before investing, carefully consider a Portfolio's investment objective, risks, charges, and expenses. For a prospectus or a summary prospectus containing this and other information about the Alger Funds call us at (800) 992-3863 or visit us at www.alger.com. Read it carefully before investing.

**Fred Alger & Company, Incorporated, Distributor. Member NYSE Euronext, SIPC.**

**NOT FDIC INSURED. NOT BANK GUARANTEED. MAY LOSE VALUE.**

Definitions:

- Standard & Poor's 500 Index (S&P 500 Index) is an index of 500 leading companies in leading industries in the United States.

- The Russell 3000 Index measures the performance of the 3,000 largest U.S. companies based on the total market capitalization, which represents 99% of the U.S. equity market. The Russell 3000 Growth Index is an unmanaged index designed to measure the performance of those Russell 3000 Index companies with higher price-to-book ratios and higher forecasted growth values.

- The Russell 1000 Index measures the performance of the large-cap segment of the U.S. equity universe. It is a subset of the Russell 3000 Index and includes approximately 1,000 of the largest securities based on a combination of their market cap and current index membership. The Russell 1000 represents approximately 92% of the Russell 3000 Index. The Russell 1000 Growth Index is an unmanaged index designed to measure the performance of the largest 1,000 companies in the Russell 3000 Index with higher price-to-book ratios and higher forecasted growth values.

- The Russell Midcap Growth Index measures the performance of the mid-cap growth segment of the U.S. equity universe. It includes those Russell Midcap

Index companies with higher price-to-book ratios and higher forecasted growth values.

- The Russell 2500 Index measures the performance of the small to mid-cap segment of the U.S. equity universe, commonly referred to as "SMid" cap. The Russell 2500 Index is a subset of the Russell 3000 Index. The Russell 2500 Growth Index measures the performance of the small to mid-cap growth segment of the U.S. equity universe. It includes those Russell 2500 companies with higher price-to-book ratios and higher forecasted growth values.

- The Russell 2000 Index measures the performance of the small-cap segment of the U.S. equity universe. The Russell 2000 Index is a subset of the Russell 3000 Index representing approximately 8% of the total market capitalization of that index. The Russell 2000 Growth Index measures the performance of the small cap growth segment of the U.S. equity universe. It includes those Russell 2000 companies with higher price-to-book ratios and higher forecasted growth values.

- The Barclays Capital U.S. Government/Credit Bond Index tracks the performance of government and corporate bonds.

- The Investment Company Institute (ICI) is a national association of U.S. investment companies.

- Moody's Investors Service and Standard & Poor's are credit rating agencies.

- The Business Roundtable is an organization of chief executive officers of leading companies.

- FactSet is a firm that provides market data and analytics to investment firms.

- Birinyi Associates, Inc. is a stock market research firm.

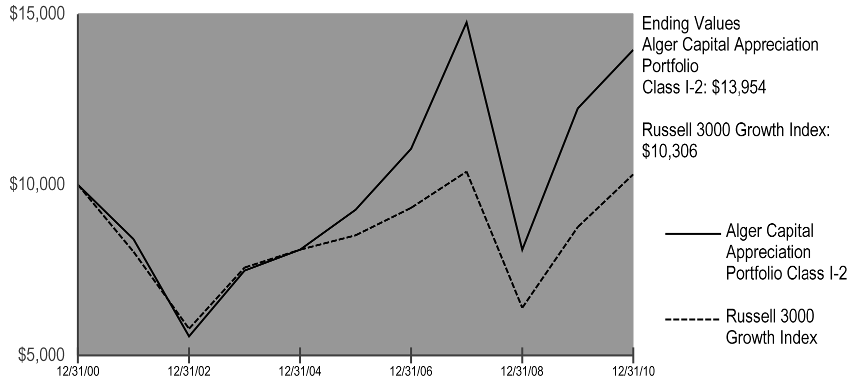
- Bloomberg is a financial publisher and provider of financial data.

- The National Association of Realtors is a trade organization representing members involved in the residential and commercial real estate industries.

- As of December 31, 2010, Wal-Mart Stores Inc. represented 0.43% of firm-wide assets under management.

HYPOTHETICAL $10,000 INVESTMENT IN CLASS I-2 SHARES

*— 10 years ended 12/31/10*




The chart above illustrates the change in value of a hypothetical $10,000 investment made in Alger Capital Appreciation Portfolio Class I-2 shares, the Russell 3000 Growth Index and the Russell 1000 Growth Index (unmanaged indexes of common stocks) for the ten years ended December 31, 2010. Figures for the Alger Capital Appreciation Portfolio Class I-2, shares the Russell 3000 Growth Index and the Russell 1000 Growth Index include reinvestment of dividends. Performance for Alger Capital Appreciation Portfolio Class S shares will be lower from the results shown above due to differences in expenses that class bears.

## PERFORMANCE COMPARISON AS OF 12/31/10

**AVERAGE ANNUAL TOTAL RETURNS**

| | 1 YEAR | 5 YEARS | 10 YEARS | SINCE INCEPTION |
|---|---|---|---|---|
| **Class I-2 (Inception 1/25/95)** | 14.03% | 8.53% | 3.39% | 12.88% |
| **Class S (Inception 5/1/02)**(i) | 13.63% | 8.23% | 3.17% | 12.62% |
| Russell 3000 Growth Index | 17.64% | 3.88% | 0.30% | 7.24% |
| Russell 1000 Growth Index | 16.71% | 3.75% | 0.02% | 7.43% |

*The performance data quoted represents past performance, which is not an indication or a guarantee of future results. Investment return and principal will fluctuate and the Portfolio's shares, when redeemed, may be worth more or less than their original cost. Current performance may be higher or lower than the performance quoted. For performance current to the most recent month end, visit us at www.alger.com or call us at (800) 992-3863.*

*Returns indicated assume reinvestment of all distributions, no transaction costs or taxes, and are net of management fees and fund operating expenses only. Total return does not include deductions at the portfolio or contract level for cost of insurance charges, premium load, administrative charges, mortality and expense risk charges or other charges that may be incurred under the variable annuity contract, variable life insurance plan or retirement plan for which the Portfolio serves as an underlying investment vehicle. If these charges were deducted, the total return figures would be lower. Please refer to the variable insurance product or retirement plan disclosure documents for any additional applicable expenses. Investing in the stock market involves gains and losses and may not be suitable for all investors.*

(i) *Since inception returns are calculated from Class I-2 inception date. Class S shares returns prior to their commencement of operations are that of Class I-2 shares adjusted to reflect the higher expenses of class S shares.*

**Portfolio Summary†**

**June 30, 2010** *(Unaudited)*

| SECTORS | |
|---|---|
| Consumer Discretionary | 15.2% |
| Consumer Staples | 3.8 |
| Energy | 11.4 |
| Financials | 5.3 |
| Health Care | 8.3 |
| Industrials | 14.8 |
| Information Technology | 33.5 |
| Materials | 4.6 |
| Short-Term and Net Other Assets | 3.1 |
| | **100.0%** |

† *Based on net assets for the Portfolio*.

| COMMON STOCKS—96.9% | SHARES | VALUE |
|---|---|---|
| **ADVERTISING—1.6%** | | |
| Focus Media Holding Ltd.#* | 222,100 | **$ 4,870,653** |
| **AEROSPACE & DEFENSE—1.1%** | | |
| Goodrich Corp. | 18,800 | 1,655,716 |
| United Technologies Corp. | 21,900 | 1,723,968 |
| | | **3,379,684** |
| **AIR FREIGHT & LOGISTICS—3.2%** | | |
| FedEx Corp. | 32,400 | 3,013,524 |
| United Parcel Service Inc., Cl. B | 84,100 | 6,103,978 |
| | | **9,117,502** |
| **AIRLINES—0.5%** | | |
| United Continental Holdings Inc.* | 66,900 | **1,593,558** |
| **APPLICATION SOFTWARE—1.4%** | | |
| Adobe Systems Inc. * | 53,900 | 1,659,042 |
| Informatica Corp. * | 16,900 | 744,107 |
| Mentor Graphics Corp. * | 24,000 | 288,000 |
| Nice Systems Ltd. #* | 42,800 | 1,493,720 |
| | | **4,184,869** |
| **ASSET MANAGEMENT & CUSTODY BANKS—1.9%** | | |
| BlackRock Inc. | 29,200 | **5,564,936** |
| **AUTO PARTS & EQUIPMENT—0.9%** | | |
| Lear Corp.* | 26,400 | **2,605,944** |
| **AUTOMOBILE MANUFACTURERS—1.7%** | | |
| Bayerische Motoren Werke AG # | 95,000 | 2,478,550 |
| Daimler AG * | 36,100 | 2,439,638 |
| | | **4,918,188** |
| **BIOTECHNOLOGY—1.1%** | | |
| Cephalon Inc. * | 23,700 | 1,462,764 |
| Human Genome Sciences Inc. * | 71,300 | 1,703,357 |
| | | **3,166,121** |
| **CASINOS & GAMING—0.6%** | | |
| Las Vegas Sands Corp.* | 37,400 | **1,718,530** |
| **COAL & CONSUMABLE FUELS—1.9%** | | |
| Peabody Energy Corp. | 87,300 | **5,585,454** |
| **COMMODITY CHEMICALS—0.6%** | | |
| Celanese Corp. | 42,000 | **1,729,140** |
| **COMMUNICATIONS EQUIPMENT—2.5%** | | |
| Cisco Systems Inc. * | 113,500 | 2,296,105 |
| Qualcomm Inc. | 101,600 | 5,028,184 |
| | | **7,324,289** |
| **COMPUTER HARDWARE—9.5%** | | |
| Apple Inc. * | 47,500 | 15,321,600 |
| Hewlett-Packard Co. | 306,100 | 12,886,810 |
| | | **28,208,410** |

| COMMON STOCKS—(CONT.) | SHARES | VALUE |
|---|---|---|
| **COMPUTER STORAGE & PERIPHERALS—1.6%** | | |
| EMC Corp.* | 203,800 | **$ 4,667,020** |
| **CONSTRUCTION & FARM MACHINERY & HEAVY TRUCKS—2.6%** | | |
| ArvinMeritor Inc. * | 99,500 | 2,041,740 |
| Caterpillar Inc. | 32,200 | 3,015,852 |
| Cummins Inc. | 24,700 | 2,717,247 |
| | | **7,774,839** |
| **DATA PROCESSING & OUTSOURCED SERVICES—0.8%** | | |
| Mastercard Inc. | 10,600 | **2,375,566** |
| **DEPARTMENT STORES—0.8%** | | |
| Kohl's Corp.* | 46,100 | **2,505,074** |
| **DIVERSIFIED METALS & MINING—2.0%** | | |
| Cliffs Natural Resources Inc. | 40,800 | 3,182,808 |
| Freeport-McMoRan Copper & Gold Inc. | 22,300 | 2,678,007 |
| | | **5,860,815** |
| **DRUG RETAIL—0.5%** | | |
| CVS Caremark Corp. | 43,500 | **1,512,495** |
| **ENVIRONMENTAL & FACILITIES SERVICES—0.5%** | | |
| Republic Services Inc. | 49,620 | **1,481,653** |
| **FERTILIZERS & AGRICULTURAL CHEMICALS—0.7%** | | |
| Mosaic Co., /The | 27,900 | **2,130,444** |
| **GOLD—0.4%** | | |
| Yamana Gold Inc. | 94,800 | **1,213,440** |
| **HEALTH CARE EQUIPMENT—1.5%** | | |
| Covidien PLC | 76,200 | 3,479,292 |
| Insulet Corp. * | 62,700 | 971,850 |
| | | **4,451,142** |
| **HEALTH CARE FACILITIES—0.8%** | | |
| Universal Health Services Inc., Cl. B | 54,200 | **2,353,364** |
| **HEALTH CARE SERVICES—1.3%** | | |
| Medco Health Solutions Inc.* | 64,700 | **3,964,169** |
| **HOME ENTERTAINMENT SOFTWARE—0.5%** | | |
| Activision Blizzard Inc. | 121,100 | **1,506,484** |
| **HOME IMPROVEMENT RETAIL—1.4%** | | |
| Lowe's Companies, Inc. | 170,500 | **4,276,140** |
| **HOTELS RESORTS & CRUISE LINES—1.9%** | | |
| Carnival Corp. | 47,300 | 2,181,003 |
| Wyndham Worldwide Corporation | 111,500 | 3,340,540 |
| | | **5,521,543** |
| **HOUSEHOLD APPLIANCES—0.5%** | | |
| Stanley Black & Decker Inc. | 22,100 | **1,477,827** |
| **HUMAN RESOURCE & EMPLOYMENT SERVICES—0.4%** | | |
| Towers Watson & Co. | 21,700 | **1,129,702** |
| **HYPERMARKETS & SUPER CENTERS—0.9%** | | |
| Wal-Mart Stores Inc. | 50,400 | **2,718,072** |

| COMMON STOCKS—(CONT.) | SHARES | VALUE |
|---|---|---|
| **INDUSTRIAL CONGLOMERATES—1.6%** | | |
| 3M Co. | 27,300 | $ 2,355,990 |
| Tyco International Ltd. | 56,700 | 2,349,648 |
| | | **4,705,638** |
| **INDUSTRIAL MACHINERY—2.4%** | | |
| Illinois Tool Works Inc. | 51,300 | 2,739,420 |
| Ingersoll-Rand PLC | 94,300 | 4,440,587 |
| | | **7,180,007** |
| **INTEGRATED OIL & GAS—2.8%** | | |
| Chevron Corp. | 39,200 | 3,577,000 |
| ConocoPhillips | 71,000 | 4,835,100 |
| | | **8,412,100** |
| **INTERNET RETAIL—2.7%** | | |
| Amazon.com Inc. * | 27,370 | 4,926,600 |
| Expedia Inc. | 123,700 | 3,103,633 |
| | | **8,030,233** |
| **INTERNET SOFTWARE & SERVICES—8.4%** | | |
| Baidu Inc. #* | 15,800 | 1,525,174 |
| eBay Inc. * | 59,500 | 1,655,885 |
| Google Inc., Cl. A * | 18,700 | 11,107,239 |
| GSI Commerce Inc. * | 161,400 | 3,744,480 |
| IAC/InterActiveCorp. * | 25,500 | 731,850 |
| Sina Corp. * | 25,900 | 1,782,438 |
| VistaPrint Ltd. * | 44,700 | 2,056,200 |
| Yahoo! Inc. * | 144,000 | 2,394,720 |
| | | **24,997,986** |
| **INVESTMENT BANKING & BROKERAGE—0.5%** | | |
| Lazard Ltd., Cl. A | 37,820 | **1,493,512** |
| **IT CONSULTING & OTHER SERVICES—0.6%** | | |
| International Business Machines Corp. | 11,600 | **1,702,416** |
| **LEISURE PRODUCTS—1.3%** | | |
| Phillips-Van Heusen Corp. | 62,300 | **3,925,523** |
| **LIFE & HEALTH INSURANCE—0.8%** | | |
| MetLife Inc. | 56,000 | **2,488,640** |
| **LIFE SCIENCES TOOLS & SERVICES—1.0%** | | |
| Thermo Fisher Scientific Inc.* | 52,300 | **2,895,328** |
| **MANAGED HEALTH CARE—0.8%** | | |
| Aetna Inc. | 77,600 | **2,367,576** |
| **MOVIES & ENTERTAINMENT—0.8%** | | |
| Walt Disney Co., /The | 64,900 | **2,434,399** |
| **OIL & GAS DRILLING—0.5%** | | |
| Nabors Industries Ltd.* | 65,200 | **1,529,592** |
| **OIL & GAS EQUIPMENT & SERVICES—2.2%** | | |
| Halliburton Company | 48,900 | 1,996,587 |
| National Oilwell Varco Inc. | 42,400 | 2,851,400 |

| COMMON STOCKS—(CONT.) | SHARES | VALUE |
|---|---|---|
| **OIL & GAS EQUIPMENT & SERVICES—(CONT.)** | | |
| Schlumberger Ltd. | 20,800 | $ 1,736,800 |
| | | **6,584,787** |
| **OIL & GAS EXPLORATION & PRODUCTION—3.1%** | | |
| Devon Energy Corp. | 41,000 | 3,218,910 |
| Nexen Inc. | 161,000 | 3,686,900 |
| Plains Exploration & Production Co. * | 64,600 | 2,076,244 |
| | | **8,982,054** |
| **OIL, GAS & CONSUMABLE FUELS—0.9%** | | |
| Williams Cos., Inc., /The | 106,500 | **2,632,680** |
| **OTHER DIVERSIFIED FINANCIAL SERVICES—1.6%** | | |
| BM&F Bovespa SA | 251,800 | 1,992,187 |
| JPMorgan Chase & Co. | 65,100 | 2,761,542 |
| | | **4,753,729** |
| **PHARMACEUTICALS—1.8%** | | |
| Abbott Laboratories | 24,700 | 1,183,377 |
| Allergan Inc. | 23,600 | 1,620,612 |
| Auxilium Pharmaceuticals Inc. * | 18,100 | 381,910 |
| Pfizer Inc. | 126,900 | 2,222,019 |
| | | **5,407,918** |
| **PRECIOUS METALS & MINERALS—0.9%** | | |
| Stillwater Mining Co.* | 128,800 | **2,749,880** |
| **RAILROADS—1.3%** | | |
| CSX Corp. | 61,500 | **3,973,515** |
| **RESEARCH & CONSULTING SERVICES—0.2%** | | |
| Verisk Analytic Inc., Cl. A* | 19,100 | **650,928** |
| **RESTAURANTS—1.0%** | | |
| McDonald's Corp. | 38,800 | **2,978,288** |
| **SEMICONDUCTOR EQUIPMENT—0.8%** | | |
| Lam Research Corp.* | 45,500 | **2,355,990** |
| **SEMICONDUCTORS—4.7%** | | |
| Avago Technologies Ltd. | 88,700 | 2,525,289 |
| Broadcom Corp., Cl. A | 37,700 | 1,641,835 |
| Marvell Technology Group Ltd. * | 145,900 | 2,706,445 |
| ON Semiconductor Corp. * | 118,700 | 1,172,756 |
| Skyworks Solutions Inc. * | 103,900 | 2,974,657 |
| Texas Instruments Inc. | 90,000 | 2,925,000 |
| | | **13,945,982** |
| **SOFT DRINKS—1.6%** | | |
| PepsiCo Inc. | 73,600 | **4,808,288** |
| **SPECIALIZED FINANCE—0.5%** | | |
| CME Group Inc. | 4,700 | **1,512,225** |
| **SYSTEMS SOFTWARE—2.7%** | | |
| Oracle Corp. | 255,700 | **8,003,410** |
| **TOBACCO—0.8%** | | |
| Philip Morris International Inc. | 38,100 | **2,229,993** |

| COMMON STOCKS—(CONT.) | SHARES | VALUE |
|---|---|---|
| **TRUCKING—1.0%** | | |
| Hertz Global Holdings Inc.* | 208,000 | **$ 3,013,920** |
| **TOTAL COMMON STOCKS** | | |
| (Cost $261,820,943) | | **287,633,604** |

| | | |
|---|---|---|
| Total Investments | | |
| (Cost $261,820,943)[(a)] | 96.9% | 287,633,604 |
| Other Assets in Excess of Liabilities | 3.1 | 9,351,300 |
| **NET ASSETS** | 100.0% | **$ 296,984,904** |

‡ *Securities classified as Level 1 for ASC 820 disclosure purposes based on valuation inputs unless otherwise noted. See Notes 2 and 8 to the Financial Statements.*

* *Non-income producing security.*
\# *American Depository Receipts.*
(a) *At December 31, 2010, the net unrealized appreciation on investments, based on cost for federal income tax purposes of $263,166,606 amounted to $24,466,998 which consisted of aggregate gross unrealized appreciation of $32,266,571 and aggregate gross unrealized depreciation of $7,799,573.*

***Industry classifications are unaudited.***
***See Notes to Financial Statements.***

**Statement of Assets and Liabilities December 31, 2010**

| | | |
|---|---|---|
| ASSETS: | | |
| Investments in securities, at value (Identified cost)* see accompanying schedule of investments | $ | 287,633,604 |
| Cash and cash equivalents | | 2,518,479 |
| Receivable for investment securities sold | | 9,365,658 |
| Receivable for shares of beneficial interest sold | | 508,004 |
| Dividends and interest receivable | | 151,587 |
| Prepaid expenses | | 40,465 |
| Total Assets | | 300,217,797 |
| LIABILITIES: | | |
| Payable for investment securities purchased | | 2,582,067 |
| Payable for shares of beneficial interest redeemed | | 355,804 |
| Accrued investment advisory fees | | 193,934 |
| Accrued transfer agent fees | | 6,406 |
| Accrued distribution fees | | 2,695 |
| Accrued administrative fees | | 6,882 |
| Accrued shareholder servicing fees | | 2,502 |
| Accrued other expenses | | 82,603 |
| Total Liabilities | | 3,232,893 |
| **NET ASSETS** | **$** | **296,984,904** |
| **Net Assets Consist of:** | | |
| Paid in capital | | 323,729,483 |
| Undistributed net investment income | | 267,733 |
| Accumulated net realized loss | | (52,825,026) |
| Net unrealized appreciation on investments | | 25,812,714 |
| **NET ASSETS** | **$** | **296,984,904** |
| **Net Asset Value Per Share** | | |
| Class I-2 | | $52.16 |
| Class S | | $51.04 |
| **Net Assets By Class** | | |
| Class I-2 | | 284,224,567 |
| Class S | | 12,760,337 |
| **Shares of Benefical Interest Outstanding— Note 6 (Par Value $.001)** | | |
| Class I-2 | | 5,449,512 |
| Class S | | 250,021 |
| *Identified Cost | $ | 261,820,943 |

***See Notes to Financial Statements.***

**Statement of Operations**

*For the year ended December 31, 2010*

| | | |
|---|---|---|
| INCOME: | | |
| Dividends (net of foreign withholding taxes*) | $ | 2,982,586 |
| Interest | | 3,184 |
| Other | | 304 |
| Total Income | | 2,986,074 |
| EXPENSES | | |
| Advisory fees—Note 3 | | 2,169,099 |
| Distribution fees Class S—Note 3 | | 31,571 |
| Administrative fees—Note 3 | | 73,642 |
| Custodian fees | | 69,258 |
| Interest expenses | | 15 |
| Transfer agent fees and expenses—Note 3 | | 43,525 |
| Printing fees | | 98,800 |
| Professional fees | | 49,689 |
| Registration fees | | 63,053 |
| Trustee fees—Note 3 | | 18,790 |
| Miscellaneous | | 51,789 |
| Total Expenses | | 2,669,231 |
| Less, expense reimbursements/waivers—Note 3 | | (93,725) |
| Net Expenses | | 2,575,506 |
| NET INVESTMENT INCOME | | 410,568 |
| REALIZED AND UNREALIZED GAIN (LOSS) ON INVESTMENTS, OPTIONS AND FOREIGN CURRENCY TRANSACTIONS: | | |
| Net realized gain on investments and purchased options | | 28,578,159 |
| Net realized loss on foreign currency transactions | | (126,979) |
| Net change in unrealized appreciation (depreciation) on investments and foreign currency | | 6,552,324 |
| Net realized and unrealized gain on investments, options and foreign currency | | 35,003,504 |
| **NET INCREASE IN NET ASSETS RESULTING FROM OPERATIONS** | **$** | **35,414,072** |
| *Foreign withholding taxes | $ | 11,302 |

***See Notes to Financial Statements.***

| | For the Year Ended December 31, 2010 | For the Year Ended December 31, 2009 |
|---|---|---|
| Net investment income | $ 410,568 | $ 1,031,396 |
| Net realized gain on investments, options and foreign currency transactions | 28,451,180 | 32,650,515 |
| Net change in unrealized appreciation on investments, options and foreign currency | 6,552,324 | 55,526,468 |
| Net increase in net assets resulting from operations | 35,414,072 | 89,208,379 |
| Dividends and distributions to shareholders from: | | |
| Net investment income | | |
| Class I-2 | (1,008,170) | — |
| Class S | (27,573) | — |
| Net realized gains | | |
| Class I-2 | — | — |
| Class S | — | — |
| Total dividends and distributions to shareholders | (1,035,743) | — |
| Increase (decrease) from shares of beneficial interest transactions: | | |
| Class I-2 | 1,833,933 | (18,822,263) |
| Class S | (2,017,960) | (299,187) |
| Net decrease from shares of beneficial interest transactions—Note 6 | (184,027) | (19,121,450) |
| Total increase | 34,194,302 | 70,086,929 |
| Net Assets: | | |
| Beginning of period | 262,790,602 | 192,703,673 |
| **END OF PERIOD** | **$ 296,984,904** | **$ 262,790,602** |
| Undistributed net investment income | $ 267,733 | $ 1,047,161 |

*See Notes to Financial Statements.*

Alger Capital Appreciation Portfolio

| | Class I-2 | | | | |
|---|---|---|---|---|---|
| | Year ended 12/31/2010 | Year ended 12/31/2009 | Year ended 12/31/2008 | Year ended 12/31/2007 | Year ended 12/31/2006 |
| Net asset value, beginning of period | $ 45.92 | $ 30.39 | $ 55.39 | $ 41.48 | $ 34.78 |
| INCOME FROM INVESTMENT OPERATIONS: | | | | | |
| Net investment income (loss)(i) | 0.08 | 0.18 | 0.05 | (0.07) | (0.07) |
| Net realized and unrealized gain (loss) on investments | 6.34 | 15.35 | (25.05) | 13.98 | 6.77 |
| Total from investment operations | 6.42 | 15.53 | (25.00) | 13.91 | 6.70 |
| Dividends from net investment income | (0.18) | — | — | — | — |
| Net asset value, end of period | $ 52.16 | $ 45.92 | $ 30.39 | $ 55.39 | $ 41.48 |
| Total return | 14.03% | 51.10% | (45.13)% | 33.53% | 19.26% |
| RATIOS/SUPPLEMENTAL DATA: | | | | | |
| Net assets, end of period (000's omitted) | $ 284,225 | $ 249,483 | $ 183,335 | $ 414,959 | $ 298,024 |
| Ratio of gross expenses to average net assets | 0.98% | 0.99% | 0.95% | 0.97% | 0.98% |
| Ratio of expense reimbursements to average net assets | (0.04)% | (0.04)% | (0.04)% | (0.04)% | 0.00% |
| Ratio of net expenses to average net assets | 0.94% | 0.95% | 0.91% | 0.93% | 0.98% |
| Ratio of net investment income to average net assets | 0.17% | 0.49% | 0.12% | (0.15)% | (0.19)% |
| Portfolio turnover rate | 203.56% | 285.33% | 317.72% | 254.03% | 245.58% |

(i) *Amount was computed based on average shares outstanding during the period.*

***See Notes to Financial Statements.***

## THE ALGER PORTFOLIOS
**Financial Highlights for a share outstanding throughout the period**

Alger Capital Appreciation Portfolio

| | Class S | | | | |
|---|---|---|---|---|---|
| | Year ended 12/31/2010 | Year ended 12/31/2009 | Year ended 12/31/2008 | Year ended 12/31/2007 | Year ended 12/31/2006 |
| Net asset value, beginning of period | $ 45.01 | $ 29.86 | $ 54.57 | $ 40.97 | $ 34.44 |
| INCOME FROM INVESTMENT OPERATIONS: | | | | | |
| Net investment income (loss)(i) | (0.08) | 0.08 | (0.05) | (0.16) | (0.17) |
| Net realized and unrealized gain (loss) on investments | 6.20 | 15.07 | (24.66) | 13.76 | 6.70 |
| Total from investment operations | 6.12 | 15.15 | (24.71) | 13.60 | 6.53 |
| Dividends from net investment income | (0.09) | — | — | — | — |
| Net asset value, end of period | $ 51.04 | $ 45.01 | $ 29.86 | $ 54.57 | $ 40.97 |
| Total return | 13.63% | 50.69% | (45.28)% | 33.20% | 18.96% |
| RATIOS/SUPPLEMENTAL DATA: | | | | | |
| Net assets, end of period (000's omitted) | $ 12,760 | $ 13,307 | $ 9,369 | $ 20,783 | $ 23,845 |
| Ratio of gross expenses to average net assets | 1.34% | 1.24% | 1.20% | 1.22% | 1.23% |
| Ratio of expense reimbursements to average net assets | (0.04)% | (0.04)% | (0.04)% | (0.04)% | 0.00% |
| Ratio of net expenses to average net assets | 1.30% | 1.20% | 1.16% | 1.18% | 1.23% |
| Ratio of net investment income to average net assets | (0.18)% | 0.23% | (0.12)% | (0.34)% | (0.45)% |
| Portfolio turnover rate | 203.56% | 285.33% | 317.72% | 254.03% | 245.58% |

(i) *Amount was computed based on average shares outstanding during the period.*

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## NOTE 1 — General:

The Alger Portfolios (the "Fund") is a diversified, open-end registered investment company organized as a business trust under the laws of the Commonwealth of Massachusetts. The Fund operates as a series company currently issuing seven series of shares of beneficial interest: the Alger Capital Appreciation Portfolio, Alger Large Cap Growth Portfolio, Alger Mid Cap Growth Portfolio, Alger SMid Cap Growth Portfolio, Alger Small Cap Growth Portfolio, Alger Growth & Income Portfolio, and Alger Balanced Portfolio (collectively the "Portfolios"). These financial statements include only the Alger Capital Appreciation Portfolio (the "Portfolio"). The Portfolio invests primarily in equity securities and has an investment objective of long-term capital appreciation. Shares of the Portfolio are available and are being marketed exclusively as a pooled funding vehicle for qualified retirement plans and for life insurance companies writing all types of variable annuity contracts and variable life insurance policies.

The Portfolio offers Class I-2 shares and Class S shares. Each class has identical rights to assets and earnings except that only Class S shares have a plan of distribution and bear the related expenses.

## NOTE 2 — Significant Accounting Policies:

*(a) Investment Valuation:* The Portfolio values its financial instruments at fair value using independent dealers or pricing services under policies approved by the Board. Investments of the Portfolio are valued on each day the New York Stock Exchange (the "NYSE") is open, as of the close of the NYSE (normally 4:00 p.m. Eastern time).

Equity securities and option contracts for which such information is readily available are valued at the last reported sales price or official closing price as reported by an independent pricing service on the primary market or exchange on which they are traded. In the absence of reported sales, securities are valued at a price within the bid and ask price or, in the absence of a recent bid or ask price, the equivalent as obtained from one or more of the major market makers for the securities to be valued.

Debt securities generally trade in the over-the-counter market. Securities with remaining maturities of more than sixty days at the time of acquisition are valued on the basis of last available bid prices or current market quotations provided by dealers or pricing services. In determining the value of a particular investment, pricing services may use certain information with respect to transactions in such investments, quotations from dealers, pricing matrixes, market transactions in comparable investments, various relationships observed in the market between investments and calculated yield measures based on valuation technology commonly employed in the market for such investments. Asset-backed and mortgage-backed securities are valued by independent pricing services using models that consider estimated cash flows of each tranche of the security, establish a benchmark yield and develop an estimated tranche specific spread to the benchmark yield based on the unique attributes of the tranche.

Securities for which market quotations are not readily available are valued at fair value, as determined in good faith pursuant to procedures established by the Board of Trustees.

Securities in which the Portfolio invests may be traded in foreign markets that close before the close of the NYSE. Developments that occur between the close of the foreign markets and the close of the NYSE may result in adjustments to the closing prices to reflect what the investment adviser, pursuant to policies established by the Board of Trustees, believes to be the fair value of these securities as of the close of the NYSE. The Portfolio may also fair value securities in other situations, for example, when a particular foreign market is closed but the Portfolio is open.

Financial Accounting Standards Board Accounting Standards Codification 820 – Fair Value Measurements and Disclosures ("ASC 820") defines fair value as the price that the Portfolio would receive upon selling an investment in a timely transaction to an independent buyer in the principal or most advantageous market of the investment. ASC 820 established a three-tier hierarchy to maximize the use of observable market data and minimize the use of unobservable inputs and to establish classification of fair value measurements for disclosure purposes. "Inputs" refer broadly to the assumptions that market participants would use in pricing the asset or liability and may be observable or unobservable. Observable inputs are based on market data obtained from sources independent of the Portfolio. Unobservable inputs are inputs that reflect the Portfolio's, own assumptions based on the best information available in the circumstances. The three-tier hierarchy of inputs is summarized in the three broad Levels listed below.

- Level 1 – quoted prices in active markets for identical investments
- Level 2 – significant other observable inputs (including quoted prices for similar investments, interest rates, prepayment speeds, credit risk, etc.)
- Level 3 – significant unobservable inputs (including the Portfolio's, own assumptions in determining the fair value of investments)

The Portfolio's valuation techniques are consistent with the market approach whereby prices and other relevant information generated by market transactions involving identical or comparable assets are used to measure fair value. Inputs for Level 1 include exchange listed prices and broker quotes in an active market. Inputs for Level 2 include the last trade price in the case of a halted security, a broker quote in an inactive market, an exchange listed price which has been adjusted for fair value factors, and prices of closely related securities. Additional Level 2 inputs include an evaluated price which is based upon on a compilation of observable market information such as spreads for fixed income and preferred securities. Inputs for Level 3 include derived prices from unobservable market information which can include cash flows and other information obtained from a company's financial statements, or from market indicators such as benchmarks and indices.

*(b) Cash and Cash Equivalents:* Cash and cash equivalents include U.S. dollars and short-term securities maturing in sixty days or less. Such short-term securities are valued at amortized cost which approximates market value.

*(c)* Security Transactions and Investment Income: Security transactions are recorded on a trade date basis. Realized gains and losses from security transactions are recorded on the

identified cost basis. Dividend income is recognized on the ex-dividend date and interest income is recognized on the accrual basis.

Premiums and discounts on debt securities purchased are amortized or accreted over the lives of the respective securities.

*(d) Foreign Currency Transactions:* The books and records of the Portfolio are maintained in U.S. dollars. Foreign currencies, investments and other assets and liabilities are translated into U.S. dollars at the prevailing rates of exchange on the valuation date. Purchases and sales of investment securities and income and expenses are translated into U.S. dollars at the prevailing exchange rates on the respective dates of such transactions.

Net realized gains and losses on foreign currency transactions represent net gains and losses from the disposition of foreign currencies, currency gains and losses realized between the trade dates and settlement dates of security transactions, and the difference between the amount of net investment income accrued and the U.S. dollar amount actually received. The effects of changes in foreign currency exchange rates on investments in securities are included in realized and unrealized gain or loss on investments in the Statement of Operations.

*(e) Option Contracts:* When a Portfolio writes an option, an amount equal to the premium received by the Portfolio is recorded as a liability and is subsequently adjusted to the current fair value of the option written. Premiums received from writing options that expire unexercised are treated by the Portfolio on the expiration date as realized gains from investments. The difference between the premium and the amount paid on effecting a closing purchase transaction, including brokerage commissions, is also treated as a realized gain, or, if the premium is less than the amount paid for the closing purchase transaction, as a realized loss. If a written call option is exercised, the premium is added to the proceeds from the sale of the underlying security in determining whether the Portfolio has realized a gain or loss. If a written put option is exercised, the premium reduces the cost basis of the securities purchased by the Portfolio. The Portfolio as writer of an option bears the market risk of an unfavorable change in the price of the security underlying the written option.

The Portfolio may also purchase put and call options. The Portfolio pays a premium which is included in the Portfolio's Statement of Assets and Liabilities as an investment and subsequently marked to market to reflect the current value of the option. Premiums paid for purchasing options which expire are treated as realized losses. The risk of loss associated with purchasing put and call options is limited to the premium paid. Premiums paid for purchasing options which are exercised or closed are added to the amounts paid or offset against the proceeds on the underlying security to determine the realized gain or loss.

*(f) Lending of Portfolio Securities*: The Portfolio may lend its securities to financial institutions, provided that the market value of the securities loaned will not at any time exceed one third of the Portfolio's total assets. The Portfolio earns fees on the securities loaned. In order to protect against the risk of failure by the borrower to return the securities loaned or any delay in the delivery of such securities, the loan is collateralized

by cash, letters of credit or U.S. Government securities that are maintained in an amount equal to at least 100 percent of the current market value of the loaned securities. The "current market value" of the loaned securities is determined at the close of business of the Portfolio and any required additional collateral is delivered to the Portfolio on the next business day. There were no securities on loan during the year ended December 31, 2010.

*(g) Dividends to Shareholders:* Dividends and distributions payable to shareholders are recorded by the Portfolio on the ex-dividend date.

Dividends from net investment income are declared and paid annually. Dividends from net realized gains, offset by any loss carryforward, are declared and paid annually after the end of the fiscal year in which earned. Each class is treated separately in determining the amounts of dividends from net investment income payable to holders of its shares.

The characterization of distributions to shareholders for financial reporting purposes is determined in accordance with federal income tax rules. Therefore, the source of the Portfolio's distributions may be shown in the accompanying financial statements as either from, or in excess of, net investment income or net realized gain on investment transactions, or return of capital, depending on the type of book/tax differences that may exist. Capital accounts within the financial statements are adjusted for permanent book/tax differences. Reclassifications result primarily from the difference in tax treatment of net operating losses, premium/discount of debt securities, realized gain or loss from foreign currency transactions, and realized gains from redemptions in kind, if any. The reclassifications have no impact on the net asset values of the Portfolio and were designed to present the Portfolio's capital accounts on a tax basis.

*(h) Federal Income Taxes:* It is the Portfolio's policy to comply with the requirements of the Internal Revenue Code Subchapter M applicable to regulated investment companies and to distribute all of the taxable income, including net realized capital gains, of the Portfolio to its respective shareholders. Therefore, no federal income tax provision is required. The Portfolio is treated as a separate entity for the purpose of determining such compliance.

Financial Accounting Standards Board Accounting Standards Codification 740 – Income Taxes ("ASC 740") requires the Portfolio to measure and recognize in its financial statements the benefit of a tax position taken (or expected to be taken) on an income tax return if such position will more likely than not be sustained upon examination based on the technical merits of the position. No tax years are currently under investigation. The Portfolio files income tax returns in the U.S. Federal jurisdiction, as well as the New York State and New York City jurisdictions. Based upon their review of tax positions for the Portfolio's open tax years of 2007-2010 in these jurisdictions, the Portfolio has determined that ASC 740 did not have a material impact on the Portfolio's financial statements for the year ended December 31, 2010.

*(i) Allocation Methods:* The Fund accounts separately for the assets, liabilities and operations of each Portfolio. Expenses directly attributable to each Portfolio are charged to that Portfolio's operations; expenses which are applicable to all Portfolios are allocated among them based on net assets. Income, realized and unrealized gains and losses, and

expenses of each Portfolio are allocated among the Portfolio's classes based on relative net assets, with the exception of distribution fees and transfer agency fees.

*(i) Estimates:* These financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America, which require using estimates and assumptions that affect the reported amounts therein. Actual results may differ from those estimates.

## NOTE 3 — Investment Advisory Fees and Other Transactions with Affiliates:

*(a) Investment Advisory and Administration Fees*: Fees incurred by the Portfolio, pursuant to the provisions of the Fund's Investment Advisory Agreement and Administration Agreement with Fred Alger Management, Inc. ("Alger Management"), are payable monthly and computed based on the average daily net assets of the Portfolio at the following annual rate:

| | Advisory Fee | Administration Fee |
|---|---|---|
| Alger Capital Appreciation Portfolio | .810% | .0275% |

As part of a settlement with the New York State Attorney General dated October 11, 2006, Alger Management has agreed to reduce its advisory fee listed above to 0.775% for the Portfolio for the period from December 1, 2006 through November 30, 2011.

*(b) Distribution Fees*: Class S shares—The Fund has adopted a Distribution Plan pursuant to which Class S shares of each Portfolio pay Fred Alger & Company, Incorporated, the Fund's distributor (the "Distributor" or "Alger Inc."), a fee at the annual rate of .25% of the respective average daily net assets of the Class S shares of the designated Portfolio to compensate Alger Inc. for its activities and expenses incurred in distributing the Class S shares. The fees paid may be more or less than the expenses incurred by Alger Inc.

*(c) Brokerage Commissions*: During the year ended December 31, 2010, the Portfolio paid the Alger Inc. $479,776, in connection with securities transactions.

*(d) Shareholder Administrative Fees*: The Fund has entered into a shareholder administrative services agreement with Alger Management to compensate Alger Management on a per account basis for its liaison and administrative oversight of Boston Financial Data Services, Inc. ("BFDS") the transfer agent, and other related services. Effective June 1, 2010 the Fund compensates Alger Management at the annual rate of 0.01% of the average daily net assets for these services. From January 1, 2010 through December 31, 2010, the Portfolio incurred fees of $15,688, for these services, which are included in transfer agent fees and expenses in the Statements of Operations.

*(e) Trustee Fees:* From January 1, 2010 through February 8, 2010, the Portfolio paid each Trustee who is not affiliated with Alger Management or its affiliates $500 for each meeting attended, to a maximum of $2,000 per annum. The Chairman of the Board of Trustees received an additional annual fee of $10,000 which is paid, pro rata, by all portfolios managed by Alger Management. Additionally, each member of the audit committee received an additional $50 from the Portfolio for each audit committee meeting attended, to a maximum of $200 per annum.

Effective February 9, 2010 the Portfolio pays each trustee who is not affiliated with Alger Management or its affiliates $750 for each meeting attended, to a maximum of $3,000 per annum, plus travel expenses incurred for attending the meeting. The chairman of the Board of Trustees receives an additional annual fee of $15,000 which is paid, pro rata, by all funds managed by Alger Management. Additionally, each member of the audit committee receives an additional $75 for each audit committee meeting attended, to a maximum of $300 per annum.

*(f) Interfund Loans:* The Portfolio, along with other funds advised by Alger Management, may borrow money from and lend money to each other for temporary or emergency purposes. To the extent permitted under its investment restrictions, the Portfolio may lend uninvested cash in an amount up to 15% of its net assets to other Portfolios, and the Portfolio may borrow in an amount up to 10% of its net assets from other Portfolios. If the Portfolio has borrowed from other Portfolios and has aggregate borrowings from all sources that exceed 10% of the Portfolio's total assets, the Portfolio will secure all of its loans from other Portfolios. The interest rate charged on interfund loans is equal to the average of the overnight time deposit rate and bank loan rate available to the Portfolios.

During the year ended December31, 2010, the Portfolio had no interfund loans.

*(g) Other Transactions With Affiliates:* Certain officers of the Trust are directors and officers of Alger Management and the Distributor.

## NOTE 4 — Securities Transactions:

Purchases and sales of securities, other than U.S. Government and short-term securities, for the year ended December 31, 2010, were as follows:

| | PURCHASES | SALES |
|---|---|---|
| Alger Capital Appreciation Portfolio | $518,344,753 | $518,999,536 |

## NOTE 5 — Borrowing:

The Portfolio may borrow from its custodian on an uncommitted basis. The Portfolio pays the custodian a market rate of interest, generally based upon the London Inter-Bank Offer Rate. The Portfolio may also borrow from other portfolios advised by Alger Management, as discussed in Note 3 (f). For the year ended December 31, 2010, the Portfolio had the following borrowings:

| | AVERAGE DAILY BORROWING | WEIGHTED AVERAGE INTEREST RATE |
|---|---|---|
| Alger Capital Appreciation Portfolio | $ 645 | 2.26% |

The highest amount borrowed during the year ended December 31, 2010 for the Portfolio was as follows:

| | HIGHEST BORROWING |
|---|---|
| Alger Capital Appreciation Portfolio | $235,450 |

## NOTE 6 — Share Capital:

The Fund has an unlimited number of authorized shares of beneficial interest of $.001 par value for each share class. During the year ended December 31, 2010 and the year ended December 31, 2009, transactions of shares of beneficial interest were as follows:

| | FOR THE YEAR ENDED DECEMBER 31, 2010 | | FOR THE YEAR ENDED DECEMBER 31, 2009 | |
|---|---|---|---|---|
| | SHARES | AMOUNT | SHARES | AMOUNT |
| **Alger Capital Appreciation Portfolio** | | | | |
| **Class I-2:** | | | | |
| Shares sold | 1,334,855 | $ 62,669,328 | 848,597 | $ 32,145,644 |
| Dividends reinvested | 21,423 | 1,008,170 | — | — |
| Shares redeemed | (1,340,201) | (61,843,565) | (1,447,904) | (50,967,907) |
| **Net increase (decrease)** | **16,077** | **$ 1,833,933** | **(599,307)** | **$ (18,822,263)** |
| **Class S:** | | | | |
| Shares sold | 44,732 | $ 2,044,736 | 75,711 | $ 2,851,694 |
| Dividends reinvested | 597 | 27,573 | — | — |
| Shares redeemed | (90,962) | (4,090,269) | (93,770) | (3,150,881) |
| **Net decrease** | **(45,633)** | **$ (2,017,960)** | **(18,059)** | **$ (299,187)** |

## NOTE 7 — Income Tax Information:

The tax character of distributions paid during the year ended December 31, 2010 and the year ended December 31, 2009 was as follows:

| | YEAR ENDED DECEMBER 31, 2010 | YEAR ENDED DECEMBER 31, 2009 |
|---|---|---|
| **Alger Capital Appreciation Portfolio** | | |
| Distributions paid from: | | |
| Ordinary Income | $ 1,035,743 | — |
| Long-term capital gain | — | — |
| **Total distributions paid** | $ 1,035,743 | — |

As of December 31, 2010, the components of accumulated gains and losses on a tax basis were as follows:

| **Alger Capital Appreciation Portfolio** | |
|---|---|
| Undistributed ordinary income | $ 225,789 |
| Undistributed long-term gains | — |
| Net accumulated earnings | 225,789 |
| Capital loss carryforwards | (51,437,420) |
| Net unrealized appreciation | 24,467,052 |
| Total accumulated losses | $ (26,744,579) |

At December 31, 2010, the Portfolio, for federal income tax purposes, had capital loss carryforwards which expire as set forth in the table below. These amounts may be applied against future net realized gains until the earlier of their utilization or expiration.

| Expiration Dates | Alger Capital Appreciation Portfolio |
|---|---|
| 2016 | $ 29,672,544 |
| 2017 | 21,764,876 |
| Total | 51,437,420 |

Net capital losses incurred after October 31 and within the taxable year are deemed to arise on the first business day of the portfolio's next taxable year.

The difference between book-basis and tax-basis unrealized appreciation (depreciation) is determined annually and is attributable primarily to the tax deferral of losses on wash sales, the tax treatment of partnership investments, and return of capital from Real Estate Investment Trust investments.

Permanent differences, primarily from real estate investment trusts and partnership investments sold by the Portfolio resulted in the following reclassifications among the Portfolio's components of net assets at December 31, 2010:

| Alger Capital Appreciation Portfolio | |
|---|---|
| Undistributed net investment income | $ (154,253) |
| Accumulated net realized loss | $ 168,870 |
| Paid in capital | $ (14,617) |

## NOTE 8 — Fair Value Measurements:

The major categories of securities and their respective fair value inputs are detailed in each Portfolio's Schedule of Investments. The following is a summary of the inputs used as of December 31, 2010 in valuing the Portfolios' investments carried at fair value. There were no significant transfers of investment assets between Levels 1 and 2 as of December 31, 2010.

| Alger Capital Appreciation Portfolio | TOTAL FUND | LEVEL 1 | LEVEL 2 | LEVEL 3 |
|---|---|---|---|---|
| **COMMON STOCKS** | | | | |
| Consumer Discretionary | $ 45,262,342 | $ 45,262,342 | — | — |
| Consumer Staples | 11,268,848 | 11,268,848 | — | — |
| Energy | 33,726,667 | 33,726,667 | — | — |
| Financials | 15,813,042 | 15,813,042 | — | — |
| Health Care | 24,605,618 | 24,605,618 | — | — |
| Industrials | 44,000,946 | 44,000,946 | — | — |
| Information Technology | 99,272,422 | 99,272,422 | — | — |
| Materials | 13,683,719 | 13,683,719 | — | — |
| **TOTAL COMMON STOCKS** | **$ 287,633,604** | **$ 287,633,604** | **—** | **—** |
| **TOTAL INVESTMENTS IN SECURITIES** | **$ 287,633,604** | **$ 287,633,604** | **—** | **—** |

## NOTE 9 — Derivatives:

Financial Accounting Standards Board Accounting Standards Codification 815 – Derivatives and Hedging ("ASC 815") requires qualitative disclosures about objectives and strategies for using derivatives, quantitative disclosures about fair value amounts of and gains and losses on derivative instruments, and disclosures about credit-risk-related contingent features in derivative agreements.

Forward currency contracts—In connection with portfolio purchases and sales of securities denominated in foreign currencies, the Portfolio may enter into forward currency contracts. Additionally, the Portfolio may enter into such contracts to economically hedge certain other foreign currency denominated investments. These contracts are valued at the current cost of covering or offsetting such contracts, and the related realized and unrealized foreign exchange gains and losses are included in the statement of operations. In the event that counterparties fail to settle these currency contracts or the related foreign security trades, the Portfolio could be exposed to foreign currency fluctuations.

Options—The Portfolio seek to capture the majority of the returns associated with equity market investments. To meet this investment goal, the Portfolio invests in a broadly diversified portfolio of common stocks, while also buying and selling call and put options on equities and equity indices. The Portfolio purchases call options to increase its exposure to stock market risk and also provide diversification of risk. The Portfolio purchases put options in order to protect from significant market declines that may occur over a short period of time. The Portfolio will write covered call and cash secured put options to generate cash flows while reducing the volatility of the portfolio. The cash flows may be an important source of the Portfolio's return, although written call options may reduce the Portfolio's ability to profit from increases in the value of the underlying security or equity portfolio. The value of a call option generally increases as the price of the underlying stock increases and decreases as the stock decreases in price. Conversely, the value of a put option generally increases as the price of the underlying stock decreases and decreases as the stock increases in price. The combination of the diversified stock portfolio and the purchase and sale of options is intended to provide the Portfolio with the majority of the returns associated with equity market investments but with reduced volatility and returns that are augmented with the cash flows from the sale of options. During the year ended December 31, 2010, written equity and index put options were used in accordance with this objective.

During the year ended December 31, 2010, the Portfolio had no derivative instruments.

## NOTE 10 — Litigation:

On August 31, 2005, the West Virginia Securities Commissioner (the "WVSC"), in an ex parte Summary Order to Cease and Desist and Notice of Right to Hearing, concluded that the Manager and the Distributor had violated the West Virginia Uniform Securities Act (the "WVUSA"), and ordered the Manager and the Distributor to cease and desist from further violations of the WVUSA by engaging in the market-timing-related conduct described in the order. The ex parte order provided notice of their right to a hearing with respect to the violations of law asserted by the WVSC. Other firms unaffiliated with the

Manager were served with similar orders. The Manager and the Distributor intend to request a hearing for the purpose of seeking to vacate or modify the order.

In addition, in 2003 and 2004 several purported class actions and shareholder derivative suits were filed against various parties in the mutual fund industry, including the Manager, certain mutual funds managed by the Manager (the "Alger Mutual Funds"), and certain current and former Alger Mutual Fund trustees and officers, alleging wrongful conduct related to market-timing and late-trading by mutual fund shareholders. These cases were transferred to the U.S. District Court of Maryland by the Judicial Panel on Multidistrict Litigation for consolidated pre-trial proceedings under the caption number 1:04-MD-15863 (JFM). After a number of the claims in the Alger lawsuits, including all claims against Alger Mutual Funds and their independent trustees, were dismissed by the court, the Alger-related class and derivative suits were settled. A Final Judgment and Order approving the settlement was entered on October 25, 2010. No appeals from the Final Judgment and Order were filed within the allotted time limit. The settlement was paid by insurance, and had no financial impact on the Alger Mutual Funds.

## NOTE 11 — Subsequent Event:

Each Portfolio has evaluated events that have occurred after December 31, 2010. No events have been identified which require recognition as of December 31, 2010.

## REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Shareholders and Board of Trustees of The Alger Portfolios:

We have audited the accompanying statement of assets and liabilities, including the schedule of investments, of the Alger Capital Appreciation Portfolio, one of the portfolios constituting The Alger Portfolios (the "Fund") as of December 31, 2010, and the related statement of operations for the year then ended, the statements of changes in net assets for each of the two years in the period then ended, and the financial highlights for each of the two years in the period then ended. These financial statements and financial highlights are the responsibility of the Fund's management. Our responsibility is to express an opinion on these financial statements and financial highlights based on our audits. The Fund's financial highlights for the respective periods ended December 31, 2008 were audited by other auditors, whose report dated February 10, 2009, expressed an unqualified opinion on such financial highlights.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements and financial highlights are free of material misstatement. The Fund is not required to have, nor were we engaged to perform, an audit of their internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Fund's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. Our procedures included confirmation of securities owned as of December 31, 2010, by correspondence with the custodian and brokers; where replies were not received from brokers, we performed other auditing procedures. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements and financial highlights referred to above, present fairly, in all material respects, the financial position of the Alger Capital Appreciation Portfolio of The Alger Portfolios as of December 31, 2010, the results of its operations for the year then ended, the changes in its net assets for each of the two years in the period then ended, and the financial highlights for each of the two years in the period then ended, in conformity with accounting principles generally accepted in the United States of America.

Deloitte & Touche LLP
New York, New York
February 17, 2011

## Shareholder Expense Example

As a shareholder of a Portfolio, you incur two types of costs: transaction costs, if applicable; and ongoing costs, including management fees, distribution (12b-1) fees, if applicable, and other fund expenses. This example is intended to help you understand your ongoing costs (in dollars) of investing in a Portfolio and to compare these costs with the ongoing costs of investing in other mutual funds.

The example below is based on an investment of $1,000 invested at the beginning of the six-month period starting July 1, 2010 and ending December 31, 2010.

## Actual Expenses

The first line for each class of shares in the table below provides information about actual account values and actual expenses. You may use the information in this line, together with the amount you invested, to estimate the expenses that you would have paid over the period. Simply divide your account value by $1,000 (for example, an $8,600 account value divided by $1,000 = 8.6), then multiply the result by the number in the first line under the heading entitled "Expenses Paid During the Period" to estimate the expenses you paid on your account during this period.

## Hypothetical Example for Comparison Purposes

The second line for each class of shares in the table below provides information about hypothetical account values and hypothetical expenses based on the Portfolio's actual expense ratios for each class of shares and an assumed rate of return of 5% per year before expenses, which is not the Portfolio's actual return. The hypothetical account values and expenses may not be used to estimate the actual ending account balance or expenses you paid for the period. You may use this information to compare the ongoing costs of investing in a Portfolio and other funds. To do so, compare this 5% hypothetical example with the 5% hypothetical examples that appear in the shareholder reports of other funds.

Please note that the expenses shown in the table are meant to highlight your ongoing costs only and do not reflect any transaction costs or deduction of insurance charges against assets or annuities. Therefore, the second line under each class of shares in the table is useful in comparing ongoing costs only, and will not help you determine the relative total costs of owning different funds. In addition, if these transactional costs were included, your costs would have been higher.

| | | Beginning Account Value July 1, 2010 | Ending Account Value December 31, 2010 | Expenses Paid During the Six Months Ended December 31, 2010(a) | Ratio of Expenses to Average Net Assets For the Six Months Ended December 31, 2010(b) |
|---|---|---|---|---|---|
| **Alger Capital Appreciation Portfolio** | | | | | |
| **Class I-2** | Actual | $ 1,000.00 | $ 1,260.21 | $ 5.38 | 0.94% |
| | Hypothetical(c) | 1,000.00 | 1,020.44 | 4.81 | 0.94 |
| **Class S** | Actual | 1,000.00 | 1,258.07 | 7.41 | 1.30 |
| | Hypothetical(c) | 1,000.00 | 1,018.64 | 6.62 | 1.30 |

*(a) Expenses are equal to the annualized expense ratio of the respective share class, multiplied by the average account value over the period, multiplied by 184/365 (to reflect the one-half year period).*
*(b) Annualized.*
*(c) 5% annual return before expenses.*

## Trustees and Officers of the Fund

Information about the trustees and officers of the Fund is set forth below. In the table the term "Alger Fund Complex" refers to the Fund, The Alger Funds, The Alger Institutional Funds, Alger China-U.S. Growth Fund and The Alger Funds II, each of which is a registered investment company managed by Fred Alger Management, Inc. ("Alger Management"). Each Trustee serves until an event of termination, such as death or resignation, or until his successor is duly elected; each officer's term of office is one year. Unless otherwise noted, the address of each person named below is 111 Fifth Avenue, New York, NY 10003.

| Name, Age, Position with the Fund | Principal Occupations | Trustee and/or Officer Since | Number of Funds in the Alger Fund Complex which are Overseen by Trustee |
|---|---|---|---|
| **INTERESTED TRUSTEE** | | | |
| Hilary M. Alger (49) | Director of Development, Pennsylvania Ballet since 2004; Associate Director of Development, College of Arts and Sciences and Graduate School, University of Virginia 1999-2003. | 2003 | 27 |
| **NON-INTERESTED TRUSTEE** | | | |
| Charles F. Baird, Jr. (57) | Managing Partner of North Castle Partners, a private equity securities group; Chairman of Leiner Health Products, Enzymatic Therapy and Caleel & Hayden (skincare business); former Chairman of Elizabeth Arden Day Spas, Naked Juice, Equinox (fitness company) and EAS (manufacturer of nutritional products). Formerly Managing Director of AEA Investors, Inc. | 2000 | 27 |
| Roger P. Cheever (65) | Associate Vice President for Principal Gifts, and Senior Associate Dean for Development in the Faculty of Arts and Sciences at Harvard University; Formerly Deputy Director of the Harvard College Fund. | 2000 | 27 |
| Lester L. Colbert Jr. (76) | Private investor since 1988; Formerly Chairman of the Board, President and Chief Executive Officer of Xidex Corporation (manufacturer of computer information media). | 2000 | 27 |
| Stephen E. O'Neil (78) | Attorney. Private Investor since 1981. Formerly of Counsel to the law firm of Kohler & Barnes. | 1986 | 27 |
| David Rosenberg (48) | Associate Professor of Law since January 2006 (Assistant Professor 2000-2005), Zicklin School of Business, Baruch College, City University of New York. | 2007 | 27 |
| Nathan E. Saint-Amand M.D. (73) | Medical doctor in private practice; Member of the Board of the Manhattan Institute (non-profit policy research) since 1988; Formerly Co-Chairman, Special Projects Committee, Memorial Sloan Kettering. | 1986 | 27 |

| Name, Age, Position with the Fund | Principal Occupations | Trustee and/or Officer Since | Number of Funds in the Alger Fund Complex which are Overseen by Trustee |
|---|---|---|---|
| **OFFICERS** | | | |
| Dan C. Chung (48)<br>President | Chief Investment Officer and Director since 2001, and Chief Executive Officer since 2006, of Alger Management; President since 2003 of Alger Associates, Inc. ("Associates"); President and Director since 2003 of Fred Alger International Advisory S.A. ("International"); President since 2003 and Director since 2003 of Analysts Resources, Inc. ("Resources"); Formerly Trustee of the Trust from 2001 to 2007. | 2001 | N/A |
| Michael D. Martins (45)<br>Treasurer | Senior Vice President of Alger Management; Assistant Treasurer since 2004. | 2005 | N/A |
| Hal Liebes (46)<br>Secretary | Executive Vice President, Chief Legal Officer, Chief Operating Officer and Secretary of Alger Management; Director since 2006 of International and Resources. | 2005 | N/A |
| Lisa A. Moss (45)<br>Assistant Secretary | Senior Vice President since 2009, and Vice President and Assistant General Counsel of Alger Management since June 2006. Formerly Director of Merrill Lynch Investment Managers, L.P. from 2005-2006. | 2006 | N/A |
| Anthony S. Caputo (55)<br>Assistant Treasurer | Employed by Alger Management since 1986, currently serving as Vice President. | 2007 | N/A |
| Sergio M. Pavone (49)<br>Assistant Treasurer | Employed by Alger Management since 2002, currently serving as Vice President. | 2007 | N/A |
| Barry J. Mullen (57)<br>Chief Compliance Officer | Senior Vice President and Chief Compliance officer for Alger Management since May 2006. Formerly Director of BlackRock, Inc. from 2004-2006. | 2006 | N/A |

Ms. Alger is an "interested person" (as defined in the Investment Company Act) of the Fund because of her affiliations with Alger Management. No Trustee is a director of any public company except as indicated under "Principal Occupations".

The Statement of Additional Information contains additional information about the Fund's Trustees and is available without charge upon request by calling (800) 992-3863.

## Investment Management Agreement Renewal

At an in-person meeting held on September 14, 2010, the Trustees, including the Independent Trustees, unanimously approved renewal of the Investment Advisory Agreement (the "Agreement") between the Fund and Fred Alger Management, Inc.

("Alger Management"). The Independent Trustees were assisted in their review by independent legal counsel and met with such counsel in executive session separate from representatives of Alger Management.

In evaluating the Agreement, the Trustees drew on materials that they had requested and which were provided to them in advance of the meeting by Alger Management and by counsel. The materials covered, among other matters, (i) the nature, extent and quality of the services provided by Alger Management under the Agreement, (ii) the investment performance of the Fund's portfolios (each a "Portfolio"), (iii) the costs to Alger Management of its services and the profits realized by Alger Management and Alger Inc. from their relationship with the Fund, and (iv) the extent to which economies of scale would be realized if and as the Portfolios grow and whether the fee levels in the Agreement reflect these economies of scale. These materials included an analysis of the Portfolios and Alger Management's services by FUSE Research Network LLC ("FUSE"), an independent consulting firm whose specialties include assistance to fund trustees and directors in their review of advisory contracts pursuant to section 15(c) of the Investment Company Act of 1940. At the meeting, senior FUSE personnel provided a presentation to the Trustees based on the FUSE materials.

In deciding whether to approve renewal of the Agreement, the Trustees considered various factors, including those enumerated above. They also considered other direct and indirect benefits to Alger Management and its affiliates from their relationship with the Fund.

**Nature, Extent and Quality of Services.** In considering the nature, extent and quality of the services provided by Alger Management pursuant to the Agreement, the Trustees relied on their prior experience as Trustees of the Fund, their familiarity with the personnel and resources of Alger Management and its affiliates, and the materials provided at the meeting. They noted that under the Agreement Alger Management is responsible for managing the investment operations of the Portfolios. They also noted that administrative, compliance, reporting and accounting services necessary for the conduct of the Fund's affairs are provided by Alger Management under the separate Administration Agreement. The Trustees reviewed the background and experience of Alger Management's senior investment management personnel, including the individuals currently responsible for the investment operations of the Portfolios. They also considered the resources, operational structures and practices of Alger Management in managing each Portfolio, as well as Alger Management's overall investment management business. They noted especially Alger Management's history of expertise in managing portfolios of "growth" stocks and that, according to an analysis provided by FUSE, the characteristics of each equity Portfolio had been consistent with those of a fund that holds itself out to investors as growth-oriented. They also took notice of the ability of the manager of the fixed-income portion of the Balanced Portfolio to manage fixed-income instruments across the credit and credit quality spectra. The Trustees concluded that Alger Management's experience, resources and strength in the areas of importance to the Fund are considerable. The Trustees considered the level and depth of Alger Management's ability to execute portfolio transactions to effect investment decisions, including those through Alger Inc. The Trustees also considered the ongoing enhancements to the control and compliance environment at Alger Management and within the Fund.

**Investment Performance of the Funds.** Drawing upon information provided at the meeting by Alger Management as well as FUSE and upon reports provided to the Trustees by Alger Management throughout the preceding year, the Trustees reviewed each Portfolio's returns for the year-to-date (at 6/30/10), second-quarter, and 1-, 3-, 5-, and 10-year periods to the extent available (and its year-by-year returns), together with supplemental data through 8/31/10, and compared them with benchmark and peer-group data for the same periods. They noted that for the year to date through 6/30/10 each of the Portfolios had underperformed both its benchmark and the median for its peers, except that the Large Cap Portfolio, Class I-2 of the Balanced Portfolio and the Small Cap Portfolio had surpassed their respective peer medians and the Small Cap Portfolio had also outperformed its benchmark. The performance of the Portfolios for the 1-, 3- and 5-year periods through 6/30/10 had been generally consistent with the shorter-term data, except that the Large Cap Portfolio had significantly outperformed both its benchmark and its peer median for the 1-year period, the Growth & Income Portfolio had surpassed both measures for the 3-year period, and the Capital Appreciation Portfolio had outperformed both measures for all three periods.

**Fund Fees and Expense Ratios; Profitability to Alger Management and its Affiliates.** The Trustees considered the profitability of the Investment Advisory Agreement to Alger Management and its affiliates, and the methodology used by Alger Management in determining such profitability. The Trustees reviewed previously-provided data on each Portfolio's profitability to Alger Management and its affiliates for the year ended June 30, 2010. In addition, the Trustees reviewed each Portfolio's management fee and expense ratio and compared them with a group of comparable funds. In order to assist the Trustees in this comparison, FUSE had provided the Trustees with comparative information with respect to fees paid, and expense ratios incurred, by similar funds. That information indicated that all of the fees and expense ratios were above the median for the applicable FUSE reference groups except that the fees of the Mid Cap and Growth & Income Portfolio, the expense ratio of Class I-2 of the Balanced Portfolio and the fee and expense ratios of the Small Cap Portfolio were below the applicable median. The Trustees determined that such information should be taken into account in weighing the size of the fee against the nature, extent and quality of the services provided. The Trustees also considered fees paid to Alger Management by other types of clients, specifically mutual funds for which Alger Management was sub-adviser and Alger Management's institutional clients. The Trustees determined that in both cases the fees were of doubtful relevance for purposes of comparison with those of the Portfolios because of the significant differences in services provided by Alger Management to those types of clients as opposed to the Portfolios, but that to the extent that meaningful comparison was practicable, the differences in services adequately explained the differences in the fees. After discussing with representatives of the Adviser and FUSE the methodologies used in computing the costs that formed the bases of the profitability calculations, the Trustees turned to the profitability data provided. After analysis and discussion, they concluded that, to the extent that Alger Management's and its affiliates' relationships with the Portfolios had been profitable to either or both of those entities in the case of one or more Portfolios, the profit margin in each case was not unacceptable.

**Economies of Scale.** On the basis of their discussions with management and their analysis of information provided at the meeting, the Trustees determined that the nature of the Portfolios and their operations is such that Alger Management is likely to realize economies of scale in the management of each Portfolio at some point as (and if) it grows in size, but that adoption of breakpoints in one or more of the advisory fees, while possibly appropriate at a later date, could await further analysis of the sources and potential scale of the economies and the fee structure that would best reflect them. Accordingly, the Trustees requested that Alger Management address this topic with the Trustees at future meetings.

**Other Benefits to Alger Management.** The Trustees considered whether Alger Management benefits in other ways from its relationship with the Fund. They noted that Alger Management maintains soft-dollar arrangements in connection with the equity Portfolios' brokerage transactions, reports on which are regularly supplied to the Trustees at their quarterly meetings and summaries of which, listing soft-dollar commissions by Portfolio for the twelve months through June 30, 2010, had been included in the materials supplied prior to the meeting. The Trustees also noted that Alger Management receives fees from the Portfolios under the Administration Agreement, that Alger, Inc. provides a substantial portion of the Portfolios' equity brokerage and that Alger Management also receives fees from the Fund under a shareholder services agreement. The Trustees had been provided with information regarding, and had considered, the administration fee, brokerage and shareholder services fee benefits in connection with their review of the profitability to Alger Management and its affiliates of their relationships with the Fund. As to other benefits received, the Trustees decided that none were so significant as to render Alger Management's fees excessive.

**Conclusions and Determinations.** At the conclusion of these discussions, each of the Independent Trustees expressed the opinion that he had been furnished with sufficient information to make an informed business decision with respect to renewal of the Investment Advisory Agreement. Based on its discussions and considerations as described above, the Board made the following conclusions and determinations:

- The Board concluded that the nature, extent and quality of the services provided to each Portfolio by Alger Management are adequate and appropriate.
- The performance of the Portfolios was acceptable to the Board.
- The Board concluded that each advisory fee paid to Alger Management was reasonable in light of comparative performance and expense and advisory fee information, costs of the services provided and profits to be realized and benefits derived or to be derived by

Alger Management and its affiliates from the relationship with the Portfolio.

- The Board determined that there were not at this time significant economies of scale to be realized by Alger Management in managing the Portfolios' assets but that, to the extent that material economies of scale should be realized in the future, the Board would seek to ensure that they were shared with the applicable Portfolio.

The Board considered these conclusions and determinations and, without any one factor being dispositive, determined with respect to each Portfolio that renewal of the Investment Advisory Agreement was in the best interests of the Portfolio and its shareholders.

## Privacy Policy

**Your Privacy Is Our Priority**
At Fred Alger & Company, Incorporated ("Alger") we value the confidence you have placed in us. In trusting us with your assets, you provide us with personal and financial data. Alger is committed to maintaining the confidentiality of the personal nonpublic information ("personal information") entrusted to us by our customers. Your privacy is very important to us, and we are dedicated to safeguarding your personal information as we serve your financial needs.

**Our Privacy Policy**
We believe you should know about Alger's Privacy Policy and how we collect and protect your personal information. This Privacy Policy ("Policy") describes our practices and policy for collecting, sharing and protecting the personal information of our prospective, current and former customers. The Policy is applicable to Alger and its affiliate, Fred Alger Management, Inc., as well as the following funds: The Alger Funds, The Alger Institutional Funds, The Alger Portfolios, Alger China-U.S. Growth Fund and The Alger Funds II. We are proud of our Policy and hope you will take a moment to read about it.

**Information We Collect**
The type of personal information we collect and use varies depending on the Alger products or services you select.

We collect personal information that enables us to serve your financial needs, develop and offer new products and services, and fulfill legal and regulatory requirements. Depending on the products or services you request, we obtain personal information about you from the following sources:

- Information, such as your name, address and social security number, provided on applications and other forms we receive from you or your representative;
- Information from your communications with Alger employees or from your representative, which may be provided to us by telephone, in writing or through Internet transactions; and

- Information about your transactions, such as the purchase and redemption of fund shares, account balances and parties to the transactions, which we receive from our affiliates or other third parties.

**Sharing of Personal Information**
We may share your personal information with our affiliates so that they may process and service your transactions.

However, Alger never sells customer lists to any third party. Further, we do not disclose personal information to nonaffiliated third parties, except as required by law or as permitted by law to service your account, such as follows:

- To third-party service providers that assist us in servicing your accounts (e.g. securities clearinghouses);
- To governmental agencies and law enforcement officials (e.g. valid subpoenas, court orders); and
- To financial institutions that perform marketing services on our behalf or with whom we have joint marketing agreements that provide for the confidentiality of personal information.

**Our Security Practices**
We protect your personal information by maintaining physical, electronic and procedural safeguards. When you visit Alger's Internet sites your information is protected by our systems that utilize 128-bit data encryption, Secure Socket Layer (SSL) protocol, user names, passwords and other precautions. We have implemented safeguards to ensure that access to customer information is limited to employees, such as customer service representatives, who require such information to carry out their job responsibilities. Our employees are aware of their strict responsibility to respect the confidentiality of your personal information.

Thank you for choosing to invest with Alger. We value your relationship with us and assure you we will abide by our policy to protect your information.

## Proxy Voting Policies

A description of the policies and procedures the Fund uses to determine how to vote proxies relating to portfolio securities and the proxy voting record is available, without charge, by calling (800) 992-3863 or online on the Fund's website at http://www.alger.com or on the SEC's website at http://www.sec.gov

## Fund Holdings

The Portfolio's most recent month end portfolio holdings are available approximately sixty days after month end on the Fund's website at www.alger.com. The Portfolio also files its complete schedule of portfolio holdings with the SEC for the first and third quarter of each fiscal year on Form N-Q. Forms N-Q are available online on the SEC's website at www.sec.gov or may be reviewed and copied at the SEC's Public Reference Room in Washington, D.C. Information regarding the operation of the SEC's Public Reference Room may be obtained by calling 1-800-SEC-0330. A copy of the most recent quarterly holdings may also be obtained from the Fund by calling (800) 992-3863.

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## THE ALGER PORTFOLIOS

111 Fifth Avenue
New York, NY 10003
(800) 992-3862
www.alger.com

### Investment Advisor

Fred Alger Management, Inc.
111 Fifth Avenue
New York, NY 10003

### Distributor

Fred Alger & Company, Incorporated
111 Fifth Avenue
New York, NY 10003

### Transfer Agent and Dividend Disbursing Agent

Boston Financial Data Services, Inc.
P.O. Box 8480
Boston, MA 02266

This report is submitted for the general information of the shareholders of The Alger American Fund. It is not authorized for distribution to prospective investors unless accompanied by an effective Prospectus for the Trust, which contains information concerning the Trust's investment policies, fees and expenses as well as other pertinent information.

ALGER

Inspired by Change, Driven by Growth.

CREDIT SUISSE

# CREDIT SUISSE FUNDS

## Annual Report

December 31, 2010

## CREDIT SUISSE TRUST
## ▪ INTERNATIONAL EQUITY FLEX III PORTFOLIO

Credit Suisse Trust (the "Trust") shares are not available directly to individual investors, but may be offered only through certain insurance products and pension and retirement plans.

The Trust's investment objectives, risks, charges and expenses (which should be considered carefully before investing), and more complete information about the Trust, are provided in the *Prospectus*, which should be read carefully before investing. You may obtain additional copies by calling 800-222-8977 or by writing to Credit Suisse Trust, P.O. Box 55030, Boston, MA 02205-5030.

Credit Suisse Asset Management Securities, Inc., Distributor, is located at Eleven Madison Avenue, New York, NY 10010. The Trust is advised by Credit Suisse Asset Management, LLC.

*The views of the Portfolio's management are as of the date of the letter and the Portfolio holdings described in this document are as of December 31, 2010; these views and Portfolio holdings may have changed subsequent to these dates. Nothing in this document is a recommendation to purchase or sell securities.*

*Portfolio shares are not deposits or other obligations of Credit Suisse Asset Management, LLC ("Credit Suisse") or any affiliate, are not FDIC-insured and are not guaranteed by Credit Suisse or any affiliate. Portfolio investments are subject to investment risks, including loss of your investment.*

**Credit Suisse Trust — International Equity Flex III Portfolio**
**Annual Investment Adviser's Report**
December 31, 2010 (unaudited)

February 3, 2011

Dear Shareholder:

For the year ended December 31, 2010, the Credit Suisse Trust — International Equity Flex III Portfolio (the "Portfolio") had a gain of 12.23%[1] versus an increase of 7.75% for the MSCI EAFE Index Net Dividends.[2]

**Market Review: A positive end to a challenging year**

The year ended December 31, 2010, was a volatile one for equities. After three quarters of choppy trading, global equity markets had a robust fourth quarter and, in general, finished the year higher. For the 12-month period, the MSCI World Index increased 11.76%, while the Dow Jones Euro STOXX Index gained 2.69%, and the FTSE All Share Index rose 14.52%. In Japan, the Topix Index finished the year up 0.96%.

Fairly encouraging economic data reports and cooperative central bankers in the United States and Europe combined with impressive economic growth in developing regions to help ease investor concerns about the threat of a double-dip recession. This change in sentiment boosted stock prices, especially during the last month of the year. Additionally, the U.S. Federal Reserve's anti-deflationary policy of implementing multiple quantitative easing measures — the first worth approximately $1.7 trillion and the second worth approximately $600 billion — together with the extension of Bush-era tax cuts injected liquidity into the global markets. In Europe, sovereign debt worries led the European Central Bank to inject liquidity into the region's troubled banks. In Asia, developing economies were on the verge of overheating, especially in China. The People's Bank of China acted several times throughout the course of the year to curb inflation by raising bank reserve requirements, but these actions were not enough to dampen equity prices in surrounding economies.

Additionally in the global market, Moody's downgraded Ireland's sovereign debt five times, warned Spain about looming debt problems, and placed Greece's sovereign debt under review for a possible downgrade. As of November 2010, inflation in China was reported at 5.10%, while the growth rate approached 9.6% over the period. Also, the Federal Reserve's dollar swap lines to the European Central Bank and the Bank of Japan were extended to August 1, 2011.

**Strategic Review and Outlook: Cautiously optimistic for the future**

For the year ended December 31, 2010, the Portfolio outperformed the benchmark due, in part, to both the Europe and Japan models. Momentum was a strong positive driver in Europe as many of the Mediterranean countries consistently underperformed Germany and the Nordic region throughout the year. And in Japan, our model benefited from the value factor as investors continued to seek bargains in a depressed economy. Overall, long positions were broadly supportive of portfolio outperformance, while short positions detracted from performance. Based on country positioning, long positions in the equities of Japan, the United Kingdom, and Sweden, as well as short positions in Spain and Italy supported portfolio performance. Short positions in the equities of Switzerland and France detracted from portfolio performance. Considering sector positioning, long positions in the industrials, materials, and consumer staples sectors, as well as short positions in the utilities sector, benefitted portfolio performance, while short positions in the consumer discretionary and energy sectors detracted from portfolio results.

Looking forward, we believe the European sovereign debt worries that were prevalent throughout the year may likely continue. Additionally, we expect that developing economies, led by China, may continue to grow at an outsized pace as 2011 progresses. This could force Central Bankers in these regions to take additional steps in order to cool their economies and mitigate any inflationary threats.

**Credit Suisse Quantitative Equities Group**

Mika Toikka
Timothy Schwider

*Short sales expose the Portfolio to the risk that it will be required to cover its short position at a time when the securities have appreciated in value, thus resulting in a loss to the Portfolio. The Portfolio's loss on a short sale could theoretically be unlimited in a case where the Portfolio is unable to close out its short position.*

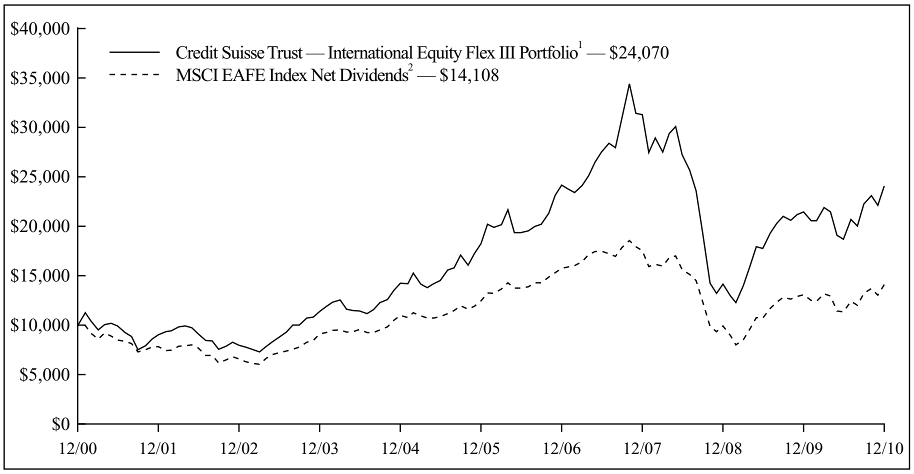
*The use of leverage subjects the Portfolio to the risk of magnified capital losses that can occur when losses affect an asset base that has been enlarged by borrowings or the creation of liabilities. The net asset value of the Portfolio, when employing leverage, will be more volatile and sensitive to market movements. Leverage may involve the creation of a liability that requires the Portfolio to pay interest.*

*International investing entails special risk considerations, including currency fluctuations, lower liquidity, economic and political risks, and differences in accounting methods.*

*Active and frequent trading increases transaction costs, which could detract from the Portfolio's performance.*

*In addition to historical information, this report contains forward-looking statements, which may concern, among other things, domestic and foreign market, industry and economic trends and developments and government regulation and their potential impact on the Portfolio's investments. These statements are subject to risks and uncertainties and actual trends, developments and regulations in the future, and their impact on the Portfolio could be materially different from those projected, anticipated or implied. The Portfolio has no obligation to update or revise forward-looking statements.*

### Comparison of Change in Value of $10,000 Investment in the Credit Suisse Trust — International Equity Flex III Portfolio[1] and the MSCI EAFE Index Net Dividends[2] for Ten Years.



**Average Annual Returns as of December 31, 2010[1]**

| 1 Year | 5 Years | 10 Years | Since Inception[3] |
| --- | --- | --- | --- |
| 12.23% | 5.70% | 9.18% | 7.21% |

*Returns represent past performance and include change in share price and reinvestment of dividends and capital gains.* ***Past performance cannot guarantee future results.*** *The current performance of the Portfolio may be lower or higher than the figures shown. Returns and share price will fluctuate, and redemption value may be more or less than original cost. The performance results do not reflect the deduction of taxes that a shareholder would pay on portfolio distributions or the redemption of portfolio shares. Performance includes the effect of deducting expenses, but does not include charges and expenses attributable to any particular variable contract or plan. Accordingly, the Prospectus of the sponsoring Participating Insurance Company separate account or plan documents or other informational materials supplied by plan sponsors should be carefully reviewed for information on relevant charges and expenses. Excluding these charges and expenses from quotations of performance has the effect of increasing the performance quoted, and the effect of these charges should be considered when comparing performance to that of other mutual funds. Performance information current to the most recent month-end is available at www.credit-suisse.com/us.*

*The annualized gross expense ratio is 2.43%. The annualized net expense ratio after fee waivers and/or expense reimbursements is 1.99%.*

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1 Fee waivers and/or expense reimbursements may reduce expenses for the Portfolio, without which performance would be lower. Waivers and/or reimbursements may be discontinued at any time.

2 The Morgan Stanley Capital International EAFE (Europe, Australasia, Far East) Index Net Dividends is a free float-adjusted market capitalization index that is designed to measure developed-market equity performance, excluding the U.S. and Canada. It is the exclusive property of Morgan Stanley Capital International Inc. Investors cannot invest directly in an index.

3 Inception date 12/31/97.

### Information About Your Portfolio's Expenses

As an investor of the Portfolio, you incur two types of costs: ongoing expenses and transaction costs. Ongoing expenses include management fees, distribution and service (12b-1) fees and other Portfolio expenses. Examples of transaction costs include sales charges (loads), redemption fees and account maintenance fees, which are not shown in this section and which would result in higher total expenses. The following table is intended to help you understand your ongoing expenses of investing in the Portfolio and to help you compare these expenses with the ongoing expenses of investing in other mutual funds. The table is based on an investment of $1,000 made at the beginning of the six month period ended December 31, 2010.

The table illustrates your Portfolio's expenses in two ways:

- **Actual Portfolio Return.** This helps you estimate the actual dollar amount of ongoing expenses paid on a $1,000 investment in the Portfolio using the Portfolio's actual return during the period. To estimate the expenses you paid over the period, simply divide your account value by $1,000 (for example, an $8,600 account value divided by $1,000 = 8.6), then multiply the result by the number in the "Expenses Paid per $1,000" line under the share class you hold.
- **Hypothetical 5% Portfolio Return.** This helps you to compare your Portfolio's ongoing expenses with those of other mutual funds using the Portfolio's actual expense ratio and a hypothetical rate of return of 5% per year before expenses. Examples using a 5% hypothetical portfolio return may be found in the shareholder reports of other mutual funds. The hypothetical account values and expenses may not be used to estimate the actual ending account balance or expenses you paid for the period.

Please note that the expenses shown in these tables are meant to highlight your ongoing expenses only and do not reflect any transaction costs, such as sales charges (loads) or redemption fees. If these transaction costs had been included, your costs would have been higher. The "Expenses Paid per $1,000" line of the tables is useful in comparing ongoing expenses only and will not help you determine the relative total expenses of owning different funds.

**Expenses and Value for a $1,000 Investment for the six month period ended December 31, 2010**

| | |
|---|---|
| **Actual Portfolio Return** | |
| Beginning Account Value 7/1/10 | $1,000.00 |
| Ending Account Value 12/31/10 | $1,287.00 |
| Expenses Paid per $1,000* | $ 9.51 |
| **Hypothetical 5% Portfolio Return** | |
| Beginning Account Value 7/1/10 | $1,000.00 |
| Ending Account Value 12/31/10 | $1,016.89 |
| Expenses Paid per $1,000* | $ 8.39 |
| **Annualized Expense Ratio*** | 1.65% |

* *Expenses are equal to the Portfolio's annualized expense ratio multiplied by the average account value over the period, multiplied by the number of days in the most recent fiscal half year period, then divided by 365.*

*The "Expenses Paid per $1,000" and the "Annualized Expense Ratio" in the tables are based on actual expenses paid by the Portfolio during the period, net of fee waivers and/or expense reimbursements. If those fee waivers and/or expense reimbursements had not been in effect, the Portfolio's actual expenses would have been higher. Expenses do not reflect additional charges and expenses that are, or may be, imposed under the variable contracts or plans. Such charges and expenses are described in the prospectus of the insurance company separate account or in the plan documents or other informational materials supplied by plan sponsors. The Portfolio's expenses should be considered with these charges and expenses in evaluating the overall cost of investing in the separate account.*

For more information, please refer to the Portfolio's prospectus.

**SECTOR BREAKDOWN***

| | Long | Short | Net |
|---|---|---|---|
| Financials | 29.6% | (5.2)% | 24.4% |
| Industrials | 20.0% | (5.4)% | 14.6% |
| Energy | 10.2% | (0.7)% | 9.5% |
| Materials | 12.5% | (3.0)% | 9.5% |
| Consumer Staples | 10.5% | (1.9)% | 8.6% |
| Health Care | 10.9% | (2.5)% | 8.4% |
| Consumer Discretionary | 11.8% | (4.1)% | 7.7% |
| Telecommunication Services | 7.1% | (0.5)% | 6.6% |
| Information Technology | 5.9% | (1.0)% | 4.9% |
| Utilities | 6.0% | (0.9)% | 5.1% |
| Short-Term Investments | 0.7% | (0.0)% | 0.7% |
| **Total** | **125.2%** | **(25.2)%** | **100.0%** |

* Expressed as a percentage of total long/short investments, respectively, (excluding security lending collateral if applicable) and may vary over time.

## Credit Suisse Trust — International Equity Flex III Portfolio
## Schedule of Investments
December 31, 2010

| | Number of Shares | Value |
|---|---|---|
| **LONG STOCK POSITIONS** (124.5%) | | |
| **COMMON STOCKS** (123.6%) | | |
| **Asia** (3.2%) | | |
| *Diversified Financial Services* (3.2%) | | |
| iShares MSCI Pacific ex-Japan Index Fund§ | 87,803 | $ 4,124,985 |
| *TOTAL ASIA* | | 4,124,985 |
| **Australia** (6.7%) | | |
| *Air Freight & Logistics* (0.0%) | | |
| Toll Holdings, Ltd.§ | 5,727 | 33,681 |
| *Airlines* (0.0%) | | |
| Qantas Airways, Ltd.* | 9,568 | 24,912 |
| *Beverages* (0.1%) | | |
| Coca-Cola Amatil, Ltd. | 4,837 | 53,905 |
| Foster's Group, Ltd. | 16,635 | 96,917 |
| | | 150,822 |
| *Biotechnology* (0.2%) | | |
| CSL, Ltd. | 4,854 | 180,588 |
| *Capital Markets* (0.1%) | | |
| Macquarie Group, Ltd. | 2,868 | 108,765 |
| *Chemicals* (0.1%) | | |
| DuluxGroup, Ltd. | 3,103 | 8,741 |
| Incitec Pivot, Ltd. | 13,901 | 56,479 |
| Nufarm, Ltd.* | 1,630 | 8,592 |
| Orica, Ltd. | 3,103 | 79,309 |
| | | 153,121 |
| *Commercial Banks* (1.8%) | | |
| Australia & New Zealand Banking Group, Ltd. | 21,593 | 516,886 |
| Bendigo and Adelaide Bank, Ltd. | 3,018 | 30,803 |
| Commonwealth Bank of Australia§ | 13,226 | 688,742 |
| National Australia Bank, Ltd. | 18,065 | 439,249 |
| Suncorp Group, Ltd. | 10,956 | 96,694 |
| Westpac Banking Corp.§ | 25,365 | 577,507 |
| | | 2,349,881 |
| *Commercial Services & Supplies* (0.1%) | | |
| Brambles, Ltd. | 12,173 | 88,864 |
| *Construction & Engineering* (0.0%) | | |
| Leighton Holdings, Ltd.§ | 1,285 | 40,591 |
| *Construction Materials* (0.0%) | | |
| Boral, Ltd. | 5,132 | 25,443 |
| *Containers & Packaging* (0.1%) | | |
| Amcor, Ltd. | 10,524 | 72,827 |

See Accompanying Notes to Financial Statements.

| | Number of Shares | Value |
|---|---|---|
| **LONG STOCK POSITIONS** | | |
| **COMMON STOCKS** | | |
| **Australia** | | |
| *Diversified Financial Services* (0.4%) | | |
| ASX, Ltd. | 1,484 | $ 57,329 |
| iShares MSCI Australia Index Fund | 18,568 | 472,370 |
| | | 529,699 |
| *Diversified Telecommunication Services* (0.1%) | | |
| Telstra Corp., Ltd.§ | 37,543 | 107,343 |
| *Electric Utilities* (0.0%) | | |
| SP AusNet | 11,478 | 10,234 |
| *Energy Equipment & Services* (0.0%) | | |
| WorleyParsons, Ltd. | 1,426 | 39,142 |
| *Food & Staples Retailing* (0.5%) | | |
| Metcash, Ltd. | 6,596 | 27,774 |
| Wesfarmers, Ltd. | 8,665 | 284,484 |
| Wesfarmers, Ltd. | 1,309 | 43,394 |
| Woolworths, Ltd. | 10,684 | 295,686 |
| | | 651,338 |
| *Food Products* (0.0%) | | |
| Goodman Fielder, Ltd. | 11,304 | 15,591 |
| *Health Care Equipment & Supplies* (0.0%) | | |
| Cochlear, Ltd. | 485 | 40,013 |
| *Health Care Providers & Services* (0.0%) | | |
| Sonic Healthcare, Ltd. | 3,181 | 37,897 |
| *Hotels, Restaurants & Leisure* (0.1%) | | |
| Aristocrat Leisure, Ltd.§ | 3,448 | 10,576 |
| Crown, Ltd. | 4,340 | 36,734 |
| TABCORP Holdings, Ltd. | 5,239 | 38,178 |
| Tatts Group, Ltd. | 10,447 | 27,647 |
| | | 113,135 |
| *Industrial Conglomerates* (0.0%) | | |
| CSR, Ltd.§ | 12,406 | 21,358 |
| *Insurance* (0.3%) | | |
| AMP, Ltd.§ | 17,660 | 95,770 |
| AXA Asia Pacific Holdings, Ltd. | 8,909 | 57,659 |
| Insurance Australia Group, Ltd. | 17,922 | 71,335 |
| QBE Insurance Group, Ltd. | 8,831 | 164,362 |
| | | 389,126 |
| *IT Services* (0.0%) | | |
| Computershare, Ltd. | 3,832 | 42,329 |
| *Media* (0.0%) | | |
| Fairfax Media, Ltd.§ | 18,247 | 26,223 |

| | Number of Shares | Value |
|---|---|---|
| **LONG STOCK POSITIONS** | | |
| **COMMON STOCKS** | | |
| **Australia** | | |
| *Metals & Mining* (1.7%) | | |
| Alumina, Ltd. | 21,036 | $ 53,593 |
| BHP Billiton, Ltd.§ | 28,931 | 1,348,284 |
| BlueScope Steel, Ltd. | 15,718 | 36,204 |
| Fortescue Metals Group, Ltd.* | 10,669 | 71,676 |
| Newcrest Mining, Ltd. | 4,169 | 173,305 |
| OneSteel, Ltd. | 11,451 | 30,402 |
| OZ Minerals, Ltd.§ | 26,908 | 47,628 |
| Rio Tinto, Ltd.§ | 3,756 | 329,625 |
| Sims Metal Management, Ltd. | 1,389 | 30,619 |
| | | 2,121,336 |
| *Multi-Utilities* (0.1%) | | |
| AGL Energy, Ltd.§ | 3,869 | 60,447 |
| *Multiline Retail* (0.0%) | | |
| Harvey Norman Holdings, Ltd.§ | 4,704 | 14,179 |
| *Oil, Gas & Consumable Fuels* (0.4%) | | |
| Caltex Australia, Ltd. | 1,163 | 17,128 |
| Dart Energy, Ltd.*§ | 2,525 | 2,983 |
| Energy Resources of Australia, Ltd.§ | 575 | 6,562 |
| Origin Energy, Ltd. | 7,570 | 129,356 |
| Paladin Energy, Ltd.*§ | 5,564 | 28,105 |
| Santos, Ltd. | 7,170 | 96,746 |
| Woodside Petroleum, Ltd. | 4,689 | 204,705 |
| | | 485,585 |
| *Real Estate Investment Trusts* (0.4%) | | |
| CFS Retail Property Trust§ | 14,987 | 27,028 |
| Dexus Property Group§ | 41,087 | 33,473 |
| Goodman Group§ | 52,342 | 34,862 |
| GPT Group | 15,995 | 48,268 |
| Mirvac Group | 23,177 | 29,144 |
| Stockland§ | 20,543 | 75,837 |
| Westfield Group | 17,905 | 175,771 |
| Westfield Retail Trust* | 17,905 | 47,169 |
| | | 471,552 |
| *Real Estate Management & Development* (0.1%) | | |
| Lend Lease Corp., Ltd. | 5,378 | 47,590 |
| *Road & Rail* (0.0%) | | |
| Asciano Group* | 23,963 | 39,206 |
| *Textiles, Apparel & Luxury Goods* (0.0%) | | |
| Billabong International, Ltd.§ | 1,743 | 14,567 |

| | Number of Shares | Value |
|---|---|---|
| **LONG STOCK POSITIONS** | | |
| **COMMON STOCKS** | | |
| **Australia** | | |
| *Transportation Infrastructure* (0.1%) | | |
| Macquarie Airports | 6,208 | $ 19,017 |
| Macquarie Atlas Roads Group*§ | 4,636 | 7,210 |
| Transurban Group§ | 10,009 | 52,662 |
| | | 78,889 |
| *TOTAL AUSTRALIA* | | 8,586,274 |
| **Austria** (1.0%) | | |
| *Air Freight & Logistics* (0.3%) | | |
| Oesterreichische Post AG | 10,552 | 350,301 |
| *Construction & Engineering* (0.2%) | | |
| Strabag SE BR | 9,658 | 266,492 |
| *Insurance* (0.1%) | | |
| Vienna Insurance Group | 1,245 | 65,144 |
| *Machinery* (0.2%) | | |
| Andritz AG | 2,963 | 273,970 |
| *Metals & Mining* (0.2%) | | |
| Voestalpine AG | 6,124 | 294,065 |
| *Real Estate Management & Development* (0.0%) | | |
| Immofinanz Anspt Nachb*§^ | 2,201 | 0 |
| *TOTAL AUSTRIA* | | 1,249,972 |
| **Belgium** (1.4%) | | |
| *Beverages* (0.7%) | | |
| Anheuser-Busch InBev NV | 15,313 | 878,404 |
| *Diversified Telecommunication Services* (0.3%) | | |
| Belgacom SA | 13,259 | 447,211 |
| *Electrical Equipment* (0.2%) | | |
| Bekaert SA | 2,382 | 274,415 |
| *Food & Staples Retailing* (0.2%) | | |
| Colruyt SA | 2,129 | 108,691 |
| Delhaize Group SA | 1,260 | 93,547 |
| | | 202,238 |
| *TOTAL BELGIUM* | | 1,802,268 |
| **Bermuda** (0.3%) | | |
| *Energy Equipment & Services* (0.1%) | | |
| Seadrill, Ltd.§ | 4,752 | 162,735 |
| *Insurance* (0.2%) | | |
| Catlin Group, Ltd. | 42,468 | 246,511 |
| *TOTAL BERMUDA* | | 409,246 |

See Accompanying Notes to Financial Statements.

| | Number of Shares | Value |
|---|---|---|
| **LONG STOCK POSITIONS** | | |
| **COMMON STOCKS** | | |
| **Cyprus** (0.1%) | | |
| *Energy Equipment & Services* (0.1%) | | |
| ProSafe SE | 20,969 | $ 167,689 |
| *TOTAL CYPRUS* | | 167,689 |
| **Denmark** (2.3%) | | |
| *Beverages* (0.3%) | | |
| Carlsberg AS Class B | 3,645 | 367,396 |
| *Commercial Banks* (0.0%) | | |
| Danske Bank AS* | 1,123 | 28,920 |
| *Construction & Engineering* (0.0%) | | |
| FLSmidth & Co. AS | 631 | 60,626 |
| *Food Products* (0.2%) | | |
| Danisco AS | 2,785 | 256,481 |
| *Health Care Equipment & Supplies* (0.4%) | | |
| Coloplast AS Class B | 3,475 | 474,200 |
| *Insurance* (0.2%) | | |
| Topdanmark AS* | 996 | 132,219 |
| Tryg AS | 3,682 | 170,507 |
| | | 302,726 |
| *Marine* (0.5%) | | |
| A P Moller - Maersk AS Class A | 21 | 185,781 |
| A P Moller - Maersk AS Class B | 46 | 418,207 |
| | | 603,988 |
| *Pharmaceuticals* (0.7%) | | |
| H Lundbeck AS§ | 7,989 | 152,834 |
| Novo Nordisk AS Class B§ | 6,933 | 784,366 |
| | | 937,200 |
| *TOTAL DENMARK* | | 3,031,537 |
| **Finland** (3.9%) | | |
| *Communications Equipment* (0.4%) | | |
| Nokia Oyj | 56,707 | 589,722 |
| *Construction & Engineering* (0.3%) | | |
| YIT Oyj | 13,988 | 350,906 |
| *Electric Utilities* (0.5%) | | |
| Fortum Oyj | 20,735 | 627,892 |
| *Food & Staples Retailing* (0.2%) | | |
| Kesko Oyj B Shares | 5,374 | 252,114 |
| *Insurance* (0.4%) | | |
| Sampo Oyj A Shares | 19,819 | 532,031 |

See Accompanying Notes to Financial Statements.

| | Number of Shares | Value |
|---|---|---|
| **LONG STOCK POSITIONS** | | |
| **COMMON STOCKS** | | |
| **Finland** | | |
| *Machinery* (1.1%) | | |
| Kone Oyj Class B | 9,137 | $ 509,482 |
| Konecranes Oyj | 5,238 | 217,276 |
| Metso Oyj | 6,684 | 375,373 |
| Wartsila Oyj | 4,840 | 370,275 |
| | | 1,472,406 |
| *Paper & Forest Products* (0.6%) | | |
| Stora Enso Oyj R Shares§ | 23,266 | 240,372 |
| UPM-Kymmene Oyj | 29,123 | 518,314 |
| | | 758,686 |
| *Pharmaceuticals* (0.4%) | | |
| Orion Oyj Class B§ | 21,272 | 467,525 |
| *TOTAL FINLAND* | | 5,051,282 |
| **France** (11.8%) | | |
| *Aerospace & Defense* (0.3%) | | |
| Safran SA | 4,325 | 153,916 |
| Zodiac Aerospace | 2,380 | 179,663 |
| | | 333,579 |
| *Auto Components* (0.3%) | | |
| Compagnie Generale des Etablissements Michelin Class B | 4,024 | 289,998 |
| Valeo SA* | 821 | 46,780 |
| | | 336,778 |
| *Automobiles* (0.3%) | | |
| PSA Peugeot Citroen* | 3,084 | 117,642 |
| Renault SA*§ | 3,962 | 231,542 |
| | | 349,184 |
| *Building Products* (0.2%) | | |
| Cie de Saint-Gobain | 5,659 | 292,613 |
| *Chemicals* (0.2%) | | |
| Arkema SA | 3,644 | 263,811 |
| *Commercial Banks* (1.5%) | | |
| BNP Paribas | 17,130 | 1,095,230 |
| Credit Agricole SA | 16,929 | 216,109 |
| Natixis* | 36,398 | 170,929 |
| Societe Generale | 8,184 | 442,083 |
| | | 1,924,351 |
| *Commercial Services & Supplies* (0.0%) | | |
| Societe BIC SA | 590 | 50,921 |

See Accompanying Notes to Financial Statements.

| | Number of Shares | Value |
|---|---|---|
| **LONG STOCK POSITIONS** | | |
| **COMMON STOCKS** | | |
| **France** | | |
| *Construction & Engineering* (0.9%) | | |
| Bouygues SA | 11,597 | $ 502,473 |
| Vinci SA | 13,348 | 729,217 |
| | | 1,231,690 |
| *Diversified Financial Services* (0.2%) | | |
| Eurazeo | 4,450 | 331,495 |
| *Diversified Telecommunication Services* (0.7%) | | |
| France Telecom SA | 40,877 | 858,741 |
| *Electrical Equipment* (0.9%) | | |
| Legrand SA | 11,192 | 458,312 |
| Nexans SA | 598 | 47,289 |
| Schneider Electric SA | 4,169 | 627,535 |
| | | 1,133,136 |
| *Energy Equipment & Services* (0.2%) | | |
| Technip SA | 2,779 | 257,880 |
| *Food & Staples Retailing* (0.1%) | | |
| Carrefour SA | 3,438 | 142,314 |
| *Food Products* (0.0%) | | |
| Danone | 668 | 42,167 |
| *Industrial Conglomerates* (0.1%) | | |
| Wendel | 1,720 | 159,174 |
| *Insurance* (1.0%) | | |
| AXA SA | 34,320 | 573,512 |
| CNP Assurances | 15,893 | 287,979 |
| SCOR SE | 18,418 | 469,900 |
| | | 1,331,391 |
| *IT Services* (0.0%) | | |
| Cap Gemini SA | 503 | 23,607 |
| *Machinery* (0.2%) | | |
| Vallourec SA | 2,035 | 214,797 |
| *Media* (0.8%) | | |
| M6-Metropole Television | 2,379 | 57,857 |
| PagesJaunes Groupe§ | 24,298 | 221,816 |
| Vivendi SA | 29,538 | 801,296 |
| | | 1,080,969 |
| *Multi-Utilities* (0.8%) | | |
| GDF Suez | 22,489 | 810,864 |
| Veolia Environnement SA | 6,145 | 180,578 |
| | | 991,442 |

| | Number of Shares | Value |
|---|---|---|
| **LONG STOCK POSITIONS** | | |
| **COMMON STOCKS** | | |
| **France** | | |
| *Office Electronics* (0.1%) | | |
| Neopost SA§ | 1,132 | $ 99,108 |
| *Oil, Gas & Consumable Fuels* (1.4%) | | |
| Total SA | 32,938 | 1,761,242 |
| *Pharmaceuticals* (1.0%) | | |
| Ipsen SA§ | 1,853 | 56,797 |
| Sanofi-Aventis SA | 18,568 | 1,195,078 |
| | | 1,251,875 |
| *Real Estate Investment Trusts* (0.3%) | | |
| Fonciere Des Regions§ | 3,816 | 370,772 |
| Mercialys SA | 1 | 38 |
| | | 370,810 |
| *Textiles, Apparel & Luxury Goods* (0.3%) | | |
| Christian Dior SA | 962 | 138,138 |
| LVMH Moet Hennessy Louis Vuitton SA | 1,189 | 196,602 |
| | | 334,740 |
| *TOTAL FRANCE* | | 15,167,815 |
| **Germany** (9.9%) | | |
| *Automobiles* (1.0%) | | |
| Bayerische Motoren Werke AG§ | 7,901 | 624,938 |
| Daimler AG*§ | 9,121 | 619,592 |
| Volkswagen AG§ | 761 | 108,365 |
| | | 1,352,895 |
| *Capital Markets* (0.2%) | | |
| Deutsche Bank AG | 6,207 | 325,874 |
| *Chemicals* (1.1%) | | |
| BASF SE§ | 10,358 | 829,841 |
| Lanxess AG | 3,325 | 262,462 |
| Linde AG | 528 | 80,189 |
| Symrise AG | 9,380 | 258,023 |
| | | 1,430,515 |
| *Computers & Peripherals* (0.2%) | | |
| Wincor Nixdorf AG | 2,700 | 221,888 |
| *Construction & Engineering* (0.1%) | | |
| Bilfinger Berger AG | 1,088 | 92,460 |
| *Diversified Telecommunication Services* (0.6%) | | |
| Deutsche Telekom AG§ | 63,770 | 825,297 |
| *Electric Utilities* (0.7%) | | |
| E.ON AG | 27,545 | 844,492 |

| | Number of Shares | Value |
|---|---|---|
| **LONG STOCK POSITIONS** | | |
| **COMMON STOCKS** | | |
| **Germany** | | |
| *Electrical Equipment* (0.1%) | | |
| Tognum AG | 6,961 | $ 183,961 |
| *Food Products* (0.2%) | | |
| Suedzucker AG | 9,400 | 252,026 |
| *Health Care Providers & Services* (0.3%) | | |
| Fresenius SE | 4,690 | 395,102 |
| *Hotels, Restaurants & Leisure* (0.2%) | | |
| TUI AG*§ | 20,085 | 282,859 |
| *Household Products* (0.2%) | | |
| Henkel AG & Co. KGaA | 5,481 | 283,705 |
| *Industrial Conglomerates* (1.2%) | | |
| Siemens AG | 12,166 | 1,512,970 |
| *Insurance* (1.7%) | | |
| Allianz SE | 8,728 | 1,041,090 |
| Hannover Rueckversicherung AG | 8,608 | 463,585 |
| Muenchener Rueckversicherungs AG§ | 4,918 | 747,776 |
| | | 2,252,451 |
| *Life Sciences Tools & Services* (0.1%) | | |
| Gerresheimer AG* | 2,115 | 93,325 |
| *Machinery* (0.1%) | | |
| GEA Group AG | 2,468 | 71,601 |
| *Metals & Mining* (0.3%) | | |
| Aurubis AG | 6,610 | 389,148 |
| *Multi-Utilities* (0.2%) | | |
| RWE AG | 2,995 | 200,820 |
| *Pharmaceuticals* (0.9%) | | |
| Bayer AG§ | 11,585 | 862,134 |
| Merck KGaA | 2,779 | 223,360 |
| Stada Arzneimittel AG | 922 | 31,530 |
| | | 1,117,024 |
| *Semiconductors & Semiconductor Equipment* (0.1%) | | |
| Infineon Technologies AG* | 19,038 | 178,155 |
| *Software* (0.3%) | | |
| SAP AG | 6,910 | 353,811 |
| *Textiles, Apparel & Luxury Goods* (0.1%) | | |
| Adidas AG | 1,188 | 77,581 |
| *TOTAL GERMANY* | | 12,737,960 |

| | Number of Shares | Value |
|---|---|---|
| **LONG STOCK POSITIONS** | | |
| **COMMON STOCKS** | | |
| **Greece** (0.3%) | | |
| *Commercial Banks* (0.1%) | | |
| Bank of Greece | 788 | $ 30,592 |
| National Bank of Greece SA* | 11,016 | 89,982 |
| | | 120,574 |
| *Electric Utilities* (0.1%) | | |
| Public Power Corp. SA | 7,529 | 109,105 |
| *Hotels, Restaurants & Leisure* (0.1%) | | |
| OPAP SA | 12,501 | 217,307 |
| *TOTAL GREECE* | | 446,986 |
| **Hong Kong** (2.1%) | | |
| *Diversified Financial Services* (2.1%) | | |
| iShares MSCI Hong Kong Index Fund§ | 140,878 | 2,664,003 |
| *TOTAL HONG KONG* | | 2,664,003 |
| **Israel** (0.6%) | | |
| *Chemicals* (0.0%) | | |
| Israel Chemicals, Ltd. | 1,555 | 26,685 |
| *Commercial Banks* (0.1%) | | |
| Bank Hapoalim BM* | 12,051 | 62,865 |
| Bank Leumi Le-Israel BM | 7,305 | 37,518 |
| | | 100,383 |
| *Diversified Telecommunication Services* (0.1%) | | |
| Bezeq Israeli Telecommunication Corp., Ltd. | 21,142 | 64,492 |
| *Pharmaceuticals* (0.4%) | | |
| Teva Pharmaceutical Industries, Ltd. ADR | 11,700 | 609,921 |
| *TOTAL ISRAEL* | | 801,481 |
| **Italy** (2.4%) | | |
| *Auto Components* (0.2%) | | |
| Pirelli & C. SpA§ | 27,040 | 219,674 |
| *Automobiles* (0.3%) | | |
| Fiat SpA | 18,390 | 381,818 |
| *Construction Materials* (0.0%) | | |
| Italcementi SpA§ | 3,275 | 27,836 |
| *Electric Utilities* (1.0%) | | |
| Enel SpA | 157,903 | 794,364 |
| Terna Rete Elettrica Nazionale SpA | 113,052 | 479,679 |
| | | 1,274,043 |
| *Electrical Equipment* (0.0%) | | |
| Prysmian SpA | 2,420 | 41,405 |

| | Number of Shares | Value |
|---|---|---|
| **LONG STOCK POSITIONS** | | |
| **COMMON STOCKS** | | |
| **Italy** | | |
| *Media* (0.1%) | | |
| Mediaset SpA§ | 11,047 | $ 67,165 |
| *Oil, Gas & Consumable Fuels* (0.8%) | | |
| ENI SpA | 49,911 | 1,098,211 |
| *TOTAL ITALY* | | 3,110,152 |
| **Japan** (28.0%) | | |
| *Air Freight & Logistics* (0.0%) | | |
| VANTEC Corp. | 15 | 22,301 |
| *Auto Components* (0.8%) | | |
| Aisan Industry Co., Ltd. | 6,026 | 54,121 |
| Aisin Seiki Co., Ltd. | 2,789 | 98,378 |
| Alpha Corp. | 1,500 | 15,889 |
| Bridgestone Corp.§ | 6,400 | 123,323 |
| Calsonic Kansei Corp.* | 11,000 | 43,774 |
| Denso Corp.§ | 3,622 | 124,651 |
| Kanto Auto Works, Ltd. | 4,056 | 34,941 |
| Koito Manufacturing Co., Ltd.§ | 3,000 | 46,688 |
| NHK Spring Co., Ltd.§ | 3,000 | 32,549 |
| Nihon Tokushu Toryo Co., Ltd. | 2,100 | 8,909 |
| OSAKA Titanium Technologies Co., Ltd.§ | 5,400 | 56,227 |
| Pacific Industrial Co., Ltd. | 5,200 | 28,559 |
| Sanden Corp. | 16,000 | 63,579 |
| The Yokohama Rubber Co., Ltd | 15,809 | 81,510 |
| Tokai Rika Co., Ltd. | 1,200 | 22,636 |
| Tokai Rubber Industries, Inc. | 2,900 | 39,983 |
| Topre Corp. | 2,833 | 21,506 |
| Toyo Tire & Rubber Co., Ltd.§ | 27,725 | 66,720 |
| Toyota Industries Corp. | 1,200 | 37,166 |
| Unipres Corp.§ | 3,924 | 78,001 |
| | | 1,079,110 |
| *Automobiles* (1.9%) | | |
| Daihatsu Motor Co., Ltd. | 4,000 | 61,259 |
| Fuji Heavy Industries, Ltd. | 11,103 | 85,714 |
| Honda Motor Co., Ltd.§ | 18,292 | 722,720 |
| Isuzu Motors, Ltd.§ | 6,921 | 31,307 |
| Nissan Motor Co., Ltd.§ | 35,600 | 337,123 |
| Suzuki Motor Corp. | 4,731 | 116,262 |
| Toyota Motor Corp.§ | 27,245 | 1,073,717 |
| Yamaha Motor Co., Ltd.* | 461 | 7,489 |
| | | 2,435,591 |
| *Beverages* (0.1%) | | |
| Kirin Holdings Co., Ltd.§ | 8,823 | 123,528 |
| Mikuni Coca-Cola Bottling Co., Ltd.§ | 3,489 | 31,706 |
| Oenon Holdings, Inc.§ | 8,000 | 19,880 |
| | | 175,114 |

| | Number of Shares | Value |
|---|---|---|
| **LONG STOCK POSITIONS** | | |
| **COMMON STOCKS** | | |
| **Japan** | | |
| *Building Products* (0.3%) | | |
| Aica Kogyo Co., Ltd. | 1,168 | $ 13,724 |
| Asahi Glass Co., Ltd.§ | 13,000 | 151,346 |
| Bunka Shutter Co., Ltd. | 5,174 | 13,612 |
| Daikin Industries, Ltd. | 1,054 | 37,272 |
| JS Group Corp. | 3,700 | 81,247 |
| Komatsu Wall Industry Co., Ltd. | 1,200 | 11,351 |
| Nippon Sheet Glass Co., Ltd. | 23,626 | 63,437 |
| Toli Corp.§ | 7,000 | 12,122 |
| | | 384,111 |
| *Capital Markets* (0.4%) | | |
| Daiwa Securities Group, Inc.§ | 35,981 | 184,762 |
| Mizuho Securities Co., Ltd.§ | 40,000 | 114,180 |
| Nomura Holdings, Inc.§ | 26,457 | 168,048 |
| Tokai Tokyo Financial Holdings, Inc. | 23,573 | 89,145 |
| | | 556,135 |
| *Chemicals* (1.9%) | | |
| Achilles Corp. | 3,912 | 5,679 |
| ADEKA Corp. | 3,300 | 36,417 |
| Air Water, Inc. | 7,000 | 89,247 |
| Arakawa Chemical Industries, Ltd. | 3,100 | 32,194 |
| Asahi Kasei Corp. | 23,996 | 156,249 |
| Chugoku Marine Paints, Ltd. | 7,759 | 65,770 |
| Daicel Chemical Industries, Ltd.§ | 9,000 | 65,561 |
| Daiso Co., Ltd. | 8,000 | 24,094 |
| Denki Kagaku Kogyo KK | 12,000 | 56,876 |
| DIC Corp. | 22,000 | 49,087 |
| Ebara-Udylite Co., Ltd. | 800 | 16,784 |
| Fujikura Kasei Co., Ltd. | 6,657 | 45,764 |
| Hitachi Chemical Co., Ltd. | 1,200 | 24,757 |
| Ihara Chemical Industry Co., Ltd. | 3,000 | 9,623 |
| JSR Corp. | 2,300 | 42,735 |
| Kaneka Corp. | 19,000 | 131,411 |
| Konishi Co., Ltd. | 1,700 | 20,486 |
| Kuraray Co., Ltd. | 1,500 | 21,435 |
| Mitsubishi Chemical Holdings Corp. | 26,047 | 176,128 |
| Mitsubishi Gas Chemical Co., Inc. | 5,124 | 36,280 |
| Mitsui Chemicals, Inc. | 8,000 | 28,552 |
| Nihon Parkerizing Co., Ltd. | 2,000 | 28,772 |
| Nippon Kayaku Co., Ltd. | 2,000 | 21,107 |
| Nippon Soda Co., Ltd. | 20,554 | 97,853 |
| Nippon Valqua Industries, Ltd. | 3,000 | 9,119 |
| Nissan Chemical Industries, Ltd. | 6,000 | 77,496 |
| Nitto Denko Corp. | 1,600 | 75,120 |
| Okura Industrial Co., Ltd.* | 3,666 | 10,593 |
| Sakata INX Corp. | 8,000 | 40,209 |

| | Number of Shares | Value |
|---|---|---|
| **LONG STOCK POSITIONS** | | |
| **COMMON STOCKS** | | |
| **Japan** | | |
| *Chemicals* | | |
| Sanyo Chemical Industries, Ltd. | 3,643 | $ 30,349 |
| Sekisui Plastics Co., Ltd. | 5,000 | 22,526 |
| Shikoku Chemicals Corp. | 3,393 | 20,380 |
| Shin-Etsu Chemical Co., Ltd.§ | 6,500 | 350,695 |
| Showa Denko KK§ | 10,000 | 22,458 |
| Sumitomo Bakelite Co., Ltd. | 9,466 | 55,611 |
| Sumitomo Chemical Co., Ltd.§ | 27,184 | 133,586 |
| Sumitomo Seika Chemicals Co., Ltd. | 10,000 | 43,270 |
| Taiyo Nippon Sanso Corp.§ | 4,000 | 35,248 |
| Toagosei Co., Ltd.§ | 13,000 | 60,724 |
| Toray Industries, Inc.§ | 3,000 | 17,903 |
| Tosoh Corp.§ | 16,261 | 52,714 |
| Toyo Ink Manufacturing Co., Ltd. | 6,000 | 29,417 |
| Ube Industries, Ltd. | 35,000 | 104,914 |
| | | 2,475,193 |
| *Commercial Banks* (2.7%) | | |
| Fukuoka Financial Group, Inc. | 18,000 | 77,995 |
| Hokuhoku Financial Group, Inc. | 59,193 | 120,126 |
| Kiyo Holdings, Inc. | 41,649 | 58,060 |
| Mitsubishi UFJ Financial Group, Inc. | 167,931 | 906,453 |
| Mizuho Financial Group, Inc.§ | 273,954 | 514,442 |
| Resona Holdings, Inc.§ | 8,003 | 47,753 |
| Senshu Ikeda Holdings, Inc.§ | 5,000 | 7,129 |
| Shinsei Bank, Ltd.*§ | 19,000 | 24,754 |
| Sumitomo Mitsui Financial Group, Inc.§ | 18,696 | 662,665 |
| The Akita Bank, Ltd. | 6,000 | 17,801 |
| The Bank of Nagoya, Ltd. | 9,000 | 28,999 |
| The Bank of Saga, Ltd. | 13,000 | 36,815 |
| The Bank of Yokohama, Ltd. | 19,000 | 98,078 |
| The Chiba Bank, Ltd. | 9,992 | 64,858 |
| The Chiba Kogyo Bank, Ltd.* | 4,663 | 27,902 |
| The Daishi Bank, Ltd. | 23,039 | 71,116 |
| The Ehime Bank, Ltd.§ | 7,000 | 18,619 |
| The Eighteenth Bank, Ltd. | 6,666 | 18,587 |
| The Gunma Bank, Ltd. | 11,992 | 65,710 |
| The Higashi-Nippon Bank, Ltd. | 16,000 | 35,011 |
| The Hiroshima Bank, Ltd§ | 1,885 | 7,936 |
| The Hokuetsu Bank, Ltd. | 19,000 | 39,221 |
| The Hyakujushi Bank, Ltd. | 9,000 | 33,065 |
| The Joyo Bank, Ltd. | 10,000 | 43,879 |
| The Keiyo Bank, Ltd. | 16,968 | 83,916 |
| The Mie Bank, Ltd. | 13,211 | 36,211 |
| The Nishi-Nippon City Bank, Ltd. | 5,997 | 18,158 |
| The Ogaki Kyoritsu Bank, Ltd. | 32,000 | 101,124 |
| The Shizuoka Bank, Ltd. | 8,000 | 73,636 |

See Accompanying Notes to Financial Statements.

| | Number of Shares | Value |
|---|---|---|
| **LONG STOCK POSITIONS** | | |
| **COMMON STOCKS** | | |
| **Japan** | | |
| *Commercial Banks* | | |
| The Sumitomo Trust & Banking Co., Ltd.§ | 4,720 | $ 29,600 |
| The Tohoku Bank, Ltd. | 6,418 | 10,598 |
| The Tokyo Tomin Bank, Ltd.§ | 554 | 7,904 |
| The Yachiyo Bank, Ltd. | 1,750 | 45,939 |
| | | 3,434,060 |
| *Commercial Services & Supplies* (0.6%) | | |
| Central Security Patrols Co., Ltd. | 600 | 6,246 |
| Dai Nippon Printing Co., Ltd. | 13,000 | 176,508 |
| Duskin Co., Ltd. | 1,200 | 22,663 |
| Itoki Corp. | 3,037 | 8,197 |
| Kokuyo Co., Ltd.§ | 800 | 6,905 |
| Kyodo Printing Co., Ltd.§ | 9,000 | 21,264 |
| Nichiban Co., Ltd. | 3,000 | 11,154 |
| Nippon Kanzai Co., Ltd.§ | 550 | 9,095 |
| Nippon Kucho Service Co., Ltd. | 800 | 7,174 |
| Nissha Printing Co., Ltd.§ | 800 | 21,174 |
| Oyo Corp. | 2,156 | 17,930 |
| Pronexus, Inc. | 1,800 | 9,793 |
| Secom Co., Ltd. | 2,653 | 125,488 |
| Sohgo Security Services Co., Ltd. | 3,976 | 47,058 |
| Tokyu Community Corp. | 600 | 17,848 |
| Toppan Forms Co., Ltd. | 7,100 | 72,744 |
| Toppan Printing Co., Ltd. | 16,746 | 152,554 |
| Tosho Printing Co., Ltd.* | 5,499 | 8,919 |
| | | 742,714 |
| *Communications Equipment* (0.1%) | | |
| Denki Kogyo Co., Ltd. | 10,009 | 48,975 |
| Hitachi Kokusai Electric, Inc. | 3,000 | 29,724 |
| NEC Mobiling, Ltd. | 1,200 | 35,082 |
| | | 113,781 |
| *Computers & Peripherals* (0.4%) | | |
| Fujitsu, Ltd.§ | 32,000 | 221,940 |
| NEC Corp.§ | 47,260 | 141,550 |
| Toshiba Corp. | 29,871 | 162,288 |
| | | 525,778 |
| *Construction & Engineering* (0.7%) | | |
| Ando Corp. | 13,500 | 19,088 |
| Asunaro Aoki Construction Co., Ltd. | 2,500 | 10,514 |
| Chugai Ro Co., Ltd. | 8,000 | 29,407 |
| CTI Engineering Co., Ltd. | 2,071 | 11,572 |
| Hazama Corp.* | 11,866 | 9,916 |
| Hibiya Engineering, Ltd. | 2,000 | 18,909 |

See Accompanying Notes to Financial Statements.

| | Number of Shares | Value |
|---|---|---|
| **LONG STOCK POSITIONS** | | |
| **COMMON STOCKS** | | |
| **Japan** | | |
| *Construction & Engineering* | | |
| Ichiken Co., Ltd. | 5,800 | $ 8,423 |
| Kajima Corp.§ | 36,000 | 95,556 |
| Mirait Holdings Corp.* | 5,300 | 37,379 |
| Nakano Corp. | 3,500 | 9,802 |
| Nippo Corp. | 8,735 | 60,788 |
| Nippon Koei Co., Ltd. | 8,000 | 24,019 |
| Nishimatsu Construction Co., Ltd. | 34,268 | 44,577 |
| Obayashi Corp. | 23,992 | 110,255 |
| Obayashi Road Corp. | 11,000 | 20,807 |
| Okumura Corp. | 5,000 | 19,014 |
| Seibu Electric Industry Co., Ltd. | 1,998 | 8,514 |
| Shimizu Corp. | 10,000 | 42,643 |
| Shinnihon Corp. | 2,308 | 6,011 |
| Sumitomo Densetsu Co., Ltd. | 5,058 | 21,458 |
| Taihei Kogyo Co., Ltd. | 5,968 | 27,959 |
| Taisei Corp. | 51,379 | 119,927 |
| The Nippon Road Co., Ltd. | 18,000 | 42,966 |
| Toa Corp. | 27,000 | 31,541 |
| TOA ROAD Corp. | 6,833 | 10,761 |
| Toda Corp. | 12,000 | 44,520 |
| Tokyu Construction Co., Ltd. | 2,516 | 7,611 |
| Yahagi Construction Co., Ltd. | 2,000 | 11,690 |
| Yondenko Corp. | 3,000 | 12,491 |
| | | 918,118 |
| *Construction Materials* (0.0%) | | |
| Sumitomo Osaka Cement Co., Ltd.§ | 3,515 | 7,942 |
| *Consumer Finance* (0.0%) | | |
| Jaccs Co., Ltd. | 13,000 | 36,703 |
| Pocket Card Co., Ltd. | 5,600 | 16,814 |
| | | 53,517 |
| *Containers & Packaging* (0.0%) | | |
| Hokkan Holdings, Ltd. | 6,333 | 19,070 |
| Tomoku Co., Ltd. | 4,000 | 11,213 |
| Toyo Seikan Kaisha, Ltd.§ | 1,260 | 23,894 |
| | | 54,177 |
| *Distributors* (0.1%) | | |
| Happinet Corp. | 800 | 10,636 |
| Nice Holdings, Inc. | 7,000 | 15,396 |
| Sankyo Seiko Co., Ltd. | 7,412 | 26,636 |
| Yokohama Reito Co., Ltd.§ | 2,000 | 13,701 |
| | | 66,369 |

| | Number of Shares | Value |
|---|---|---|
| **LONG STOCK POSITIONS** | | |
| **COMMON STOCKS** | | |
| **Japan** | | |
| *Diversified Consumer Services* (0.0%) | | |
| Studio Alice Co., Ltd. | 1,700 | $ 16,066 |
| Tac Co., Ltd. | 3,400 | 14,242 |
| Watabe Wedding Corp. | 1,040 | 11,495 |
| | | 41,803 |
| *Diversified Financial Services* (0.2%) | | |
| Century Tokyo Leasing Corp. | 5,200 | 84,336 |
| Daiko Clearing Services Corp. | 2,066 | 7,931 |
| Fuyo General Lease Co., Ltd. | 1,600 | 52,343 |
| ORIX Corp.§ | 760 | 74,539 |
| Ricoh Leasing Co., Ltd. | 1,000 | 27,441 |
| | | 246,590 |
| *Diversified Telecommunication Services* (0.3%) | | |
| Nippon Telegraph & Telephone Corp. | 7,800 | 355,567 |
| *Electric Utilities* (0.9%) | | |
| Chubu Electric Power Co., Inc.§ | 10,897 | 267,783 |
| Kyushu Electric Power Co., Inc. | 1,100 | 24,653 |
| The Kansai Electric Power Co., Inc. | 11,500 | 283,873 |
| The Okinawa Electric Power Co., Inc. | 200 | 9,972 |
| The Tokyo Electric Power Co., Inc. | 17,100 | 417,378 |
| Tohoku Electric Power Co., Inc.§ | 6,700 | 149,327 |
| | | 1,152,986 |
| *Electrical Equipment* (0.4%) | | |
| Denyo Co., Ltd. | 2,600 | 21,432 |
| Fuji Electric Holdings Co., Ltd. | 10,000 | 31,022 |
| Helios Techno Holdings Co., Ltd. | 2,743 | 7,579 |
| Mitsubishi Electric Corp.§ | 13,654 | 142,824 |
| Nidec Corp.§ | 600 | 60,564 |
| Sumitomo Electric Industries, Ltd. | 15,200 | 210,272 |
| Ushio, Inc.§ | 685 | 13,020 |
| | | 486,713 |
| *Electronic Equipment, Instruments & Components* (1.6%) | | |
| Ai Holdings Corp.§ | 12,648 | 46,548 |
| Alps Electric Co., Ltd. | 1,000 | 11,553 |
| Canon Electronics, Inc. | 700 | 19,730 |
| Citizen Holdings Co., Ltd. | 2,500 | 17,172 |
| Elematec Corp.§ | 1,100 | 15,571 |
| Excel Co., Ltd. | 1,300 | 16,298 |
| FUJIFILM Holdings Corp. | 3,192 | 115,092 |
| Hakuto Co., Ltd. | 6,100 | 61,492 |
| Hitachi, Ltd. | 67,874 | 360,732 |
| Hochiki Corp. | 3,000 | 15,776 |
| Hosiden Corp. | 8,080 | 94,855 |
| HOYA Corp.§ | 8,200 | 198,477 |

| | Number of Shares | Value |
|---|---|---|
| **LONG STOCK POSITIONS** | | |
| **COMMON STOCKS** | | |
| **Japan** | | |
| *Electronic Equipment, Instruments & Components* | | |
| ITC Networks Corp. | 2,654 | $ 15,307 |
| JBCC Holdings, Inc. | 3,234 | 20,746 |
| Kaga Electronics Co., Ltd. | 5,200 | 66,394 |
| Kanematsu Electronics, Ltd. | 1,600 | 16,390 |
| Keyence Corp.§ | 182 | 52,568 |
| Kyocera Corp. | 2,186 | 222,325 |
| Mitsumi Electric Co., Ltd. | 800 | 14,635 |
| Murata Manufacturing Co., Ltd. | 718 | 50,173 |
| Nippon Electric Glass Co., Ltd. | 2,000 | 28,738 |
| Nohmi Bosai, Ltd. | 5,666 | 36,886 |
| Omron Corp. | 1,700 | 44,848 |
| ONO Sokki Co., Ltd.* | 4,000 | 13,654 |
| Optex Co., Ltd. | 1,100 | 16,313 |
| Osaki Electric Co., Ltd. | 3,174 | 27,499 |
| Ryosan Co., Ltd. | 1,700 | 43,982 |
| Ryoyo Electro Corp. | 6,400 | 74,434 |
| Sanshin Electronics Co., Ltd. | 800 | 6,627 |
| Shinko Shoji Co., Ltd. | 3,396 | 28,287 |
| Siix Corp. | 2,900 | 34,010 |
| SMK Corp. | 7,000 | 38,430 |
| Sumida Corp. | 1,625 | 17,697 |
| Tachibana Eletech Co., Ltd. | 1,965 | 16,526 |
| TDK Corp.§ | 2,082 | 144,301 |
| Tomen Devices Corp. | 600 | 13,923 |
| Tomen Electronics Corp. | 1,680 | 24,691 |
| Toyo Corp. | 5,100 | 54,575 |
| | | 2,097,255 |
| *Energy Equipment & Services* (0.0%) | | |
| Toyo Kanetsu KK | 30,203 | 53,719 |
| *Food & Staples Retailing* (0.6%) | | |
| Aeon Co., Ltd.§ | 10,598 | 132,383 |
| Belc Co., Ltd. | 2,200 | 25,792 |
| Cawachi, Ltd. | 900 | 18,538 |
| Cocokara fine, Inc. | 1,900 | 40,262 |
| Echo Trading Co., Ltd. | 1,234 | 12,623 |
| Itochu-Shokuhin Co., Ltd. | 954 | 33,596 |
| Kasumi Co., Ltd.§ | 7,593 | 42,245 |
| Kato Sangyo Co., Ltd. | 3,260 | 54,573 |
| Kirindo Co., Ltd. | 3,154 | 15,460 |
| Ministop Co., Ltd. | 800 | 13,861 |
| Okuwa Co., Ltd. | 5,000 | 52,252 |
| Ryoshoku, Ltd. | 600 | 13,346 |
| S Foods, Inc. | 1,000 | 8,572 |
| Seven & I Holdings Co., Ltd. | 7,600 | 202,403 |
| Universe Co., Ltd. | 1,000 | 15,055 |

See Accompanying Notes to Financial Statements.

| | Number of Shares | Value |
|---|---|---|
| **LONG STOCK POSITIONS** | | |
| **COMMON STOCKS** | | |
| **Japan** | | |
| *Food & Staples Retailing* | | |
| UNY Co., Ltd.§ | 6,000 | $ 60,489 |
| Valor Co., Ltd. | 8,900 | 76,764 |
| | | 818,214 |
| *Food Products* (0.6%) | | |
| Ajinomoto Co., Inc. | 3,089 | 32,122 |
| Chubu Shiryo Co., Ltd | 2,333 | 15,924 |
| J-Oil Mills, Inc. | 30,457 | 95,479 |
| Kyodo Shiryo Co., Ltd. | 23,000 | 28,322 |
| Maruha Nichiro Holdings, Inc. | 26,794 | 44,547 |
| MEIJI Holdings Co., Ltd. | 2,100 | 94,865 |
| Mitsui Sugar Co., Ltd. | 12,000 | 45,488 |
| Morinaga & Co., Ltd. | 23,428 | 55,105 |
| Morinaga Milk Industry Co., Ltd. | 3,532 | 14,965 |
| Nichimo Co., Ltd. | 5,000 | 10,016 |
| Nichirei Corp. | 6,000 | 27,663 |
| Nippon Flour Mills Co., Ltd. | 19,261 | 95,332 |
| Nippon Meat Packers, Inc. | 2,000 | 26,088 |
| Nippon Suisan Kaisha, Ltd.§ | 18,059 | 56,870 |
| Prima Meat Packers, Ltd. | 27,882 | 31,211 |
| Showa Sangyo Co., Ltd. | 4,000 | 11,718 |
| Starzen Co., Ltd. | 8,000 | 23,343 |
| Warabeya Nichiyo Co., Ltd. | 3,225 | 42,033 |
| Yonekyu Corp. | 6,136 | 50,898 |
| | | 801,989 |
| *Gas Utilities* (0.2%) | | |
| Osaka Gas Co., Ltd. | 21,000 | 81,490 |
| Toho Gas Co., Ltd. | 3,000 | 14,992 |
| Tokyo Gas Co., Ltd. | 25,000 | 110,823 |
| | | 207,305 |
| *Health Care Equipment & Supplies* (0.1%) | | |
| Aloka Co., Ltd. | 2,210 | 28,581 |
| Nipro Corp. | 4,000 | 80,120 |
| Terumo Corp. | 400 | 22,458 |
| | | 131,159 |
| *Health Care Providers & Services* (0.1%) | | |
| As One Corp. | 1,133 | 23,319 |
| Mediceo Paltac Holdings Co., Ltd. | 5,224 | 57,544 |
| Ship Healthcare Holdings, Inc. | 2,000 | 26,193 |
| | | 107,056 |
| *Hotels, Restaurants & Leisure* (0.2%) | | |
| Hurxley Corp. | 1,850 | 11,398 |
| Kyoritsu Maintenance Co., Ltd. | 2,926 | 49,762 |

See Accompanying Notes to Financial Statements.

| | Number of Shares | Value |
|---|---|---|
| **LONG STOCK POSITIONS** | | |
| **COMMON STOCKS** | | |
| **Japan** | | |
| *Hotels, Restaurants & Leisure* | | |
| McDonald's Holdings Co. Japan, Ltd.§ | 760 | $ 19,063 |
| Pacific Golf Group International Holdings KK§ | 120 | 83,063 |
| Resort Solution Co., Ltd. | 4,000 | 7,835 |
| Tokyo Dome Corp. | 31,796 | 86,331 |
| | | 257,452 |
| *Household Durables* (1.1%) | | |
| Casio Computer Co., Ltd.§ | 8,242 | 66,222 |
| Corona Corp. | 2,420 | 23,424 |
| Foster Electric Co., Ltd. | 700 | 20,661 |
| Fuji Corp. | 3,600 | 19,171 |
| Fujitsu General, Ltd.§ | 9,000 | 54,094 |
| Hitachi Koki Co., Ltd.§ | 2,090 | 19,611 |
| Mitsui Home Co., Ltd. | 5,000 | 26,449 |
| PanaHome Corp. | 11,000 | 69,392 |
| Panasonic Corp. | 21,880 | 309,243 |
| Pioneer Corp.* | 5,900 | 24,323 |
| Sangetsu Co., Ltd. | 2,300 | 53,907 |
| Sanyo Housing Nagoya Co., Ltd. | 22 | 22,604 |
| Sharp Corp.§ | 11,983 | 123,097 |
| Sony Corp.§ | 10,838 | 388,023 |
| Sumitomo Forestry Co., Ltd. | 8,800 | 77,133 |
| Tact Home Co., Ltd. | 28 | 32,713 |
| Token Corp. | 690 | 25,932 |
| | | 1,355,999 |
| *Independent Power Producers & Energy Traders* (0.1%) | | |
| Electric Power Development Co., Ltd.§ | 2,800 | 87,782 |
| *Insurance* (0.4%) | | |
| Mitsui Sumitomo Insurance Group Holdings, Inc. | 4,881 | 121,970 |
| NKSJ Holdings, Inc.* | 13,573 | 99,672 |
| T&D Holdings, Inc.§ | 1,650 | 41,666 |
| The Dai-ichi Life Insurance Co., Ltd. | 54 | 87,484 |
| Tokio Marine Holdings, Inc. | 7,548 | 224,467 |
| | | 575,259 |
| *Internet & Catalog Retail* (0.1%) | | |
| Image Holdings Co., Ltd.*§ | 2,818 | 9,295 |
| Nissen Holdings Co., Ltd. | 8,063 | 41,256 |
| Scroll Corp. | 4,883 | 20,940 |
| Senshukai Co., Ltd.§ | 1,825 | 11,183 |
| | | 82,674 |
| *Internet Software & Services* (0.0%) | | |
| Asahi Net, Inc. | 2,000 | 7,783 |
| eAccess, Ltd.§ | 76 | 45,805 |
| | | 53,588 |

See Accompanying Notes to Financial Statements.

| | Number of Shares | Value |
|---|---|---|
| **LONG STOCK POSITIONS** | | |
| **COMMON STOCKS** | | |
| **Japan** | | |
| *IT Services* (0.1%) | | |
| Argo Graphics, Inc. | 800 | $ 10,281 |
| CAC Corp.§ | 4,500 | 34,702 |
| JBIS Holdings, Inc. | 2,368 | 9,781 |
| NEC Fielding, Ltd. | 1,300 | 16,845 |
| NS Solutions Corp. | 1,300 | 28,322 |
| NTT Data Corp. | 12 | 41,426 |
| Obic Co., Ltd. | 40 | 8,223 |
| Panasonic Electric Works Information Systems Co., Ltd. | 400 | 10,862 |
| | | 160,442 |
| *Leisure Equipment & Products* (0.3%) | | |
| Daikoku Denki Co., Ltd. | 1,100 | 14,046 |
| GLOBERIDE, Inc.§ | 16,666 | 20,094 |
| Mizuno Corp. | 12,607 | 64,817 |
| Namco Bandai Holdings, Inc.§ | 7,700 | 82,622 |
| Nikon Corp. | 2,900 | 58,603 |
| Roland Corp. | 600 | 7,452 |
| Sankyo Co., Ltd. | 754 | 42,528 |
| Sega Sammy Holdings, Inc. | 700 | 13,290 |
| SRI Sports, Ltd. | 33 | 36,458 |
| Yamaha Corp. | 2,100 | 25,953 |
| | | 365,863 |
| *Machinery* (1.6%) | | |
| Aida Engineering, Ltd. | 4,300 | 19,611 |
| Amada Co., Ltd. | 5,279 | 42,826 |
| Bando Chemical Industries, Ltd. | 12,703 | 50,432 |
| CKD Corp. | 1,000 | 8,540 |
| Daido Kogyo Co., Ltd. | 4,000 | 7,961 |
| Daifuku Co., Ltd. | 16,000 | 111,709 |
| Ebara Corp.* | 8,000 | 39,185 |
| Fanuc, Ltd.§ | 2,058 | 314,908 |
| Hitachi Zosen Corp.§ | 32,158 | 48,644 |
| Hosokawa Micron Corp. | 2,250 | 9,395 |
| IHI Corp.§ | 17,000 | 37,782 |
| JTEKT Corp. | 7,792 | 91,524 |
| Kato Works Co., Ltd. | 14,836 | 32,752 |
| Kito Corp. | 3 | 2,924 |
| Komatsu, Ltd. | 6,448 | 194,268 |
| Kubota Corp.§ | 4,000 | 37,724 |
| Kyokuto Kaihatsu Kogyo Co., Ltd. | 4,914 | 20,598 |
| Maezawa Kyuso Industries Co., Ltd. | 632 | 7,788 |
| Makita Corp. | 2,889 | 117,682 |
| Max Co., Ltd. | 4,000 | 47,283 |
| Minebea Co., Ltd. | 6,878 | 43,192 |
| Mitsubishi Heavy Industries, Ltd.§ | 20,000 | 74,948 |
| Mitsuboshi Belting Co., Ltd. | 6,000 | 34,808 |

| | Number of Shares | Value |
|---|---|---|
| **LONG STOCK POSITIONS** | | |
| **COMMON STOCKS** | | |
| **Japan** | | |
| *Machinery* | | |
| Mitsui Engineering & Shipbuilding Co., Ltd.§ | 30,072 | $ 79,375 |
| Nachi-Fujikoshi Corp. | 3,000 | 10,052 |
| Nippon Yusoki Co., Ltd. | 3,666 | 9,439 |
| NSK, Ltd. | 7,580 | 68,241 |
| NTN Corp. | 21,796 | 115,147 |
| O-M, Ltd. | 9,333 | 37,154 |
| Obara Corp. | 1,339 | 14,170 |
| Oiles Corp. | 1,300 | 24,031 |
| Ryobi, Ltd.*§ | 3,000 | 13,692 |
| Sasebo Heavy Industries Co., Ltd.§ | 44,190 | 90,243 |
| Shinmaywa Industries, Ltd. | 10,000 | 43,180 |
| SMC Corp. | 193 | 32,969 |
| Sumitomo Heavy Industries, Ltd. | 5,908 | 37,829 |
| Tadano, Ltd.§ | 1,286 | 6,902 |
| TOKYO KEIKI, Inc. | 8,058 | 12,423 |
| Tokyo Kikai Seisakusho, Ltd.* | 20,000 | 18,899 |
| Tsurumi Manufacturing Co., Ltd. | 2,000 | 13,544 |
| | | 2,023,774 |
| *Marine* (0.2%) | | |
| Iino Kaiun Kaisha Ltd.§ | 4,500 | 20,247 |
| Japan Transcity Corp. | 7,500 | 26,010 |
| Kawasaki Kisen Kaisha, Ltd.§ | 10,000 | 43,583 |
| Mitsui OSK Lines, Ltd. | 10,000 | 67,832 |
| Nippon Yusen KK§ | 22,706 | 100,070 |
| | | 257,742 |
| *Media* (0.2%) | | |
| Amuse, Inc. | 800 | 9,561 |
| Avex Group Holdings, Inc. | 1,959 | 28,629 |
| Horipro, Inc. | 1,635 | 14,158 |
| Nippon Television Network Corp. | 290 | 45,530 |
| SKY Perfect JSAT Holdings, Inc.§ | 227 | 87,655 |
| Tow Co., Ltd. | 2,666 | 15,522 |
| TV Asahi Corp. | 5 | 8,693 |
| Zenrin Co., Ltd.§ | 2,100 | 23,404 |
| | | 233,152 |
| *Metals & Mining* (0.7%) | | |
| Aichi Steel Corp. | 5,000 | 34,199 |
| Dowa Holdings Co., Ltd. | 4,000 | 26,160 |
| JFE Holdings, Inc. | 4,300 | 149,247 |
| Kobe Steel, Ltd. | 16,621 | 42,041 |
| Maruichi Steel Tube, Ltd. | 500 | 10,613 |
| Mitsubishi Materials Corp.*§ | 7,262 | 23,101 |
| Mitsui Mining & Smelting Co., Ltd. | 14,000 | 46,093 |
| Nichia Steel Works, Ltd. | 9,000 | 23,796 |

| | Number of Shares | Value |
|---|---|---|
| **LONG STOCK POSITIONS** | | |
| **COMMON STOCKS** | | |
| **Japan** | | |
| *Metals & Mining* | | |
| Nippon Steel Corp. | 31,977 | $ 114,676 |
| Nittetsu Mining Co., Ltd. | 18,799 | 94,500 |
| Pacific Metals Co., Ltd.§ | 5,000 | 42,353 |
| Sumitomo Metal Industries, Ltd. | 20,263 | 49,727 |
| Sumitomo Metal Mining Co., Ltd. | 5,000 | 87,182 |
| Toho Zinc Co., Ltd. | 8,000 | 42,482 |
| Tokyo Tekko Co., Ltd. | 14,039 | 36,919 |
| Yamato Kogyo Co., Ltd. | 300 | 9,029 |
| Yodogawa Steel Works, Ltd. | 4,000 | 18,580 |
| | | 850,698 |
| *Office Electronics* (0.9%) | | |
| Brother Industries, Ltd. | 6,500 | 96,033 |
| Canon, Inc.§ | 14,814 | 761,722 |
| Konica Minolta Holdings, Inc. | 4,173 | 43,175 |
| Ricoh Co., Ltd. | 12,985 | 189,533 |
| Toshiba TEC Corp. | 5,000 | 24,164 |
| | | 1,114,627 |
| *Oil, Gas & Consumable Fuels* (0.5%) | | |
| AOC Holdings, Inc.*§ | 9,474 | 64,512 |
| Cosmo Oil Co., Ltd.§ | 17,802 | 58,198 |
| Idemitsu Kosan Co., Ltd. | 100 | 10,608 |
| INPEX Corp. | 17 | 99,374 |
| Itochu Enex Co., Ltd. | 12,836 | 69,466 |
| JX Holdings, Inc. | 23,700 | 160,547 |
| San-Ai Oil Co., Ltd. | 8,800 | 43,259 |
| Showa Shell Sekiyu KK§ | 11,500 | 105,182 |
| Sinanen Co., Ltd. | 2,000 | 9,201 |
| TonenGeneral Sekiyu KK§ | 7,614 | 83,165 |
| | | 703,512 |
| *Paper & Forest Products* (0.1%) | | |
| Chuetsu Pulp & Paper Co., Ltd. | 7,000 | 12,667 |
| Nakabayashi Co., Ltd. | 3,428 | 7,720 |
| Nippon Paper Group, Inc.§ | 3,200 | 83,853 |
| | | 104,240 |
| *Personal Products* (0.1%) | | |
| Kao Corp. | 3,000 | 80,710 |
| *Pharmaceuticals* (1.1%) | | |
| ASKA Pharmaceutical Co., Ltd. | 4,833 | 36,446 |
| Astellas Pharma, Inc.§ | 7,900 | 300,557 |
| Daiichi Sankyo Co., Ltd.§ | 4,891 | 106,936 |
| Eisai Co., Ltd.§ | 5,300 | 191,675 |
| Kaken Pharmaceutical Co., Ltd. | 6,000 | 72,850 |
| Kyorin Co., Ltd. | 2,000 | 34,904 |

**Credit Suisse Trust — International Equity Flex III Portfolio**
**Schedule of Investments (continued)**
December 31, 2010

| | Number of Shares | Value |
|---|---|---|
| **LONG STOCK POSITIONS** | | |
| **COMMON STOCKS** | | |
| **Japan** | | |
| *Pharmaceuticals* | | |
| Mochida Pharmaceutical Co., Ltd.§ | 7,000 | $ 74,990 |
| Ono Pharmaceutical Co., Ltd. | 1,600 | 74,689 |
| Shionogi & Co., Ltd. | 1,000 | 19,728 |
| Takeda Pharmaceutical Co., Ltd.§ | 10,700 | 526,197 |
| | | 1,438,972 |
| *Professional Services* (0.0%) | | |
| Pasona Group, Inc. | 23 | 17,169 |
| *Real Estate Investment Trusts* (0.3%) | | |
| Japan Prime Realty Investment Corp.§ | 20 | 61,565 |
| Japan Real Estate Investment Corp. | 6 | 62,223 |
| Japan Retail Fund Investment Corp. | 49 | 93,803 |
| Nippon Building Fund, Inc.§ | 3 | 30,777 |
| Nomura Real Estate Office Fund, Inc. | 15 | 108,332 |
| | | 356,700 |
| *Real Estate Management & Development* (0.5%) | | |
| Airport Facilities Co., Ltd. | 6,700 | 29,176 |
| Daito Trust Construction Co., Ltd. | 1,393 | 95,301 |
| Daiwa House Industry Co., Ltd. | 3,000 | 36,788 |
| Mitsubishi Estate Co., Ltd. | 8,559 | 158,346 |
| Mitsui Fudosan Co., Ltd. | 6,910 | 137,470 |
| Nisshin Fudosan Co., Ltd. | 4,900 | 39,733 |
| Sumitomo Realty & Development Co., Ltd. | 1,000 | 23,815 |
| Tokyo Tatemono Co., Ltd.§ | 11,000 | 50,753 |
| Tokyu Land Corp. | 21,811 | 109,260 |
| | | 680,642 |
| *Road & Rail* (0.7%) | | |
| Central Japan Railway Co.§ | 22 | 184,100 |
| East Japan Railway Co. | 4,300 | 279,316 |
| ICHINEN HOLDINGS Co., Ltd. | 4,050 | 20,843 |
| KRS Corp. | 960 | 10,166 |
| Maruwn Corp. | 2,300 | 6,172 |
| Nippon Express Co., Ltd. | 16,000 | 71,929 |
| Sankyu, Inc. | 10,000 | 45,342 |
| Senko Co., Ltd. | 6,800 | 24,271 |
| Tokyu Corp. | 13,000 | 59,531 |
| Tonami Holdings Co., Ltd. | 6,332 | 12,083 |
| West Japan Railway Co. | 39 | 145,720 |
| | | 859,473 |
| *Semiconductors & Semiconductor Equipment* (0.2%) | | |
| Dainippon Screen Manufacturing Co., Ltd.* | 2,000 | 14,157 |
| Elpida Memory, Inc.*§ | 1,900 | 21,998 |
| Mimasu Semiconductor Industry Co., Ltd. | 4,800 | 55,595 |
| Rohm Co., Ltd.§ | 600 | 39,061 |

See Accompanying Notes to Financial Statements.

| | Number of Shares | Value |
|---|---|---|
| **LONG STOCK POSITIONS** | | |
| **COMMON STOCKS** | | |
| **Japan** | | |
| *Semiconductors & Semiconductor Equipment* | | |
| Shinko Electric Industries Co., Ltd.§ | 1,700 | $ 18,986 |
| Tokyo Electron, Ltd.§ | 1,966 | 123,912 |
| | | 273,709 |
| *Software* (0.4%) | | |
| Computer Engineering & Consulting, Ltd. | 1,900 | 9,793 |
| Computer Institute of Japan, Ltd. | 2,504 | 8,503 |
| Jastec Co., Ltd. | 1,088 | 6,391 |
| Konami Corp.§ | 2,523 | 53,437 |
| Nintendo Co., Ltd.§ | 1,200 | 350,709 |
| SRA Holdings | 2,884 | 31,852 |
| Trend Micro, Inc.*§ | 1,500 | 49,330 |
| | | 510,015 |
| *Specialty Retail* (0.4%) | | |
| Aoyama Trading Co., Ltd. | 2,333 | 42,104 |
| Arc Land Sakamoto Co., Ltd. | 2,052 | 25,166 |
| Chiyoda Co., Ltd.§ | 4,004 | 53,076 |
| DCM Holdings Co., Ltd.§ | 16,900 | 106,276 |
| EDION Corp. | 2,400 | 21,501 |
| Fast Retailing Co., Ltd. | 72 | 11,433 |
| Geo Corp. | 43 | 48,920 |
| Hard Off Corp. Co., Ltd. | 1,600 | 8,235 |
| Hikari Tsushin, Inc.§ | 1,287 | 28,039 |
| K's Holding Corp. | 300 | 8,152 |
| Keiyo Co., Ltd.§ | 6,073 | 31,113 |
| Right On Co., Ltd.§ | 3,307 | 18,916 |
| T-Gaia Corp.§ | 33 | 58,680 |
| Taka-Q, Ltd. | 4,000 | 8,020 |
| Top Culture Co., Ltd. | 1,433 | 6,372 |
| Yamada Denki Co., Ltd.§ | 268 | 18,252 |
| | | 494,255 |
| *Textiles, Apparel & Luxury Goods* (0.3%) | | |
| Atsugi Co., Ltd. | 26,926 | 34,766 |
| Daidoh, Ltd.§ | 1,036 | 9,209 |
| Kurabo Industries, Ltd. | 22,418 | 40,537 |
| Nisshinbo Holdings, Inc. | 8,969 | 98,002 |
| Onward Holdings Co., Ltd.§ | 3,000 | 25,946 |
| Tasaki Shinju Co., Ltd.* | 7,679 | 6,705 |
| The Japan Wool Textile Co., Ltd. | 3,000 | 24,444 |
| Toyobo Co., Ltd. | 40,000 | 71,340 |
| Yamato International, Inc. | 1,600 | 7,363 |
| | | 318,312 |
| *Thrifts & Mortgage Finance* (0.0%) | | |
| Asax Co., Ltd. | 7 | 7,668 |

| | Number of Shares | Value |
|---|---|---|
| **LONG STOCK POSITIONS** | | |
| **COMMON STOCKS** | | |
| **Japan** | | |
| *Tobacco* (0.1%) | | |
| Japan Tobacco, Inc. | 50 | $ 184,822 |
| *Trading Companies & Distributors* (1.7%) | | |
| Furusato Industries, Ltd. | 1,416 | 9,165 |
| Hanwa Co., Ltd.§ | 20,159 | 92,536 |
| Inaba Denki Sangyo Co., Ltd | 3,013 | 85,203 |
| Inabata & Co., Ltd. | 3,466 | 21,013 |
| ITOCHU Corp. | 15,621 | 157,558 |
| Iwatani Corp. | 16,000 | 48,240 |
| Jalux, Inc.* | 1,900 | 15,961 |
| Japan Pulp & Paper Co., Ltd. | 9,273 | 33,043 |
| JFE Shoji Holdings, Inc.§ | 10,000 | 46,521 |
| Kamei Corp. | 5,000 | 24,172 |
| Kanaden Corp. | 1,000 | 6,061 |
| Kanematsu Corp.*§ | 110,000 | 105,359 |
| Kuroda Electric Co., Ltd. | 5,937 | 83,093 |
| Kyokuto Boeki Kaisha, Ltd. | 4,666 | 8,482 |
| Marubeni Corp. | 24,827 | 173,991 |
| Mitsubishi Corp. | 12,115 | 326,862 |
| Mitsui & Co., Ltd.§ | 17,183 | 283,024 |
| NEC Capital Solutions Ltd. | 4,055 | 60,084 |
| Onoken Co., Ltd. | 4,800 | 43,917 |
| Sato Shoji Corp. | 1,500 | 9,265 |
| Seika Corp. | 10,759 | 27,511 |
| Shinwa Co., Ltd. | 800 | 9,671 |
| Sojitz Corp.§ | 31,281 | 68,471 |
| Sumikin Bussan Corp. | 25,666 | 61,874 |
| Sumitomo Corp.§ | 14,379 | 202,629 |
| Tokyo Sangyo Co., Ltd. | 2,500 | 7,753 |
| Toyota Tsusho Corp. | 4,300 | 75,378 |
| Tsubakimoto Kogyo Co., Ltd. | 4,000 | 10,858 |
| Yamazen Corp. | 4,600 | 24,594 |
| | | 2,122,289 |
| *Transportation Infrastructure* (0.1%) | | |
| Mitsui-Soko Co., Ltd. | 21,000 | 87,416 |
| Nissin Corp. | 10,500 | 26,798 |
| The Yasuda Warehouse Co., Ltd. | 3,000 | 17,938 |
| | | 132,152 |
| *Wireless Telecommunication Services* (0.6%) | | |
| KDDI Corp.§ | 41 | 236,684 |
| NTT DoCoMo, Inc. | 172 | 299,870 |
| Softbank Corp. | 6,400 | 220,906 |
| | | 757,460 |
| *TOTAL JAPAN* | | 36,005,519 |

| | Number of Shares | Value |
|---|---|---|
| **LONG STOCK POSITIONS** | | |
| **COMMON STOCKS** | | |
| **Luxembourg** (0.6%) | | |
| *Energy Equipment & Services* (0.4%) | | |
| Tenaris SA | 23,178 | $ 570,661 |
| *Metals & Mining* (0.2%) | | |
| ArcelorMittal | 6,805 | 259,992 |
| *TOTAL LUXEMBOURG* | | 830,653 |
| **Netherlands** (3.6%) | | |
| *Beverages* (0.1%) | | |
| Heineken NV | 2,445 | 120,390 |
| *Chemicals* (0.4%) | | |
| Koninklijke DSM NV | 9,361 | 535,698 |
| *Construction & Engineering* (0.3%) | | |
| Imtech NV | 3,171 | 120,930 |
| Koninklijke BAM Groep NV | 13,118 | 81,005 |
| Koninklijke Boskalis Westminster NV | 2,561 | 122,759 |
| | | 324,694 |
| *Construction Materials* (0.0%) | | |
| James Hardie Industries NV* | 3,734 | 25,949 |
| *Diversified Financial Services* (0.2%) | | |
| ING Groep NV* | 20,482 | 200,601 |
| *Diversified Telecommunication Services* (0.5%) | | |
| Koninklijke KPN NV | 47,006 | 689,258 |
| *Energy Equipment & Services* (0.0%) | | |
| Fugro NV | 381 | 31,493 |
| *Food & Staples Retailing* (0.4%) | | |
| Koninklijke Ahold NV | 38,283 | 507,711 |
| *Food Products* (1.1%) | | |
| CSM | 8,039 | 282,692 |
| Nutreco Holding NV | 4,491 | 342,433 |
| Unilever NV | 25,667 | 803,889 |
| | | 1,429,014 |
| *Industrial Conglomerates* (0.2%) | | |
| Koninklijke Philips Electronics NV | 7,813 | 240,465 |
| *Insurance* (0.1%) | | |
| Brit Insurance Holdings NV* | 7,257 | 118,756 |
| *Real Estate Investment Trusts* (0.3%) | | |
| Wereldhave NV | 4,219 | 413,994 |
| *TOTAL NETHERLANDS* | | 4,638,023 |

| | Number of Shares | Value |
|---|---|---|
| **LONG STOCK POSITIONS** | | |
| **COMMON STOCKS** | | |
| **Norway** (1.2%) | | |
| *Chemicals* (0.2%) | | |
| Yara International ASA§ | 4,911 | $ 286,972 |
| *Diversified Telecommunication Services* (0.4%) | | |
| Telenor ASA | 35,726 | 584,426 |
| *Energy Equipment & Services* (0.1%) | | |
| Aker Solutions ASA§ | 6,137 | 105,107 |
| *Industrial Conglomerates* (0.0%) | | |
| Orkla ASA | 1,304 | 12,769 |
| *Insurance* (0.1%) | | |
| Storebrand ASA* | 9,405 | 70,841 |
| *Oil, Gas & Consumable Fuels* (0.4%) | | |
| StatoilHydro ASA§ | 20,021 | 478,711 |
| *TOTAL NORWAY* | | 1,538,826 |
| **Portugal** (0.7%) | | |
| *Commercial Banks* (0.2%) | | |
| Banco Comercial Portugues SA R Shares§ | 257,922 | 201,363 |
| *Electric Utilities* (0.2%) | | |
| EDP - Energias de Portugal SA | 58,709 | 196,244 |
| *Food & Staples Retailing* (0.1%) | | |
| Jeronimo Martins SGPS SA | 11,594 | 177,472 |
| *Transportation Infrastructure* (0.2%) | | |
| Brisa Auto-Estradas de Portugal SA§ | 41,522 | 290,765 |
| *TOTAL PORTUGAL* | | 865,844 |
| **Singapore** (1.3%) | | |
| *Diversified Financial Services* (1.3%) | | |
| iShares MSCI Singapore Index Fund | 117,181 | 1,622,957 |
| *TOTAL SINGAPORE* | | 1,622,957 |
| **Spain** (4.7%) | | |
| *Commercial Banks* (1.1%) | | |
| Banco Bilbao Vizcaya Argentaria SA§ | 44,255 | 452,784 |
| Banco Popular Espanol SA§ | 23,637 | 122,359 |
| Banco Santander SA | 74,783 | 800,000 |
| | | 1,375,143 |
| *Construction & Engineering* (0.7%) | | |
| ACS Actividades de Construccion y Servicios SA§ | 6,137 | 289,350 |
| Ferrovial SA§ | 22,908 | 229,668 |
| Fomento de Construcciones y Contratas SA§ | 16,852 | 445,551 |
| | | 964,569 |

See Accompanying Notes to Financial Statements.

| | Number of Shares | Value |
|---|---|---|
| **LONG STOCK POSITIONS** | | |
| **COMMON STOCKS** | | |
| **Spain** | | |
| *Diversified Financial Services* (0.4%) | | |
| Criteria Caixacorp SA§ | 86,328 | $ 462,886 |
| *Diversified Telecommunication Services* (1.2%) | | |
| Telefonica SA | 64,778 | 1,484,685 |
| *Electric Utilities* (0.6%) | | |
| Endesa SA§ | 16,037 | 417,175 |
| Iberdrola SA§ | 41,275 | 321,285 |
| | | 738,460 |
| *Food Products* (0.1%) | | |
| Ebro Foods SA | 3,352 | 71,395 |
| *IT Services* (0.0%) | | |
| Indra Sistemas SA§ | 2,660 | 45,772 |
| *Media* (0.1%) | | |
| Gestevision Telecinco SA | 14,685 | 162,394 |
| *Oil, Gas & Consumable Fuels* (0.4%) | | |
| Repsol YPF SA | 19,618 | 551,530 |
| *Specialty Retail* (0.1%) | | |
| Inditex SA§ | 2,111 | 158,636 |
| *TOTAL SPAIN* | | 6,015,470 |
| **Sweden** (6.0%) | | |
| *Building Products* (0.2%) | | |
| Assa Abloy AB Class B | 7,310 | 206,291 |
| *Capital Markets* (0.0%) | | |
| Ratos AB B Shares | 1,148 | 42,462 |
| *Commercial Banks* (0.3%) | | |
| Nordea Bank AB | 9,808 | 106,685 |
| Svenska Handelsbanken AB A Shares | 10,407 | 332,804 |
| | | 439,489 |
| *Commercial Services & Supplies* (0.2%) | | |
| Securitas AB B Shares§ | 26,901 | 315,142 |
| *Communications Equipment* (0.3%) | | |
| Telefonaktiebolaget LM Ericsson B Shares | 37,100 | 430,124 |
| *Construction & Engineering* (0.4%) | | |
| Skanska AB B Shares§ | 26,025 | 516,153 |
| *Diversified Financial Services* (0.2%) | | |
| Industrivarden AB A Shares | 13,775 | 245,554 |
| *Diversified Telecommunication Services* (0.5%) | | |
| Tele2 AB B Shares | 20,612 | 427,827 |
| TeliaSonera AB | 22,443 | 178,241 |
| | | 606,068 |

See Accompanying Notes to Financial Statements.

| | Number of Shares | Value |
|---|---|---|
| **LONG STOCK POSITIONS** | | |
| **COMMON STOCKS** | | |
| **Sweden** | | |
| *Health Care Equipment & Supplies* (0.1%) | | |
| Elekta AB B Shares | 2,757 | $ 106,015 |
| Getinge AB B Shares | 912 | 19,100 |
| | | 125,115 |
| *Household Durables* (0.3%) | | |
| Electrolux AB Series B | 3,617 | 102,685 |
| Husqvarna AB B Shares§ | 26,464 | 221,221 |
| | | 323,906 |
| *Machinery* (2.0%) | | |
| Alfa Laval AB§ | 25,190 | 532,058 |
| Atlas Copco AB A Shares§ | 24,549 | 619,960 |
| Atlas Copco AB B Shares | 8,305 | 188,081 |
| Hexagon AB B Shares | 8,284 | 177,991 |
| Sandvik AB | 4,473 | 87,313 |
| Scania AB B Shares | 22,031 | 507,344 |
| SKF AB B Shares | 11,817 | 337,359 |
| Volvo AB B Shares* | 3,287 | 57,927 |
| | | 2,508,033 |
| *Metals & Mining* (0.2%) | | |
| Boliden AB | 9,733 | 198,382 |
| *Paper & Forest Products* (0.6%) | | |
| Holmen AB B Shares | 8,392 | 276,373 |
| Svenska Cellulosa AB B Shares§ | 33,678 | 531,958 |
| | | 808,331 |
| *Pharmaceuticals* (0.0%) | | |
| Meda AB | 6,083 | 46,391 |
| *Specialty Retail* (0.3%) | | |
| Hennes & Mauritz AB B Shares | 11,503 | 383,268 |
| *Tobacco* (0.4%) | | |
| Swedish Match AB | 18,371 | 532,581 |
| *TOTAL SWEDEN* | | 7,727,290 |
| **Switzerland** (7.7%) | | |
| *Biotechnology* (0.1%) | | |
| BB Biotech AG | 1,860 | 123,302 |
| *Building Products* (0.0%) | | |
| Geberit AG | 134 | 31,080 |
| *Capital Markets* (0.4%) | | |
| Julius Baer Group, Ltd. | 1,065 | 50,022 |
| UBS AG* | 29,606 | 487,603 |
| | | 537,625 |

| | Number of Shares | Value |
|---|---|---|
| **LONG STOCK POSITIONS** | | |
| **COMMON STOCKS** | | |
| **Switzerland** | | |
| *Chemicals* (0.2%) | | |
| Clariant AG* | 4,398 | $ 89,391 |
| Syngenta AG | 317 | 93,213 |
| | | 182,604 |
| *Diversified Telecommunication Services* (0.3%) | | |
| Swisscom AG | 974 | 429,489 |
| *Electrical Equipment* (0.2%) | | |
| ABB, Ltd.* | 10,029 | 224,623 |
| *Energy Equipment & Services* (0.2%) | | |
| Transocean, Ltd.* | 3,500 | 241,861 |
| *Food Products* (2.0%) | | |
| Nestle SA§ | 43,771 | 2,572,244 |
| *Insurance* (0.9%) | | |
| Baloise Holding AG | 4,988 | 486,720 |
| Helvetia Holding AG | 703 | 271,231 |
| Zurich Financial Services AG | 1,357 | 352,511 |
| | | 1,110,462 |
| *Machinery* (0.4%) | | |
| Schindler Holding AG | 3,520 | 417,695 |
| Sulzer AG | 706 | 108,043 |
| | | 525,738 |
| *Pharmaceuticals* (2.6%) | | |
| Novartis AG | 31,630 | 1,867,711 |
| Roche Holding AG§ | 10,399 | 1,529,161 |
| | | 3,396,872 |
| *Textiles, Apparel & Luxury Goods* (0.4%) | | |
| Compagnie Financiere Richemont SA Class A | 2,170 | 128,001 |
| The Swatch Group AG | 2,652 | 214,652 |
| The Swatch Group AG BR Shares | 322 | 144,017 |
| | | 486,670 |
| *TOTAL SWITZERLAND* | | 9,862,570 |
| **United Kingdom** (23.8%) | | |
| *Aerospace & Defense* (0.2%) | | |
| BAE Systems PLC | 51,584 | 266,816 |
| Rolls-Royce Group PLC* | 5,323 | 52,081 |
| | | 318,897 |
| *Auto Components* (0.1%) | | |
| GKN PLC | 28,693 | 100,013 |
| *Beverages* (0.1%) | | |
| Diageo PLC | 9,561 | 177,892 |

## Credit Suisse Trust — International Equity Flex III Portfolio
## Schedule of Investments (continued)
December 31, 2010

| | Number of Shares | Value |
|---|---|---|
| **LONG STOCK POSITIONS** | | |
| **COMMON STOCKS** | | |
| **United Kingdom** | | |
| *Biotechnology* (0.0%) | | |
| Genus PLC | 2,410 | $ 32,380 |
| *Capital Markets* (1.1%) | | |
| 3i Group PLC§ | 93,478 | 482,246 |
| Aberdeen Asset Management PLC | 709 | 2,259 |
| Collins Stewart PLC | 22,253 | 27,263 |
| Intermediate Capital Group PLC | 15,921 | 83,292 |
| Man Group PLC | 79,206 | 368,814 |
| Schroders PLC§ | 16,491 | 480,225 |
| | | 1,444,099 |
| *Chemicals* (0.4%) | | |
| Croda International PLC§ | 15,111 | 384,125 |
| Filtrona PLC | 23,480 | 89,286 |
| Yule Catto & Co. PLC | 10,068 | 31,684 |
| | | 505,095 |
| *Commercial Banks* (2.8%) | | |
| Barclays PLC | 175,194 | 727,103 |
| HSBC Holdings PLC§ | 172,331 | 1,768,654 |
| Lloyds Banking Group PLC* | 169,979 | 176,207 |
| Royal Bank of Scotland Group PLC* | 122,888 | 75,785 |
| Standard Chartered PLC | 33,487 | 907,805 |
| | | 3,655,554 |
| *Communications Equipment* (0.1%) | | |
| Spirent Communications PLC | 49,379 | 114,377 |
| *Construction & Engineering* (0.5%) | | |
| Carillion PLC | 73,636 | 444,491 |
| Interserve PLC | 49,053 | 177,363 |
| | | 621,854 |
| *Consumer Finance* (0.1%) | | |
| International Personal Finance PLC | 12,131 | 73,155 |
| *Containers & Packaging* (0.1%) | | |
| DS Smith PLC | 50,627 | 160,443 |
| *Distributors* (0.1%) | | |
| Inchcape PLC* | 11,753 | 65,829 |
| *Diversified Telecommunication Services* (0.5%) | | |
| BT Group PLC | 232,403 | 662,849 |
| *Electronic Equipment, Instruments & Components* (0.4%) | | |
| Diploma PLC | 12,909 | 56,288 |
| Domino Printing Sciences | 4,080 | 41,543 |
| Electrocomponents PLC | 16,786 | 70,021 |

See Accompanying Notes to Financial Statements.

| | Number of Shares | Value |
|---|---|---|
| **LONG STOCK POSITIONS** | | |
| **COMMON STOCKS** | | |
| **United Kingdom** | | |
| *Electronic Equipment, Instruments & Components* | | |
| Premier Farnell PLC | 63,264 | $ 284,269 |
| TT electronics PLC | 23,115 | 62,534 |
| | | 514,655 |
| *Energy Equipment & Services* (0.1%) | | |
| Petrofac, Ltd. | 6,404 | 159,790 |
| *Food & Staples Retailing* (0.5%) | | |
| J Sainsbury PLC | 60,191 | 355,102 |
| Tesco PLC | 39,089 | 260,290 |
| | | 615,392 |
| *Food Products* (0.3%) | | |
| Unilever PLC | 12,690 | 391,428 |
| *Health Care Providers & Services* (0.0%) | | |
| Synergy Health PLC | 2,704 | 37,164 |
| *Hotels, Restaurants & Leisure* (0.1%) | | |
| Compass Group PLC | 4,761 | 43,392 |
| Rank Group PLC | 25,848 | 51,246 |
| | | 94,638 |
| *Household Durables* (0.0%) | | |
| Persimmon PLC | 7,958 | 52,006 |
| *Household Products* (0.1%) | | |
| McBride PLC | 12,202 | 35,957 |
| Reckitt Benckiser Group PLC | 2,260 | 124,857 |
| | | 160,814 |
| *Independent Power Producers & Energy Traders* (0.4%) | | |
| International Power PLC | 77,148 | 530,563 |
| *Industrial Conglomerates* (0.2%) | | |
| Cookson Group PLC* | 14,567 | 150,643 |
| Smiths Group PLC | 3,104 | 60,595 |
| | | 211,238 |
| *Insurance* (1.2%) | | |
| Aviva PLC | 47,328 | 292,142 |
| Legal & General Group PLC | 324,760 | 493,931 |
| Old Mutual PLC | 293,461 | 567,498 |
| RSA Insurance Group PLC | 66,965 | 131,468 |
| | | 1,485,039 |
| *IT Services* (0.1%) | | |
| Computacenter PLC§ | 12,316 | 74,487 |
| *Machinery* (0.8%) | | |
| Fenner PLC§ | 28,820 | 161,758 |
| IMI PLC | 14,043 | 208,161 |

| | Number of Shares | Value |
|---|---|---|
| **LONG STOCK POSITIONS** | | |
| **COMMON STOCKS** | | |
| **United Kingdom** | | |
| *Machinery* | | |
| Melrose PLC | 40,514 | $ 197,320 |
| Senior PLC | 76,831 | 181,278 |
| The Weir Group PLC§ | 10,816 | 301,762 |
| | | 1,050,279 |
| *Media* (0.3%) | | |
| Euromoney Institutional Investor PLC§ | 5,536 | 60,042 |
| Pearson PLC | 13,527 | 214,070 |
| Trinity Mirror PLC* | 68,091 | 74,092 |
| | | 348,204 |
| *Metals & Mining* (2.8%) | | |
| Anglo American PLC | 7,222 | 379,391 |
| BHP Billiton PLC | 35,346 | 1,428,013 |
| Hill & Smith Holdings PLC | 8,340 | 36,234 |
| Kazakhmys PLC | 2,757 | 70,279 |
| Rio Tinto PLC | 19,699 | 1,410,081 |
| Xstrata PLC | 12,091 | 287,716 |
| | | 3,611,714 |
| *Multi-Utilities* (0.6%) | | |
| Centrica PLC§ | 142,459 | 741,228 |
| *Multiline Retail* (0.4%) | | |
| Next PLC | 14,858 | 460,817 |
| *Oil, Gas & Consumable Fuels* (4.9%) | | |
| BG Group PLC | 18,153 | 369,787 |
| BP PLC | 241,265 | 1,785,832 |
| Royal Dutch Shell PLC A Shares§ | 66,871 | 2,662,957 |
| Royal Dutch Shell PLC B Shares | 44,881 | 1,492,467 |
| | | 6,311,043 |
| *Paper & Forest Products* (0.3%) | | |
| Mondi PLC | 51,962 | 419,733 |
| *Pharmaceuticals* (2.3%) | | |
| AstraZeneca PLC | 26,864 | 1,229,462 |
| GlaxoSmithKline PLC | 78,587 | 1,530,435 |
| Shire PLC | 9,599 | 232,426 |
| | | 2,992,323 |
| *Specialty Retail* (0.3%) | | |
| Kingfisher PLC | 41,374 | 171,166 |
| WH Smith PLC | 19,525 | 149,503 |
| | | 320,669 |
| *Thrifts & Mortgage Finance* (0.1%) | | |
| Paragon Group of Cos. PLC | 45,025 | 126,780 |

| | Number of Shares | Value |
|---|---|---|
| **LONG STOCK POSITIONS** | | |
| **COMMON STOCKS** | | |
| **United Kingdom** | | |
| *Tobacco* (0.4%) | | |
| British American Tobacco PLC | 14,789 | $ 571,267 |
| *Trading Companies & Distributors* (0.1%) | | |
| Bunzl PLC | 4,102 | 46,252 |
| Wolseley PLC* | 3,100 | 99,655 |
| | | 145,907 |
| *Wireless Telecommunication Services* (1.0%) | | |
| Vodafone Group PLC | 481,635 | 1,269,679 |
| *TOTAL UNITED KINGDOM* | | 30,629,294 |
| **TOTAL COMMON STOCKS** (Cost $132,077,454) | | 159,088,096 |
| **PREFERRED STOCKS** (0.9%) | | |
| **Germany** (0.9%) | | |
| *Automobiles* (0.5%) | | |
| Porsche Automobil Holding SE | 2,009 | 161,102 |
| Volkswagen AG | 2,434 | 397,293 |
| | | 558,395 |
| *Health Care Providers & Services* (0.0%) | | |
| Fresenius SE | 411 | 35,351 |
| *Household Products* (0.4%) | | |
| Henkel AG & Co. KGaA | 8,924 | 555,473 |
| *TOTAL GERMANY* | | 1,149,219 |
| **TOTAL PREFERRED STOCKS** (Cost $830,877) | | 1,149,219 |
| **TOTAL LONG STOCK POSITIONS** (Cost $132,908,331) | | 160,237,315 |
| **RIGHTS** (0.0%) | | |
| **United Kingdom** (0.0%) | | |
| *Chemicals* (0.0%) | | |
| Yule Catto & Co. PLC, strike price 1.16 GBP, expires 01/17/11* (Cost $6,760) | 13,424 | 18,548 |
| *TOTAL UNITED KINGDOM* | | 18,548 |
| **WARRANTS** (0.0%) | | |
| **Italy** (0.0%) | | |
| *Capital Markets* (0.0%) | | |
| Mediobanca SpA, strike price 0.04 EUR, expires 03/18/11* | 4,093 | 30 |
| *Commercial Banks* (0.0%) | | |
| Unione di Banche Italiane SCPA, strike price 12.30 EUR, expires 06/30/11* | 1,496 | 7 |
| *TOTAL ITALY* | | 37 |
| **TOTAL WARRANTS** (Cost $0) | | 37 |

| | Number of Shares | Value |
|---|---|---|
| **SHORT-TERM INVESTMENTS** (9.1%) | | |
| State Street Navigator Prime Portfolio, 0.3426%§§ | 10,797,489 | $ 10,797,489 |
| | **Par (000)** | |
| State Street Bank and Trust Co. Euro Time Deposit, 0.010%, 01/03/11 | $898 | 898,000 |
| **TOTAL SHORT-TERM INVESTMENTS** (Cost $11,695,489) | | 11,695,489 |
| **TOTAL INVESTMENTS AT VALUE** (133.6%) (Cost $144,610,580) | | 171,951,389 |
| **TOTAL SECURITIES SOLD SHORT** (-25.2%) (Proceeds $30,249,352) | | (32,413,945) |
| **LIABILITIES IN EXCESS OF OTHER ASSETS** (-8.4%) | | (10,789,051) |
| **NET ASSETS** (100.0%) | | $128,748,393 |
| | **Number of Shares** | |
| **SHORT STOCK POSITIONS** (-25.2%) | | |
| **COMMON STOCKS** (-25.2%) | | |
| **Austria** (-0.1%) | | |
| *Metals & Mining* (-0.1%) | | |
| Randgold Resources, Ltd. | (851) | (70,471) |
| *TOTAL AUSTRIA* | | (70,471) |
| **Belgium** (-0.9%) | | |
| *Chemicals* (-0.1%) | | |
| Solvay SA | (1,513) | (161,961) |
| *Commercial Banks* (-0.1%) | | |
| Dexia SA* | (33,069) | (115,338) |
| KBC Groep NV* | (1,359) | (46,487) |
| | | (161,825) |
| *Diversified Financial Services* (-0.4%) | | |
| Ackermans & van Haaren NV | (436) | (36,550) |
| Groupe Bruxelles Lambert SA | (3,529) | (298,090) |
| Nationale A Portefeuille | (2,288) | (112,398) |
| | | (447,038) |
| *Insurance* (-0.1%) | | |
| Fortis | (50,000) | (114,729) |
| *Real Estate Investment Trusts* (-0.2%) | | |
| Cofinimmo | (1,625) | (212,366) |
| *Wireless Telecommunication Services* (-0.0%) | | |
| Mobistar SA | (398) | (25,927) |
| *TOTAL BELGIUM* | | (1,123,846) |

See Accompanying Notes to Financial Statements.

| | Number of Shares | Value |
|---|---|---|
| **SHORT STOCK POSITIONS** | | |
| **COMMON STOCKS** | | |
| **Canada** (0.0%) | | |
| *Independent Power Producers & Energy Traders* (-0.0%) | | |
| Etrion Corp.* | (7,234) | $ (4,982) |
| *TOTAL CANADA* | | (4,982) |
| **Denmark** (-0.5%) | | |
| *Chemicals* (-0.1%) | | |
| Novozymes AS B Shares | (1,151) | (161,273) |
| *Electrical Equipment* (-0.1%) | | |
| Vestas Wind Systems AS* | (4,029) | (128,132) |
| *Marine* (-0.1%) | | |
| D/S Norden | (2,267) | (82,749) |
| *Road & Rail* (-0.2%) | | |
| DSV AS | (12,918) | (287,548) |
| *TOTAL DENMARK* | | (659,702) |
| **Finland** (-0.7%) | | |
| *Diversified Financial Services* (-0.2%) | | |
| Pohjola Bank PLC | (19,177) | (230,971) |
| *Diversified Telecommunication Services* (-0.1%) | | |
| Elisa Oyj | (7,604) | (166,204) |
| *Media* (-0.2%) | | |
| Sanoma Oyj | (10,774) | (234,591) |
| *Metals & Mining* (-0.2%) | | |
| Rautaruukki Oyj | (9,180) | (216,406) |
| *Oil, Gas & Consumable Fuels* (-0.0%) | | |
| Neste Oil Oyj | (1,588) | (25,492) |
| *TOTAL FINLAND* | | (873,664) |
| **France** (-3.4%) | | |
| *Aerospace & Defense* (-0.0%) | | |
| Thales SA | (1,564) | (54,997) |
| *Airlines* (-0.2%) | | |
| Air France-KLM* | (15,869) | (290,820) |
| *Beverages* (-0.2%) | | |
| Pernod-Ricard SA | (2,056) | (194,289) |
| *Communications Equipment* (-0.1%) | | |
| Alcatel-Lucent* | (20,985) | (61,633) |
| *Construction & Engineering* (-0.2%) | | |
| Eiffage SA | (4,993) | (221,326) |
| *Construction Materials* (-0.1%) | | |
| Imerys SA | (1,974) | (132,276) |

| | Number of Shares | Value |
|---|---|---|
| **SHORT STOCK POSITIONS** | | |
| **COMMON STOCKS** | | |
| **France** | | |
| *Diversified Telecommunication Services* (-0.2%) | | |
| Iliad SA | (2,192) | $ (239,459) |
| *Electric Utilities* (-0.1%) | | |
| Electricite de France | (4,128) | (170,192) |
| *Energy Equipment & Services* (-0.1%) | | |
| Cie Generale de Geophysique-Veritas* | (2,133) | (65,370) |
| *Food & Staples Retailing* (-0.1%) | | |
| Casino Guichard Perrachon SA | (1,514) | (148,307) |
| *Health Care Equipment & Supplies* (-0.3%) | | |
| BioMerieux | (2,345) | (232,331) |
| Cie Generale d'Optique Essilor International SA | (3,123) | (202,007) |
| | | (434,338) |
| *Hotels, Restaurants & Leisure* (-0.4%) | | |
| Accor SA | (6,568) | (293,868) |
| Sodexo | (2,447) | (169,516) |
| | | (463,384) |
| *Media* (-0.5%) | | |
| JC Decaux SA* | (6,959) | (215,112) |
| Lagardere SCA | (2,137) | (88,453) |
| Publicis Groupe | (5,797) | (303,682) |
| Societe Television Francaise 1 | (4,556) | (79,513) |
| | | (686,760) |
| *Metals & Mining* (-0.1%) | | |
| Eramet | (428) | (147,449) |
| *Professional Services* (-0.2%) | | |
| Bureau Veritas SA | (480) | (36,569) |
| Teleperformance | (7,073) | (239,736) |
| | | (276,305) |
| *Real Estate Investment Trusts* (-0.3%) | | |
| ICADE | (2,388) | (244,800) |
| Klepierre | (2,222) | (80,568) |
| Unibail-Rodamco SE | (460) | (91,436) |
| | | (416,804) |
| *Transportation Infrastructure* (-0.3%) | | |
| Aeroports de Paris | (3,050) | (242,002) |
| Groupe Eurotunnel SA | (13,572) | (119,905) |
| | | (361,907) |
| *TOTAL FRANCE* | | (4,365,616) |

See Accompanying Notes to Financial Statements.

| | Number of Shares | Value |
|---|---|---|
| **SHORT STOCK POSITIONS** | | |
| **COMMON STOCKS** | | |
| **Germany** (-2.1%) | | |
| *Aerospace & Defense* (-0.1%) | | |
| MTU Aero Engines Holding AG | (1,533) | $ (103,912) |
| *Airlines* (-0.2%) | | |
| Deutsche Lufthansa AG* | (12,477) | (272,473) |
| *Chemicals* (-0.2%) | | |
| K+S AG | (1,302) | (98,520) |
| Wacker Chemie AG | (1,055) | (184,656) |
| | | (283,176) |
| *Construction Materials* (-0.3%) | | |
| HeidelbergCement AG | (5,206) | (328,026) |
| *Food & Staples Retailing* (-0.0%) | | |
| Metro AG | (770) | (55,794) |
| *Health Care Providers & Services* (-0.5%) | | |
| Celesio AG | (6,499) | (162,594) |
| Fresenius Medical Care AG & Co. KGaA | (1,911) | (110,300) |
| Rhoen-Klinikum AG | (17,000) | (375,654) |
| | | (648,548) |
| *Industrial Conglomerates* (-0.1%) | | |
| Rheinmetall AG | (753) | (60,557) |
| *Internet Software & Services* (-0.0%) | | |
| United Internet AG | (1,943) | (31,738) |
| *Machinery* (-0.0%) | | |
| MAN SE | (473) | (56,558) |
| *Metals & Mining* (-0.2%) | | |
| Salzgitter AG | (3,558) | (276,162) |
| *Personal Products* (-0.2%) | | |
| Beiersdorf AG | (4,720) | (262,941) |
| *Software* (-0.0%) | | |
| Software AG | (217) | (31,932) |
| *Transportation Infrastructure* (-0.3%) | | |
| Fraport AG Frankfurt Airport Services Worldwide | (5,529) | (350,450) |
| *TOTAL GERMANY* | | (2,762,267) |
| **Italy** (-2.7%) | | |
| *Aerospace & Defense* (-0.3%) | | |
| Finmeccanica SpA | (29,040) | (331,692) |
| *Capital Markets* (-0.2%) | | |
| Mediobanca SpA | (24,993) | (223,804) |

| | Number of Shares | Value |
|---|---|---|
| **SHORT STOCK POSITIONS** | | |
| **COMMON STOCKS** | | |
| **Italy** | | |
| *Commercial Banks* (-0.7%) | | |
| Banca Monte dei Paschi di Siena SpA* | (49,999) | $ (57,309) |
| Banca Popolare di Milano Scarl | (49,999) | (175,918) |
| Banco Popolare SC | (49,999) | (227,840) |
| Intesa Sanpaolo SpA | (50,000) | (136,465) |
| Unione di Banche Italiane SCPA | (31,513) | (277,586) |
| | | (875,118) |
| *Diversified Financial Services* (-0.1%) | | |
| Exor SpA | (5,407) | (179,163) |
| *Diversified Telecommunication Services* (-0.0%) | | |
| Telecom Italia SpA | (49,999) | (54,632) |
| *Energy Equipment & Services* (-0.1%) | | |
| Saipem SpA | (3,185) | (157,870) |
| *Food Products* (-0.1%) | | |
| Parmalat SpA | (47,472) | (130,730) |
| *Gas Utilities* (-0.1%) | | |
| Snam Rete Gas SpA | (16,341) | (81,693) |
| *Hotels, Restaurants & Leisure* (-0.2%) | | |
| Autogrill SpA* | (17,137) | (243,573) |
| *Insurance* (-0.2%) | | |
| Assicurazioni Generali SpA | (6,705) | (128,162) |
| Societa Cattolica di Assicurazioni Scrl | (6,889) | (175,958) |
| | | (304,120) |
| *Multi-Utilities* (-0.2%) | | |
| A2A SpA | (50,000) | (69,089) |
| ACEA SpA* | (20,533) | (237,084) |
| | | (306,173) |
| *Oil, Gas & Consumable Fuels* (-0.1%) | | |
| Saras SpA* | (49,999) | (106,002) |
| *Textiles, Apparel & Luxury Goods* (-0.2%) | | |
| Luxottica Group SpA | (6,526) | (200,281) |
| *Transportation Infrastructure* (-0.2%) | | |
| Atlantia SpA | (15,913) | (326,237) |
| *TOTAL ITALY* | | (3,521,088) |
| **Japan** (-5.9%) | | |
| *Air Freight & Logistics* (-0.1%) | | |
| Kintetsu World Express, Inc. | (700) | (19,948) |
| Yamato Holdings Co., Ltd. | (3,000) | (42,601) |
| Yusen Air & Sea Service Co., Ltd. | (1,400) | (20,351) |
| | | (82,900) |

| | Number of Shares | Value |
|---|---|---|
| **SHORT STOCK POSITIONS** | | |
| **COMMON STOCKS** | | |
| **Japan** | | |
| *Auto Components* (-0.3%) | | |
| Exedy Corp. | (500) | $ (16,184) |
| FCC Co., Ltd. | (800) | (18,600) |
| Futaba Industrial Co., Ltd.* | (2,700) | (19,512) |
| Kayaba Industry Co., Ltd. | (4,000) | (30,562) |
| Keihin Corp. | (700) | (15,715) |
| Musashi Seimitsu Industry Co., Ltd. | (700) | (17,379) |
| Nifco, Inc. | (700) | (18,932) |
| Nissan Shatai Co., Ltd. | (3,000) | (26,120) |
| Nissin Kogyo Co., Ltd. | (1,100) | (20,478) |
| Press Kogyo Co., Ltd.* | (5,000) | (23,896) |
| Showa Corp.* | (2,200) | (16,752) |
| Stanley Electric Co., Ltd. | (800) | (14,892) |
| T RAD Co., Ltd. | (7,000) | (28,722) |
| Tachi-S Co., Ltd. | (400) | (6,532) |
| Takata Corp. | (800) | (23,583) |
| Teikoku Piston Ring Co., Ltd. | (2,300) | (23,265) |
| Toyoda Gosei Co., Ltd. | (900) | (21,079) |
| Toyota Boshoku Corp. | (800) | (14,080) |
| | | (356,283) |
| *Beverages* (-0.1%) | | |
| Coca-Cola Central Japan Co., Ltd. | (1,600) | (21,377) |
| Coca-Cola West Co., Ltd. | (900) | (16,308) |
| Ito En, Ltd. | (1,300) | (21,608) |
| Sapporo Holdings, Ltd. | (5,000) | (22,608) |
| Takara Holdings, Inc. | (1,000) | (5,875) |
| | | (87,776) |
| *Building Products* (-0.1%) | | |
| Central Glass Co., Ltd. | (5,000) | (23,201) |
| Nitto Boseki Co., Ltd. | (4,000) | (10,067) |
| Noritz Corp. | (1,100) | (19,405) |
| Sanwa Holdings Corp. | (5,000) | (15,754) |
| Sekisui Jushi Corp. | (2,000) | (20,407) |
| Takasago Thermal Engineering Co., Ltd. | (2,000) | (16,728) |
| TOTO, Ltd. | (5,000) | (36,172) |
| | | (141,734) |
| *Capital Markets* (-0.1%) | | |
| Jafco Co., Ltd. | (800) | (23,153) |
| Marusan Securities Co., Ltd. | (2,900) | (17,307) |
| Matsui Securities Co., Ltd. | (3,300) | (23,399) |
| Mizuho Investors Securities Co., Ltd.* | (16,000) | (17,305) |
| Okasan Securities Group, Inc. | (4,000) | (16,438) |
| SBI Holdings, Inc. | (279) | (42,118) |
| | | (139,720) |

| | Number of Shares | Value |
|---|---|---|
| **SHORT STOCK POSITIONS** | | |
| **COMMON STOCKS** | | |
| **Japan** | | |
| *Chemicals* (-0.3%) | | |
| Dainichiseika Color & Chemicals Manufacturing Co., Ltd. | (4,000) | $ (21,853) |
| Kansai Paint Co., Ltd. | (3,000) | (28,997) |
| KUREHA Corp. | (3,000) | (18,073) |
| Lintec Corp. | (700) | (18,505) |
| Mitsubishi Chemical Holdings Corp. | (3,138) | (21,219) |
| Nippon Paint Co., Ltd. | (3,000) | (22,958) |
| NOF Corp. | (5,000) | (24,419) |
| Okamoto Industries, Inc. | (4,000) | (16,554) |
| Sakai Chemical Industry Co., Ltd. | (4,000) | (19,789) |
| Shin-Etsu Polymer Co., Ltd. | (1,300) | (8,110) |
| T Hasegawa Co., Ltd. | (1,000) | (16,992) |
| Taiyo Ink Manufacturing Co., Ltd. | (600) | (19,197) |
| Takasago International Corp. | (1,000) | (5,972) |
| Takiron Co., Ltd. | (2,000) | (6,858) |
| Teijin, Ltd. | (9,000) | (38,358) |
| Tenma Corp. | (1,400) | (15,432) |
| Tokai Carbon Co., Ltd. | (3,000) | (18,596) |
| Tokuyama Corp. | (3,000) | (15,479) |
| Tokyo Ohka Kogyo Co., Ltd. | (1,100) | (23,600) |
| | | (360,961) |
| *Commercial Banks* (-0.5%) | | |
| Aozora Bank, Ltd. | (14,000) | (28,906) |
| Bank of the Ryukyus, Ltd. | (2,500) | (29,495) |
| Mizuho Trust & Banking Co., Ltd.* | (8,700) | (8,971) |
| Sapporo Hokuyo Holdings, Inc. | (8,300) | (38,824) |
| Suruga Bank, Ltd. | (3,000) | (27,867) |
| The 77 Bank, Ltd. | (5,000) | (26,442) |
| The Aichi Bank, Ltd. | (400) | (24,846) |
| The Awa Bank, Ltd. | (3,000) | (18,082) |
| The Bank of Kyoto, Ltd. | (3,000) | (28,387) |
| The Bank of Okinawa, Ltd. | (700) | (27,139) |
| The Chugoku Bank, Ltd. | (4,000) | (48,318) |
| The Chukyo Bank, Ltd. | (5,000) | (13,104) |
| The Fukui Bank, Ltd. | (7,000) | (21,643) |
| The Fukushima Bank, Ltd. | (33,000) | (19,860) |
| The Hachijuni Bank, Ltd. | (4,000) | (22,310) |
| The Hokkoku Bank, Ltd. | (4,000) | (13,896) |
| The Hyakugo Bank, Ltd. | (5,000) | (21,532) |
| The Iyo Bank, Ltd. | (4,000) | (31,946) |
| The Kagoshima Bank, Ltd. | (2,000) | (13,366) |
| The Musashino Bank, Ltd. | (200) | (6,050) |
| The Nanto Bank, Ltd. | (6,000) | (30,024) |
| The Oita Bank, Ltd. | (7,000) | (25,067) |
| The San-In Godo Bank, Ltd. | (3,000) | (21,595) |
| The Shiga Bank, Ltd. | (3,000) | (16,304) |

| | Number of Shares | Value |
|---|---|---|
| **SHORT STOCK POSITIONS** | | |
| **COMMON STOCKS** | | |
| **Japan** | | |
| *Commercial Banks* | | |
| The Tochigi Bank, Ltd. | (4,000) | $ (18,935) |
| The Tsukuba Bank, Ltd.* | (7,600) | (26,504) |
| The Yamagata Bank, Ltd. | (6,000) | (27,742) |
| The Yamanashi Chuo Bank, Ltd. | (2,000) | (8,987) |
| Yamaguchi Financial Group, Inc. | (2,000) | (20,163) |
| | | (666,305) |
| *Commercial Services & Supplies* (-0.0%) | | |
| Moshi Moshi Hotline, Inc. | (1,100) | (28,870) |
| Park24 Co., Ltd. | (1,500) | (16,032) |
| Pilot Corp. | (10) | (17,690) |
| | | (62,592) |
| *Communications Equipment* (-0.0%) | | |
| Icom, Inc. | (800) | (21,912) |
| Uniden Corp.* | (6,000) | (18,475) |
| | | (40,387) |
| *Computers & Peripherals* (-0.0%) | | |
| Eizo Nanao Corp. | (400) | (9,369) |
| Japan Digital Laboratory Co., Ltd. | (2,200) | (24,992) |
| Melco Holdings, Inc. | (700) | (24,428) |
| | | (58,789) |
| *Construction & Engineering* (-0.3%) | | |
| Chiyoda Corp. | (2,000) | (19,830) |
| Chudenko Corp. | (2,700) | (32,200) |
| COMSYS Holdings Corp. | (2,000) | (21,267) |
| Kandenko Co., Ltd. | (3,000) | (20,124) |
| Kinden Corp. | (4,166) | (38,430) |
| Maeda Road Construction Co., Ltd. | (1,000) | (7,989) |
| NEC Networks & System Integration Corp. | (2,400) | (31,125) |
| Nippon Densetsu Kogyo Co., Ltd. | (2,000) | (19,282) |
| Penta-Ocean Construction Co., Ltd. | (11,000) | (18,643) |
| Sanki Engineering Co., Ltd. | (2,000) | (13,732) |
| SHO-BOND Holdings Co., Ltd. | (800) | (16,865) |
| Taihei Dengyo Kaisha, Ltd. | (3,000) | (24,539) |
| Taikisha, Ltd. | (1,900) | (33,646) |
| Toshiba Plant Systems & Services Corp. | (2,000) | (28,671) |
| | | (326,343) |
| *Consumer Finance* (-0.0%) | | |
| Aeon Credit Service Co., Ltd. | (1,900) | (26,763) |
| Hitachi Capital Corp. | (1,200) | (18,499) |
| | | (45,262) |

| | Number of Shares | Value |
|---|---|---|
| **SHORT STOCK POSITIONS** | | |
| **COMMON STOCKS** | | |
| **Japan** | | |
| *Containers & Packaging* (-0.1%) | | |
| FP Corp. | (300) | $ (16,619) |
| Fuji Seal International, Inc. | (400) | (9,238) |
| Nihon Yamamura Glass Co., Ltd. | (7,000) | (19,199) |
| Rengo Co., Ltd. | (4,000) | (27,102) |
| | | (72,158) |
| *Distributors* (-0.0%) | | |
| Canon Marketing Japan, Inc. | (1,300) | (18,485) |
| Doshisha Co., Ltd. | (700) | (16,350) |
| | | (34,835) |
| *Diversified Consumer Services* (-0.0%) | | |
| Benesse Corp. | (700) | (32,241) |
| *Diversified Financial Services* (-0.0%) | | |
| IBJ Leasing Co., Ltd. | (900) | (22,618) |
| Japan Securities Finance Co., Ltd. | (2,800) | (20,469) |
| | | (43,087) |
| *Electric Utilities* (-0.1%) | | |
| Hokkaido Electric Power Co., Inc. | (1,600) | (32,707) |
| Hokuriku Electric Power Co. | (1,499) | (36,846) |
| Shikoku Electric Power Co., Inc. | (600) | (17,642) |
| The Chugoku Electric Power Co., Inc | (800) | (16,254) |
| | | (103,449) |
| *Electrical Equipment* (-0.1%) | | |
| Cosel Co., Ltd. | (1,400) | (20,694) |
| Daihen Corp. | (2,000) | (9,723) |
| Fujikura, Ltd. | (4,000) | (20,141) |
| Futaba Corp. | (900) | (17,499) |
| Hitachi Cable, Ltd. | (8,000) | (22,016) |
| Mabuchi Motor Co., Ltd. | (400) | (20,583) |
| Nippon Signal Co., Ltd. | (2,000) | (15,851) |
| Nitto Kogyo Corp. | (1,700) | (19,210) |
| SWCC Showa Holdings Co., Ltd.* | (20,000) | (23,071) |
| | | (168,788) |
| *Electronic Equipment, Instruments & Components* (-0.2%) | | |
| CMK Corp. | (5,500) | (31,249) |
| Hamamatsu Photonics KK | (500) | (18,246) |
| Hirose Electric Co., Ltd. | (441) | (49,608) |
| Hitachi High-Technologies Corp. | (1,000) | (23,325) |
| Horiba, Ltd. | (600) | (16,976) |
| Ibiden Co., Ltd. | (1,200) | (37,681) |
| Koa Corp. | (2,000) | (25,558) |
| Shimadzu Corp. | (3,000) | (23,261) |
| Tamura Corp. | (6,000) | (18,258) |

See Accompanying Notes to Financial Statements.

| | Number of Shares | Value |
|---|---|---|
| **SHORT STOCK POSITIONS** | | |
| **COMMON STOCKS** | | |
| **Japan** | | |
| *Electronic Equipment, Instruments & Components* | | |
| Yamatake Corp. | (400) | $ (9,452) |
| Yaskawa Electric Corp. | (3,000) | (28,277) |
| Yokogawa Electric Corp. | (3,600) | (28,537) |
| | | (310,428) |
| *Food & Staples Retailing* (-0.2%) | | |
| Circle K Sunkus Co., Ltd. | (1,300) | (20,844) |
| FamilyMart Co., Ltd. | (700) | (26,363) |
| Lawson, Inc. | (600) | (29,651) |
| Matsumotokiyoshi Holdings Co., Ltd. | (900) | (19,524) |
| Sugi Holdings Co., Ltd. | (1,400) | (33,704) |
| Sundrug Co., Ltd. | (1,100) | (32,028) |
| Tsuruha Holdings, Inc. | (400) | (19,070) |
| Yaoko Co., Ltd. | (800) | (24,428) |
| | | (205,612) |
| *Food Products* (-0.3%) | | |
| Dydo Drinco, Inc. | (600) | (23,072) |
| Hokuto Corp. | (800) | (18,589) |
| Itoham Foods, Inc. | (5,000) | (17,974) |
| Kikkoman Corp. | (2,000) | (22,372) |
| Marudai Food Co., Ltd. | (6,000) | (19,573) |
| Nisshin Seifun Group, Inc. | (2,000) | (25,344) |
| Nissin Foods Holdings Co., Ltd. | (1,196) | (42,848) |
| QP Corp. | (2,500) | (31,714) |
| Sakata Seed Corp. | (2,400) | (32,384) |
| Toyo Suisan Kaisha, Ltd. | (1,000) | (22,226) |
| Yakult Honsha Co., Ltd. | (1,200) | (34,537) |
| Yamazaki Baking Co., Ltd. | (3,224) | (38,861) |
| | | (329,494) |
| *Gas Utilities* (-0.0%) | | |
| Shizuoka Gas Co., Ltd. | (3,500) | (20,923) |
| *Health Care Equipment & Supplies* (-0.1%) | | |
| Hitachi Medical Corp. | (2,000) | (19,735) |
| Hogy Medical Co., Ltd. | (400) | (19,460) |
| Jeol, Ltd. | (3,000) | (10,508) |
| Nihon Kohden Corp. | (1,000) | (21,529) |
| Olympus Corp. | (900) | (27,128) |
| Sysmex Corp. | (400) | (27,694) |
| | | (126,054) |
| *Health Care Providers & Services* (-0.1%) | | |
| BML, Inc. | (500) | (14,010) |
| Miraca Holdings, Inc. | (500) | (20,092) |
| Nichii Gakkan Co. | (2,600) | (22,910) |

See Accompanying Notes to Financial Statements.

| | Number of Shares | Value |
|---|---|---|
| **SHORT STOCK POSITIONS** | | |
| **COMMON STOCKS** | | |
| **Japan** | | |
| *Health Care Providers & Services* | | |
| Suzuken Co., Ltd. | (700) | $ (21,366) |
| Toho Holdings Co., Ltd. | (2,100) | (28,708) |
| | | (107,086) |
| *Hotels, Restaurants & Leisure* (-0.2%) | | |
| Accordia Golf Co., Ltd. | (36) | (34,908) |
| Doutor Nichires Holdings Co., Ltd. | (700) | (9,541) |
| HIS Co., Ltd. | (1,500) | (37,290) |
| Kisoji Co., Ltd. | (800) | (17,014) |
| Kura Corp. | (1,400) | (21,943) |
| Oriental Land Co. Japan, Ltd. | (400) | (37,036) |
| Plenus Co., Ltd. | (2,000) | (30,566) |
| Saizeriya Co., Ltd. | (1,600) | (32,349) |
| | | (220,647) |
| *Household Durables* (-0.1%) | | |
| Alpine Electronics, Inc. | (1,600) | (22,714) |
| Arnest One Corp. | (800) | (10,260) |
| Cleanup Corp. | (2,800) | (19,124) |
| Funai Electric Co., Ltd. | (500) | (17,371) |
| Rinnai Corp. | (500) | (30,513) |
| Sekisui Chemical Co., Ltd. | (4,000) | (28,647) |
| Takamatsu Construction Group Co., Ltd. | (700) | (9,439) |
| | | (138,068) |
| *Household Products* (-0.1%) | | |
| Lion Corp. | (3,000) | (16,363) |
| Pigeon Corp. | (1,000) | (33,987) |
| Unicharm Corp. | (900) | (35,776) |
| | | (86,126) |
| *Industrial Conglomerates* (-0.0%) | | |
| Hankyu Hanshin Holdings, Inc. | (3,000) | (13,919) |
| *Insurance* (-0.1%) | | |
| Sony Financial Holdings, Inc. | (12) | (48,379) |
| The Fuji Fire & Marine Insurance Co., Ltd.* | (11,000) | (14,971) |
| | | (63,350) |
| *Internet & Catalog Retail* (-0.0%) | | |
| Rakuten, Inc.* | (35) | (29,320) |
| *Internet Software & Services* (-0.0%) | | |
| Kakaku.com, Inc. | (3) | (17,824) |
| Yahoo! Japan Corp. | (89) | (34,437) |
| | | (52,261) |

See Accompanying Notes to Financial Statements.

| | Number of Shares | Value |
|---|---|---|
| **SHORT STOCK POSITIONS** | | |
| **COMMON STOCKS** | | |
| **Japan** | | |
| *IT Services* (-0.1%) | | |
| Ines Corp. | (2,200) | $ (17,902) |
| Information Services International-Dentsu, Ltd. | (2,300) | (16,573) |
| Itochu Techno-Science Corp. | (500) | (18,725) |
| NET One Systems Co., Ltd. | (14) | (20,694) |
| Nihon Unisys, Ltd. | (3,000) | (23,972) |
| TKC | (800) | (16,933) |
| | | (114,799) |
| *Leisure Equipment & Products* (-0.0%) | | |
| Nidec Copal Corp. | (1,100) | (19,715) |
| Shimano, Inc. | (500) | (25,374) |
| | | (45,089) |
| *Machinery* (-0.4%) | | |
| Aichi Corp. | (4,000) | (17,164) |
| Asahi Diamond Industrial Co., Ltd. | (1,000) | (18,983) |
| Daiwa Industries, Ltd. | (3,000) | (15,245) |
| Fujitec Co., Ltd. | (2,000) | (10,171) |
| Furukawa Co., Ltd.* | (14,000) | (16,514) |
| Glory, Ltd. | (700) | (17,248) |
| Hino Motors, Ltd. | (6,000) | (32,380) |
| Komori Corp. | (1,700) | (20,092) |
| Kurita Water Industries, Ltd. | (1,300) | (40,852) |
| Makino Milling Machine Co., Ltd.* | (4,000) | (32,824) |
| Miura Co., Ltd. | (700) | (18,665) |
| Mori Seiki Co., Ltd. | (1,900) | (22,448) |
| Nabtesco Corp. | (1,000) | (21,284) |
| Nippon Thompson Co., Ltd. | (3,000) | (24,134) |
| Noritake Co., Ltd. | (4,000) | (14,273) |
| OSG Corp. | (3,000) | (36,169) |
| Shima Seiki Manufacturing, Ltd. | (900) | (21,646) |
| Takuma Co., Ltd.* | (6,000) | (16,644) |
| The Japan Steel Works, Ltd. | (3,000) | (31,278) |
| THK Co., Ltd. | (1,300) | (29,766) |
| Tocalo Co., Ltd. | (1,100) | (21,165) |
| Toshiba Machine Co., Ltd. | (4,000) | (20,172) |
| Tsukishima Kikai Co., Ltd. | (2,000) | (14,817) |
| Union Tool Co. | (900) | (25,855) |
| | | (539,789) |
| *Marine* (-0.0%) | | |
| Inui Steamship Co., Ltd. | (5,700) | (33,837) |
| *Media* (-0.1%) | | |
| Asatsu-DK, Inc. | (1,000) | (27,232) |
| Dentsu, Inc. | (500) | (15,465) |
| Gakken Co., Ltd. | (10,000) | (21,944) |

See Accompanying Notes to Financial Statements.

| | Number of Shares | Value |
|---|---|---|
| **SHORT STOCK POSITIONS** | | |
| **COMMON STOCKS** | | |
| **Japan** | | |
| *Media* | | |
| Hakuhodo DY Holdings, Inc. | (429) | $ (24,525) |
| Jupiter Telecommunications Co., Ltd. | (38) | (39,907) |
| Toho Co., Ltd. | (1,400) | (22,471) |
| | | (151,544) |
| *Metals & Mining* (-0.2%) | | |
| Aichi Steel Corp. | (4,000) | (27,359) |
| Furukawa-Sky Aluminum Corp. | (4,000) | (11,639) |
| Godo Steel, Ltd. | (5,000) | (10,606) |
| Hitachi Metals, Ltd. | (2,000) | (23,934) |
| Neturen Co., Ltd. | (1,400) | (11,731) |
| Nippon Denko Co., Ltd. | (3,000) | (23,727) |
| Nippon Yakin Kogyo Co., Ltd.* | (5,500) | (16,211) |
| Nisshin Steel Co., Ltd. | (10,000) | (22,218) |
| Osaka Steel Co., Ltd. | (1,100) | (19,546) |
| Sanyo Special Steel Co., Ltd. | (3,000) | (18,055) |
| Tokyo Rope Manufacturing Co., Ltd. | (9,000) | (29,940) |
| Tokyo Steel Manufacturing Co., Ltd. | (3,300) | (35,889) |
| Toyo Kohan Co., Ltd. | (4,000) | (24,588) |
| | | (275,443) |
| *Multiline Retail* (-0.2%) | | |
| Don Quijote Co., Ltd. | (1,200) | (36,552) |
| Fuji Co., Ltd. | (1,600) | (33,531) |
| H2O Retailing Corp. | (2,000) | (14,574) |
| Isetan Mitsukoshi Holdings, Ltd. | (3,400) | (39,447) |
| Izumi Co., Ltd. | (1,200) | (17,664) |
| J Front Retailing Co., Ltd. | (5,000) | (27,276) |
| Marui Group Co., Ltd. | (3,304) | (26,855) |
| Takashimaya Co., Ltd. | (5,000) | (42,750) |
| | | (238,649) |
| *Oil, Gas & Consumable Fuels* (-0.1%) | | |
| Japan Petroleum Exploration Co. | (1,000) | (37,962) |
| Kanto Natural Gas Development, Ltd. | (3,000) | (16,165) |
| Nippon Gas Co., Ltd. | (1,500) | (20,736) |
| | | (74,863) |
| *Paper & Forest Products* (-0.0%) | | |
| Daio Paper Corp. | (2,000) | (14,370) |
| Mitsubishi Paper Mills, Ltd.* | (24,000) | (28,616) |
| | | (42,986) |
| *Personal Products* (-0.1%) | | |
| Aderans Holdings Co., Ltd.* | (1,300) | (17,413) |
| Fancl Corp. | (1,500) | (22,509) |
| Kobayashi Pharmaceutical Co., Ltd. | (700) | (32,511) |

| | Number of Shares | Value |
|---|---|---|
| **SHORT STOCK POSITIONS** | | |
| **COMMON STOCKS** | | |
| **Japan** | | |
| *Personal Products* | | |
| Kose Corp. | (1,200) | $ (31,024) |
| Mandom Corp. | (700) | (18,955) |
| Milbon Co., Ltd. | (770) | (20,262) |
| | | (142,674) |
| *Pharmaceuticals* (-0.3%) | | |
| Chugai Pharmaceutical Co., Ltd. | (1,900) | (34,827) |
| Hisamitsu Pharmaceutical Co., Inc. | (800) | (33,659) |
| Kissei Pharmaceutical Co., Ltd. | (1,000) | (19,657) |
| Kyowa Hakko Kirin Co., Ltd. | (3,000) | (30,842) |
| Mitsubishi Tanabe Pharma Corp. | (1,000) | (16,875) |
| Nippon Shinyaku Co., Ltd. | (2,000) | (28,634) |
| Rohto Pharmaceutical Co., Ltd. | (1,000) | (11,699) |
| Santen Pharmaceutical Co., Ltd. | (1,019) | (35,366) |
| Taisho Pharmaceutical Co., Ltd. | (1,339) | (29,296) |
| Torii Pharmaceutical Co., Ltd. | (1,000) | (21,677) |
| Towa Pharmaceutical Co., Ltd. | (400) | (22,213) |
| Tsumura & Co. | (1,400) | (45,279) |
| | | (330,024) |
| *Professional Services* (-0.0%) | | |
| Meitec Corp.* | (1,300) | (27,758) |
| *Real Estate Management & Development* (-0.1%) | | |
| Aeon Mall Co., Ltd. | (1,068) | (28,600) |
| Daibiru Corp. | (2,700) | (22,169) |
| Goldcrest Co., Ltd. | (730) | (19,041) |
| Iida Home Max | (2,400) | (25,986) |
| Nomura Real Estate Holdings, Inc. | (700) | (12,715) |
| NTT Urban Development Corp. | (24) | (23,585) |
| Shoei Co., Ltd./Chiyoda-ku | (2,300) | (20,970) |
| | | (153,066) |
| *Road & Rail* (-0.1%) | | |
| Fukuyama Transporting Co., Ltd. | (4,000) | (21,251) |
| Hitachi Transport System, Ltd. | (2,000) | (30,934) |
| Keihin Electric Express Railway Co., Ltd. | (2,983) | (26,338) |
| Keio Corp. | (5,000) | (34,092) |
| Keisei Electric Railway Co., Ltd. | (4,000) | (26,653) |
| Nippon Konpo Unyu Soko Co., Ltd. | (1,000) | (12,156) |
| Nishi-Nippon Railroad Co., Ltd. | (4,000) | (16,753) |
| Tobu Railway Co., Ltd. | (4,000) | (22,457) |
| | | (190,634) |
| *Semiconductors & Semiconductor Equipment* (-0.1%) | | |
| Advantest Corp. | (1,400) | (31,509) |
| Mitsui High-Tec, Inc.* | (1,900) | (11,180) |

See Accompanying Notes to Financial Statements.

| | Number of Shares | Value |
|---|---|---|
| **SHORT STOCK POSITIONS** | | |
| **COMMON STOCKS** | | |
| **Japan** | | |
| *Semiconductors & Semiconductor Equipment* | | |
| Sanken Electric Co., Ltd. | (2,000) | $ (8,783) |
| Shinkawa, Ltd. | (2,900) | (29,635) |
| Sumco Corp.* | (1,100) | (15,680) |
| | | (96,787) |
| *Software* (-0.1%) | | |
| Capcom Co., Ltd. | (1,000) | (16,054) |
| DTS Corp. | (1,200) | (14,853) |
| Fuji Soft, Inc. | (800) | (13,806) |
| NSD Co., Ltd. | (1,600) | (18,895) |
| Oracle Corp. | (500) | (24,536) |
| Square Enix Co., Ltd. | (1,100) | (19,477) |
| Sumisho Computer Systems Corp. | (1,000) | (17,902) |
| | | (125,523) |
| *Specialty Retail* (-0.2%) | | |
| ABC-Mart, Inc. | (800) | (28,525) |
| Alpen Co., Ltd. | (900) | (16,022) |
| AOKI Holdings, Inc. | (1,200) | (21,683) |
| Autobacs Seven Co., Ltd. | (500) | (19,621) |
| Komeri Co., Ltd. | (1,000) | (22,923) |
| Nishimatsuya Chain Co., Ltd. | (2,500) | (24,239) |
| Nitori Co., Ltd. | (444) | (38,839) |
| Point, Inc. | (300) | (13,155) |
| Shimachu Co., Ltd. | (900) | (21,027) |
| Shimamura Co., Ltd. | (300) | (27,797) |
| Tsutsumi Jewelry Co., Ltd. | (600) | (15,988) |
| USS Co., Ltd. | (379) | (30,961) |
| Xebio Co., Ltd. | (1,600) | (34,566) |
| | | (315,346) |
| *Textiles, Apparel & Luxury Goods* (-0.1%) | | |
| Asics Corp. | (2,051) | (26,279) |
| Gunze, Ltd. | (3,000) | (12,647) |
| Wacoal Holdings Corp. | (2,000) | (28,686) |
| | | (67,612) |
| *Trading Companies & Distributors* (-0.1%) | | |
| MISUMI Corp. | (900) | (22,354) |
| Nagase & Co., Ltd. | (1,000) | (12,921) |
| Shinsho Corp. | (4,000) | (9,930) |
| Trusco Nakayama Corp. | (1,400) | (23,472) |
| | | (68,677) |
| *Transportation Infrastructure* (-0.1%) | | |
| Japan Airport Terminal Co., Ltd. | (1,900) | (29,282) |
| Kamigumi Co., Ltd. | (3,964) | (33,211) |

| | Number of Shares | Value |
|---|---|---|
| **SHORT STOCK POSITIONS** | | |
| **COMMON STOCKS** | | |
| **Japan** | | |
| *Transportation Infrastructure* | | |
| Mitsubishi Logistics Corp. | (2,000) | $ (26,529) |
| The Sumitomo Warehouse Co., Ltd. | (2,000) | (10,515) |
| | | (99,537) |
| *TOTAL JAPAN* | | (7,661,535) |
| **Luxembourg** (-0.4%) | | |
| *Media* (-0.1%) | | |
| SES SA | (1,553) | (37,126) |
| *Personal Products* (-0.2%) | | |
| Oriflame Cosmetics SA | (4,876) | (256,843) |
| *Wireless Telecommunication Services* (-0.1%) | | |
| Millicom International Cellular SA | (1,695) | (162,764) |
| *TOTAL LUXEMBOURG* | | (456,733) |
| **Netherlands** (-1.9%) | | |
| *Aerospace & Defense* (-0.0%) | | |
| European Aeronautic Defence & Space Co. NV* | (2,008) | (47,041) |
| *Air Freight & Logistics* (-0.1%) | | |
| TNT NV | (4,529) | (120,243) |
| *Beverages* (-0.1%) | | |
| Heineken Holding NV | (1,436) | (62,696) |
| *Chemicals* (-0.2%) | | |
| Akzo Nobel NV | (3,523) | (220,051) |
| *Computers & Peripherals* (-0.0%) | | |
| Gemalto NV | (1,091) | (46,658) |
| *Energy Equipment & Services* (-0.1%) | | |
| SBM Offshore NV | (7,414) | (166,997) |
| *Insurance* (-0.2%) | | |
| Aegon NV* | (44,783) | (275,224) |
| *Life Sciences Tools & Services* (-0.2%) | | |
| QIAGEN NV* | (13,750) | (270,929) |
| *Media* (-0.5%) | | |
| Reed Elsevier NV | (23,707) | (294,652) |
| Wolters Kluwer NV | (14,039) | (309,094) |
| | | (603,746) |
| *Professional Services* (-0.1%) | | |
| Randstad Holding NV* | (1,526) | (80,964) |
| *Real Estate Investment Trusts* (-0.2%) | | |
| Corio NV | (4,233) | (272,862) |

See Accompanying Notes to Financial Statements.

| | Number of Shares | Value |
|---|---|---|
| **SHORT STOCK POSITIONS** | | |
| **COMMON STOCKS** | | |
| **Netherlands** | | |
| *Semiconductors & Semiconductor Equipment* (-0.1%) | | |
| STMicroelectronics NV | (10,410) | $ (108,683) |
| *Transportation Infrastructure* (-0.1%) | | |
| Koninklijke Vopak NV | (2,611) | (123,926) |
| *TOTAL NETHERLANDS* | | (2,400,020) |
| **Norway** (-0.2%) | | |
| *Commercial Banks* (-0.0%) | | |
| DnB NOR ASA | (1,002) | (14,151) |
| *Metals & Mining* (-0.2%) | | |
| Norsk Hydro ASA | (36,391) | (269,087) |
| *TOTAL NORWAY* | | (283,238) |
| **Spain** (-0.6%) | | |
| *Airlines* (-0.2%) | | |
| Iberia Lineas Aereas de Espana SA* | (50,000) | (215,389) |
| *Electric Utilities* (-0.1%) | | |
| Acciona SA | (1,554) | (110,738) |
| *Electrical Equipment* (-0.1%) | | |
| Gamesa Corp. Tecnologica SA* | (10,703) | (82,257) |
| *Independent Power Producers & Energy Traders* (-0.1%) | | |
| Iberdrola Renovables SA | (50,000) | (178,396) |
| *Machinery* (-0.1%) | | |
| Zardoya Otis SA | (14,568) | (206,284) |
| *TOTAL SPAIN* | | (793,064) |
| **Sweden** (-0.7%) | | |
| *Commercial Banks* (-0.1%) | | |
| Skandinaviska Enskilda Banken AB A Shares | (19,141) | (159,879) |
| *Diversified Financial Services* (-0.1%) | | |
| Kinnevik Investment AB | (6,627) | (135,016) |
| *Internet & Catalog Retail* (-0.0%) | | |
| CDON Group AB* | (1,005) | (4,649) |
| *Machinery* (-0.1%) | | |
| Volvo AB* | (8,361) | (143,057) |
| *Media* (-0.1%) | | |
| Modern Times Group AB B Shares | (1,005) | (66,610) |
| *Metals & Mining* (-0.2%) | | |
| SSAB AB A Shares | (14,518) | (244,790) |
| *Real Estate Management & Development* (-0.1%) | | |
| Castellum AB | (9,483) | (129,182) |
| *TOTAL SWEDEN* | | (883,183) |

| | Number of Shares | Value |
|---|---|---|
| **SHORT STOCK POSITIONS** | | |
| **COMMON STOCKS** | | |
| **Switzerland** (-2.6%) | | |
| *Biotechnology* (-0.2%) | | |
| Actelion, Ltd.* | (2,601) | $ (142,869) |
| Basilea Pharmaceutica AG* | (1,619) | (112,935) |
| | | (255,804) |
| *Construction Materials* (-0.2%) | | |
| Holcim, Ltd. | (2,722) | (206,621) |
| *Electric Utilities* (-0.1%) | | |
| BKW FMB Energie AG | (1,176) | (89,172) |
| *Food Products* (-0.1%) | | |
| Aryzta AG* | (3,379) | (156,571) |
| *Health Care Equipment & Supplies* (-0.6%) | | |
| Nobel Biocare Holding AG | (9,992) | (189,048) |
| Sonova Holding AG | (1,281) | (165,643) |
| Straumann Holding AG | (1,077) | (247,406) |
| Synthes, Inc. | (1,459) | (197,544) |
| | | (799,641) |
| *Insurance* (-0.3%) | | |
| Swiss Life Holding AG* | (1,790) | (258,979) |
| Swiss Reinsurance Co., Ltd. | (3,169) | (170,536) |
| | | (429,515) |
| *Life Sciences Tools & Services* (-0.1%) | | |
| Lonza Group AG | (2,416) | (194,257) |
| *Machinery* (-0.1%) | | |
| Georg Fischer AG* | (256) | (144,810) |
| *Marine* (-0.1%) | | |
| Kuehne + Nagel International AG | (532) | (74,247) |
| *Oil, Gas & Consumable Fuels* (-0.2%) | | |
| Petroplus Holdings AG* | (17,025) | (225,089) |
| *Professional Services* (-0.1%) | | |
| Adecco SA | (2,915) | (191,759) |
| *Real Estate Management & Development* (-0.5%) | | |
| PSP Swiss Property AG* | (2,711) | (217,907) |
| Swiss Prime Site AG* | (5,445) | (407,499) |
| | | (625,406) |
| *TOTAL SWITZERLAND* | | (3,392,892) |
| **United Kingdom** (-2.5%) | | |
| *Aerospace & Defense* (-0.0%) | | |
| Cobham PLC | (16,984) | (54,231) |

| | Number of Shares | Value |
|---|---|---|
| **SHORT STOCK POSITIONS** | | |
| **COMMON STOCKS** | | |
| **United Kingdom** | | |
| *Chemicals* (-0.1%) | | |
| Johnson Matthey PLC | (2,756) | $ (88,175) |
| *Commercial Services & Supplies* (-0.1%) | | |
| G4S PLC | (16,317) | (65,002) |
| Serco Group PLC | (6,678) | (58,215) |
| | | (123,217) |
| *Construction & Engineering* (-0.1%) | | |
| Balfour Beatty PLC | (13,826) | (67,891) |
| *Containers & Packaging* (-0.0%) | | |
| Rexam PLC | (8,272) | (43,140) |
| *Food & Staples Retailing* (-0.1%) | | |
| WM Morrison Supermarkets PLC | (42,076) | (176,535) |
| *Food Products* (-0.1%) | | |
| Associated British Foods PLC | (4,367) | (80,960) |
| *Health Care Equipment & Supplies* (-0.1%) | | |
| Smith & Nephew PLC | (9,314) | (98,759) |
| *Hotels, Restaurants & Leisure* (-0.3%) | | |
| Carnival PLC | (5,054) | (236,063) |
| Ladbrokes PLC | (49,999) | (96,415) |
| Thomas Cook Group PLC | (18,473) | (54,912) |
| | | (387,390) |
| *Household Durables* (-0.2%) | | |
| Berkeley Group Holdings PLC* | (16,298) | (227,686) |
| *Independent Power Producers & Energy Traders* (-0.0%) | | |
| Drax Group PLC | (8,303) | (48,027) |
| *Insurance* (-0.1%) | | |
| Admiral Group PLC | (2,922) | (69,403) |
| *Internet & Catalog Retail* (-0.0%) | | |
| Home Retail Group PLC | (15,455) | (45,863) |
| *Machinery* (-0.1%) | | |
| Invensys PLC | (13,872) | (76,990) |
| *Media* (-0.2%) | | |
| Reed Elsevier PLC | (36,311) | (308,009) |
| *Metals & Mining* (-0.2%) | | |
| Antofagasta PLC | (5,116) | (129,995) |
| Fresnillo PLC | (1,892) | (49,717) |
| Lonmin PLC* | (4,527) | (139,938) |
| | | (319,650) |

| | Number of Shares | Value |
|---|---|---|
| **SHORT STOCK POSITIONS** | | |
| **COMMON STOCKS** | | |
| **United Kingdom** | | |
| *Multi-Utilities* (-0.1%) | | |
| United Utilities Group PLC | (7,847) | $ (72,903) |
| *Multiline Retail* (-0.1%) | | |
| Marks & Spencer Group PLC | (15,274) | (88,448) |
| *Oil, Gas & Consumable Fuels* (-0.1%) | | |
| Tullow Oil PLC | (4,030) | (79,917) |
| *Professional Services* (-0.1%) | | |
| The Capita Group PLC | (13,685) | (149,458) |
| *Real Estate Investment Trusts* (-0.2%) | | |
| Hammerson PLC | (42,004) | (274,885) |
| *Road & Rail* (-0.0%) | | |
| Firstgroup PLC | (9,292) | (58,058) |
| *Software* (-0.2%) | | |
| Autonomy Corp. PLC* | (6,313) | (149,146) |
| The Sage Group PLC | (16,996) | (72,903) |
| | | (222,049) |
| *TOTAL UNITED KINGDOM* | | (3,161,644) |
| **TOTAL COMMON STOCKS** (Proceeds $30,249,352) | | (32,413,945) |
| **TOTAL SECURITIES SOLD SHORT** (Proceeds $30,249,352) | | $ (32,413,945) |

**INVESTMENT ABBREVIATION**

ADR = America Depository Receipt

* Non-income producing security.

§ Security or portion thereof is out on loan.

§§ Represents security purchased with cash collateral received for securities on loan. The rate shown is the annualized seven day yield at December 31, 2010.

^ Not readily marketable security; security is valued at fair value as determined in good faith by, or under the direction of, the Board of Trustees.

## Credit Suisse Trust — International Equity Flex III Portfolio
## Statement of Assets and Liabilities
December 31, 2010

| | |
|---|---|
| ***Assets*** | |
| Investments at value, including collateral for securities on loan of $10,797,489 (Cost $144,610,580) (Note 2) | $171,951,389[1] |
| Cash | 848 |
| Foreign currency at value (cost $47,141) | 48,220 |
| Cash segregated at brokers for short sales | 33,817,253 |
| Dividend and interest receivable | 215,811 |
| Receivable for portfolio shares sold | 39,034 |
| Receivable for investments sold | 533 |
| Prepaid expenses and other assets | 8,107 |
| Total Assets | 206,081,195 |
| ***Liabilities*** | |
| Advisory fee payable (Note 3) | 48,626 |
| Administrative services fee payable (Note 3) | 50,371 |
| Payable upon return of securities loaned (Note 2) | 44,614,742 |
| Securities sold short, at value (Proceeds $30,249,352) (Note 2) | 32,413,945 |
| Payable for portfolio shares redeemed | 49,108 |
| Dividend expense payable on securities sold short | 19,108 |
| Trustees' fee payable | 112 |
| Other accrued expenses payable | 136,790 |
| Total Liabilities | 77,332,802 |
| ***Net Assets*** | |
| Capital stock, $.001 par value (Note 6) | 19,603 |
| Paid-in capital (Note 6) | 119,606,306 |
| Undistributed net investment income | 2,889,920 |
| Accumulated net realized loss on investments, short sales and foreign currency transactions | (18,956,082) |
| Net unrealized appreciation from investments, short sales and foreign currency translations | 25,188,646 |
| Net Assets | $128,748,393 |
| Shares outstanding | 19,602,527 |
| Net asset value, offering price and redemption price per share | $6.57 |

[1] Including $42,701,658 of securities on loan.

**Credit Suisse Trust — International Equity Flex III Portfolio**
**Statement of Operations**
For the Year Ended December 31, 2010

| | |
|---|---|
| ***Investment Income*** (Note 2) | |
| Dividends | $ 5,104,918 |
| Interest | 57 |
| Securities lending | 210,575 |
| Foreign taxes withheld | (465,588) |
| Total investment income | 4,849,962 |
| ***Expenses*** | |
| Investment advisory fees (Note 3) | 1,220,310 |
| Administrative services fees (Note 3) | 273,915 |
| Dividend expense for securities sold short | 774,362 |
| Custodian fees | 279,053 |
| Short sales expense | 172,760 |
| Printing fees (Note 3) | 64,882 |
| Audit and tax fees | 52,233 |
| Transfer agent fees | 29,165 |
| Trustees' fees | 24,895 |
| Legal fees | 23,293 |
| Insurance expense | 7,016 |
| Commitment fees (Note 4) | 1,599 |
| Miscellaneous expense | 34,600 |
| Total expenses | 2,958,083 |
| Less: fees waived (Note 3) | (533,368) |
| Net expenses | 2,424,715 |
| Net investment income | 2,425,247 |
| ***Net Realized and Unrealized Gain (Loss) from Investments, Short Sales and Foreign Currency Related Items*** | |
| Net realized gain from investments | 5,673,272 |
| Net realized loss from short sales | (167,512) |
| Net realized loss from foreign currency transactions | (8,963) |
| Net change in unrealized appreciation (depreciation) from investments | 7,645,202 |
| Net change in unrealized appreciation (depreciation) from short sales | (1,806,202) |
| Net change in unrealized appreciation (depreciation) from foreign currency translations | 12,907 |
| Net realized and unrealized gain from investments, short sales and foreign currency related items | 11,348,704 |
| Net increase in net assets resulting from operations | $13,773,951 |

See Accompanying Notes to Financial Statements.

## Credit Suisse Trust — International Equity Flex III Portfolio
## Statements of Changes in Net Assets

| | For the Year Ended December 31, 2010 | For the Year Ended December 31, 2009 |
|---|---|---|
| ***From Operations*** | | |
| Net investment income | $ 2,425,247 | $ 999,305 |
| Net realized gain from investments, short sales and foreign currency transactions | 5,496,797 | 2,408,103 |
| Net change in unrealized appreciation (depreciation) from investments, short sales and foreign currency translations | 5,851,907 | 21,660,958 |
| Net increase in net assets resulting from operations | 13,773,951 | 25,068,366 |
| ***From Dividends and Distributions*** | | |
| Dividends from net investment income | (119,025) | (1,577,832) |
| Distributions from net realized gains | — | (2,147,844) |
| Net decrease in net assets resulting from dividends and distributions | (119,025) | (3,725,676) |
| ***From Capital Share Transactions*** (Note 6) | | |
| Proceeds from sale of shares | 16,551,125 | 17,093,006 |
| Exchange value of shares due to merger | — | 59,791,876 |
| Reinvestment of dividends and distributions | 119,025 | 3,725,676 |
| Net asset value of shares redeemed | (32,096,551) | (24,678,017) |
| Net increase (decrease) in net assets from capital share transactions | (15,426,401) | 55,932,541 |
| Net increase (decrease) in net assets | (1,771,475) | 77,275,231 |
| ***Net Assets*** | | |
| Beginning of year | 130,519,868 | 53,244,637 |
| End of year | $128,748,393 | $130,519,868 |
| *Undistributed net investment income* | $ 2,889,920 | $ 118,830 |

See Accompanying Notes to Financial Statements.

## Credit Suisse Trust — International Equity Flex III Portfolio
## Statement of Cash Flows
For the Year Ended December 31, 2010

| | | |
|---|---|---|
| ***Cash Flows from Operating Activities*** | | |
| Dividends, interest and securities lending income received | $ 4,793,089 | |
| Gain received from litigation | 69,614 | |
| Operating expenses paid | (1,677,147) | |
| Dividend expense paid on securities sold short | (767,987) | |
| Purchases of long-term securities | (252,070,202) | |
| Proceeds from sales of long-term securities | 259,240,815 | |
| Purchases to cover securities sold short | (141,776,252) | |
| Proceeds from securities sold short | 146,593,574 | |
| Proceeds from short-term securities, net | 995,000 | |
| Net cash provided by operating activities | | $ 15,400,504 |
| ***Cash Flows from Financing Activities*** | | |
| Proceeds from sale of shares | 16,724,112 | |
| Cost of shares redeemed | (32,234,360) | |
| Net cash used by financing activities | | (15,510,248) |
| Effect of exchange rate on cash | | 3,944 |
| Net decrease in cash | | (105,800) |
| Cash — beginning of year | | 154,868 |
| Cash — end of year | | $ 49,068 |
| ***RECONCILIATION OF NET INCREASE IN NET ASSETS FROM OPERATIONS TO NET CASH PROVIDED BY OPERATING ACTIVITIES*** | | |
| Net increase in net assets resulting from operations | | $ 13,773,951 |
| ***Adjustments to Reconcile Net Increase in Net Assets from Operations to Net Cash Provided by Operating Activities*** | | |
| Change in dividends and interest receivable | $ (56,873) | |
| Change in accrued expenses | (36,209) | |
| Change in prepaid expenses and other assets | 3,061 | |
| Change in advisory fee payable | 6,354 | |
| Change in dividend expense payable on securities sold short | 6,375 | |
| Purchases of long-term securities | (252,070,202) | |
| Proceeds from sales of long-term securities | 259,240,815 | |
| Purchases to cover securities sold short | (141,776,252) | |
| Proceeds from securities sold short | 146,593,574 | |
| Proceeds from short-term securities, net | 995,000 | |
| Net change in unrealized appreciation from investments, short sales and foreign currency translations | (5,851,907) | |
| Net realized gain from investments, short sales and foreign currency transactions | (5,427,183) | |
| Total adjustments | | 1,626,553 |
| Net cash provided by operating activities | | $ 15,400,504 |
| ***Non-Cash Activity:*** | | |
| Dividend reinvestments | | $ 119,025 |

See Accompanying Notes to Financial Statements.

**Credit Suisse Trust — International Equity Flex III Portfolio**
**Financial Highlights**
(For a Share of the Portfolio Outstanding Throughout Each Year)

| | For the Year Ended December 31, | | | | |
|---|---|---|---|---|---|
| | 2010 | 2009 | 2008 | 2007 | 2006 |
| **Per share data** | | | | | |
| Net asset value, beginning of year | $ 5.86 | $ 4.08 | $ 23.58 | $ 21.85 | $ 16.82 |
| ***INVESTMENT OPERATIONS*** | | | | | |
| Net investment income | 0.12 | 0.08 | 0.25 | 0.37 | 0.21 |
| Net gain (loss) on investments, short sales and foreign currency related items (both realized and unrealized) | 0.60 | 2.01 | (10.11)[1] | 5.58 | 5.19 |
| Total from investment operations | 0.72 | 2.09 | (9.86) | 5.95 | 5.40 |
| ***LESS DIVIDENDS AND DISTRIBUTIONS*** | | | | | |
| Dividends from net investment income | (0.01) | (0.13) | (0.34) | (0.37) | (0.11) |
| Distributions from net realized gains | — | (0.18) | (9.30) | (3.85) | (0.26) |
| Total dividends and distributions | (0.01) | (0.31) | (9.64) | (4.22) | (0.37) |
| ***Net asset value, end of year*** | $ 6.57 | $ 5.86 | $ 4.08 | $ 23.58 | $ 21.85 |
| Total return[2] | 12.23% | 51.62% | (54.80)% | 29.44% | 32.51% |
| ***RATIOS AND SUPPLEMENTAL DATA*** | | | | | |
| Net assets, end of year (000s omitted) | $128,748 | $130,520 | $53,245 | $179,817 | $242,319 |
| Ratio of expenses to average net assets | 1.99% | 1.14% | 1.04% | 1.30% | 1.36% |
| Ratio of expenses to average net assets excluding short sales dividend expense | 1.35% | 1.08% | — | — | — |
| Ratio of net investment income to average net assets | 1.99% | 1.57% | 1.40% | 0.94% | 1.11% |
| Decrease reflected in above operating expense ratios due to waivers/reimbursements | 0.44% | 0.40% | 0.25% | 0.15% | 0.23% |
| Portfolio turnover rate | 213% | 196% | 61% | 62% | 80% |

[1] The investment adviser fully reimbursed the Portfolio for a loss on a transaction not meeting the Portfolio's investment guidelines, which otherwise would have reduced the amount by $0.01.

[2] Total returns are historical and assume changes in share price and reinvestment of all dividends and distributions. Had certain expenses not been reduced during the years shown, total returns would have been lower. Total returns do not reflect charges and expenses attributable to any particular variable contract or plan.

### Note 1. Organization

Credit Suisse Trust (the "Trust") is an open-end management investment company registered under the Investment Company Act of 1940, as amended (the "1940 Act"), and currently offers three managed investment portfolios of which one, the International Equity Flex III Portfolio (the "Portfolio"), is included in this report. The Portfolio is a diversified investment fund that seeks capital appreciation. Shares of the Portfolio are not available directly to individual investors but may be offered only through (a) variable annuity contracts and variable life insurance contracts offered by separate accounts of certain insurance companies and (b) tax-qualified pension and retirement plans. The Portfolio may not be available in connection with a particular contract or plan. The Trust was organized under the laws of the Commonwealth of Massachusetts as a business trust on March 15, 1995. Effective May 1, 2009, the name of the Portfolio was changed from Emerging Markets Portfolio.

### Note 2. Significant Accounting Policies

A) SECURITY VALUATION — The net asset value of the Portfolio is determined daily as of the close of regular trading on the New York Stock Exchange, Inc. (the "Exchange") on each day the Exchange is open for business. Equity investments are valued at market value, which is generally determined using the closing price on the exchange or market on which the security is primarily traded at the time of valuation (the "Valuation Time"). If no sales are reported, equity investments are generally valued at the most recent bid quotation as of the Valuation Time or at the lowest asked quotation in the case of a short sale of securities. Equity investments are generally categorized as Level 1. Debt securities with a remaining maturity greater than 60 days are valued in accordance with the price supplied by a pricing service, which may use a matrix, formula or other objective method that takes into consideration market indices, yield curves and other specific adjustments. For certain international equity securities, in order to adjust for events which may occur between the close of the foreign stock exchanges and the close of the Exchange, the Portfolio may utilize a fair valuation service provided by an independent third party which has been approved by the Board of Trustees. Securities priced using this fair valuation model are generally categorized as Level 2. Debt obligations that will mature in 60 days or less are valued on the basis of amortized cost, which approximates market value, unless it is determined that using this method would not represent fair value. Debt securities are generally categorized as Level 2. Investments in open-end investment companies are valued at their net asset value each business day and are generally categorized as Level 1. Securities and other assets for

**Note 2. Significant Accounting Policies**

which market quotations are not readily available, or whose values have been materially affected by events occurring before the Portfolio's Valuation Time but after the close of the securities' primary markets, are valued at fair value as determined in good faith by, or under the direction of, the Board of Trustees under procedures established by the Board of Trustees and are generally categorized as Level 3. When fair value pricing is employed, the prices of securities used by a portfolio to calculate its net asset value may differ from quoted or published prices for the same securities.

In accordance with the authoritative guidance on fair value measurements and disclosures under accounting principles generally accepted in the United States of America ("GAAP"), the Portfolio discloses the fair value of its investments in a hierarchy that prioritizes the inputs to valuation techniques used to measure the fair value. In accordance with GAAP, fair value is defined as the price that the Portfolio would receive upon selling an investment in a timely transaction to an independent buyer in the principal or most advantageous market of the investment. GAAP established a three-tier hierarchy to maximize the use of observable market data and minimize the use of unobservable inputs and to establish classification of fair value measurements for disclosure purposes. Inputs refer broadly to the assumptions that market participants would use in pricing the asset or liability, including assumptions about risk, for example, the risk inherent in a particular valuation technique used to measure fair value including such a pricing model and/or the risk inherent in the inputs to the valuation technique. Inputs may be observable or unobservable. Observable inputs are inputs that reflect the assumptions market participants would use in pricing the asset or liability developed based on market data obtained from sources independent of the reporting entity. Unobservable inputs are inputs that reflect the reporting entity's own assumptions about the assumptions market participants would use in pricing the asset or liability developed based on the best information available in the circumstances. In accordance with the Portfolio's valuation procedures, factors used in determining value may include, but are not limited to, the type of the security, the size of the holding, the initial cost of the security, the existence of any contractual restrictions on the security's disposition, the price and extent of public trading in similar securities of the issuer or of comparable companies, quotations or evaluated prices from broker-dealers and/or pricing services, information obtained from the issuer, analysts, and/or the appropriate stock exchange (for exchange-traded securities), an analysis of the company's or issuer's financial statements, an evaluation of the forces that influence the issuer and the market(s) in which the security is purchased and

### Note 2. Significant Accounting Policies

sold and with respect to debt securities, the maturity, coupon, creditworthiness, currency denomination, and the movement of the market in which the security is normally traded. The three-tier hierarchy of inputs is summarized in the three broad Levels listed below.

- Level 1 – quoted prices in active markets for identical investments
- Level 2 – other significant observable inputs (including quoted prices for similar investments, interest rates, prepayment speeds, credit risk, etc.)
- Level 3 – significant unobservable inputs (including the Portfolio's own assumptions in determining the fair value of investments)

The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities.

The following is a summary of the inputs used as of December 31, 2010 in valuing the Portfolio's investments carried at value:

| | Level 1 | Level 2 | Level 3 | Total |
|---|---|---|---|---|
| Investments In Securities | | | | |
| Common Stocks | | | | |
| Asia | $ 4,124,985 | $ — | $— | $ 4,124,985 |
| Australia | 727,829 | 7,858,445 | — | 8,586,274 |
| Austria | — | 1,249,972 | — | 1,249,972 |
| Belgium | — | 1,802,268 | — | 1,802,268 |
| Bermuda | — | 409,246 | — | 409,246 |
| Cyprus | — | 167,689 | — | 167,689 |
| Denmark | — | 3,031,537 | — | 3,031,537 |
| Finland | — | 5,051,282 | — | 5,051,282 |
| France | 370,772 | 14,797,043 | — | 15,167,815 |
| Germany | — | 12,737,960 | — | 12,737,960 |
| Greece | — | 446,986 | — | 446,986 |
| Hong Kong | 2,664,003 | — | — | 2,664,003 |
| Israel | 710,304 | 91,177 | — | 801,481 |
| Italy | — | 3,110,152 | — | 3,110,152 |
| Japan | 37,379 | 35,968,140 | — | 36,005,519 |
| Luxembourg | — | 830,653 | — | 830,653 |
| Netherlands | 1,243,832 | 3,394,191 | — | 4,638,023 |
| Norway | — | 1,538,826 | — | 1,538,826 |
| Portugal | — | 865,844 | — | 865,844 |
| Singapore | 1,622,957 | — | — | 1,622,957 |
| Spain | — | 6,015,470 | — | 6,015,470 |
| Sweden | — | 7,727,290 | — | 7,727,290 |
| Switzerland | — | 9,862,570 | — | 9,862,570 |
| United Kingdom | 350,551 | 30,278,743 | — | 30,629,294 |
| Preferred Stocks | | | | |
| Germany | 397,293 | 751,926 | — | 1,149,219 |
| Rights | | | | |
| United Kingdom | 18,548 | — | — | 18,548 |

## Note 2. Significant Accounting Policies

| | Level 1 | Level 2 | Level 3 | Total |
|---|---|---|---|---|
| Warrants | | | | |
| Italy | $ 37 | $ — | $— | $ 37 |
| Short-Term Investments | 10,797,489 | 898,000 | — | 11,695,489 |
| Securities Sold Short | | | | |
| Common Stocks | | | | |
| Austria | — | (70,471) | — | (70,471) |
| Belgium | (212,366) | (911,480) | — | (1,123,846) |
| Canada | (4,982) | — | — | (4,982) |
| Denmark | — | (659,702) | — | (659,702) |
| Finland | — | (873,664) | — | (873,664) |
| France | (80,568) | (4,285,048) | — | (4,365,616) |
| Germany | (262,941) | (2,499,326) | — | (2,762,267) |
| Italy | — | (3,521,088) | — | (3,521,088) |
| Japan | — | (7,661,535) | — | (7,661,535) |
| Luxembourg | — | (456,733) | — | (456,733) |
| Netherlands | — | (2,400,020) | — | (2,400,020) |
| Norway | — | (283,238) | — | (283,238) |
| Spain | — | (793,064) | — | (793,064) |
| Sweden | (4,649) | (878,534) | — | (883,183) |
| Switzerland | — | (3,392,892) | — | (3,392,892) |
| United Kingdom | — | (3,161,644) | — | (3,161,644) |
| Other Financial Instruments* | — | — | — | — |
| | $22,500,473 | $117,036,971 | $— | $139,537,444 |

*Other financial instruments include futures, forwards and swap contracts.

Effective January 1, 2010, the Portfolio adopted FASB amendments to authoritative guidance which requires the Portfolio to disclose details of significant transfers in and out of Level 1 and Level 2 measurements and the reasons for the transfers. For the year ended December 31, 2010, as a result of the fair value pricing procedures for international investments utilized by the Portfolio, certain securities may have transferred in and out of Level 1 and Level 2 measurements during the period. The only investment held by the Portfolio whose fair value was determined using Level 3 inputs had a value of $0 at December 31, 2010.

B) DERIVATIVE INSTRUMENTS AND HEDGING ACTIVITIES — Effective January 1, 2009, the Portfolio adopted amendments to authoritative guidance on disclosures about derivative instruments and hedging activities which require that the Portfolio disclose (a) how and why an entity uses derivative instruments, (b) how derivative instruments and hedging activities are accounted for, and (c) how derivative instruments and related hedging activities affect a portfolio's financial position, financial performance, and cash flows. The Portfolio has not entered into any derivative or hedging activities during the period covered by this report.

**Note 2. Significant Accounting Policies**

C) SECURITY TRANSACTIONS AND INVESTMENT INCOME — Security transactions are accounted for on a trade date basis. Interest income is recorded on the accrual basis. Dividends and dividend expense on short sales are recorded on the ex-dividend date. The cost of investments sold is determined by use of the specific identification method for both financial reporting and income tax purposes.

D) DIVIDENDS AND DISTRIBUTIONS TO SHAREHOLDERS — Dividends from net investment income and distributions of net realized capital gains, if any, are declared and paid at least annually. However, to the extent that a net realized capital gain can be reduced by a capital loss carryforward, such gain will not be distributed. Income and capital gain distributions are determined in accordance with federal income tax regulations, which may differ from GAAP.

E) FEDERAL INCOME TAXES — No provision is made for federal taxes as it is the Portfolio's intention to continue to qualify for and elect the tax treatment applicable to regulated investment companies under the Internal Revenue Code of 1986, as amended, and to make the requisite distributions to its shareholders, which will be sufficient to relieve it from federal income and excise taxes.

The Portfolio adopted the authoritative guidance for uncertainty in income taxes and recognizes a tax benefit or liability from an uncertain position only if it is more likely than not that the position is sustainable based solely on its technical merits and consideration of the relevant taxing authority's widely understood administrative practices and procedures. The Portfolio has reviewed its current tax positions and has determined that no provision for income tax is required in the Portfolio's financial statements. The Portfolio's federal tax returns for the prior three fiscal years remain subject to examination by the Internal Revenue Service.

F) USE OF ESTIMATES — The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of income and expenses during the reporting period. Actual results could differ from these estimates.

G) SHORT-TERM INVESTMENTS — The Portfolio, together with other funds/portfolios advised by Credit Suisse Asset Management, LLC ("Credit Suisse"), an indirect, wholly-owned subsidiary of Credit Suisse Group AG, pools available cash into a short-term variable rate time deposit issued by State

**Note 2. Significant Accounting Policies**

Street Bank and Trust Company ("SSB"), the Portfolio's custodian. The short-term time deposit issued by SSB is a variable rate account classified as a short-term investment.

H) SHORT SALES — The Portfolio enters into short sales transactions collateralized by cash deposits received from brokers in connection with securities lending activities (see note I) and securities. Cash deposits are shown as cash segregated at brokers on the Statement of Assets and Liabilities. The collateral amounts required are determined daily by reference to the market value of the short positions. Short sales expose the Portfolio to the risk that it will be required to cover its short position at a time when the securities have appreciated in value, thus resulting in a loss to the Portfolio. The Portfolio's loss on a short sale could theoretically be unlimited in a case where the Portfolio is unable, for whatever reason, to close out its short position. Short sales also involve transaction and other costs that will reduce potential gains and increase potential portfolio losses. The use by the Portfolio of short sales in combination with long positions in its portfolio in an attempt to improve performance may not be successful and may result in greater losses or lower positive returns than if the Portfolio held only long positions. It is possible that the Portfolio's long equity positions will decline in value at the same time that the value of the securities it has sold short increases, thereby increasing potential losses to the Portfolio. In addition, the Portfolio's short selling strategies may limit its ability to fully benefit from increases in the equity markets. Short selling also involves a form of financial leverage that may exaggerate any losses realized by the Portfolio. Also, there is the risk that the counterparty to a short sale may fail to honor its contractual terms, causing a loss to the Portfolio.

I) SECURITIES LENDING — Loans of securities are required at all times to be secured by collateral at least equal to 102% of the market value of domestic securities on loan (including any accrued interest thereon) and 105% of the market value of foreign securities on loan (including any accrued interest thereon). Cash collateral received by the Portfolio in connection with securities lending activity is either in the form of cash segregated at brokers or pooled together with cash collateral for other funds/portfolios advised by Credit Suisse and may be invested in a variety of investments, including funds advised by SSB, the Portfolio's securities lending agent, or money market instruments. However, in the event of default or bankruptcy by the other party to the agreement, realization and/or retention of the collateral may be subject to legal proceedings.

SSB has been engaged by the Portfolio to act as the Portfolio's securities lending agent. The Portfolio's securities lending arrangement provides that

### Note 2. Significant Accounting Policies

the Portfolio and SSB will share the net income earned from securities lending activities. During the year ended December 31, 2010, total earnings from the Portfolio's investment in cash collateral received in connection with securities lending arrangements was $284,077, of which $18,898 was rebated to borrowers (brokers). The Portfolio retained $210,575 in income from the cash collateral investment, and SSB, as lending agent, was paid $54,604. Securities lending income is accrued as earned.

J) FOREIGN CURRENCY TRANSACTIONS — The books and records of the Portfolio are maintained in U.S. dollars. Transactions denominated in foreign currencies are recorded at the current prevailing exchange rates. All assets and liabilities denominated in foreign currencies are translated into U.S. dollar amounts at the current exchange rate at the end of the period. Translation gains or losses resulting from changes in the exchange rate during the reporting period and realized gains and losses on the settlement of foreign currency transactions are reported in the results of operations for the current period. The Portfolio does not isolate that portion of realized gains and losses on investments in *equity* securities which is due to changes in the foreign exchange rate from that which is due to changes in market prices of equity securities. The Portfolio isolates that portion of realized gains and losses on investments in *debt* securities which is due to changes in the foreign exchange rate from that which is due to changes in market prices of debt securities.

K) OTHER — The Portfolio invests in securities of foreign countries which involve certain risks in addition to those inherent in domestic investments. Such risks generally include, among others, currency risk (fluctuations in currency exchange rates), information risk (key information may be inaccurate or unavailable) and political risk (expropriation, nationalization or the imposition of capital or currency controls or punitive taxes). Other risks of investing in foreign securities include liquidity and valuation risks.

L) SUBSEQUENT EVENTS — In preparing the financial statements as of December 31, 2010, management considered the impact of subsequent events for potential recognition or disclosure in these financial statements.

### Note 3. Transactions with Affiliates and Related Parties

Credit Suisse serves as investment adviser for the Portfolio. For its investment advisory services, Credit Suisse is entitled to receive a fee from the Portfolio at an annual rate of 1.00% of the Portfolio's average daily net assets. For the year ended December 31, 2010, investment advisory fees earned and

**Note 3. Transactions with Affiliates and Related Parties**

voluntarily waived were $1,220,310 and $533,368, respectively. Credit Suisse will not recapture from the Portfolio any fees it waived during the year ended December 31, 2010. Effective January 1, 2011, Credit Suisse will waive fees and reimburse expenses so that the Portfolio's annual operating expenses, excluding dividend expense for securities sold short, will not exceed 1.45% of the Portfolio's average daily net assts. Fee waivers and expense reimbursements are voluntary and may be discontinued by Credit Suisse at any time.

Credit Suisse Asset Management Securities, Inc. ("CSAMSI"), an affiliate of Credit Suisse, and SSB serve as co-administrators to the Portfolio. For its co-administrative services, CSAMSI currently receives a fee calculated at an annual rate of 0.09% of the Portfolio's average daily net assets. For the year ended December 31, 2010, co-administrative services fees earned by CSAMSI were $109,828.

For its co-administrative services, SSB receives a fee, exclusive of out-of-pocket expenses, calculated in total for all the Credit Suisse funds/portfolios co-administered by SSB and allocated based upon the relative average net assets of each fund/portfolio, subject to an annual minimum fee. For the year ended December 31, 2010, co-administrative services fees earned by SSB (including out-of-pocket expenses) were $164,087.

In addition to serving as the Portfolio's co-administrator, CSAMSI currently serves as distributor of the Portfolio's shares without compensation.

Merrill Corporation ("Merrill"), an affiliate of Credit Suisse, has been engaged by the Portfolio to provide certain financial printing services. For the year ended December 31, 2010, Merrill was paid $39,926 for its services by the Portfolio.

**Note 4. Line of Credit**

The Portfolio, together with other funds/portfolios advised by Credit Suisse (collectively, the "Participating Funds"), participates in a committed, unsecured line of credit facility ("Credit Facility") for temporary or emergency purposes with SSB. Under the terms of the Credit Facility, the Participating Funds pay an aggregate commitment fee on the average unused amount of the Credit Facility, which is allocated among the Participating Funds in such manner as is determined by the governing Boards of the Participating Funds. In addition, the Participating Funds pay interest on borrowings at either the Overnight Federal Funds rate or the Overnight LIBOR rate plus a spread. At December 31,

### Note 4. Line of Credit

2010, and during the year ended December 31, 2010, the Portfolio had no borrowings under the Credit Facility.

### Note 5. Purchases and Sales of Securities

For the year ended December 31, 2010, purchases and sales of investment securities (excluding short sales and short-term investments) were $251,635,673 and $259,062,017, respectively. Securities sold short and purchases to cover securities sold short were $146,013,190 and $141,201,677, respectively.

### Note 6. Capital Share Transactions

The Trust is authorized to issue an unlimited number of full and fractional shares of beneficial interest, $.001 par value per share. Transactions in capital shares of the Portfolio were as follows:

| | For the Year Ended December 31, 2010 | For the Year Ended December 31, 2009 |
|---|---|---|
| Shares sold | 2,807,356 | 3,357,893 |
| Shares exchanged due to merger | — | 10,314,385 |
| Shares issued in reinvestment of dividends and distributions | 20,557 | 643,468 |
| Shares redeemed | (5,511,004) | (5,091,113) |
| Net increase (decrease) | (2,683,091) | 9,224,633 |

On December 31, 2010, the number of shareholders that held 5% or more of the outstanding shares of the Portfolio was as follows:

| Number of Shareholders | Approximate Percentage of Outstanding Shares |
|---|---|
| 5 | 81% |

Some of the shareholders are omnibus accounts, which hold shares on behalf of individual shareholders.

### Note 7. Federal Income Taxes

Income and capital gain distributions are determined in accordance with federal income tax regulations, which may differ from GAAP.

The tax characteristics of dividends and distributions paid during the years ended December 31, 2010 and 2009, respectively, by the Portfolio were as follows:

| Ordinary Income | | Long-Term Capital Gain | |
|---|---|---|---|
| 2010 | 2009 | 2010 | 2009 |
| $119,025 | $1,577,884 | $0 | $2,147,792 |

**Note 7. Federal Income Taxes**

The tax basis components of distributable earnings differ from the amounts reflected in the Statement of Assets and Liabilities by temporary book/tax differences. These differences are primarily due to losses deferred on wash sales and mark-to-market income from Passive Foreign Investment Companies.

At December 31, 2010, the components of distributable earnings on a tax basis were as follows:

| | |
|---|---|
| Undistributed net investment income | $ 3,400,012 |
| Accumulated realized loss | (16,291,883) |
| Unrealized appreciation | 22,024,893 |
| Deferral of post-October capital losses | (10,538) |
| | $ 9,122,484 |

At December 31, 2010, the Portfolio had capital loss carryforwards available to offset possible future capital gains as follows:

| Expires December 31, | |
|---|---|
| 2016 | 2017 |
| $14,924,052 | $1,367,831 |

During the tax year ended December 31, 2010, the Portfolio utilized $6,352,852 of the capital loss carryforwards.

It is uncertain whether the Portfolio will be able to realize the benefits of the capital loss carryforwards before they expire.

Included in the Portfolio's capital loss carryforwards which expire in 2016 is $5,420,346, acquired in the Credit Suisse Trust — International Equity Flex I Portfolio merger, which is subject to limitations.

Included in the Portfolio's capital loss carryforwards which expire in 2016 is $9,503,706, acquired in the Credit Suisse Trust — International Equity Flex II Portfolio merger, which is subject to limitations.

At December 31, 2010, the identified cost for federal income tax purposes, as well as the gross unrealized appreciation from investments for those securities having an excess of value over cost, gross unrealized depreciation from investments for those securities having an excess of cost over value and the net unrealized appreciation from investments were $147,774,335, $26,347,233, $(2,170,179) and $24,177,054, respectively.

At December 31, 2010, the identified proceeds for federal income tax purposes, as well as the gross unrealized appreciation from securities sold

**Note 7. Federal Income Taxes**

short for those securities having an excess of proceeds over value, gross unrealized depreciation from investments for those securities having an excess of value over proceeds and the net unrealized depreciation from securities sold short were $(30,249,352), $670,984, $(2,835,577) and $(2,164,593), respectively.

At December 31, 2010, the Portfolio reclassified $464,868 to undistributed net investment income and $1,596,146 to paid in capital from accumulated realized loss, to adjust for current period permanent book/tax differences which arose principally from foreign currency gain/(loss), reclassification of short sale substitute payments and Passive Foreign Investment Companies. Net assets were not affected by these reclassifications.

**Note 8. Acquisition of Credit Suisse Trust — International Equity Flex I Portfolio and Credit Suisse Trust — International Equity Flex II Portfolio**

On December 11, 2009, Credit Suisse Trust — International Equity Flex III Portfolio acquired all of the net assets of Credit Suisse Trust — International Equity Flex I Portfolio and Credit Suisse Trust — International Equity Flex II Portfolio, both open-end investment companies, pursuant to a plan of reorganization approved by the Board of Trustees on August 18, 2009. The purpose of the transaction was to combine three funds managed by Credit Suisse with comparable investment objectives and strategies. The acquisition was accomplished by a tax-free exchange of 2,140,708 shares of Credit Suisse Trust — International Equity Flex I Portfolio valued at $21,716,138 and 4,055,155 shares of Credit Suisse Trust — International Equity Flex II Portfolio valued at $38,075,738 for 10,314,385 shares of Credit Suisse Trust — International Equity Flex III Portfolio. The investment portfolios of Credit Suisse Trust — International Equity Flex I Portfolio and Credit Suisse Trust — International Equity Flex II Portfolio had a fair value at December 11, 2009 of $21,695,471 and $38,080,582 and identified costs of $18,350,197 and $32,684,366, respectively, which were the principal assets acquired by Credit Suisse Trust — International Equity Flex III Portfolio. For financial reporting purposes, assets received and shares issued by Credit Suisse Trust — International Equity Flex III Portfolio were recorded at fair value; however the cost basis of the investments received from Credit Suisse Trust — International Equity Flex I Portfolio and Credit Suisse Trust — International Equity Flex II Portfolio were carried forward to align ongoing reporting of Credit Suisse Trust — International Equity Flex III Portfolio's realized and unrealized gains and losses with amounts distributable to shareholders for tax purposes. Immediately prior

## Note 8. Acquisition of Credit Suisse Trust — International Equity Flex I Portfolio and Credit Suisse Trust — International Equity Flex II Portfolio

to the merger, the net assets of Credit Suisse Trust — International Equity Flex III Portfolio were $69,332,521.

Credit Suisse Trust — International Equity Flex III Portfolio pro forma results of operations for the year ended December 31, 2009 are as follows:

| | |
|---|---|
| Net investment income | $ 2,421,259[1] |
| Net gain from investments, short sales and foreign currency related items | 38,720,089[2] |
| Net increase in net assets resulting from operations | $41,141,348 |

Because the combined investment portfolios have been managed as a single integrated portfolio since the acquisition was completed, it is not practicable to separate the amounts of net investment income and net gain on investments of Credit Suisse Trust — International Equity Flex I Portfolio and Credit Suisse Trust — International Equity Flex II Portfolio that have been included in Credit Suisse Trust — International Equity Flex III Portfolio's statement of operations since December 11, 2009.

[1] $999,305 as reported, plus $784,313 and $475,788 for Credit Suisse Trust — International Equity Flex I Portfolio and Credit Suisse Trust — International Equity Flex II Portfolio, respectively, premerger, plus $161,853 of pro-forma gross expenses eliminated.

[2] $24,069,061 as reported, plus $6,002,603 and $8,648,425 for Credit Suisse Trust — International Equity Flex I Portfolio and Credit Suisse Trust — International Equity Flex II Portfolio, respectively, premerger.

## Note 9. Contingencies

In the normal course of business, the Portfolio may provide general indemnifications pursuant to certain contracts and organizational documents. The Portfolio's maximum exposure under these arrangements is dependent on future claims that may be made against the Portfolio and, therefore, cannot be estimated; however, based on experience, the risk of loss from such claims is considered remote.

## Report of Independent Registered Public Accounting Firm

To the Board of Trustees and Shareholders of
Credit Suisse Trust — International Equity Flex III Portfolio:

In our opinion, the accompanying statement of assets and liabilities, including the schedule of investments, and the related statements of operations and of changes in net assets and of cash flows and the financial highlights present fairly, in all material respects, the financial position of Credit Suisse Trust — International Equity Flex III Portfolio (the "Portfolio"), at December 31, 2010, the results of its operations and its cash flow for the year then ended and the changes in its net assets and financial highlights for the periods presented, in conformity with accounting principles generally accepted in the United States of America. These financial statements and financial highlights (hereafter referred to as "financial statements") are the responsibility of the Portfolio's management. Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit of these financial statements in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audit, which included confirmation of securities at December 31, 2010 by correspondence with the custodian and brokers, provides a reasonable basis for our opinion.

PricewaterhouseCoopers LLP

Boston, Massachusetts
February 23, 2011

In approving the renewal of the current Advisory Agreement, the Board of Trustees (the "Board") of the Credit Suisse Trust — International Equity Flex III Portfolio (the "Portfolio"), including a majority of the Trustees who are not "interested persons" of the Fund as defined in the Investment Company Act of 1940 (the "Independent Trustees"), at a meeting held on November 15 and 16, 2010, considered the following factors:

## Investment Advisory Fee Rates and Expenses

The Board reviewed and considered the contractual advisory fee rate of 1.00% for the Portfolio ("Contractual Advisory Fee") in light of the extent and quality of the advisory services provided by Credit Suisse Asset Management, LLC ("Credit Suisse"). The Board also reviewed and considered the voluntary fee waivers currently in place for the Portfolio and considered the actual fee rate of 0.57% paid by the Portfolio after taking waivers into account ("Net Advisory Fee") as of September 30, 2010. The Board acknowledged that voluntary fee waivers could be discontinued at any time.

Additionally, the Board received and considered information comparing the Portfolio's Contractual Advisory Fee, Net Advisory Fee and the Portfolio's overall expenses with those of funds in both the relevant expense group ("Expense Group") and universe of funds ("Expense Universe") provided by Lipper Inc., an independent provider of investment company data.

The Board noted that Credit Suisse planned to reduce the voluntary fee waiver so that the Portfolio's total expense ratio would be in line with the Lipper median.

## Nature, Extent and Quality of the Services under the Advisory Agreement

The Board received and considered information regarding the nature, extent and quality of services provided to the Portfolio by Credit Suisse under the Advisory Agreement. The Board also noted information received at regular meetings throughout the year related to the services rendered by Credit Suisse. The Board reviewed background information about Credit Suisse, including its Form ADV. The Board considered the background and experience of Credit Suisse's senior management and the expertise of, and the amount of attention given to the Portfolio by, senior personnel of Credit Suisse. In addition, the Board reviewed the qualifications, backgrounds and responsibilities of the portfolio management team primarily responsible for the day-to-day portfolio management of the Portfolio and the extent of the resources devoted to research and analysis of actual and potential investments. The Board evaluated the ability of Credit Suisse, based on its resources, reputation and other attributes, to attract and retain qualified investment professionals, including research, advisory, and supervisory personnel. The Board also received and considered information about the nature, extent and quality of services and fee rates offered to other Credit Suisse clients for comparable services.

Portfolio Performance

The Board received and considered performance results of the Portfolio over time, along with comparisons both to the relevant performance group ("Performance Group") and universe of funds ("Performance Universe") for the Portfolio. The Board was provided with a description of the methodology used to arrive at the funds included in the Performance Group and the Performance Universe.

Credit Suisse Profitability

The Board received and considered a profitability analysis of Credit Suisse based on the fees payable under the Advisory Agreement for the Portfolio, including any fee waivers, as well as other relationships between the Portfolio on the one hand and Credit Suisse affiliates on the other. The Board also considered Credit Suisse's methodology for allocating costs to the Portfolio, recognizing that cost allocation methodologies are inherently subjective. The Board received profitability information for the other funds in the Credit Suisse family of funds.

Economies of Scale

The Board considered information regarding whether there have been economies of scale with respect to the management of the Portfolio, whether the Portfolio has appropriately benefited from any economies of scale, and whether there is potential for realization of any further economies of scale. Accordingly, the Board considered whether breakpoints in the Portfolio's advisory fee structure would be appropriate or reasonable taking into consideration economies of scale or other efficiencies that might accrue from increases in the Portfolio's asset levels.

Other Benefits to Credit Suisse

The Board considered other benefits received by Credit Suisse and its affiliates as a result of their relationship with the Portfolio. Such benefits include, among others, benefits potentially derived from an increase in Credit Suisse's businesses as a result of its relationship with the Portfolio (such as the ability to market to shareholders other financial products offered by Credit Suisse and its affiliates) and the fees paid to affiliates of Credit Suisse for co-administration and distribution services.

The Board considered the standards applied in seeking best execution, and also reviewed Credit Suisse's method for allocating portfolio investment opportunities among its advisory clients. Credit Suisse confirmed there were no soft dollar arrangements during the past year.

### Other Factors and Broader Review

As discussed above, the Board reviews detailed materials received from Credit Suisse as part of the annual re-approval process. The Board also reviews and assesses the quality of the services that the Portfolio receives throughout the year. In this regard, the Board reviews reports of Credit Suisse at least quarterly, which include, among other things, detailed portfolio and market reviews, detailed fund performance reports and Credit Suisse's compliance procedures.

### Conclusions

In selecting Credit Suisse and approving the Advisory Agreement and the investment advisory fee under such agreement, the Board concluded that:

- Although the combined Contractual Advisory Fee and co-administration fee were near the highest in the Expense Group, the fees were reasonable, recognizing that the Net Advisory Fee was among the lowest in the Expense Group.
- The Portfolio's performance was at or above the median for all periods in the Performance Group and Performance Universe. The Board also noted the change to the Portfolio's investment strategy that occurred in 2009.
- The Board was satisfied with the nature, extent and quality of the investment advisory services provided to the Portfolio by Credit Suisse and that, based on dialogue with management and counsel, the services provided by Credit Suisse under the Advisory Agreement are typical of, and consistent with, those provided to similar mutual funds by other investment advisers.
- In light of the costs of providing investment management and other services to the Portfolio and Credit Suisse's ongoing commitment to the

Portfolio and willingness to waive fees, Credit Suisse's profitability based on fees payable under the Advisory Agreement, as well as other ancillary benefits that Credit Suisse and its affiliates received, were considered reasonable.

- In light of the fee waivers and the Net Advisory Fee, the Portfolio's current fee structure (without breakpoints) was considered reasonable.

No single factor reviewed by the Board was identified by the Board as the principal factor in determining whether to approve the Advisory Agreement. The Independent Trustees were advised by separate independent legal counsel throughout the process.

| Name, Address (Year of Birth) | Position(s) Held with Trust | Term of Office[1] and Length of Time Served | Principal Occupation(s) During Past Five Years | Number of Portfolios in Fund Complex Overseen by Trustee | Other Directorships Held by Trustee |
|---|---|---|---|---|---|
| **Independent Trustees** | | | | | |
| Enrique Arzac<br>c/o Credit Suisse Asset Management, LLC<br>Attn: General Counsel<br>Eleven Madison Avenue<br>New York, New York 10010<br>(1941) | Trustee, Audit Committee Chairman and Nominating Committee Member | Since 2005 | Professor of Finance and Economics, Graduate School of Business, Columbia University since 1971. | 9 | Director of Epoch Holding Corporation (an investment management and investment advisory services company); Director of Starcomms PLC., (telecommunications company); Director of Mirae Asset Discovery Funds (6 open-end portfolios); Director of Aberdeen Asia-Pacific Income Investment Company Limited (a Canadian closed-end fund); Director of The Adams Express Company, Petroleum and Resources Corporation, Aberdeen Chile Fund, Inc., Aberdeen Indonesia Fund, Inc., Aberdeen Israel Fund, Inc., Aberdeen Latin America Equity Fund, Inc. and Aberdeen Emerging Markets Telecommunications and Infrastructure Fund, Inc. (each a closed-end investment company). |

[1] Each Trustee and Officer serves until his or her respective successor has been duly elected and qualified.

| Name, Address (Year of Birth) | Position(s) Held with Trust | Term of Office[1] and Length of Time Served | Principal Occupation(s) During Past Five Years | Number of Portfolios in Fund Complex Overseen by Trustee | Other Directorships Held by Trustee |
|---|---|---|---|---|---|
| **Independent Trustees** | | | | | |
| Jeffrey E. Garten[2]<br>Box 208200<br>New Haven, Connecticut<br>06520-8200<br>(1946) | Trustee, Audit and Nominating Committee Member | Since 1998 | The Juan Trippe Professor in the Practice of International Trade, Finance and Business from July 2005 to present; Partner and Chairman of Garten Rothkopf (consulting firm) from October 2005 to present; Dean of Yale School of Management from November 1995 to June 2005. | 7 | Director of Aetna, Inc. (insurance company); Director of CarMax Group (used car dealers); Member of Standard & Poor's Board of Managers. |
| Peter F. Krogh<br>c/o Credit Suisse Asset Management, LLC<br>Attn: General Counsel<br>Eleven Madison Avenue<br>New York, New York<br>10010<br>(1937) | Trustee, Audit and Nominating Committee Member | Since 2001 | Dean Emeritus and Distinguished Professor of International Affairs at the Edmund A. Walsh School of Foreign Service, Georgetown University from June 1995 to June 2009. | 7 | None |

[2] Mr. Garten was initially appointed as a Trustee of the Portfolio on February 6, 1998. He resigned as Trustee on February 3, 2000 and was subsequently reappointed on December 21, 2000.

| Name, Address (Year of Birth) | Position(s) Held with Trust | Term of Office[1] and Length of Time Served | Principal Occupation(s) During Past Five Years | Number of Portfolios in Fund Complex Overseen by Trustee | Other Directorships Held by Trustee |
|---|---|---|---|---|---|
| **Independent Trustees** | | | | | |
| Steven N. Rappaport<br>Lehigh Court, LLC<br>555 Madison Avenue<br>29th Floor<br>New York, New York 10022<br>(1948) | Chairman of the Board of Trustees, Audit Committee Member and Nominating Committee Chairman | Trustee since 1999 and Chairman since 2005 | Partner of Lehigh Court, LLC and RZ Capital (private investment firms) from July 2002 to present. | 9 | Director of iCAD, Inc. (a surgical and medical instruments and apparatus company); Director of Presstek, Inc. (digital imaging technologies company); Director of Wood Resources, LLC. (plywood manufacturing company); Director of Aberdeen Chile Fund, Inc., Aberdeen Indonesia Fund, Inc., Aberdeen Israel Fund, Inc., Aberdeen Latin America Equity Fund, Inc. and Aberdeen Emerging Markets Telecommunications and Infrastructure Fund, Inc. (each a closed-end investment company). |

| Name, Address (Year of Birth) | Position(s) Held with Trust | Term of Office[1] and Length of Time Served | Principal Occupation(s) During Past Five Years |
|---|---|---|---|
| **Officers**** | | | |
| John G. Popp<br>Credit Suisse Asset Management, LLC<br>Eleven Madison Avenue<br>New York, New York 10010<br>(1956) | Chief Executive Officer and President | Since 2010 | Managing Director of Credit Suisse; Group Manager and Senior Portfolio Manager for Performing Credit Strategies; Associated with Credit Suisse or its predecessor since 1997; Officer of other Credit Suisse Funds. |
| Michael A. Pignataro<br>Credit Suisse Asset Management, LLC<br>Eleven Madison Avenue<br>New York, New York 10010<br>(1959) | Chief Financial Officer | Since 1999 | Director and Director of Fund Administration of Credit Suisse; Associated with Credit Suisse or its predecessor since 1984; Officer of other Credit Suisse Funds. |
| Emidio Morizio<br>Credit Suisse Asset Management, LLC<br>One Madison Avenue<br>New York, New York 10010<br>(1966) | Chief Compliance Officer | Since 2004 | Managing Director and Global Head of Compliance of Credit Suisse; Associated with Credit Suisse since July 2000; Officer of other Credit Suisse Funds. |
| Roger Machlis<br>Credit Suisse Asset Management, LLC<br>One Madison Avenue<br>New York, New York 10010<br>(1961) | Chief Legal Officer | Since 2010 | Managing Director and General Counsel for Credit Suisse; Associated with Credit Suisse Group AG since 1997; Officer of other Credit Suisse Funds. |
| Cecilia Chau<br>Credit Suisse Asset Management, LLC<br>Eleven Madison Avenue<br>New York, New York 10010<br>(1973) | Treasurer | Since 2008 | Vice President of Credit Suisse since 2009; Assistant Vice President of Credit Suisse from June 2007 to December 2008; Associated with Alliance Bernstein L.P. from January 2007 to May 2007; Associated with Credit Suisse from August 2000 to December 2006; Officer of other Credit Suisse Funds. |
| Karen Regan<br>Credit Suisse Asset Management, LLC<br>Eleven Madison Avenue<br>New York, New York 10010<br>(1963) | Vice President and Secretary | Since 2010 | Vice President of Credit Suisse; Associated with Credit Suisse since December 2004; Officer of other Credit Suisse Funds |

** The officers of the Portfolio shown are officers that make policy decisions.

The Statement of Additional Information includes additional information about the Trustees and is available, without charge, upon request, by calling 800-222-8977.

**Credit Suisse Trust — International Equity Flex III Portfolio**
**Proxy Voting and Portfolio Holdings Information** (unaudited)

Information regarding how the Portfolio voted proxies related to its portfolio securities during the 12 month period ended June 30 of each year, as well as the policies and procedures that the Portfolio uses to determine how to vote proxies relating to its portfolio securities are available:

- By calling 1-800-222-8977
- On the Portfolio's website, www.credit-suisse.com/us
- On the website of the Securities and Exchange Commission, www.sec.gov.

The Portfolio files a complete schedule of its portfolio holdings for the first and third quarters of its fiscal year with the SEC on Form N-Q. The Portfolio's Forms N-Q are available on the SEC's website at www.sec.gov and may be reviewed and copied at the SEC's Public Reference Room in Washington, DC. Information on the operation of the SEC's Public Reference Room may be obtained by calling 1-202-551-8090.

CREDIT SUISSE

P.O. Box 55030, Boston, MA 02205-5030
800-222-8977 ■ www.credit-suisse.com/us

CREDIT SUISSE ASSET MANAGEMENT SECURITIES, INC., DISTRIBUTOR. TREMK-AR-1210

# Dreyfus Investment Portfolios, MidCap Stock Portfolio

**ANNUAL REPORT** December 31, 2010

BNY MELLON
ASSET MANAGEMENT

Dreyfus

# Contents

## THE FUND



## FOR MORE INFORMATION

# The Fund

## A LETTER FROM THE CHAIRMAN AND CEO

Dear Shareholder:

We are pleased to present this annual report for Dreyfus Investment Portfolios, MidCap Stock Portfolio, covering the 12-month period from January 1, 2010, through December 31, 2010.

Although 2010 proved to be a volatile year for stocks, the reporting period ended with a sustained market rally that produced above-average returns across most market-cap segments for the calendar year. Investors' early concerns regarding sovereign debt issues in Europe and stubbornly high unemployment in the United States later gave way to optimism that massive economic stimulus programs, robust growth in the world's emerging markets, a strong holiday retail season and rising corporate earnings signaled better economic times ahead.

We are aware that stocks have recently reached higher valuations, and that any new economic setbacks could result in market volatility as investors adjust their expectations. Nonetheless, we see potential value in many segments of the equity market. For example, investors in volatile markets may turn to high-quality stocks of U.S. companies with track records of consistent growth in a variety of economic climates, and international equities could benefit from a declining U.S. dollar and potentially higher growth opportunities abroad. With 2011 now upon us, we suggest talking to your financial advisor, who can help you identify potential opportunities and suggest strategies suitable for your individual needs in today's market environment.

For information about how the fund performed during the reporting period, as well as general market perspectives, we provide a Discussion of Fund Performance on the pages that follow.

Thank you for your continued confidence and support.

Sincerely,

Jonathan R. Baum
Chairman and Chief Executive Officer
The Dreyfus Corporation
January 18, 2011

# DISCUSSION OF FUND PERFORMANCE

*For the period of January 1, 2010, through December 31, 2010, as provided by Patrick Slattery, Portfolio Manager*

## Fund and Market Performance Overview

For the 12-month period ended December 31, 2010, Dreyfus Investment Portfolios, MidCap Stock Portfolio's Initial shares produced a total return of 27.10%, and its Service shares produced a total return of 26.94%.[1] In comparison, the fund's benchmark, the Standard & Poor's MidCap 400 Index (the "S&P 400 Index"), produced a total return of 26.64% for the same period.[2]

Equity prices were driven higher in 2010 by improving corporate earnings and revenues, as well as renewed confidence late in the year that the U.S. economy was emerging from recession. Small- and midcap stocks performed particularly well in this environment. The fund produced higher returns than its benchmark, primarily due to the success of our stock selection process across most of the market sectors represented in the S&P 400 Index.

## The Fund's Investment Approach

The fund seeks investment results that are greater than the total return performance of publicly traded common stocks of medium-size domestic companies in the aggregate, as represented by the S&P 400 Index. To pursue this goal, the fund normally invests at least 80% of its assets in stocks of midsize companies. The fund invests in growth and value stocks, which are chosen through a disciplined investment process that combines computer modeling techniques, fundamental analysis and risk management. Consistency of returns compared to the S&P 400 Index is a primary goal of the investment process.

## Economic Developments Sparked Heightened Volatility

Throughout 2010, the U.S. economy continued to emerge from recession at a slow but steady pace. However, investor sentiment proved volatile in light of unsettling global developments and uncertainty regarding the recovery's sustainability. After generally positive economic data sent stocks higher from February through late April 2010, the market retreated on news of an intensifying sovereign debt crisis in

Europe. During the summer, stubbornly high levels of U.S. unemployment and troubled housing markets, along with growing inflationary pressures in China, constrained equity prices near their lows for the year. However, continuing U.S. economic improvement in the fall led to a growing consensus that a return to recession was unlikely, and political developments following the midterm elections provided greater clarity regarding U.S. economic and tax policies. As investor confidence rose, stocks climbed sharply during the fourth quarter of 2010.

## Quantitative Factors Proved Broadly Positive

A broad range of the quantitative modeling factors that drive the fund's stock selection process enhanced performance during the reporting period. Behavioral factors, such as price momentum, and quality-related factors, such as earnings quality, contributed strongly to the fund's relative outperformance. Value-related factors generated more volatile results, particularly during times of market weakness, but generally added to returns for the year as a whole.

## Health Care and Industrials Sectors Led Performance

Investments in health care companies produced some of the fund's better returns compared to the benchmark. OSI Pharmaceuticals was acquired by Astellas Pharma at a significant premium to its then-prevailing stock price. Endo Pharmaceuticals Holdings rose on the strength of favorable quarterly reports and positive market reaction to the company's agreement to acquire generic drug manufacturer Qualitest Pharmaceuticals. Such gains overshadowed results from health care holdings that failed to keep pace with the sector's advance, such as biotechnology product maker Techne.

The fund generated relatively robust returns in other areas as well. Strong gains among industrial holdings, such as diversified machinery parts manufacturer Timken, more than made up for the underperformance of others, such as truck maker Oshkosh. The fund also produced strong results in the commercial services sector by holding outperforming IT services providers such as *Gartner*, and with the exception of services outsourcing provider Computer Sciences, avoided most of the sector's weaker performers. Top holdings in other areas included fashion accessory designer Fossil and aftermarket automobile parts maker *Advance Auto Parts*.

The fund generally kept pace with the market's gains in the technology sector. Enterprise software developer *Sybase* rose sharply on news of a takeover offer, while equipment maker F5 Networks and electrical components manufacturer Vishay Intertechnology both delivered strong financial results. On the other hand, computer wholesaler Tech Data and communications equipment maker *CommScope* both underperformed early in the reporting period after providing weaker-than-expected guidance.

Utilities proved to be the fund's weakest sector. Several holdings, such as Constellation Energy Group and DPL, undermined the fund's relative performance.

## Continued Commitment to Our Disciplined Process

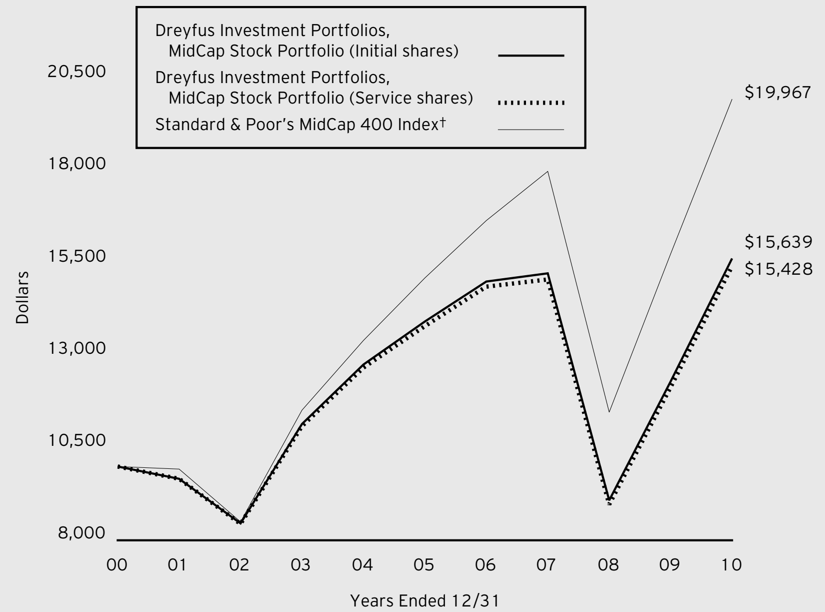
We are pleased that, as of the end of the reporting period, prevailing market conditions appeared to favor our disciplined stock selection process. Our consistent commitment to this process across the full range of market cycles remains the cornerstone of our investment approach.

January 18, 2011

*Please note, the position in any security highlighted with italicized typeface was sold during the reporting period.*
*Equity funds are subject generally to market, market sector, market liquidity, issuer and investment style risks, among other factors, to varying degrees, all of which are more fully described in the fund's prospectus.*
*Stocks of midcap companies often experience sharper price fluctuations than stocks of large-cap companies.*
*The fund is only available as a funding vehicle under variable life insurance policies or variable annuity contracts issued by insurance companies. Individuals may not purchase shares of the fund directly. A variable annuity is an insurance contract issued by an insurance company that enables investors to accumulate assets on a tax-deferred basis for retirement or other long-term goals.*

1 *Total return includes reinvestment of dividends and any capital gains paid. Past performance is no guarantee of future results. Share price and investment return fluctuate such that upon redemption, fund shares may be worth more or less than their original cost. The fund's performance does not reflect the deduction of additional charges and expenses imposed in connection with investing in variable insurance contracts, which will reduce returns. Return figures provided reflect the absorption of certain fund expenses by The Dreyfus Corporation pursuant to an agreement in effect through August 31, 2010. Had these expenses not been absorbed, the fund's returns would have been lower.*

2 *SOURCE: LIPPER INC. — Reflects reinvestment of dividends and, where applicable, capital gain distributions. The Standard & Poor's MidCap 400 Index is a widely accepted, unmanaged total return index measuring the performance of the midsize-company segment of the U.S. market. Investors cannot invest directly in an index.*




Comparison of change in value of $10,000 investment in Dreyfus Investment Portfolios, MidCap Stock Portfolio Initial shares and Service shares and the Standard & Poor's MidCap 400 Index

## Average Annual Total Returns *as of 12/31/10*

| | 1 Year | 5 Years | 10 Years |
|---|---|---|---|
| **Initial shares** | **27.10%** | **2.33%** | **4.57%** |
| **Service shares** | **26.94%** | **2.24%** | **4.43%** |
| **Standard & Poor's MidCap 400 Index** | **26.64%** | **5.73%** | **7.16%** |

*† Source: Lipper Inc.*

*Past performance is not predictive of future performance. The fund's performance shown in the graph and table does not reflect the deduction of taxes that a shareholder would pay on fund distributions or the redemption of fund shares.*

***The fund's performance does not reflect the deduction of additional charges and expenses imposed in connection with investing in variable insurance contracts which will reduce returns.***

*The above graph compares a $10,000 investment made in Initial and Service shares of Dreyfus Investment Portfolios, MidCap Stock Portfolio on 12/31/00 to a $10,000 investment made in the Standard & Poor's MidCap 400 Index (the "Index") on that date.*

*The fund's Initial shares are not subject to a Rule 12b-1 fee. The fund's Service shares are subject to a 0.25% annual Rule 12b-1 fee. The performance figures for Service shares reflect certain expense reimbursements, without which the performance of Service shares would have been lower. All dividends and capital gain distributions are reinvested.*

*The fund's performance shown in the line graph takes into account all applicable fund fees and expenses (after any expense reimbursements). The Index is a widely accepted, unmanaged total return index measuring the performance of the midsize company segment of the U.S. stock market. Unlike a mutual fund, the Index is not subject to charges, fees and other expenses. Investors cannot invest directly in any index. Further information relating to fund performance, including expense reimbursements, if applicable, is contained in the Financial Highlights section of the prospectus and elsewhere in this report.*

# UNDERSTANDING YOUR FUND'S EXPENSES (Unaudited)

*As a mutual fund investor, you pay ongoing expenses, such as management fees and other expenses. Using the information below, you can estimate how these expenses affect your investment and compare them with the expenses of other funds. You also may pay one-time transaction expenses, including sales charges (loads) and redemption fees, and expenses associated with variable annuity or insurance contracts, which are not shown in this section and would have resulted in higher total expenses. For more information, see your fund's prospectus or talk to your financial adviser.*

### Review your fund's expenses

The table below shows the expenses you would have paid on a $1,000 investment in Dreyfus Investment Portfolios, MidCap Stock Portfolio from July 1, 2010 to December 31, 2010. It also shows how much a $1,000 investment would be worth at the close of the period, assuming actual returns and expenses.

**Expenses and Value of a $1,000 Investment**
assuming actual returns for the six months ended December 31, 2010

| | Initial Shares | Service Shares |
|---|---|---|
| Expenses paid per $1,000† | $ 4.94 | $ 5.98 |
| Ending value (after expenses) | $1,281.10 | $1,280.20 |

# COMPARING YOUR FUND'S EXPENSES WITH THOSE OF OTHER FUNDS (Unaudited)

### Using the SEC's method to compare expenses

The Securities and Exchange Commission (SEC) has established guidelines to help investors assess fund expenses. Per these guidelines, the table below shows your fund's expenses based on a $1,000 investment, assuming a hypothetical 5% annualized return. You can use this information to compare the ongoing expenses (but not transaction expenses or total cost) of investing in the fund with those of other funds. All mutual fund shareholder reports will provide this information to help you make this comparison. Please note that you cannot use this information to estimate your actual ending account balance and expenses paid during the period.

**Expenses and Value of a $1,000 Investment**
assuming a hypothetical 5% annualized return for the six months ended December 31, 2010

| | Initial Shares | Service Shares |
|---|---|---|
| Expenses paid per $1,000† | $ 4.38 | $ 5.30 |
| Ending value (after expenses) | $1,020.87 | $1,019.96 |

† *Expenses are equal to the fund's annualized expense ratio of .86% for Initial Shares and 1.04% for Service Shares, multiplied by the average account value over the period, multiplied by 184/365 (to reflect the one-half year period).*

# STATEMENT OF INVESTMENTS

December 31, 2010

| Common Stocks—99.6% | Shares | | Value ($) |
|---|---|---|---|
| **Consumer Discretionary—13.9%** | | | |
| Aeropostale | 21,162 | a | 521,432 |
| American Greetings, Cl. A | 42,000 | b | 930,720 |
| AnnTaylor Stores | 24,900 | a,b | 682,011 |
| Autoliv | 20,900 | | 1,649,846 |
| Brinker International | 64,350 | | 1,343,628 |
| Cheesecake Factory | 53,400 | a,b | 1,637,244 |
| Fossil | 33,300 | a | 2,346,984 |
| ITT Educational Services | 7,100 | a,b | 452,199 |
| J Crew Group | 35,800 | a | 1,544,412 |
| PetSmart | 41,600 | | 1,656,512 |
| Ross Stores | 11,400 | | 721,050 |
| Scholastic | 39,100 | | 1,155,014 |
| Signet Jewelers | 30,500 | a | 1,323,700 |
| Sotheby's | 37,900 | | 1,705,500 |
| Timberland, Cl. A | 26,700 | a | 656,553 |
| TRW Automotive Holdings | 11,900 | a | 627,130 |
| Warnaco Group | 31,450 | a | 1,731,951 |
| Williams-Sonoma | 44,000 | | 1,570,360 |
| Wyndham Worldwide | 28,100 | | 841,876 |
| | | | **23,098,122** |
| **Consumer Staples—4.3%** | | | |
| ConAgra Foods | 21,600 | | 487,728 |
| Corn Products International | 23,000 | | 1,058,000 |
| Dr. Pepper Snapple Group | 43,700 | | 1,536,492 |
| Energizer Holdings | 27,700 | a | 2,019,330 |
| Flowers Foods | 21,600 | b | 581,256 |
| Hormel Foods | 16,650 | | 853,479 |
| Tyson Foods, Cl. A | 34,800 | | 599,256 |
| | | | **7,135,541** |
| **Energy—6.4%** | | | |
| Arch Coal | 20,200 | | 708,212 |
| Cimarex Energy | 39,500 | | 3,496,935 |
| EXCO Resources | 35,000 | | 679,700 |
| Forest Oil | 17,800 | a | 675,866 |
| Oceaneering International | 16,100 | a | 1,185,443 |

| **Common Stocks (continued)** | Shares | | Value ($) |
|---|---|---|---|
| **Energy (continued)** | | | |
| Oil States International | 15,600 | a,b | 999,804 |
| Pioneer Natural Resources | 3,600 | | 312,552 |
| SEACOR Holdings | 4,200 | | 424,578 |
| Southern Union | 60,100 | | 1,446,607 |
| Whiting Petroleum | 6,200 | a | 726,578 |
| | | | **10,656,275** |
| **Financial—18.5%** | | | |
| American Financial Group | 59,575 | | 1,923,677 |
| Apartment Investment & Management, Cl. A | 59,700 | b,c | 1,542,648 |
| CB Richard Ellis Group, Cl. A | 48,100 | a | 985,088 |
| Comerica | 16,300 | b | 688,512 |
| Digital Realty Trust | 5,100 | b,c | 262,854 |
| Eaton Vance | 42,600 | b | 1,287,798 |
| Equity One | 21,600 | b,c | 392,688 |
| Fifth Third Bancorp | 77,900 | | 1,143,572 |
| First Citizens Bancshares/NC, Cl. A | 5,300 | | 1,001,965 |
| HCC Insurance Holdings | 45,450 | | 1,315,323 |
| Highwoods Properties | 15,500 | b,c | 493,675 |
| Hospitality Properties Trust | 80,000 | c | 1,843,200 |
| International Bancshares | 81,800 | | 1,638,454 |
| Jones Lang LaSalle | 18,400 | | 1,544,128 |
| Liberty Property Trust | 18,200 | b,c | 580,944 |
| Macerich | 32,847 | c | 1,555,962 |
| Nasdaq OMX Group | 9,000 | a,b | 213,390 |
| NewAlliance Bancshares | 23,300 | | 349,034 |
| Potlatch | 30,100 | c | 979,755 |
| Rayonier | 29,700 | c | 1,559,844 |
| Reinsurance Group of America | 26,300 | | 1,412,573 |
| SEI Investments | 77,600 | | 1,846,104 |
| SL Green Realty | 18,000 | c | 1,215,180 |
| StanCorp Financial Group | 41,300 | | 1,864,282 |
| SVB Financial Group | 24,500 | a | 1,299,725 |

| Common Stocks (continued) | Shares | | Value ($) |
|---|---|---|---|
| **Financial (continued)** | | | |
| Weingarten Realty Investors | 44,200 | b,c | 1,050,192 |
| Westamerica Bancorporation | 14,600 | | 809,862 |
| | | | **30,800,429** |
| **Health Care—10.6%** | | | |
| Cephalon | 27,700 | a | 1,709,644 |
| Cooper | 23,700 | | 1,335,258 |
| Endo Pharmaceuticals Holdings | 12,800 | a | 457,088 |
| Health Net | 45,600 | a | 1,244,424 |
| Henry Schein | 3,400 | a | 208,726 |
| Hologic | 89,200 | a | 1,678,744 |
| Humana | 25,700 | a | 1,406,818 |
| IDEXX Laboratories | 9,800 | a,b | 678,356 |
| Kinetic Concepts | 28,900 | a,b | 1,210,332 |
| LifePoint Hospitals | 15,000 | a | 551,250 |
| Medicis Pharmaceutical, Cl. A | 58,700 | | 1,572,573 |
| Mettler-Toledo International | 2,700 | a | 408,267 |
| STERIS | 43,500 | | 1,586,010 |
| Techne | 33,300 | | 2,186,811 |
| United Therapeutics | 4,000 | a | 252,880 |
| Waters | 16,200 | a | 1,258,902 |
| | | | **17,746,083** |
| **Industrial—14.6%** | | | |
| Alaska Air Group | 43,600 | a | 2,471,684 |
| Copart | 44,100 | a,b | 1,647,135 |
| Corrections Corp. of America | 21,300 | a | 533,778 |
| Donaldson | 11,800 | | 687,704 |
| Graco | 46,700 | | 1,842,315 |
| Joy Global | 23,800 | | 2,064,650 |
| Kansas City Southern | 42,700 | a | 2,043,622 |
| KBR | 24,800 | | 755,656 |
| Kennametal | 29,700 | | 1,171,962 |
| Oshkosh | 62,400 | a | 2,198,976 |

| **Common Stocks (continued)** | Shares | | Value ($) |
|---|---|---|---|
| **Industrial (continued)** | | | |
| Owens Corning | 21,300 | a | 663,495 |
| Regal-Beloit | 17,800 | | 1,188,328 |
| Ryder System | 14,300 | | 752,752 |
| Textron | 52,700 | b | 1,245,828 |
| Timken | 72,900 | | 3,479,517 |
| Toro | 16,300 | | 1,004,732 |
| URS | 15,900 | a | 661,599 |
| | | | **24,413,733** |
| **Information Technology—17.3%** | | | |
| Advent Software | 22,400 | a | 1,297,408 |
| Amdocs | 27,600 | a | 758,172 |
| Broadridge Financial Solutions | 44,300 | | 971,499 |
| Computer Sciences | 27,400 | | 1,359,040 |
| Convergys | 55,400 | a | 729,618 |
| Cypress Semiconductor | 63,800 | a | 1,185,404 |
| DST Systems | 13,800 | | 612,030 |
| F5 Networks | 9,000 | a | 1,171,440 |
| FactSet Research Systems | 31,000 | b | 2,906,560 |
| Fairchild Semiconductor International | 177,000 | a | 2,762,970 |
| Harris | 7,000 | | 317,100 |
| IAC/InterActiveCorp | 16,100 | a,b | 462,070 |
| Lam Research | 9,100 | a | 471,198 |
| Lender Processing Services | 25,100 | | 740,952 |
| Parametric Technology | 16,100 | a | 362,733 |
| Plantronics | 65,000 | | 2,419,300 |
| SanDisk | 34,300 | a | 1,710,198 |
| SRA International, Cl. A | 71,600 | a | 1,464,220 |
| Synopsys | 74,000 | a | 1,991,340 |
| Tech Data | 39,500 | a | 1,738,790 |
| Vishay Intertechnology | 163,000 | a | 2,392,840 |
| WebMD Health, Cl. A | 21,700 | a | 1,108,002 |
| | | | **28,932,884** |

| Common Stocks (continued) | Shares | | Value ($) |
|---|---|---|---|
| **Materials—5.5%** | | | |
| Ball | 5,000 | | 340,250 |
| Cabot | 15,900 | | 598,635 |
| Domtar | 11,200 | | 850,304 |
| Lubrizol | 30,100 | | 3,217,088 |
| MeadWestvaco | 14,100 | | 368,856 |
| Minerals Technologies | 41,300 | | 2,701,433 |
| NewMarket | 2,400 | b | 296,088 |
| Reliance Steel & Aluminum | 14,100 | | 720,510 |
| | | | **9,093,164** |
| **Telecommunication Services—1.6%** | | | |
| Telephone & Data Systems | 72,900 | | **2,664,495** |
| **Utilities—6.9%** | | | |
| CMS Energy | 25,700 | | 478,020 |
| Constellation Energy Group | 29,400 | | 900,522 |
| DPL | 98,600 | | 2,535,006 |
| DTE Energy | 23,400 | | 1,060,488 |
| Energen | 39,100 | | 1,886,966 |
| Great Plains Energy | 66,600 | | 1,291,374 |
| NV Energy | 37,300 | | 524,065 |
| Questar | 97,400 | | 1,695,734 |
| Westar Energy | 27,300 | | 686,868 |
| WGL Holdings | 11,200 | | 400,624 |
| | | | **11,459,667** |
| **Total Common Stocks** (cost $141,006,064) | | | **166,000,393** |

| Other Investment—.5% | | | |
|---|---|---|---|
| **Registered Investment Company;** | | | |
| Dreyfus Institutional Preferred Plus Money Market Fund (cost $912,000) | 912,000 | d | **912,000** |

| **Investment of Cash Collateral for Securities Loaned—1.2%** | Shares | Value ($) |
|---|---|---|
| **Registered Investment Company;** | | |
| Dreyfus Institutional Cash Advantage Fund (cost $2,072,631) | 2,072,631 [d] | **2,072,631** |
| **Total Investments** (cost $143,990,695) | **101.3%** | **168,985,024** |
| **Liabilities, Less Cash and Receivables** | **(1.3%)** | **(2,244,161)** |
| **Net Assets** | **100.0%** | **166,740,863** |

[a] *Non-income producing security.*

[b] *Security, or portion thereof, on loan. At December 31, 2010, the market value of the fund's securities on loan was $2,004,062 and the market value of the collateral held by the fund was $2,072,631.*

[c] *Investment in real estate investment trust.*

[d] *Investment in affiliated money market mutual fund.*

## Portfolio Summary (Unaudited)†

| | Value (%) | | Value (%) |
|---|---|---|---|
| Financial | 18.5 | Energy | 6.4 |
| Information Technology | 17.3 | Materials | 5.5 |
| Industrial | 14.6 | Consumer Staples | 4.3 |
| Consumer Discretionary | 13.9 | Money Market Investments | 1.7 |
| Health Care | 10.6 | Telecommunication Services | 1.6 |
| Utilities | 6.9 | | **101.3** |

† *Based on net assets.*

*See notes to financial statements.*

# STATEMENT OF ASSETS AND LIABILITIES

December 31, 2010

| | Cost | Value |
|---|---|---|
| **Assets ($):** | | |
| Investments in securities—See Statement of Investments (including securities on loan, valued at $2,004,062)—Note 1(b): | | |
| Unaffiliated issuers | 141,006,064 | 166,000,393 |
| Affiliated issuers | 2,984,631 | 2,984,631 |
| Cash | | 58,191 |
| Dividends receivable | | 102,683 |
| Receivable for shares of Beneficial Interest subscribed | | 13,674 |
| | | **169,159,572** |
| **Liabilities ($):** | | |
| Due to The Dreyfus Corporation and affiliates—Note 3(b) | | 116,152 |
| Liability for securities on loan—Note 1(b) | | 2,072,631 |
| Payable for shares of Beneficial Interest redeemed | | 170,408 |
| Accrued expenses | | 59,518 |
| | | **2,418,709** |
| **Net Assets ($)** | | **166,740,863** |
| **Composition of Net Assets ($):** | | |
| Paid-in capital | | 199,422,798 |
| Accumulated undistributed investment income—net | | 791,970 |
| Accumulated net realized gain (loss) on investments | | (58,468,234) |
| Accumulated net unrealized appreciation (depreciation) on investments | | 24,994,329 |
| **Net Assets ($)** | | **166,740,863** |

## Net Asset Value Per Share

| | Initial Shares | Service Shares |
|---|---|---|
| Net Assets ($) | 147,155,315 | 19,585,548 |
| Shares Outstanding | 11,173,229 | 1,488,073 |
| **Net Asset Value Per Share ($)** | **13.17** | **13.16** |

*See notes to financial statements.*

# STATEMENT OF OPERATIONS

Year Ended December 31, 2010

| | |
|---|---|
| **Investment Income ($):** | |
| **Income:** | |
| Cash dividends: | |
| Unaffiliated issuers | 2,084,390 |
| Affiliated issuers | 1,753 |
| Income from securities lending—Note 1(b) | 15,136 |
| **Total Income** | **2,101,279** |
| **Expenses:** | |
| Investment advisory fee—Note 3(a) | 1,145,414 |
| Professional fees | 52,323 |
| Distribution fees—Note 3(b) | 43,370 |
| Prospectus and shareholders' reports | 42,188 |
| Custodian fees—Note 3(b) | 17,284 |
| Shareholder servicing costs—Note 3(b) | 6,079 |
| Loan commitment fees—Note 2 | 5,029 |
| Trustees' fees and expenses—Note 3(c) | 3,444 |
| Interest expense—Note 2 | 241 |
| Miscellaneous | 12,898 |
| **Total Expenses** | **1,328,270** |
| Less—waiver of fees due to undertaking—Note 3(a) | (20,350) |
| Less—reduction in fees due to earnings credits—Note 3(b) | (7) |
| **Net Expenses** | **1,307,913** |
| **Investment Income—Net** | **793,366** |
| **Realized and Unrealized Gain (Loss) on Investments—Note 4 ($):** | |
| Net realized gain (loss) on investments | 17,733,437 |
| Net unrealized appreciation (depreciation) on investments | 18,149,709 |
| **Net Realized and Unrealized Gain (Loss) on Investments** | **35,883,146** |
| **Net Increase in Net Assets Resulting from Operations** | **36,676,512** |

*See notes to financial statements.*

# STATEMENT OF CHANGES IN NET ASSETS

| | Year Ended December 31, | |
|---|---|---|
| | 2010 | 2009 |
| **Operations ($):** | | |
| Investment income—net | 793,366 | 1,512,565 |
| Net realized gain (loss) on investments | 17,733,437 | (28,024,642) |
| Net unrealized appreciation (depreciation) on investments | 18,149,709 | 67,186,562 |
| **Net Increase (Decrease) in Net Assets Resulting from Operations** | **36,676,512** | **40,674,485** |
| **Dividends to Shareholders from ($):** | | |
| Investment income—net: | | |
| Initial Shares | (1,351,353) | (1,799,027) |
| Service Shares | (158,748) | (141,551) |
| **Total Dividends** | **(1,510,101)** | **(1,940,578)** |
| **Beneficial Interest Transactions ($):** | | |
| Net proceeds from shares sold: | | |
| Initial Shares | 11,148,281 | 7,850,230 |
| Service Shares | 3,623,506 | 883,388 |
| Dividends reinvested: | | |
| Initial Shares | 1,351,353 | 1,799,027 |
| Service Shares | 158,748 | 141,551 |
| Cost of shares redeemed: | | |
| Initial Shares | (28,547,371) | (37,882,349) |
| Service Shares | (4,212,318) | (3,056,034) |
| **Increase (Decrease) in Net Assets from Beneficial Interest Transactions** | **(16,477,801)** | **(30,264,187)** |
| **Total Increase (Decrease) in Net Assets** | **18,688,610** | **8,469,720** |
| **Net Assets ($):** | | |
| Beginning of Period | 148,052,253 | 139,582,533 |
| **End of Period** | **166,740,863** | **148,052,253** |
| Undistributed investment income—net | 791,970 | 1,508,705 |

| | Year Ended December 31, | |
|---|---|---|
| | 2010 | 2009 |
| **Capital Share Transactions:** | | |
| **Initial Shares** | | |
| Shares sold | 968,273 | 925,743 |
| Shares issued for dividends reinvested | 115,896 | 248,142 |
| Shares redeemed | (2,528,129) | (4,564,894) |
| **Net Increase (Decrease) in Shares Outstanding** | **(1,443,960)** | **(3,391,009)** |
| **Service Shares** | | |
| Shares sold | 305,583 | 105,477 |
| Shares issued for dividends reinvested | 13,603 | 19,524 |
| Shares redeemed | (369,298) | (362,450) |
| **Net Increase (Decrease) in Shares Outstanding** | **(50,112)** | **(237,449)** |

*See notes to financial statements.*

# FINANCIAL HIGHLIGHTS

The following tables describe the performance for each share class for the fiscal periods indicated. All information (except portfolio turnover rate) reflects financial results for a single fund share. Total return shows how much your investment in the fund would have increased (or decreased) during each period, assuming you had reinvested all dividends and distributions. The fund's total returns do not reflect expenses associated with variable annuity or insurance contracts. These figures have been derived from the fund's financial statements.

| | Year Ended December 31, | | | | |
|---|---|---|---|---|---|
| **Initial Shares** | 2010 | 2009 | 2008 | 2007 | 2006 |
| **Per Share Data ($):** | | | | | |
| Net asset value, beginning of period | 10.46 | 7.85 | 15.52 | 17.39 | 19.15 |
| Investment Operations: | | | | | |
| Investment income—net [a] | .06 | .11 | .09 | .12 | .08 |
| Net realized and unrealized gain (loss) on investments | 2.76 | 2.62 | (5.63) | .19 | 1.39 |
| Total from Investment Operations | 2.82 | 2.73 | (5.54) | .31 | 1.47 |
| Distributions: | | | | | |
| Dividends from investment income—net | (.11) | (.12) | (.12) | (.07) | (.07) |
| Dividends from net realized gain on investments | – | – | (2.01) | (2.11) | (3.16) |
| Total Distributions | (.11) | (.12) | (2.13) | (2.18) | (3.23) |
| Net asset value, end of period | 13.17 | 10.46 | 7.85 | 15.52 | 17.39 |
| **Total Return (%)** | 27.10 | 35.51 | (40.42) | 1.50 | 7.75 |
| **Ratios/Supplemental Data (%):** | | | | | |
| Ratio of total expenses to average net assets | .84 | .84 | .82 | .80 | .80 |
| Ratio of net expenses to average net assets | .84 | .84 | .81 | .80 | .80 |
| Ratio of net investment income to average net assets | .54 | 1.22 | .76 | .73 | .48 |
| Portfolio Turnover Rate | 79.28 | 75.42 | 86.74 | 116.83 | 149.02 |
| Net Assets, end of period ($ x 1,000) | 147,155 | 131,962 | 125,701 | 277,602 | 338,081 |

[a] *Based on average shares outstanding at each month end.*
*See notes to financial statements.*

| | Year Ended December 31, | | | | |
|---|---|---|---|---|---|
| **Service Shares** | 2010 | 2009 | 2008 | 2007 | 2006 |
| **Per Share Data ($):** | | | | | |
| Net asset value, beginning of period | 10.46 | 7.82 | 15.45 | 17.31 | 19.06 |
| Investment Operations: | | | | | |
| Investment income—net[a] | .05 | .10 | .08 | .09 | .06 |
| Net realized and unrealized gain (loss) on investments | 2.76 | 2.63 | (5.60) | .21 | 1.39 |
| Total from Investment Operations | 2.81 | 2.73 | (5.52) | .30 | 1.45 |
| Distributions: | | | | | |
| Dividends from investment income—net | (.11) | (.09) | (.10) | (.05) | (.04) |
| Dividends from net realized gain on investments | – | – | (2.01) | (2.11) | (3.16) |
| Total Distributions | (.11) | (.09) | (2.11) | (2.16) | (3.20) |
| Net asset value, end of period | 13.16 | 10.46 | 7.82 | 15.45 | 17.31 |
| **Total Return (%)** | 26.94 | 35.33 | (40.44) | 1.39 | 7.68 |
| **Ratios/Supplemental Data (%):** | | | | | |
| Ratio of total expenses to average net assets | 1.09 | 1.09 | 1.06 | 1.05 | 1.05 |
| Ratio of net expenses to average net assets | .97 | .90 | .90 | .90 | .91 |
| Ratio of net investment income to average net assets | .40 | 1.16 | .62 | .58 | .37 |
| Portfolio Turnover Rate | 79.28 | 75.42 | 86.74 | 116.83 | 149.02 |
| Net Assets, end of period ($ x 1,000) | 19,586 | 16,090 | 13,881 | 39,009 | 85,277 |

[a] *Based on average shares outstanding at each month end.*
*See notes to financial statements.*

### NOTE 1—Significant Accounting Policies:

Dreyfus Investment Portfolios (the "Company") is registered under the Investment Company Act of 1940, as amended (the "Act"), as an open-end management investment company, operating as a series company currently offering four series, including the MidCap Stock Portfolio (the "fund"). The fund is only offered to separate accounts established by insurance companies to fund variable annuity contracts and variable life insurance policies. The fund is a diversified series. The fund's investment objective is to seek investment results that are greater than the total return performance of publicly traded common stocks of medium-size domestic companies in the aggregate, as represented by the Standard & Poor's MidCap 400 Index. The Dreyfus Corporation (the "Manager" or "Dreyfus"), a wholly-owned subsidiary of The Bank of New York Mellon Corporation ("BNY Mellon"), serves as the fund's investment adviser.

MBSC Securities Corporation (the "Distributor"), a wholly-owned subsidiary of the Manager, is the distributor of the fund's shares, which are sold without a sales charge. The fund is authorized to issue an unlimited number of $.001 par value shares of Beneficial Interest in each of the following classes of shares: Initial and Service. Each class of shares has identical rights and privileges, except with respect to the distribution plan, the expenses borne by each class, the allocation of certain transfer agency costs and certain voting rights. Income, expenses (other than expenses attributable to a specific class), and realized and unrealized gains or losses on investments are allocated to each class of shares based on its relative net assets.

The Company accounts separately for the assets, liabilities and operations of each series. Expenses directly attributable to each series are charged to that series' operations; expenses which are applicable to all series are allocated among them on a pro rata basis.

The Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") is the exclusive reference of authoritative U.S. generally accepted accounting principles ("GAAP") recognized by the FASB to be applied by nongovernmental entities. Rules and interpretive releases of the Securities and Exchange Commission ("SEC") under authority of federal laws are also sources of authoritative GAAP for SEC registrants. The fund's financial statements are prepared in accordance with GAAP, which may require the use of management estimates and assumptions. Actual results could differ from those estimates.

The Company enters into contracts that contain a variety of indemnifications. The fund's maximum exposure under these arrangements is unknown. The fund does not anticipate recognizing any loss related to these arrangements.

**(a) Portfolio valuation:** Investments in securities are valued at the last sales price on the securities exchange or national securities market on which such securities are primarily traded. Securities listed on the National Market System for which market quotations are available are valued at the official closing price or, if there is no official closing price that day, at the last sales price. Securities not listed on an exchange or the national securities market, or securities for which there were no transactions, are valued at the average of the most recent bid and asked prices, except for open short positions, where the asked price is used for valuation purposes. Bid price is used when no asked price is available. Registered investment companies that are not traded on an exchange are valued at their net asset value. When market quotations or official closing prices are not readily available, or are determined not to reflect accurately fair value, such as when the value of a security has been significantly affected by events after the close of the exchange or market on which the security is principally traded (for example, a foreign exchange or market), but before the fund calculates its net asset value, the fund may value these investments at fair value as determined in accordance with the procedures approved by the Board of Trustees. Fair valuing of securities may be determined with the assistance of a pricing service using calculations based on indices of domestic securities and other appropriate indicators, such as prices of relevant American Depository Receipts and futures contracts. For other securities that are fair valued by the Board of Trustees, certain factors may be considered such as: fundamental analytical data, the nature and duration of restrictions on disposition, an evaluation of the forces that influence the market in which the securities are purchased and sold, and public trading in similar securities of the issuer or comparable issuers.

The fair value of a financial instrument is the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (i.e. the exit price). GAAP establishes a fair value hierarchy that prioritizes the inputs of valuation techniques used to measure fair value. This hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements).

Additionally, GAAP provides guidance on determining whether the volume and activity in a market has decreased significantly and whether such a decrease in activity results in transactions that are not orderly. GAAP requires enhanced disclosures around valuation inputs and techniques used during annual and interim periods.

Various inputs are used in determining the value of the fund's investments relating to fair value measurements. These inputs are summarized in the three broad levels listed below:

**Level 1**—unadjusted quoted prices in active markets for identical investments.

**Level 2**—other significant observable inputs (including quoted prices for similar investments, interest rates, prepayment speeds, credit risk, etc.).

**Level 3**—significant unobservable inputs (including the fund's own assumptions in determining the fair value of investments).

| | Level 1–Unadjusted Quoted Prices | Level 2–Other Significant Observable Inputs | Level 3–Significant Unobservable Inputs | Total |
|---|---|---|---|---|
| **Assets ($)** | | | | |
| Investments in Securities: | | | | |
| Equity Securities–Domestic† | 163,026,847 | – | – | **163,026,847** |
| Equity Securities–Foreign† | 2,973,546 | – | – | **2,973,546** |
| Mutual Funds | 2,984,631 | – | – | **2,984,631** |

† *See Statement of Investments for additional detailed categorizations.*

In January 2010, FASB issued Accounting Standards Update ("ASU") No. 2010-06 "Improving Disclosures about Fair Value Measurements". The portions of ASU No. 2010-06 which require reporting entities to prepare new disclosures surrounding amounts and reasons for significant transfers in and out of Level 1 and Level 2 fair value measurements as well as inputs and valuation techniques used to measure fair value for both recurring and nonrecurring fair value measurements that fall in either Level 2 or Level 3 have been adopted by the fund. No significant transfers between Level 1 or Level 2 fair value measurements occurred at December 31, 2010. The remaining portion of ASU No. 2010-06 requires reporting entities to make new disclosures about information on purchases, sales, issuances and settlements on a gross basis in the reconciliation of activity in Level 3 fair value measurements. These new and revised disclosures are required to be implemented for fiscal years beginning after December 15, 2010. Management is currently evaluating the impact that the adoption of this remaining portion of ASU No. 2010-06 may have on the fund's financial statement disclosures.

**(b) Securities transactions and investment income:** Securities transactions are recorded on a trade date basis. Realized gains and losses from securities transactions are recorded on the identified cost basis. Dividend income is recognized on the ex-dividend date and interest income, including, where applicable, accretion of discount and amortization of premium on investments, is recognized on the accrual basis.

Pursuant to a securities lending agreement with The Bank of New York Mellon, a subsidiary of BNY Mellon and an affiliate of Dreyfus, the fund may lend securities to qualified institutions. It is the fund's policy that, at origination, all loans are secured by collateral of at least 102% of the value of U.S. securities loaned and 105% of the value of foreign securities loaned. Collateral equivalent to at least 100% of the market value of securities on loan is maintained at all times. Collateral is either in the form of cash, which can be invested in certain money market mutual funds managed by the Manager, U.S. Government and Agency securities or letters of credit. The fund is entitled to receive all income on securities loaned, in addition to income earned as a result of the lending transaction. Although each security loaned is fully collateralized, the fund bears the risk of delay in recovery of, or loss of rights in, the securities loaned should a borrower fail to return the securities in a timely manner. During the period ended December 31, 2010, The Bank of New York Mellon earned $6,487 from lending portfolio securities, pursuant to the securities lending agreement.

**(c) Affiliated issuers:** Investments in other investment companies advised by Dreyfus are defined as "affiliated" in the Act.

The fund may invest in shares of certain affiliated investment companies also advised or managed by Dreyfus. Investments in affiliated investment companies for the period ended December 31, 2010 were as follows:

| Affiliated Investment Company | Value 12/31/2009 ($) | Purchases ($) | Sales ($) | Value 12/31/2010 ($) | Net Assets (%) |
|---|---|---|---|---|---|
| Dreyfus Institutional Preferred Plus Money Market Fund | 1,435,000 | 20,504,000 | 21,027,000 | 912,000 | .5 |
| Dreyfus Institutional Cash Advantage Fund | 20,534,022 | 61,307,591 | 79,768,982 | 2,072,631 | 1.2 |
| **Total** | **21,969,022** | **81,811,591** | **100,795,982** | **2,984,631** | **1.7** |

**(d) Dividends to shareholders:** Dividends are recorded on the ex-dividend date. Dividends from investment income-net and dividends from net realized capital gains, if any, are normally declared and paid annually, but the fund may make distributions on a more frequent basis to comply with the distribution requirements of the Internal Revenue Code of 1986, as amended (the "Code"). To the extent that net realized capital gains can be offset by capital loss carryovers, it is the policy of the fund not to distribute such gains. Income and capital gain distributions are determined in accordance with income tax regulations, which may differ from GAAP.

**(e) Federal income taxes:** It is the policy of the fund to continue to qualify as a regulated investment company, if such qualification is in the best interests of its shareholders, by complying with the applicable provisions of the Code, and to make distributions of taxable income sufficient to relieve it from substantially all federal income and excise taxes.

As of and during the period ended December 31, 2010, the fund did not have any liabilities for any uncertain tax positions. The fund recognizes interest and penalties, if any, related to uncertain tax positions as income tax expense in the Statement of Operations. During the period, the fund did not incur any interest or penalties.

Each of the tax years in the four-year period ended December 31, 2010 remains subject to examination by the Internal Revenue Service and state taxing authorities.

At December 31, 2010, the components of accumulated earnings on a tax basis were as follows: undistributed ordinary income $791,814, accumulated capital losses $58,430,851 and unrealized appreciation $24,956,945.

The accumulated capital loss carryover is available for federal income tax purposes to be applied against future net securities profits, if any, realized subsequent to December 31, 2010. If not applied, $12,514,855 of the carryover expires in fiscal 2016 and $45,915,996 expires in fiscal 2017.

The tax character of distributions paid to shareholders during the fiscal periods ended December 31, 2010 and December 31, 2009 were as follows: ordinary income $1,510,101 and $1,940,578, respectively.

### NOTE 2—Bank Lines of Credit:

The fund participates with other Dreyfus-managed funds in a $225 million unsecured credit facility led by Citibank, N.A. and a $300 million unsecured credit facility provided by The Bank of New York Mellon (each, a "Facility"), each to be utilized primarily for temporary or emergency purposes, including the financing of redemptions. In connection therewith, the fund has agreed to pay its pro rata portion of commitment fees for each Facility. Interest is charged to the fund based on rates determined pursuant to the terms of the respective Facility at the time of borrowing.

The average amount of borrowings outstanding under the Facilities during the period ended December 31, 2010 was approximately $15,900, with a related weighted average annualized interest rate of 1.52%.

### NOTE 3—Investment Advisory Fee and Other Transactions With Affiliates:

**(a)** Pursuant to an investment advisory agreement with the Manager, the investment advisory fee is computed at the annual rate of .75% of the value of the fund's average daily net assets and is payable monthly.

The Manager had agreed, from March 1, 2010 to August 31, 2010, to waive receipt of its fees and/or assume the expenses of the fund so that the expenses of neither class exclusive of taxes, brokerage fees, interest on borrowings, commitment fees and extraordinary expenses, do not exceed .90% of the value of the average daily net assets of such class. During the period ended December 31, 2010, the Manager waived $20,350 for Service shares, pursuant to the undertaking.

**(b)** Under the Distribution Plan (the "Plan") adopted pursuant to Rule 12b-1 under the Act, Service shares pay the Distributor for distributing their shares, for servicing and/or maintaining Service shares' shareholder accounts and for advertising and marketing for Service shares. The Plan provides for payments to be made at an annual rate of .25% of the value of the Service shares' average daily net assets. The Distributor may make payments to participating insurance companies and to brokers and dealers acting as principal underwriter for their variable insurance products. The fees payable under the Plan are payable without regard to actual expenses incurred. During the period ended December 31, 2010, Service shares were charged $43,370 pursuant to the Plan.

The fund compensates Dreyfus Transfer, Inc., a wholly-owned subsidiary of the Manager under a transfer agency agreement for providing personnel and facilities to perform transfer agency services for the fund. During the period ended December 31, 2010, the fund was charged $837 pursuant to the transfer agency agreement, which is included in Shareholder servicing costs in the Statement of Operations.

The fund has arrangements with the custodian and cash management bank whereby the fund may receive earnings credits when positive cash balances are maintained, which are used to offset custody and cash management fees. For financial reporting purposes, the fund includes net earnings credits as an expense offset in the Statement of Operations.

The fund compensates The Bank of New York Mellon under a cash management agreement for performing cash management services related to fund subscriptions and redemptions. During the period ended December 31, 2010, the fund was charged $118 pursuant to the cash management agreement, which is included in Shareholder servicing costs in the Statement of Operations. These fees were partially offset by earnings credits of $7.

The fund also compensates The Bank of New York Mellon under a custody agreement for providing custodial services for the fund. During the period ended December 31, 2010, the fund was charged $17,284 pursuant to the custody agreement.

During the period ended December 31, 2010, the fund was charged $6,243 for services performed by the Chief Compliance Officer.

The components of "Due to The Dreyfus Corporation and affiliates" in the Statement of Assets and Liabilities consist of: investment advisory fees $106,291, Rule 12b-1 distribution plan fees $4,139, custodian fees $3,840, chief compliance officer fees $1,728 and transfer agency per account fees $154.

(c) Each Board member also serves as a Board member of other funds within the Dreyfus complex. Annual retainer fees and attendance fees are allocated to each fund based on net assets.

## NOTE 4—Securities Transactions:

The aggregate amount of purchases and sales of investment securities, excluding short-term securities, during the period ended December 31, 2010, amounted to $119,009,605 and $135,460,861, respectively.

The provisions of ASC Topic 815 "Derivatives and Hedging" require qualitative disclosures about objectives and strategies for using derivatives, quantitative disclosures about fair value amounts of gains and losses on derivative instruments and disclosures about credit-risk related contingent features in derivative agreements. The fund held no derivatives during the period ended December 31, 2010.

At December 31, 2010, the cost of investments for federal income tax purposes was $144,028,079; accordingly, accumulated net unrealized appreciation on investments was $24,956,945, consisting of $29,606,178 gross unrealized appreciation and $4,649,233 gross unrealized depreciation.

# REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

**Shareholders and Board of Trustees**
**Dreyfus Investment Portfolios, MidCap Stock Portfolio**

We have audited the accompanying statement of assets and liabilities, including the statement of investments, of Dreyfus Investment Portfolios, MidCap Stock Portfolio (one of the series comprising Dreyfus Investment Portfolios) as of December 31, 2010, and the related statement of operations for the year then ended, the statement of changes in net assets for each of the two years in the period then ended, and financial highlights for each of the years indicated therein. These financial statements and financial highlights are the responsibility of the Fund's management. Our responsibility is to express an opinion on these financial statements and financial highlights based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements and financial highlights are free of material misstatement. We were not engaged to perform an audit of the Fund's internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Fund's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements and financial highlights, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our procedures included confirmation of securities owned as of December 31, 2010 by correspondence with the custodian and others. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements and financial highlights referred to above present fairly, in all material respects, the financial position of Dreyfus Investment Portfolios, MidCap Stock Portfolio at December 31, 2010, the results of its operations for the year then ended, the changes in its net assets for each of the two years in the period then ended, and the financial highlights for each of the indicated years, in conformity with U.S. generally accepted accounting principles.

Ernst & Young LLP

New York, New York
February 10, 2011

## IMPORTANT TAX INFORMATION (Unaudited)

For federal tax purposes, the fund hereby designates 100% of the ordinary dividends paid during the fiscal year ended December 31, 2010 as qualifying for the corporate dividends received deduction. Shareholders will receive notification in early 2011 of the percentage applicable to the preparation of their 2010 income tax returns.

# INFORMATION ABOUT THE REVIEW AND APPROVAL OF THE FUND'S INVESTMENT ADVISORY AGREEMENT (Unaudited)

At a meeting of the Board of Trustees of the Company held on July 14 and 15, 2010, the Board considered the re-approval for an annual period (through August 31, 2011) of the fund's Investment Advisory Agreement (the "Management Agreement") with the Manager, pursuant to which the Manager provides the fund with investment advisory and administrative services. The Board members, none of whom are "interested persons" (as defined in the Investment Company Act of 1940, as amended) of the Company, were assisted in their review by independent legal counsel and met with counsel in executive session separate from representatives of the Manager.

Analysis of Nature, Extent and Quality of Services Provided to the Fund. The Board members received a presentation from representatives of the Manager regarding services provided to the fund and other funds in the Dreyfus fund complex, and discussed the nature, extent and quality of the services provided to the fund pursuant to its Management Agreement. The Manager's representatives reviewed the fund's distribution of accounts and the relationships the Manager has with various intermediaries and the different needs of each. The Board noted that the fund's shares are offered only to separate accounts established by insurance companies to fund variable annuity contracts and variable life insurance policies. The Manager's representatives noted the diversity of distribution among the funds in the Dreyfus fund complex, and the Manager's corresponding need for broad, deep and diverse resources to be able to provide ongoing shareholder services to each distribution channel, including that of the fund. The Manager also provided the number of separate accounts investing in the fund, as well as the fund's asset size.

The Board members also considered the Manager's research and portfolio management capabilities and that the Manager also provides oversight of day-to-day fund operations, including fund accounting and administration and assistance in meeting legal and regulatory requirements. The Board members also considered the Manager's extensive administrative, accounting and compliance infrastructure. The Board also considered the Manager's brokerage policies and practices, the standards applied in seeking best execution and the Manager's policies and practices regarding soft dollars.

Comparative Analysis of the Fund's Performance and Investment Advisory Fee and Expense Ratio. The Board members reviewed the fund's performance and comparisons to a group of mid-cap core funds underlying variable insurance products (the "Performance Group") and to a larger universe of funds consisting of all mid-cap core funds underlying variable insurance products (the "Performance Universe"), selected and provided by Lipper, Inc., an independent provider of investment company data. The Board was provided with a description of the methodology Lipper used to select the Performance Group and Performance Universe, as well as the Expense Group and Expense Universe (discussed below). The Board members discussed the results of the comparisons for various periods ended May 31, 2010. The Board members noted that the fund's total return performance was below the Performance Group and Performance Universe medians for all periods, except for the 1-year period of the Performance Group where the fund's performance was at the median. Representatives of the Manager reminded the Board of the changes made to portfolio management's investment process for the fund and noted the fund's performance had improved more recently. The Manager also provided a comparison of the fund's calendar year total returns to the returns of the fund's benchmark index.

The Board members also discussed the fund's investment advisory fee and expense ratio and reviewed the range of investment advisory fees and expense ratios as compared to a comparable group of funds (the "Expense Group") and a broader group of funds (the "Expense Universe"), each selected and provided by Lipper. The Board members noted that the actual and contractual investment advisory fees and total expense ratio of the fund's Initial shares (which are not subject to a Rule 12b-1 plan) were lower than the Expense Group medians. They noted that the fund's actual investment advisory fee was higher than the Expense Universe median, but that the fund's total expense ratio was lower than the Expense Universe median. In addition, the Board noted that the total expense ratio of the fund's Service shares (which are subject to a Rule 12b-1 plan) was higher than the Expense Group median and lower than the Expense Universe median. The Board also considered the current fee waiver and expense reimbursement arrangement undertaken by the Manager.

Representatives of the Manager reviewed with the Board members the investment advisory fees paid by other accounts managed by the Manager or its affiliates with similar investment objectives, policies and strategies as the fund (the "Similar Accounts"). The Manager's representatives explained the nature of the Similar Accounts and the differences in providing services to such Similar Accounts as compared to managing and providing services to the fund. Representatives of the Manager noted that the Manager or its affiliates do not manage other mutual funds with similar investment objectives, policies and strategies as the fund underlying variable insurance products and included within the fund's Lipper category. The Board analyzed the differences in fees paid to the Manager and discussed the relationship of the fees paid in light of the services provided. The Board members considered the relevance of the fee information provided for the Similar Accounts to evaluate the appropriateness and reasonableness of the fund's investment advisory fee.

Analysis of Profitability and Economies of Scale. The Manager's representatives reviewed the dollar amount of expenses allocated and profit received by the Manager and the method used to determine such expenses and profit. The Board previously had been provided with information prepared by an independent consulting firm regarding the Manager's approach to allocating costs to, and determining the profitability of, individual funds and the entire Dreyfus mutual fund complex. The Board members also had been informed that the methodology had been reviewed by an independent registered public accounting firm which, like the consultant, found the methodology to be reasonable. The consulting firm also analyzed where any economies of scale might emerge in connection with the management of the fund. The Board members evaluated the profitability analysis in light of the relevant circumstances for the fund, and the extent to which economies of scale would be realized if the fund grows and whether fee levels reflect these economies of scale for the benefit of fund investors. The Board members also considered potential benefits to the Manager from acting as investment adviser to the fund, including any soft dollar arrangements with respect to trading the fund's investments.

It was noted that the Board members should consider the Manager's profitability with respect to the fund as part of their evaluation of whether the fee under the Management Agreement bears a reasonable relationship to the mix of services provided by the Manager, including the nature, extent and quality of such services and that a discussion of economies of scale is predicated on increasing assets and that, if a fund's assets had been decreasing, the possibility that the Manager may have realized any economies of scale would be less. It also was noted that the Manager did not realize a profit on the fund's operations.

At the conclusion of these discussions, the Board agreed that it had been furnished with sufficient information to make an informed business decision with respect to continuation of the Management Agreement. Based on the discussions and considerations as described above, the Board made the following conclusions and determinations.

- The Board concluded that the nature, extent and quality of the services provided by the Manager are adequate and appropriate.
- The Board was concerned with the fund's performance, but noted changes made to portfolio management's investment process for the fund and the fund's improved short-term performance.
- The Board concluded that the fee paid by the fund to the Manager was reasonable in light of the services provided, comparative performance, expense and investment advisory fee information (including the fee waiver and expense reimbursement arrangement), costs of the services provided and profits to be realized and benefits derived or to be derived by the Manager from its relationship with the fund.

- The Board determined that the economies of scale which may accrue to the Manager and its affiliates in connection with the management of the fund had been adequately considered by the Manager in connection with the investment advisory fee rate charged to the fund, and that, to the extent in the future it were determined that material economies of scale had not been shared with the fund, the Board would seek to have those economies of scale shared with the fund.

The Board members considered these conclusions and determinations, along with information received on a routine and regular basis throughout the year, and, without any one factor being dispositive, the Board determined that re-approval of the Management Agreement was in the best interests of the fund and its shareholders.

## BOARD MEMBERS INFORMATION (Unaudited)

**Joseph S. DiMartino (67)**
**Chairman of the Board (1998)**

*Principal Occupation During Past 5 Years:*
• Corporate Director and Trustee

*Other Public Company Board Memberships During Past 5 Years:*
• CBIZ (formerly, Century Business Services, Inc.), a provider of outsourcing functions for small and medium size companies, Director (1997-present)
• The Newark Group, a provider of a national market of paper recovery facilities, paperboard mills and paperboard converting plants, Director (2000-2010)
• Sunair Services Corporation, a provider of certain outdoor-related services to homes and businesses, Director (2005-2009)

*No. of Portfolios for which Board Member Serves:* 169

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**Clifford L. Alexander, Jr. (77)**
**Board Member (1998)**

*Principal Occupation During Past 5 Years:*
• President of Alexander & Associates, Inc., a management consulting firm (January 1981-present)

*No. of Portfolios for which Board Member Serves:* 46

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**David W. Burke (74)**
**Board Member (2003)**

*Principal Occupation During Past 5 Years:*
• Corporate Director and Trustee

*No. of Portfolios for which Board Member Serves:* 84

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**Whitney I. Gerard (76)**
**Board Member (2003)**

*Principal Occupation During Past 5 Years:*
• Partner of Chadbourne & Parke LLP

*No. of Portfolios for which Board Member Serves:* 26

**Nathan Leventhal (67)**
**Board Member (2009)**

*Principal Occupation During Past 5 Years:*
- Commissioner, NYC Planning Commission (March 2007-present)
- Chairman of the Avery-Fisher Artist Program (November 1997-present)

*Other Public Company Board Memberships During Past 5 Years:*
- Movado Group, Inc., Director

*No. of Portfolios for which Board Member Serves:* 44

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**George L. Perry (76)**
**Board Member (2003)**

*Principal Occupation During Past 5 Years:*
- Economist and Senior Fellow at Brookings Institution

*No. of Portfolios for which Board Member Serves:* 26

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**Benaree Pratt Wiley (64)**
**Board Member (2009)**

*Principal Occupation During Past 5 Years:*
- Principal, The Wiley Group, a firm specializing in strategy and business development (2005-present)
- President and CEO, The Partnership, an organization dedicated to increasing the representation of African Americans in positions of leadership, influence and decision-making in Boston, MA (1991-2005)

*Other Public Company Board Memberships During Past 5 Years:*
- CBIZ (formerly, Century Business Services, Inc.), a provider of outsourcing functions for small and medium size companies, Director (2008-present)

*No. of Portfolios for which Board Member Serves:* 72

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*Once elected all Board Members serve for an indefinite term, but achieve Emeritus status upon reaching age 80. The address of the Board Members and Officers is in c/o The Dreyfus Corporation, 200 Park Avenue, New York, New York 10166. Additional information about the Board Members is available in the fund's Statement of Additional Information which can be obtained from Dreyfus free of charge by calling this toll free number: 1-800-554-4611.*

*Lucy Wilson Benson, Emeritus Board Member*
*Arthur A. Hartman, Emeritus Board Member*

# OFFICERS OF THE FUND (Unaudited)

**BRADLEY J. SKAPYAK, President since January 2010.**

Chief Operating Officer and a director of the Manager since June 2009. From April 2003 to June 2009, Mr. Skapyak was the head of the Investment Accounting and Support Department of the Manager. He is an officer of 76 investment companies (comprised of 169 portfolios) managed by the Manager. He is 52 years old and has been an employee of the Manager since February 1988.

**PHILLIP N. MAISANO, Executive Vice President since July 2007.**

Chief Investment Officer, Vice Chair and a director of the Manager, and an officer of 76 investment companies (comprised of 169 portfolios) managed by the Manager. Mr. Maisano also is an officer and/or Board member of certain other investment management subsidiaries of The Bank of New York Mellon Corporation, each of which is an affiliate of the Manager. He is 63 years old and has been an employee of the Manager since November 2006. Prior to joining the Manager, Mr. Maisano served as Chairman and Chief Executive Officer of EACM Advisors, an affiliate of the Manager, since August 2004.

**MICHAEL A. ROSENBERG, Vice President and Secretary since August 2005.**

Assistant General Counsel of BNY Mellon, and an officer of 77 investment companies (comprised of 194 portfolios) managed by the Manager. He is 50 years old and has been an employee of the Manager since October 1991.

**KIESHA ASTWOOD, Vice President and Assistant Secretary since January 2010.**

Counsel of BNY Mellon, and an officer of 77 investment companies (comprised of 194 portfolios) managed by the Manager. She is 37 years old and has been an employee of the Manager since July 1995.

**JAMES BITETTO, Vice President and Assistant Secretary since August 2005.**

Senior Counsel of BNY Mellon and Secretary of the Manager, and an officer of 77 investment companies (comprised of 194 portfolios) managed by the Manager. He is 44 years old and has been an employee of the Manager since December 1996.

**JONI LACKS CHARATAN, Vice President and Assistant Secretary since August 2005.**

Senior Counsel of BNY Mellon, and an officer of 77 investment companies (comprised of 194 portfolios) managed by the Manager. She is 55 years old and has been an employee of the Manager since October 1988.

**JOSEPH M. CHIOFFI, Vice President and Assistant Secretary since August 2005.**

Senior Counsel of BNY Mellon, and an officer of 77 investment companies (comprised of 194 portfolios) managed by the Manager. He is 49 years old and has been an employee of the Manager since June 2000.

**KATHLEEN DENICHOLAS, Vice President and Assistant Secretary since January 2010.**

Senior Counsel of BNY Mellon, and an officer of 77 investment companies (comprised of 194 portfolios) managed by the Manager. She is 36 years old and has been an employee of the Manager since February 2001.

**JANETTE E. FARRAGHER, Vice President and Assistant Secretary since August 2005.**

Assistant General Counsel of BNY Mellon, and an officer of 77 investment companies (comprised of 194 portfolios) managed by the Manager. She is 48 years old and has been an employee of the Manager since February 1984.

**JOHN B. HAMMALIAN, Vice President and Assistant Secretary since August 2005.**

Managing Counsel of BNY Mellon, and an officer of 77 investment companies (comprised of 194 portfolios) managed by the Manager. He is 47 years old and has been an employee of the Manager since February 1991.

**M. CRISTINA MEISER, Vice President and Assistant Secretary since January 2010.**

Senior Counsel of BNY Mellon, and an officer of 77 investment companies (comprised of 194 portfolios) managed by the Manager. She is 40 years old and has been an employee of the Manager since August 2001.

**ROBERT R. MULLERY, Vice President and Assistant Secretary since August 2005.**

Managing Counsel of BNY Mellon, and an officer of 77 investment companies (comprised of 194 portfolios) managed by the Manager. He is 58 years old and has been an employee of the Manager since May 1986.

**JEFF PRUSNOFSKY, Vice President and Assistant Secretary since August 2005.**

Managing Counsel of BNY Mellon, and an officer of 77 investment companies (comprised of 194 portfolios) managed by the Manager. He is 45 years old and has been an employee of the Manager since October 1990.

**JAMES WINDELS, Treasurer since November 2001.**

Director – Mutual Fund Accounting of the Manager, and an officer of 77 investment companies (comprised of 194 portfolios) managed by the Manager. He is 52 years old and has been an employee of the Manager since April 1985.

**RICHARD CASSARO, Assistant Treasurer since January 2008.**

Senior Accounting Manager – Money Market and Municipal Bond Funds of the Manager, and an officer of 77 investment companies (comprised of 194 portfolios) managed by the Manager. He is 51 years old and has been an employee of the Manager since September 1982.

**GAVIN C. REILLY, Assistant Treasurer since December 2005.**

Tax Manager of the Investment Accounting and Support Department of the Manager, and an officer of 77 investment companies (comprised of 194 portfolios) managed by the Manager. He is 42 years old and has been an employee of the Manager since April 1991.

**ROBERT ROBOL, Assistant Treasurer since August 2005.**

Senior Accounting Manager – Fixed Income Funds of the Manager, and an officer of 77 investment companies (comprised of 194 portfolios) managed by the Manager. He is 46 years old and has been an employee of the Manager since October 1988.

**ROBERT SALVIOLO, Assistant Treasurer since July 2007.**

Senior Accounting Manager – Equity Funds of the Manager, and an officer of 77 investment companies (comprised of 194 portfolios) managed by the Manager. He is 43 years old and has been an employee of the Manager since June 1989.

**ROBERT SVAGNA, Assistant Treasurer since December 2002.**

Senior Accounting Manager – Equity Funds of the Manager, and an officer of 77 investment companies (comprised of 194 portfolios) managed by the Manager. He is 43 years old and has been an employee of the Manager since November 1990.

**JOSEPH W. CONNOLLY, Chief Compliance Officer since October 2004.**

Chief Compliance Officer of the Manager and The Dreyfus Family of Funds (77 investment companies, comprised of 194 portfolios). From November 2001 through March 2004, Mr. Connolly was first Vice-President, Mutual Fund Servicing for Mellon Global Securities Services. In that capacity, Mr. Connolly was responsible for managing Mellon's Custody, Fund Accounting and Fund Administration services to third-party mutual fund clients. He is 53 years old and has served in various capacities with the Manager since 1980, including manager of the firm's Fund Accounting Department from 1997 through October 2001.

**NATALIA GRIBAS, Anti-Money Laundering Compliance Officer since July 2010.**

Anti-Money Laundering Compliance Officer of the Distributor, and the Anti-Money Laundering Compliance Officer of 73 investment companies (comprised of 190 portfolios) managed by the Manager. She is 40 years old and has been an employee of the Distributor since September 2008.

# For More Information

**Dreyfus Investment Portfolios, MidCap Stock Portfolio**
200 Park Avenue
New York, NY 10166

**Investment Adviser**

The Dreyfus Corporation
200 Park Avenue
New York, NY 10166

**Custodian**

The Bank of New York Mellon
One Wall Street
New York, NY 10286

**Transfer Agent & Dividend Disbursing Agent**

Dreyfus Transfer, Inc.
200 Park Avenue
New York, NY 10166

**Distributor**

MBSC Securities Corporation
200 Park Avenue
New York, NY 10166

**Telephone** 1-800-554-4611 or 1-516-338-3300

**Mail** The Dreyfus Family of Funds, 144 Glenn Curtiss Boulevard, Uniondale, NY 11556-0144
Attn: Investments Division

The fund files its complete schedule of portfolio holdings with the Securities and Exchange Commission ("SEC") for the first and third quarters of each fiscal year on Form N-Q. The fund's Forms N-Q are available on the SEC's website at http://www.sec.gov and may be reviewed and copied at the SEC's Public Reference Room in Washington, DC. Information on the operation of the Public Reference Room may be obtained by calling 1-800-SEC-0330.

A description of the policies and procedures that the fund uses to determine how to vote proxies relating to portfolio securities, and information regarding how the fund voted these proxies for the most recent 12-month period ended June 30 is available at http://www.dreyfus.com and on the SEC's website at http://www.sec.gov. The description of the policies and procedures is also available without charge, upon request, by calling 1-800-645-6561.



0174AR1210

# The Dreyfus Socially Responsible Growth Fund, Inc.

**ANNUAL REPORT** December 31, 2010

BNY MELLON
ASSET MANAGEMENT

Dreyfus

# Contents

## THE FUND



## FOR MORE INFORMATION

## A LETTER FROM THE CHAIRMAN AND CEO

Dear Shareholder:

We are pleased to present this annual report for The Dreyfus Socially Responsible Growth Fund, Inc., covering the 12-month period from January 1, 2010, through December 31, 2010.

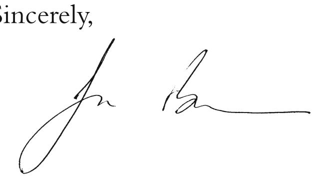
Although 2010 proved to be a volatile year for stocks, the reporting period ended with a sustained market rally that produced above-average returns across most market-cap segments for the calendar year. Investors' early concerns regarding sovereign debt issues in Europe and stubbornly high unemployment in the United States later gave way to optimism that massive economic stimulus programs, robust growth in the world's emerging markets, a strong holiday retail season and rising corporate earnings signaled better economic times ahead.

We are aware that stocks have recently reached higher valuations, and that any new economic setbacks could result in market volatility as investors adjust their expectations. Nonetheless, we see potential value in many segments of the equity market. For example, investors in volatile markets may turn to high-quality stocks of U.S. companies with track records of consistent growth in a variety of economic climates, and international equities could benefit from a declining U.S. dollar and potentially higher growth opportunities abroad. With 2011 now upon us, we suggest talking to your financial advisor, who can help you identify potential opportunities and suggest strategies suitable for your individual needs in today's market environment.

For information about how the fund performed during the reporting period, as well as general market perspectives, we provide a Discussion of Fund Performance on the pages that follow.

Thank you for your continued confidence and support.

Sincerely,



Jonathan R. Baum
Chairman and Chief Executive Officer
The Dreyfus Corporation
January 18, 2011

# DISCUSSION OF FUND PERFORMANCE

*For the period of January 1, 2010, through December 31, 2010, as provided by Jocelin Reed, Portfolio Manager*

## Fund and Market Performance Overview

For the 12-month period ended December 31, 2010, The Dreyfus Socially Responsible Growth Fund's Initial shares produced a total return of 14.82%, and the fund's Service shares returned 14.54%.[1] In comparison, the fund's benchmark, the Standard & Poor's 500 Composite Stock Price Index (the "S&P 500 Index"), produced a total return of 15.08% for the same period.[2]

After weathering a volatile market stemming from economic uncertainty over the first half of 2010, a rally later in the year more than offset earlier weakness. The fund produced returns that were only slightly below its benchmark, as strong results in the health care, consumer staples and information technology sectors were balanced by lagging returns among energy, industrial and financial stocks.

## The Fund's Investment Approach

The fund seeks capital growth, with current income as a secondary objective. To pursue these goals, the fund invests at least 80% of its assets in the common stocks of companies that, in our opinion, meet traditional investment standards while simultaneously conducting their businesses in a manner that contributes to the enhancement of the quality of life in America. In selecting stocks, we use quantitative research to identify and rank stocks within an industry or sector. Next, using fundamental analysis, we designate the most attractive of the higher ranked securities as potential purchase candidates. We then evaluate whether each company meets the fund's socially responsible investment criteria in order to determine whether the company is eligible for purchase or retention by the fund. With respect to those eligible securities, we then select investments that we consider to be the most attractive based on financial considerations.

The fund normally focuses on large-cap growth stocks; however, the fund also may invest in value-oriented stocks, midcap stocks and small-cap stocks.

## Waning Economic Concerns Fueled a Market Rally

Soon after the start of 2010, a number of new developments shook investors' confidence in ongoing global and domestic economic recoveries. Europe was roiled by a sovereign debt crisis that led to austerity measures throughout the region, and mixed housing and employment data in the United States weighed on already mild growth. As a result, U.S. stocks generally declined over the first half of the year.

However, investors' economic concerns at the time may have been overblown. Corporate earnings exceeded analysts' expectations during the second half of the year, commodity prices climbed amid robust demand from the world's emerging markets, and the U.S. and global economies remained on upward trajectories. The resolution of midterm elections and new stimulative programs by the Federal Reserve Board also boosted investor sentiment, helping the S&P 500 Index end the year with double-digit gains.

## Security Selections Successful in Most Sectors

The fund participated to a substantial degree in the stock market's gains in 2010. Our stock selection strategy proved particularly effective in the health care sector, where pharmaceutical developer *Millipore* was acquired by the German affiliate of Merck & Co. However, we maintained underweighted exposure to large pharmaceutical companies overall, and instead we favored biotechnology firms such as *Genzyme*, which rallied sharply amid takeover speculation. The fund also achieved strong relative performance in the consumer staples sector, where higher-end retailers, such as organic grocery chain Whole Foods Market, benefited from improved consumer sentiment. Mass merchandiser Costco Wholesale also encountered a more confident consumer and greater pricing power, and cosmetics seller Estee Lauder bolstered financial results through a successful expansion into fast-growing emerging markets. In the information technology sector, overweighted exposure to electronics innovator Apple and holding no position in personal computer maker Hewlett-Packard Co. also supported the fund's relative performance.

Positive contributions from these areas were offset by lagging results in the energy sector, where underweighted exposure and disappointing stock selections weighed on returns. Natural gas producers such as Nexen and EnCana struggled with low commodity prices, while better performing oil refiners and integrated energy companies did not meet the fund's socially responsible investment criteria. Deep water driller Noble declined due to intensifying regulatory scrutiny after the April 2010 oil spill in the Gulf of Mexico. In the industrials sector, the fund focused on traditionally defensive companies, such as 3M, which lagged market averages. An underweighted position in the financials sector also detracted from the fund's relative performance.

## Positioned for a More Selective Market Environment

Although headwinds remain, we expect the U.S. and global economic recoveries to persist in 2011. However, investors are likely to become more selective, favoring companies that can grow consistently in a slow economy. Therefore, we have reduced our emphasis on higher-quality information technology companies and other growth-oriented investments, allocating more assets to value-oriented stocks, including those in the financials sector and, to a lesser extent, the energy sector.

January 18, 2011

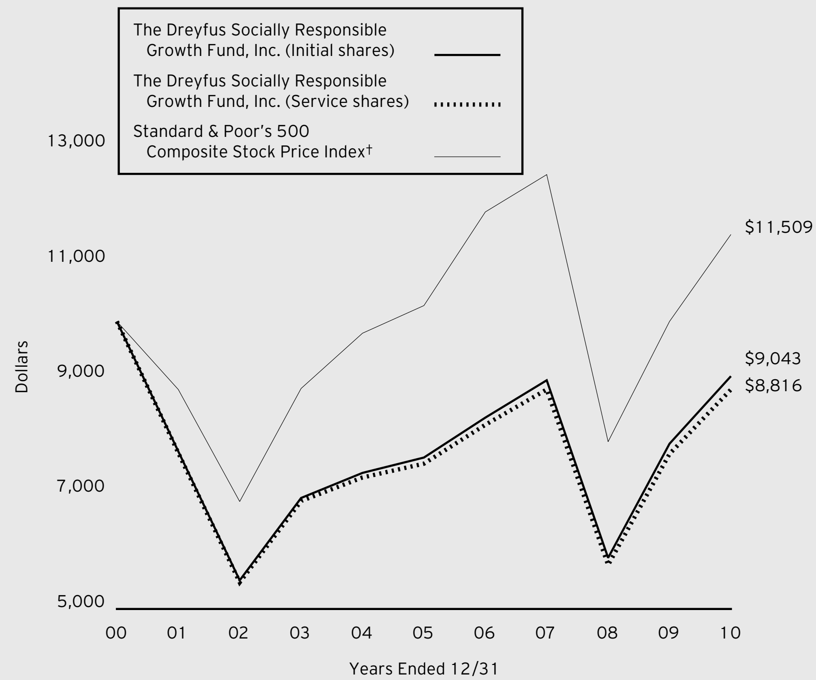
*Please note, the position in any secruity highlighted with italicized typeface was sold during the reporting period.*

*Equity funds are subject generally to market, market sector, market liquidity, issuer and investment style risks, among other factors, to varying degrees, all of which are more fully described in the fund's prospectus.*

*The fund is only available as a funding vehicle under variable life insurance policies or variable annuity contracts issued by insurance companies. Individuals may not purchase shares of the fund directly. A variable annuity is an insurance contract issued by an insurance company that enables investors to accumulate assets on a tax-deferred basis for retirement or other long-term goals.*

1 *Total return includes reinvestment of dividends and any capital gains paid. Past performance is no guarantee of future results. Share price and investment return fluctuate such that upon redemption, fund shares may be worth more or less than their original cost. The fund's performance does not reflect the deduction of additional charges and expenses imposed in connection with investing in variable insurance contracts, which will reduce returns.*

2 *SOURCE: LIPPER INC. — Reflects reinvestment of dividends and, where applicable, capital gain distributions. The Standard & Poor's 500 Composite Stock Price Index is a widely accepted, unmanaged index of U.S. stock market performance. Investors cannot invest directly in any index.*




Comparison of change in value of $10,000 investment in The Dreyfus Socially Responsible Growth Fund, Inc. Initial shares and Service shares and the Standard & Poor's 500 Composite Stock Price Index

## Average Annual Total Returns *as of 12/31/10*

| | 1 Year | 5 Years | 10 Years |
|---|---|---|---|
| **Initial shares** | **14.82%** | **3.46%** | **-1.00%** |
| **Service shares** | **14.54%** | **3.21%** | **-1.25%** |
| **Standard & Poor's 500 Composite Stock Price Index** | **15.08%** | **2.29%** | **1.42%** |

† *Source: Lipper Inc.*

*Past performance is not predictive of future performance. The fund's performance shown in the graph and table does not reflect the deduction of taxes that a shareholder would pay on fund distributions or the redemption of fund shares.*

***The fund's performance does not reflect the deduction of additional charges and expenses imposed in connection with investing in variable insurance contracts which will reduce returns.***

*The above graph compares a $10,000 investment made in Initial and Service shares of The Dreyfus Socially Responsible Growth Fund, Inc. on 12/31/00 to a $10,000 investment made in the Standard & Poor's 500 Composite Stock Price Index (the "Index") on that date.*

*The fund's Initial shares are not subject to a Rule 12b-1 fee. The fund's Service shares are subject to a 0.25% annual Rule 12b-1 fee. All dividends and capital gain distributions are reinvested.*
*The fund's performance shown in the line graph takes into account all applicable fund fees and expenses. The Index is a widely accepted, unmanaged index of U.S. stock market performance. Unlike a mutual fund, the Index is not subject to charges, fees and other expenses. Investors cannot invest directly in any index. Further information relating to fund performance, including expense reimbursements, if applicable, is contained in the Financial Highlights section of the prospectus and elsewhere in this report.*

# UNDERSTANDING YOUR FUND'S EXPENSES (Unaudited)

*As a mutual fund investor, you pay ongoing expenses, such as management fees and other expenses. Using the information below, you can estimate how these expenses affect your investment and compare them with the expenses of other funds. You also may pay one-time transaction expenses, including sales charges (loads), redemption fees and expenses associated with variable annuity or insurance contracts, which are not shown in this section and would have resulted in higher total expenses. For more information, see your fund's prospectus or talk to your financial adviser.*

## Review your fund's expenses

The table below shows the expenses you would have paid on a $1,000 investment in The Dreyfus Socially Responsible Growth Fund, Inc. from July 1, 2010 to December 31, 2010. It also shows how much a $1,000 investment would be worth at the close of the period, assuming actual returns and expenses.

**Expenses and Value of a $1,000 Investment**
assuming actual returns for the six months ended December 31, 2010

| | Initial Shares | Service Shares |
|---|---|---|
| Expenses paid per $1,000† | $ 4.73 | $ 6.14 |
| Ending value (after expenses) | $1,235.00 | $1,233.80 |

# COMPARING YOUR FUND'S EXPENSES WITH THOSE OF OTHER FUNDS (Unaudited)

## Using the SEC's method to compare expenses

The Securities and Exchange Commission (SEC) has established guidelines to help investors assess fund expenses. Per these guidelines, the table below shows your fund's expenses based on a $1,000 investment, assuming a hypothetical 5% annualized return. You can use this information to compare the ongoing expenses (but not transaction expenses or total cost) of investing in the fund with those of other funds. All mutual fund shareholder reports will provide this information to help you make this comparison. Please note that you cannot use this information to estimate your actual ending account balance and expenses paid during the period.

**Expenses and Value of a $1,000 Investment**
assuming a hypothetical 5% annualized return for the six months ended December 31, 2010

| | Initial Shares | Service Shares |
|---|---|---|
| Expenses paid per $1,000† | $ 4.28 | $ 5.55 |
| Ending value (after expenses) | $1,020.97 | $1,019.71 |

† *Expenses are equal to the fund's annualized expense ratio of .84% for Initial Shares and 1.09% for Service Shares, multiplied by the average account value over the period, multiplied by 184/365 (to reflect the one-half year period).*

# STATEMENT OF INVESTMENTS

December 31, 2010

| Common Stocks—99.7% | Shares | | Value ($) |
|---|---|---|---|
| **Consumer Discretionary—12.6%** | | | |
| Discovery Communications, Cl. C | 40,250 | a | 1,476,773 |
| Gap | 164,375 | | 3,639,263 |
| Garmin | 59,750 | b | 1,851,653 |
| Limited Brands | 108,850 | | 3,344,960 |
| McDonald's | 26,775 | | 2,055,249 |
| McGraw-Hill | 69,850 | | 2,543,238 |
| New York Times, Cl. A | 269,450 | a,b | 2,640,610 |
| Staples | 69,450 | | 1,581,377 |
| Starbucks | 114,600 | | 3,682,098 |
| Target | 40,300 | | 2,423,239 |
| TJX | 74,625 | | 3,312,604 |
| Weight Watchers International | 27,875 | | 1,045,034 |
| | | | **29,596,098** |
| **Consumer Staples—12.2%** | | | |
| Church & Dwight | 41,400 | | 2,857,428 |
| Costco Wholesale | 69,800 | | 5,040,258 |
| Estee Lauder, Cl. A | 52,900 | | 4,269,030 |
| General Mills | 30,300 | | 1,078,377 |
| Kimberly-Clark | 20,475 | | 1,290,744 |
| PepsiCo | 46,600 | | 3,044,378 |
| Procter & Gamble | 97,925 | | 6,299,515 |
| Unilever (NY Shares) | 59,175 | | 1,858,095 |
| Whole Foods Market | 56,550 | | 2,860,864 |
| | | | **28,598,689** |
| **Energy—7.3%** | | | |
| Cenovus Energy | 74,525 | b | 2,477,211 |
| Devon Energy | 48,850 | | 3,835,214 |
| EnCana | 53,325 | | 1,552,824 |
| Forest Oil | 86,300 | a | 3,276,811 |
| Nexen | 91,625 | | 2,098,212 |
| Noble | 108,125 | | 3,867,631 |
| | | | **17,107,903** |
| **Financial—13.5%** | | | |
| Berkshire Hathaway, Cl. B | 34,300 | a | 2,747,773 |
| Comerica | 72,300 | | 3,053,952 |

| Common Stocks (continued) | Shares | | Value ($) |
|---|---|---|---|
| **Financial (continued)** | | | |
| Discover Financial Services | 205,300 | | 3,804,209 |
| First Horizon National | 175,821 | a | 2,071,166 |
| International Bancshares | 120,450 | | 2,412,613 |
| Investment Technology Group | 79,750 | a | 1,305,507 |
| Marshall & Ilsley | 283,200 | | 1,959,744 |
| PNC Financial Services Group | 67,150 | | 4,077,348 |
| State Street | 39,300 | | 1,821,162 |
| T. Rowe Price Group | 44,700 | | 2,884,938 |
| Travelers | 42,350 | | 2,359,318 |
| Waddell & Reed Financial, Cl. A | 87,350 | | 3,082,581 |
| | | | **31,580,311** |
| **Health Care—12.9%** | | | |
| Aetna | 87,950 | | 2,683,355 |
| Allergan | 36,650 | | 2,516,756 |
| Amgen | 56,975 | a | 3,127,928 |
| AstraZeneca, ADR | 41,950 | b | 1,937,671 |
| Becton Dickinson & Co. | 30,875 | | 2,609,555 |
| Biogen Idec | 37,500 | a | 2,514,375 |
| Gilead Sciences | 59,850 | a | 2,168,964 |
| Humana | 41,800 | a | 2,288,132 |
| Johnson & Johnson | 69,600 | | 4,304,760 |
| Kinetic Concepts | 44,700 | a | 1,872,036 |
| Life Technologies | 53,100 | a | 2,947,050 |
| Novartis, ADR | 22,600 | b | 1,332,270 |
| | | | **30,302,852** |
| **Industrial—9.5%** | | | |
| 3M | 46,250 | | 3,991,375 |
| Brink's | 40,650 | | 1,092,672 |
| Donaldson | 22,525 | | 1,312,757 |
| Dun & Bradstreet | 18,275 | | 1,500,195 |
| Emerson Electric | 83,725 | | 4,786,558 |
| Equifax | 38,050 | | 1,354,580 |
| Ryder System | 37,825 | | 1,991,108 |
| United Technologies | 79,075 | | 6,224,784 |
| | | | **22,254,029** |

| Common Stocks (continued) | Shares | | Value ($) |
|---|---|---|---|
| **Materials—3.3%** | | | |
| Alcoa | 289,100 | | 4,449,249 |
| Schnitzer Steel Industries, Cl. A | 30,050 | | 1,995,020 |
| Worthington Industries | 69,950 | b | 1,287,080 |
| | | | **7,731,349** |
| **Technology—25.7%** | | | |
| Accenture, Cl. A | 84,100 | | 4,078,009 |
| Apple | 20,350 | a | 6,564,096 |
| Avnet | 44,375 | a | 1,465,706 |
| CA | 74,750 | | 1,826,890 |
| Cisco Systems | 93,675 | a | 1,895,045 |
| EMC | 168,225 | a | 3,852,353 |
| Google, Cl. A | 8,950 | a | 5,316,032 |
| Intel | 169,550 | | 3,565,636 |
| International Business Machines | 62,275 | | 9,139,479 |
| Microsoft | 318,600 | | 8,895,312 |
| National Semiconductor | 104,525 | | 1,438,264 |
| Oracle | 183,375 | | 5,739,637 |
| QUALCOMM | 70,425 | | 3,485,333 |
| Symantec | 76,950 | a | 1,288,143 |
| Western Union | 90,325 | | 1,677,335 |
| | | | **60,227,270** |
| **Utilities—2.7%** | | | |
| NextEra Energy | 48,700 | | 2,531,913 |
| Sempra Energy | 55,650 | | 2,920,511 |
| WGL Holdings | 26,575 | | 950,588 |
| | | | **6,403,012** |
| **Total Common Stocks** (cost $196,640,163) | | | **233,801,513** |

| Other Investment—.3% | | | |
|---|---|---|---|
| **Registered Investment Company;** | | | |
| Dreyfus Institutional Preferred Plus Money Market Fund (cost $772,000) | 772,000 | c | **772,000** |

| **Investment of Cash Collateral for Securities Loaned–3.2%** | Shares | Value ($) |
|---|---|---|
| **Registered Investment Company;** | | |
| Dreyfus Institutional Cash Advantage Plus Fund (cost $7,366,570) | 7,366,570 [c] | **7,366,570** |
| **Total Investments** (cost $204,778,733) | **103.2%** | **241,940,083** |
| **Liabilities, Less Cash and Receivables** | **(3.2%)** | **(7,552,720)** |
| **Net Assets** | **100.0%** | **234,387,363** |

*ADR—American Depository Receipts*

[a] *Non-income producing security.*

[b] *Security, or portion thereof, on loan. At December 31, 2010, the market value of the fund's securities on loan was $7,212,436 and the market value of the collateral held by the fund was $7,366,570.*

[c] *Investment in affiliated money market mutual fund.*

## Portfolio Summary (Unaudited)†

| | Value (%) | | Value (%) |
|---|---|---|---|
| Technology | 25.7 | Energy | 7.3 |
| Financial | 13.5 | Money Market Investments | 3.5 |
| Health Care | 12.9 | Materials | 3.3 |
| Consumer Discretionary | 12.6 | Utilities | 2.7 |
| Consumer Staples | 12.2 | | |
| Industrial | 9.5 | | **103.2** |

† *Based on net assets.*

*See notes to financial statements.*

# STATEMENT OF ASSETS AND LIABILITIES

December 31, 2010

| | Cost | Value |
|---|---|---|
| **Assets ($):** | | |
| Investments in securities—See Statement of Investments (including securities on loan, valued at $7,212,436)—Note 1(b): | | |
| Unaffiliated issuers | 196,640,163 | 233,801,513 |
| Affiliated issuers | 8,138,570 | 8,138,570 |
| Cash | | 61,110 |
| Dividends receivable | | 117,563 |
| Receivable for shares of Common Stock subscribed | | 7,652 |
| Prepaid expenses | | 21,128 |
| | | **242,147,536** |
| **Liabilities ($):** | | |
| Due to The Dreyfus Corporation and affiliates—Note 3(c) | | 159,213 |
| Liability for securities on loan—Note 1(b) | | 7,366,570 |
| Payable for shares of Common Stock redeemed | | 148,586 |
| Accrued expenses | | 85,804 |
| | | **7,760,173** |
| **Net Assets ($)** | | **234,387,363** |
| **Composition of Net Assets ($):** | | |
| Paid-in capital | | 232,067,627 |
| Accumulated undistributed investment income—net | | 2,034,574 |
| Accumulated net realized gain (loss) on investments | | (36,876,188) |
| Accumulated net unrealized appreciation (depreciation) on investments | | 37,161,350 |
| **Net Assets ($)** | | **234,387,363** |

| **Net Asset Value Per Share** | Initial Shares | Service Shares |
|---|---|---|
| Net Assets ($) | 227,893,311 | 6,494,052 |
| Shares Outstanding | 7,620,761 | 218,599 |
| **Net Asset Value Per Share ($)** | **29.90** | **29.71** |

*See notes to financial statements.*

## STATEMENT OF OPERATIONS

Year Ended December 31, 2010

| | |
|---|---|
| **Investment Income ($):** | |
| **Income:** | |
| Cash dividends (net of $33,995 foreign taxes withheld at source): | |
| Unaffiliated issuers | 3,959,060 |
| Affiliated issuers | 1,679 |
| Income from securities lending—Note 1(b) | 54,548 |
| **Total Income** | **4,015,287** |
| **Expenses:** | |
| Management fee—Note 3(a) | 1,659,333 |
| Prospectus and shareholders' reports | 150,254 |
| Professional fees | 81,411 |
| Shareholder servicing costs—Note 3(c) | 28,627 |
| Custodian fees—Note 3(c) | 20,907 |
| Distribution fees—Note 3(b) | 14,937 |
| Loan commitment fees—Note 2 | 5,022 |
| Directors' fees and expenses—Note 3(d) | 4,508 |
| Miscellaneous | 15,025 |
| **Total Expenses** | **1,980,024** |
| Less—reduction in fees due to earnings credits—Note 3(c) | (12) |
| **Net Expenses** | **1,980,012** |
| **Investment Income—Net** | **2,035,275** |
| **Realized and Unrealized Gain (Loss) on Investments—Note 4 ($):** | |
| Net realized gain (loss) on investments | 9,806,504 |
| Net unrealized appreciation (depreciation) on investments | 18,869,439 |
| **Net Realized and Unrealized Gain (Loss) on Investments** | **28,675,943** |
| **Net Increase in Net Assets Resulting from Operations** | **30,711,218** |

*See notes to financial statements.*

## STATEMENT OF CHANGES IN NET ASSETS

| | Year Ended December 31, | |
|---|---|---|
| | 2010 | 2009 |
| **Operations ($):** | | |
| Investment income—net | 2,035,275 | 1,923,908 |
| Net realized gain (loss) on investments | 9,806,504 | (6,385,410) |
| Net unrealized appreciation (depreciation) on investments | 18,869,439 | 63,945,275 |
| **Net Increase (Decrease) in Net Assets Resulting from Operations** | **30,711,218** | **59,483,773** |
| **Dividends to Shareholders from ($):** | | |
| Investment income—net: | | |
| Initial Shares | (1,883,935) | (1,888,082) |
| Service Shares | (39,024) | (34,740) |
| **Total Dividends** | **(1,922,959)** | **(1,922,822)** |
| **Capital Stock Transactions ($):** | | |
| Net proceeds from shares sold: | | |
| Initial Shares | 7,813,132 | 8,146,232 |
| Service Shares | 926,055 | 545,430 |
| Dividends reinvested: | | |
| Initial Shares | 1,883,935 | 1,888,082 |
| Service Shares | 39,024 | 34,740 |
| Cost of shares redeemed: | | |
| Initial Shares | (32,411,083) | (28,291,376) |
| Service Shares | (1,322,352) | (1,034,582) |
| **Increase (Decrease) in Net Assets from Capital Stock Transactions** | **(23,071,289)** | **(18,711,474)** |
| **Total Increase (Decrease) in Net Assets** | **5,716,970** | **38,849,477** |
| **Net Assets ($):** | | |
| Beginning of Period | 228,670,393 | 189,820,916 |
| **End of Period** | **234,387,363** | **228,670,393** |
| Undistributed investment income—net | 2,034,574 | 1,922,258 |

| | Year Ended December 31, | |
|---|---|---|
| | 2010 | 2009 |
| **Capital Share Transactions:** | | |
| **Initial Shares** | | |
| Shares sold | 291,119 | 375,522 |
| Shares issued for dividends reinvested | 69,518 | 103,912 |
| Shares redeemed | (1,215,789) | (1,309,522) |
| **Net Increase (Decrease) in Shares Outstanding** | **(855,152)** | **(830,088)** |
| **Service Shares** | | |
| Shares sold | 35,315 | 25,829 |
| Shares issued for dividends reinvested | 1,447 | 1,920 |
| Shares redeemed | (50,731) | (49,261) |
| **Net Increase (Decrease) in Shares Outstanding** | **(13,969)** | **(21,512)** |

*See notes to financial statements.*

# FINANCIAL HIGHLIGHTS

The following tables describe the performance for each share class for the fiscal periods indicated. All information (except portfolio turnover rate) reflects financial results for a single fund share. Total return shows how much your investment in the fund would have increased (or decreased) during each period, assuming you had reinvested all dividends and distributions. The fund's total returns do not reflect expenses associated with variable annuity or insurance contracts. These figures have been derived from the fund's financial statements.

| | Year Ended December 31, | | | | |
|---|---|---|---|---|---|
| **Initial Shares** | 2010 | 2009 | 2008 | 2007 | 2006 |
| **Per Share Data ($):** | | | | | |
| Net asset value, beginning of period | 26.26 | 19.86 | 30.50 | 28.45 | 26.08 |
| Investment Operations: | | | | | |
| Investment income—net [a] | .25 | .21 | .19 | .17 | .13 |
| Net realized and unrealized gain (loss) on investments | 3.62 | 6.40 | (10.64) | 2.04 | 2.27 |
| Total from Investment Operations | 3.87 | 6.61 | (10.45) | 2.21 | 2.40 |
| Distributions: | | | | | |
| Dividends from investment income—net | (.23) | (.21) | (.19) | (.16) | (.03) |
| Net asset value, end of period | 29.90 | 26.26 | 19.86 | 30.50 | 28.45 |
| **Total Return (%)** | 14.82 | 33.75 | (34.42) | 7.78 | 9.20 |
| **Ratios/Supplemental Data (%):** | | | | | |
| Ratio of total expenses to average net assets | .89 | .89 | .85 | .82 | .83 |
| Ratio of net expenses to average net assets | .89 | .89 | .85 | .82 | .83 |
| Ratio of net investment income to average net assets | .93 | .97 | .72 | .58 | .50 |
| Portfolio Turnover Rate | 32.75 | 34.00 | 31.74 | 22.71 | 32.19 |
| Net Assets, end of period ($ x 1,000) | 227,893 | 222,600 | 184,813 | 331,313 | 374,537 |

[a] *Based on average shares outstanding at each month end.*
*See notes to financial statements.*

| Service Shares | 2010 | 2009 | 2008 | 2007 | 2006 |
|---|---|---|---|---|---|
| | Year Ended December 31, | | | | |
| **Per Share Data ($):** | | | | | |
| Net asset value, beginning of period | 26.10 | 19.71 | 30.25 | 28.21 | 25.90 |
| Investment Operations: | | | | | |
| Investment income—net[a] | .18 | .16 | .12 | .10 | .07 |
| Net realized and unrealized gain (loss) on investments | 3.60 | 6.37 | (10.55) | 2.02 | 2.24 |
| Total from Investment Operations | 3.78 | 6.53 | (10.43) | 2.12 | 2.31 |
| Distributions: | | | | | |
| Dividends from investment income—net | (.17) | (.14) | (.11) | (.08) | – |
| Net asset value, end of period | 29.71 | 26.10 | 19.71 | 30.25 | 28.21 |
| **Total Return (%)** | 14.54 | 33.44 | (34.58) | 7.49 | 8.96 |
| **Ratios/Supplemental Data (%):** | | | | | |
| Ratio of total expenses to average net assets | 1.14 | 1.14 | 1.10 | 1.07 | 1.08 |
| Ratio of net expenses to average net assets | 1.14 | 1.14 | 1.10 | 1.07 | 1.08 |
| Ratio of net investment income to average net assets | .68 | .72 | .47 | .33 | .25 |
| Portfolio Turnover Rate | 32.75 | 34.00 | 31.74 | 22.71 | 32.19 |
| Net Assets, end of period ($ x 1,000) | 6,494 | 6,070 | 5,008 | 8,924 | 11,372 |

[a] *Based on average shares outstanding at each month end.*
*See notes to financial statements.*

## NOTE 1—Significant Accounting Policies:

The Dreyfus Socially Responsible Growth Fund, Inc. (the "fund") is registered under the Investment Company Act of 1940, as amended (the "Act"), as a diversified open-end management investment company. The fund's investment objective is to provide capital growth, with current income as a secondary goal. The fund is only offered to separate accounts established by insurance companies to fund variable annuity contracts and variable life insurance policies. The Dreyfus Corporation (the "Manager" or "Dreyfus"), a wholly-owned subsidiary of The Bank of New York Mellon Corporation ("BNY Mellon"), serves as the fund's investment adviser.

MBSC Securities Corporation (the "Distributor"), a wholly-owned subsidiary of the Manager, is the distributor of the fund's shares, which are sold without a sales charge. The fund is authorized to issue 300 million shares of $.001 par value Common Stock. The fund currently offers two classes of shares: Initial shares (150 million shares authorized) and Service shares (150 million shares authorized). Initial shares are subject to a shareholder services fee and Service shares are subject to a distribution fee. Each class of shares has identical rights and privileges, except with respect to the distribution plan, shareholder services plan and the expenses borne by each class, the allocation of certain transfer agency costs and certain voting rights. Income, expenses (other than expenses attributable to a specific class), and realized and unrealized gains or losses on investments are allocated to each class of shares based on its relative net assets.

The Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") is the exclusive reference of authoritative U.S. generally accepted accounting principles ("GAAP") recognized by the FASB to be applied by nongovernmental entities. Rules and interpretive releases of the Securities and Exchange Commission ("SEC") under authority of federal laws are also sources of authoritative GAAP for SEC registrants. The fund's financial statements are prepared in accordance with GAAP, which may require the use of management estimates and assumptions. Actual results could differ from those estimates.

The fund enters into contracts that contain a variety of indemnifications. The fund's maximum exposure under these arrangements is unknown. The fund does not anticipate recognizing any loss related to these arrangements.

**(a) Portfolio valuation:** Investments in securities are valued at the last sales price on the securities exchange or national securities market on which such securities are primarily traded. Securities listed on the National Market System for which market quotations are available, are valued at the official closing price or, if there is no official closing price that day, at the last sales price. Securities not listed on an exchange or the national securities market, or securities for which there were no transactions, are valued at the average of the most recent bid and asked prices, except for open short positions, where the asked price is used for valuation purposes. Bid price is used when no asked price is available. Registered investment companies that are not traded on an exchange are valued at their net asset value. When market quotations or official closing prices are not readily available, or are determined not to reflect accurately fair value, such as when the value of a security has been significantly affected by events after the close of the exchange or market on which the security is principally traded (for example, a foreign exchange or market), but before the fund calculates its net asset value, the fund may value these investments at fair value as determined in accordance with the procedures approved by the Board of Directors. Fair valuing of securities may be determined with the assistance of a pricing service using calculations based on indices of domestic securities and other appropriate indicators, such as prices of relevant ADRs and futures contracts. For other securities that are fair valued by the Board of Directors, certain factors may be considered such as: fundamental analytical data, the nature and duration of restrictions on disposition, an evaluation of the forces that influence the market in which the securities are purchased and sold, and public trading in similar securities of the issuer or comparable issuers.

The fair value of a financial instrument is the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (i.e. the exit price). GAAP establishes a fair value hierarchy that prioritizes the inputs of valuation techniques used to measure fair value. This hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements).

Additionally, GAAP provides guidance on determining whether the volume and activity in a market has decreased significantly and whether such a decrease in activity results in transactions that are not orderly. GAAP requires enhanced disclosures around valuation inputs and techniques used during annual and interim periods.

Various inputs are used in determining the value of the fund's investments relating to fair value measurements. These inputs are summarized in the three broad levels listed below:

**Level 1**—unadjusted quoted prices in active markets for identical investments.

**Level 2**—other significant observable inputs (including quoted prices for similar investments, interest rates, prepayment speeds, credit risk, etc.).

**Level 3**—significant unobservable inputs (including the fund's own assumptions in determining the fair value of investments).

The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities.

The following is a summary of the inputs used as of December 31, 2010 in valuing the fund's investments:

| | Level 1– Unadjusted Quoted Prices | Level 2–Other Significant Observable Inputs | Level 3– Significant Unobservable Inputs | Total |
|---|---|---|---|---|
| **Assets ($)** | | | | |
| Investments in Securities: | | | | |
| Equity Securities– Domestic† | 224,403,325 | – | – | **224,403,325** |
| Equity Securities– Foreign† | 9,398,188 | – | – | **9,398,188** |
| Mutual Funds | 8,138,570 | – | – | **8,138,570** |

† *See Statement of Investments for additional detailed categorizations.*

In January 2010, FASB issued Accounting Standards Update ("ASU") No. 2010-06 "Improving Disclosures about Fair Value Measurements". The portions of ASU No. 2010-06 which require reporting entities to prepare new disclosures surrounding amounts and reasons for significant transfers in and out of Level 1 and Level 2 fair value measurements as well as inputs and valuation techniques used to measure fair value for both recurring and nonrecurring fair value measurements that fall in either Level 2 or Level 3 have been adopted by the fund. No significant transfers between Level 1 or Level 2 fair value measurements occurred at December 31, 2010. The remaining portion of ASU No. 2010-06 requires reporting entities to make new disclosures about information on purchases, sales, issuances and settlements on a gross basis in the reconciliation of activity in Level 3 fair value measurements. These new and revised disclosures are required to be implemented for fiscal years beginning after December 15, 2010. Management is currently evaluating the impact that the adoption of this remaining portion of ASU No. 2010-06 may have on the fund's financial statement disclosures.

**(b) Securities transactions and investment income:** Securities transactions are recorded on a trade date basis. Realized gains and losses from securities transactions are recorded on the identified cost basis. Dividend income is recognized on the ex-dividend date and interest income, including, where applicable, accretion of discount and amortization of premium on investments, is recognized on the accrual basis.

Pursuant to a securities lending agreement with The Bank of New York Mellon, a subsidiary of BNY Mellon and an affiliate of Dreyfus, the fund may lend securities to qualified institutions. It is the fund's policy that, at origination, all loans are secured by collateral of at least 102% of the value of U.S. securities loaned and 105% of the value of foreign securities loaned. Collateral equivalent to at least 100% of the market value of securities on loan is maintained at all times. Collateral is either in the form of cash, which can be invested in certain money market mutual funds managed by the Manager, U.S. Government and Agency securities or letters of credit. The fund is entitled to receive all income on securities loaned, in addition to income earned as a result of the lending transaction. Although each security loaned is fully collateralized, the fund bears the risk of delay in recovery of, or loss of rights in, the securities loaned should a borrower fail to return the securities in a timely manner. During the period ended December 31, 2010, The Bank of New York Mellon earned $23,378 from lending portfolio securities, pursuant to the securities lending agreement.

**(c) Affiliated issuers:** Investments in other investment companies advised by Dreyfus are defined as "affiliated" in the Act.

The fund may invest in shares of certain affiliated investment companies also advised or managed by Dreyfus. Investments in affiliated investment companies for the period ended December 31, 2010 were as follows:

| Affiliated Investment Company | Value 12/31/2009 ($) | Purchases ($) | Sales ($) | Value 12/31/2010 ($) | Net Assets (%) |
|---|---|---|---|---|---|
| Dreyfus Institutional Preferred Plus Money Market Fund | 2,919,000 | 21,742,000 | 23,889,000 | 772,000 | .3 |
| Dreyfus Institutional Cash Advantage Plus Fund | 5,552,208 | 64,395,699 | 62,581,337 | 7,366,570 | 3.2 |
| **Total** | **8,471,208** | **86,137,699** | **86,470,337** | **8,138,570** | **3.5** |

**(d) Dividends to shareholders:** Dividends are recorded on the ex-dividend date. Dividends from investment income-net and dividends from net realized capital gains, if any, are normally declared and paid annually, but the fund may make distributions on a more frequent basis to comply with the distribution requirements of the Internal Revenue Code of 1986, as amended (the "Code"). To the extent that net realized capital gains can be offset by capital loss carryovers, it is the policy of the fund not to distribute such gains. Income and capital gain distributions are determined in accordance with income tax regulations, which may differ from GAAP.

**(e) Federal income taxes:** It is the policy of the fund to continue to qualify as a regulated investment company, if such qualification is in the best interests of its shareholders, by complying with the applicable provisions of the Code, and to make distributions of taxable income sufficient to relieve it from substantially all federal income and excise taxes.

As of and during the period ended December 31, 2010, the fund did not have any liabilities for any uncertain tax positions. The fund recognizes interest and penalties, if any, related to uncertain tax positions as income tax expense in the Statement of Operations. During the period, the fund did not incur any interest or penalties.

Each of the tax years in the four-year period ended December 31, 2010 remains subject to examination by the Internal Revenue Service and state taxing authorities.

At December 31, 2010, the components of accumulated earnings on a tax basis were as follows: undistributed ordinary income $2,034,574, accumulated capital losses $36,867,794 and unrealized appreciation $37,152,956.

The accumulated capital loss carryover is available for federal income tax purposes to be applied against future net securities profits, if any, realized subsequent to December 31, 2010. If not applied, $19,771,483 of the carryover expires in fiscal 2011 and $17,096,311 expires in fiscal 2017.

The tax character of distributions paid to shareholders during the fiscal periods ended December 31, 2010 and December 31, 2009 were as follows: ordinary income $1,922,959 and $1,922,822, respectively.

During the period ended December 31, 2010, as a result of permanent book to tax differences, primarily due to the tax treatment for capital loss carryover expiration, the fund increased accumulated net realized gain (loss) on investments by $94,035,280 and decreased paid-in-capital by the same amount. Net assets and net asset value per share were not affected by this reclassification.

## NOTE 2—Bank Lines of Credit:

The fund participates with other Dreyfus-managed funds in a $225 million unsecured credit facility led by Citibank, N.A. and a $300 million unsecured credit facility provided by The Bank of New York Mellon, (each, a "Facility"), each to be utilized primarily for temporary or emergency purposes, including the financing of redemptions. In connection therewith, the fund has agreed to pay its pro rata portion of commitment fees for each Facility. Interest is charged to the fund based on rates determined pursuant to the terms of the respective Facility at the time of borrowing. During the period ended December 31, 2010, the fund did not borrow under the Facilities.

## NOTE 3—Management Fee and Other Transactions With Affiliates:

(a) Pursuant to a management agreement with the Manager, the management fee is computed at the annual rate of .75% of the value of the fund's average daily net assets and is payable monthly.

(b) Under the Distribution Plan (the "Plan") adopted pursuant to Rule 12b-1 under the Act, Service shares pay the Distributor for distributing their shares, for servicing and/or maintaining Service shares' shareholder accounts and for advertising and marketing for Service shares. The Plan provides for payments to be made at an annual rate of .25% of the value of the Service shares' average daily net assets. The Distributor may make payments to Participating Insurance Companies and to brokers and dealers acting as principal underwriter for their variable insurance products. The fees payable under the Plan are payable without regard to actual expenses incurred. During the period ended December 31, 2010, Service shares were charged $14,937 pursuant to the Plan.

(c) Under the Shareholder Services Plan, Initial shares reimburse the Distributor an amount not to exceed an annual rate of .25% of the value of the Initial shares average daily net assets for certain allocated expenses with respect to servicing and/or maintaining Initial shares shareholder accounts. During the period ended December 31, 2010, Initial shares were charged $17,389 pursuant to the Shareholder Services Plan.

The fund compensates Dreyfus Transfer, Inc., a wholly-owned subsidiary of the Manager, under a transfer agency agreement for providing personnel and facilities to perform transfer agency services for the fund. During the period ended December 31, 2010, the fund was charged $1,379 pursuant to the transfer agency agreement, which is included in Shareholder servicing costs in the Statement of Operations.

The fund has arrangements with the custodian and cash management bank whereby the fund may receive earnings credits when positive cash balances are maintained, which are used to offset custody and cash management fees. For financial reporting purposes, the fund includes net earnings credits as an expense offset in the Statement of Operations.

The fund compensates The Bank of New York Mellon under a cash management agreement for performing cash management services related to fund subscriptions and redemptions. During the period ended December 31, 2010, the fund was charged $196 pursuant to the cash management agreement, which is included in Shareholder servicing costs in the Statement of Operations. These fees were partially offset by earnings credits of $12.

The fund also compensates The Bank of New York Mellon under a custody agreement for providing custodial services for the fund. During the period ended December 31, 2010, the fund was charged $20,907 pursuant to the custody agreement.

During the period ended December 31, 2010, the fund was charged $6,243 for services performed by the Chief Compliance Officer.

The components of "Due to The Dreyfus Corporation and affiliates" in the Statement of Assets and Liabilities consist of: management fees $149,912, Rule 12b-1 distribution plan fees $1,363, custodian fees $6,000, chief compliance officer fees $1,728 and transfer agency per account fees $210.

**(d)** Each Board member also serves as a Board member of other funds within the Dreyfus complex. Annual retainer fees and attendance fees are allocated to each fund based on net assets.

## NOTE 4—Securities Transactions:

The aggregate amount of purchases and sales of investment securities, excluding short-term securities, during the period ended December 31, 2010, amounted to $71,555,357 and $91,909,400, respectively.

The provisions of ASC Topic 815 "Derivatives and Hedging" require qualitative disclosures about objectives and strategies for using derivatives, quantitative disclosures about fair value amounts of gains and losses on derivative instruments and disclosures about credit-risk-related contingent features in derivative agreements. The fund held no derivatives during the period ended December 31, 2010.

At December 31, 2010, the cost of investments for federal income tax purposes was $204,787,127; accordingly, accumulated net unrealized appreciation on investments was $37,152,956, consisting of $44,484,560 gross unrealized appreciation and $7,331,604 gross unrealized depreciation.

# REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

**Shareholders and Board of Directors**
**The Dreyfus Socially Responsible Growth Fund, Inc.**

We have audited the accompanying statement of assets and liabilities of The Dreyfus Socially Responsible Growth Fund, Inc., including the statement of investments, as of December 31, 2010, and the related statement of operations for the year then ended, the statement of changes in net assets for each of the two years in the period then ended, and financial highlights for each of the years indicated therein. These financial statements and financial highlights are the responsibility of the Fund's management. Our responsibility is to express an opinion on these financial statements and financial highlights based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements and financial highlights are free of material misstatement. We were not engaged to perform an audit of the Fund's internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Fund's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements and financial highlights, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our procedures included confirmation of securities owned as of December 31, 2010 by correspondence with the custodian and others. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements and financial highlights referred to above present fairly, in all material respects, the financial position of The Dreyfus Socially Responsible Growth Fund, Inc., at December 31, 2010, the results of its operations for the year then ended, the changes in its net assets for each of the two years in the period then ended, and the financial highlights for each of the indicated years, in conformity with U.S. generally accepted accounting principles.

Ernst + Young LLP

New York, New York
February 10, 2011

## IMPORTANT TAX INFORMATION (Unaudited)

For federal tax purposes, the fund hereby designates 100% of the ordinary dividends paid during the fiscal year ended December 31, 2010 as qualifying for the corporate dividends received deduction. Shareholders will receive notification in early 2011 of the percentage applicable to the preparation of their 2010 income tax returns.

# INFORMATION ABOUT THE REVIEW AND APPROVAL OF THE FUND'S MANAGEMENT AGREEMENT (Unaudited)

At a meeting of the Board of Directors of the fund held on July 14 and 15, 2010, the Board considered the re-approval for an annual period (through August 31, 2011) of the fund's Management Agreement with the Manager, pursuant to which the Manager provides the fund with investment advisory and administrative services. The Board members, none of whom are "interested persons" (as defined in the Investment Company Act of 1940, as amended) of the fund, were assisted in their review by independent legal counsel and met with counsel in executive session separate from representatives of the Manager.

<u>Analysis of Nature, Extent and Quality of Services Provided to the Fund.</u> The Board members received a presentation from representatives of the Manager regarding services provided to the fund and other funds in the Dreyfus fund complex, and discussed the nature, extent and quality of the services provided to the fund pursuant to its Management Agreement. The Manager's representatives reviewed the fund's distribution of accounts and the relationships the Manager has with various intermediaries and the different needs of each. The Board members noted that the fund's shares are offered only to separate accounts established by insurance companies to fund variable annuity contracts and variable life insurance policies. The Manager's representatives noted the diversity of distribution of the funds in the Dreyfus fund complex, and the Manager's corresponding need for broad, deep and diverse resources to be able to provide ongoing shareholder services to each distribution channel, including those of the fund. The Manager also provided the number of shareholder accounts in the fund, as well as the fund's asset size.

The Board members also considered the Manager's research and portfolio management capabilities and that the Manager also provides oversight of day-to-day fund operations, including fund accounting and administration and assistance in meeting legal and regulatory requirements. The Board members also considered the Manager's extensive administrative, accounting and compliance infrastructure.

The Board also considered the Manager's brokerage policies and practices, the standards applied in seeking best execution and the Manager's policies and practices regarding soft dollars.

Comparative Analysis of the Fund's Performance and Management Fee and Expense Ratio. The Board members reviewed the fund's performance and comparisons to a group of large-cap growth funds underlying variable insurance products ("VIPs") and to a larger universe of funds, consisting solely of large-cap growth funds underlying VIPs, each of which are not required to use one or more social screens when choosing securities for the funds' portfolios ("Performance Group I" and "Performance Universe I," respectively) and to a group of funds underlying VIPs and to a larger universe of funds underlying VIPs from different categories, each of which is required to use one or more social screens when choosing securities for the funds' portfolios ("Performance Group II" and "Performance Universe II," respectively). The fund's portfolio manager uses social screens when choosing securities for the fund's portfolio, as described in the fund's prospectus. Each Performance Group and Performance Universe was selected and provided by Lipper, Inc., an independent provider of investment company data. The Board was provided with a description of the methodology Lipper used to select each Performance Group and Performance Universe, as well as each Expense Group and Expense Universe (discussed below). The Board members discussed the results of the comparisons for various periods ended May 31, 2010. The Board members noted that the fund's total return performance for its Initial shares was above the medians for each Performance Group and Performance Universe for the reported periods, except for the 1- and 10-year periods of each Performance Group and Performance Universe and the 5-year period of Performance Group II. The Manager also provided a comparison of the fund's total returns to the returns of its benchmark index for each of the last ten calendar years.

The Board members also discussed the fund's management fee and expense ratio and reviewed the range of management fees and expense ratios as compared to a comparable group of funds and a broader group of funds that were selected by Lipper and are not required to use one or more social screens when choosing securities for the funds' portfolios ("Expense Group I" and "Expense Universe I," respectively) and with a group of funds and a broader group of funds that were selected by Lipper and use one or more social screens when choosing securities for the funds' portfolios ("Expense Group II" and "Expense Universe II," respectively). The Board members noted that the contractual and actual management fees and expense ratio of the fund's Initial shares (which are not subject to a Rule 12b-1 plan) were at or higher than each Expense Group and Expense Universe median, except that the expense ratio for the fund's Initial shares was lower than the Expense Group II and Expense Universe II medians. The Board members also noted that the expense ratio of the fund's Service shares (which are subject to a Rule 12b-1 plan) was higher than each Expense Group and Expense Universe median.

Representatives of the Manager noted that the Manager or its affiliates do not manage other mutual funds or accounts with substantially similar investment objectives, policies and strategies as the fund.

<u>Analysis of Profitability and Economies of Scale.</u> The Manager's representatives reviewed the dollar amount of expenses allocated and profit received by the Manager and the method used to determine such expenses and profit. The Board previously had been provided with information prepared by an independent consulting firm regarding the Manager's approach to allocating costs to, and determining the profitability of, individual funds and the entire Dreyfus mutual fund complex. The Board members also had been informed that the methodology had been reviewed by an independent registered public accounting firm which, like the consultant, found the methodology to be reasonable. The consulting firm also analyzed where any economies

of scale might emerge in connection with the management of the fund. The Board members evaluated the profitability analysis in light of the relevant circumstances applicable to the fund, including any decline in assets, and the extent to which economies of scale would be realized if the fund grows and whether fee levels reflect these economies of scale for the benefit of fund investors. The Board members also considered potential benefits to the Manager from acting as investment adviser to the fund, including any soft dollar arrangements with respect to trading the fund's investments.

It was noted that the Board members should consider the Manager's profitability with respect to the fund as part of their evaluation of whether the fee under the Management Agreement bears a reasonable relationship to the mix of services provided by the Manager, including the nature, extent and quality of such services. It also was noted that a discussion of economies of scale is predicated on increasing assets and that, if a fund's assets had been decreasing, the possibility that the Manager may have realized economies of scale would be less. It also was noted that the Manager did not realize a profit on the fund's operations.

At the conclusion of these discussions, the Board agreed that it had been furnished with sufficient information to make an informed business decision with respect to continuation of the Management Agreement. Based on the discussions and considerations as described above, the Board made the following conclusions and determinations.

- The Board concluded that the nature, extent and quality of the services provided by the Manager were adequate and appropriate.
- The Board was satisfied with the fund's overall performance.
- The Board concluded that the fee paid by the fund to the Manager was reasonable in light of the services provided, comparative performance and expense and management fee information, costs of the services provided and profits to be realized and benefits derived or to be derived by the Manager from its relationship with the fund.

- The Board determined that the economies of scale which may accrue to the Manager and its affiliates in connection with the management of the fund had been adequately considered by the Manager in connection with the management fee rate charged to the fund, and that, to the extent in the future it were determined that material economies of scale had not been shared with the fund, the Board would seek to have those economies of scale shared with the fund.

The Board members considered these conclusions and determinations, along with the information received on a routine and regular basis throughout the year, and, without any one factor being dispositive, the Board determined that re-approval of the Management Agreement was in the best interests of the fund and its shareholders.

## BOARD MEMBERS INFORMATION (Unaudited)

**Joseph S. DiMartino (67)**
**Chairman of the Board (1995)**

*Principal Occupation During Past 5 Years:*
- Corporate Director and Trustee

*Other Public Company Board Memberships During Past 5 Years:*
- CBIZ (formerly, Century Business Services, Inc.), a provider of outsourcing functions for small and medium size companies, Director (1997-present)
- The Newark Group, a provider of a national market of paper recovery facilities, paperboard mills and paperboard converting plants, Director (2000-2010)
- Sunair Services Corporation, a provider of certain outdoor-related services to homes and businesses, Director (2005-2009)

*No. of Portfolios for which Board Member Serves:* 169

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**Clifford L. Alexander, Jr. (77)**
**Board Member (1992)**

*Principal Occupation During Past 5 Years:*
- President of Alexander & Associates, Inc., a management consulting firm (January 1981-present)

*No. of Portfolios for which Board Member Serves:* 46

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**David W. Burke (74)**
**Board Member (2003)**

*Principal Occupation During Past 5 Years:*
- Corporate Director and Trustee

*No. of Portfolios for which Board Member Serves:* 84

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**Whitney I. Gerard (76)**
**Board Member (2003)**

*Principal Occupation During Past 5 Years:*
- Partner of Chadbourne & Parke LLP

*No. of Portfolios for which Board Member Serves:* 26

**Nathan Leventhal (67)**
**Board Member (2009)**

*Principal Occupation During Past 5 Years:*
• Commissioner, NYC Planning Commission (March 2007-present)
• Chairman of the Avery-Fisher Artist Program (November 1997-present)

*Other Public Company Board Memberships During Past 5 Years:*
• Movado Group, Inc., Director

*No. of Portfolios for which Board Member Serves:* 44

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**George L. Perry (76)**
**Board Member (2003)**

*Principal Occupation During Past 5 Years:*
• Economist and Senior Fellow at Brookings Institution

*No. of Portfolios for which Board Member Serves:* 26

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**Benaree Pratt Wiley (64)**
**Board Member (2009)**

*Principal Occupation During Past 5 Years:*
• Principal, The Wiley Group, a firm specializing in strategy and business development (2005-present)
• President and CEO, The Partnership, an organization dedicated to increasing the representation of African Americans in positions of leadership, influence and decision-making in Boston, MA (1991-2005)

*Other Public Company Board Memberships During Past 5 Years:*
• CBIZ (formerly, Century Business Services, Inc.), a provider of outsourcing functions for small and medium size companies, Director (2008-present)

*No. of Portfolios for which Board Member Serves:* 72

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*Once elected all Board Members serve for an indefinite term, but achieve Emeritus status upon reaching age 80. The address of the Board Members and Officers is in c/o The Dreyfus Corporation, 200 Park Avenue, New York, New York 10166. Additional information about the Board Members is available in the fund's Statement of Additional Information which can be obtained from Dreyfus free of charge by calling this toll free number: 1-800-554-4611.*

*Lucy Wilson Benson, Emeritus Board Member*
*Arthur A. Hartman, Emeritus Board Member*

## OFFICERS OF THE FUND (Unaudited)

**BRADLEY J. SKAPYAK, President since January 2010.**

Chief Operating Officer and a director of the Manager since June 2009. From April 2003 to June 2009, Mr. Skapyak was the head of the Investment Accounting and Support Department of the Manager. He is an officer of 76 investment companies (comprised of 169 portfolios) managed by the Manager. He is 52 years old and has been an employee of the Manager since February 1988.

**PHILLIP N. MAISANO, Executive Vice President since July 2007.**

Chief Investment Officer,Vice Chair and a director of the Manager, and an officer of 76 investment companies (comprised of 169 portfolios) managed by the Manager. Mr. Maisano also is an officer and/or Board member of certain other investment management subsidiaries of The Bank of New York Mellon Corporation, each of which is an affiliate of the Manager. He is 63 years old and has been an employee of the Manager since November 2006. Prior to joining the Manager, Mr. Maisano served as Chairman and Chief Executive Officer of EACM Advisors, an affiliate of the Manager, since August 2004.

**MICHAEL A. ROSENBERG, Vice President and Secretary since August 2005.**

Assistant General Counsel of BNY Mellon, and an officer of 77 investment companies (comprised of 194 portfolios) managed by the Manager. He is 50 years old and has been an employee of the Manager since October 1991.

**KIESHA ASTWOOD, Vice President and Assistant Secretary since January 2010.**

Counsel of BNY Mellon, and an officer of 77 investment companies (comprised of 194 portfolios) managed by the Manager. She is 37 years old and has been an employee of the Manager since July 1995.

**JAMES BITETTO, Vice President and Assistant Secretary since August 2005.**

Senior Counsel of BNY Mellon and Secretary of the Manager, and an officer of 77 investment companies (comprised of 194 portfolios) managed by the Manager. He is 44 years old and has been an employee of the Manager since December 1996.

**JONI LACKS CHARATAN, Vice President and Assistant Secretary since August 2005.**

Senior Counsel of BNY Mellon, and an officer of 77 investment companies (comprised of 194 portfolios) managed by the Manager. She is 55 years old and has been an employee of the Manager since October 1988.

**JOSEPH M. CHIOFFI, Vice President and Assistant Secretary since August 2005.**

Senior Counsel of BNY Mellon, and an officer of 77 investment companies (comprised of 194 portfolios) managed by the Manager. He is 49 years old and has been an employee of the Manager since June 2000.

**KATHLEEN DENICHOLAS, Vice President and Assistant Secretary since January 2010.**

Senior Counsel of BNY Mellon, and an officer of 77 investment companies (comprised of 194 portfolios) managed by the Manager. She is 36 years old and has been an employee of the Manager since February 2001.

**JANETTE E. FARRAGHER, Vice President and Assistant Secretary since August 2005.**

Assistant General Counsel of BNY Mellon, and an officer of 77 investment companies (comprised of 194 portfolios) managed by the Manager. She is 48 years old and has been an employee of the Manager since February 1984.

**JOHN B. HAMMALIAN, Vice President and Assistant Secretary since August 2005.**

Managing Counsel of BNY Mellon, and an officer of 77 investment companies (comprised of 194 portfolios) managed by the Manager. He is 47 years old and has been an employee of the Manager since February 1991.

**M. CRISTINA MEISER, Vice President and Assistant Secretary since January 2010.**

Senior Counsel of BNY Mellon, and an officer of 77 investment companies (comprised of 194 portfolios) managed by the Manager. She is 40 years old and has been an employee of the Manager since August 2001.

**ROBERT R. MULLERY, Vice President and Assistant Secretary since August 2005.**

Managing Counsel of BNY Mellon, and an officer of 77 investment companies (comprised of 194 portfolios) managed by the Manager. He is 58 years old and has been an employee of the Manager since May 1986.

**JEFF PRUSNOFSKY, Vice President and Assistant Secretary since August 2005.**

Managing Counsel of BNY Mellon, and an officer of 77 investment companies (comprised of 194 portfolios) managed by the Manager. He is 45 years old and has been an employee of the Manager since October 1990.

**JAMES WINDELS, Treasurer since November 2001.**

Director – Mutual Fund Accounting of the Manager, and an officer of 77 investment companies (comprised of 194 portfolios) managed by the Manager. He is 52 years old and has been an employee of the Manager since April 1985.

**RICHARD CASSARO, Assistant Treasurer since January 2008.**

Senior Accounting Manager – Money Market and Municipal Bond Funds of the Manager, and an officer of 77 investment companies (comprised of 194 portfolios) managed by the Manager. He is 51 years old and has been an employee of the Manager since September 1982.

**GAVIN C. REILLY, Assistant Treasurer since December 2005.**

Tax Manager of the Investment Accounting and Support Department of the Manager, and an officer of 77 investment companies (comprised of 194 portfolios) managed by the Manager. He is 42 years old and has been an employee of the Manager since April 1991.

**ROBERT ROBOL, Assistant Treasurer since August 2005.**

Senior Accounting Manager – Fixed Income Funds of the Manager, and an officer of 77 investment companies (comprised of 194 portfolios) managed by the Manager. He is 46 years old and has been an employee of the Manager since October 1988.

**ROBERT SALVIOLO, Assistant Treasurer since July 2007.**

Senior Accounting Manager – Equity Funds of the Manager, and an officer of 77 investment companies (comprised of 194 portfolios) managed by the Manager. He is 43 years old and has been an employee of the Manager since June 1989.

**ROBERT SVAGNA, Assistant Treasurer since December 2002.**

Senior Accounting Manager – Equity Funds of the Manager, and an officer of 77 investment companies (comprised of 194 portfolios) managed by the Manager. He is 43 years old and has been an employee of the Manager since November 1990.

**JOSEPH W. CONNOLLY, Chief Compliance Officer since October 2004.**

Chief Compliance Officer of the Manager and The Dreyfus Family of Funds (77 investment companies, comprised of 194 portfolios). From November 2001 through March 2004, Mr. Connolly was first Vice-President, Mutual Fund Servicing for Mellon Global Securities Services. In that capacity, Mr. Connolly was responsible for managing Mellon's Custody, Fund Accounting and Fund Administration services to third-party mutual fund clients. He is 53 years old and has served in various capacities with the Manager since 1980, including manager of the firm's Fund Accounting Department from 1997 through October 2001.

**NATALIA GRIBAS, Anti-Money Laundering Compliance Officer since July 2010.**

Anti-Money Laundering Compliance Officer of the Distributor, and the Anti-Money Laundering Compliance Officer of 73 investment companies (comprised of 190 portfolios) managed by the Manager. She is 40 years old and has been an employee of the Distributor since September 2008.

NOTES

# For More Information

**The Dreyfus Socially Responsible Growth Fund, Inc.**
200 Park Avenue
New York, NY 10166

**Manager**

The Dreyfus Corporation
200 Park Avenue
New York, NY 10166

**Custodian**

The Bank of New York Mellon
One Wall Street
New York, NY 10286

**Transfer Agent & Dividend Disbursing Agent**

Dreyfus Transfer, Inc.
200 Park Avenue
New York, NY 10166

**Distributor**

MBSC Securities Corporation
200 Park Avenue
New York, NY 10166

**Telephone** 1-800-554-4611 or 1-516-338-3300

**Mail** The Dreyfus Family of Funds, 144 Glenn Curtiss Boulevard, Uniondale, NY 11556-0144
Attn: Investments Division

The fund files its complete schedule of portfolio holdings with the Securities and Exchange Commission ("SEC") for the first and third quarters of each fiscal year on Form N-Q. The fund's Forms N-Q are available on the SEC's website at http://www.sec.gov and may be reviewed and copied at the SEC's Public Reference Room in Washington, DC. Information on the operation of the Public Reference Room may be obtained by calling 1-800-SEC-0330.

A description of the policies and procedures that the fund uses to determine how to vote proxies relating to portfolio securities, and information regarding how the fund voted these proxies for the most recent 12-month period ended June 30 is available at http://www.dreyfus.com and on the SEC's website at http://www.sec.gov. The description of the policies and procedures is also available without charge, upon request, by calling 1-800-645-6561.

Printed on recycled paper.
50% post-consumer.
Process chlorine free.
Vegetable-based ink.

Printed in U.S.A.



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DECEMBER 31, 2010

# ANNUAL REPORT

DWS INVESTMENTS VIT FUNDS

## DWS Equity 500 Index VIP

DWS INVESTMENTS
Deutsche Bank Group

# Contents



**This report must be preceded or accompanied by a prospectus. To obtain an additional prospectus or summary prospectus, if available, call (800) 728-3337 or your financial representative. We advise you to consider the Fund's objectives, risks, charges and expenses carefully before investing. The summary prospectus and prospectus contain this and other important information about the Fund. Please read the prospectus carefully before you invest.**

Investing in derivatives entails special risks relating to liquidity, leverage and credit that may reduce returns and/or increase volatility. Various factors, including costs, cash flows and security selection, may cause the fund's performance to differ from that of the index. Any decline in value of a fund security that is out on loan by the portfolio will adversely affect performance. Financial failure of the borrower may mean a delay in recovery or loss of rights in the collateral. Stocks may decline in value. See the prospectus for details.

*DWS Investments is part of Deutsche Bank's Asset Management division and, within the US, represents the retail asset management activities of Deutsche Bank AG, Deutsche Bank Trust Company Americas, Deutsche Investment Management Americas Inc. and DWS Trust Company.*

*NOT FDIC/NCUA INSURED NO BANK GUARANTEE MAY LOSE VALUE NOT A DEPOSIT*
*NOT INSURED BY ANY FEDERAL GOVERNMENT AGENCY*

# Performance Summary

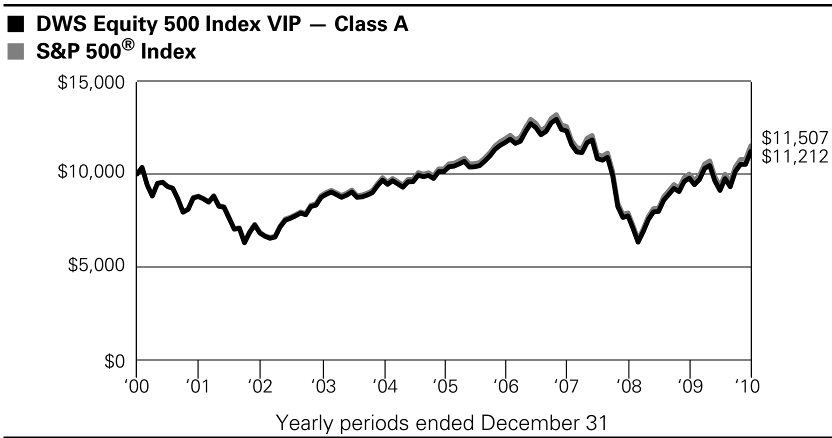
**December 31, 2010**

**All performance shown is historical, assumes reinvestment of all dividend and capital gain distributions, and does not guarantee future results. Investment return and principal value fluctuate with changing market conditions so that, when sold, shares may be worth more or less than their original cost. Current performance may be lower or higher than the performance data quoted. Please contact your participating insurance company for the Fund's most recent month-end performance. Performance figures for Classes A, B and B2 differ because each class maintains a distinct expense structure. Performance doesn't reflect charges and fees ("contract charges") associated with the separate account that invests in the Fund or any variable life insurance policy or variable annuity contract for which the Fund is an investment option. These charges and fees will reduce returns.**

**The gross expense ratios of the Fund, as stated in the fee table of the prospectus dated May 1, 2010 are 0.34%, 0.59% and 0.74% for Class A, Class B and Class B2 shares, respectively, and may differ from the expense ratios disclosed in the Financial Highlights tables in this report.**

Fund returns during the 3-year, 5-year and 10-year periods shown reflect a fee waiver/and or expense reimbursement. Without this waiver/reimbursement, returns would have been lower.

## Growth of an Assumed $10,000 Investment




*The Standard & Poor's 500® (S&P 500) Index is an unmanaged, capitalization-weighted index of 500 stocks. The index is designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries.*

*Index returns assume reinvestment of dividends and, unlike fund returns, do not reflect any fees or expenses. It is not possible to invest directly into an index.*

## Comparative Results (as of December 31, 2010)

| DWS Equity 500 Index VIP | | 1-Year | 3-Year | 5-Year | 10-Year |
|---|---|---|---|---|---|
| **Class A** | Growth of $10,000 | $11,470 | $9,107 | $11,077 | $11,212 |
| | Average annual total return | 14.70% | –3.07% | 2.07% | 1.15% |
| S&P 500 Index | Growth of $10,000 | $11,506 | $9,168 | $11,199 | $11,507 |
| | Average annual total return | 15.06% | –2.86% | 2.29% | 1.41% |

| DWS Equity 500 Index VIP | | 1-Year | 3-Year | 5-Year | Life of Class* |
|---|---|---|---|---|---|
| **Class B** | Growth of $10,000 | $11,452 | $9,044 | $10,947 | $13,288 |
| | Average annual total return | 14.52% | –3.30% | 1.83% | 3.33% |
| S&P 500 Index | Growth of $10,000 | $11,506 | $9,168 | $11,199 | $13,864 |
| | Average annual total return | 15.06% | –2.86% | 2.29% | 3.84% |

| DWS Equity 500 Index VIP | | 1-Year | 3-Year | 5-Year | Life of Class** |
|---|---|---|---|---|---|
| **Class B2** | Growth of $10,000 | $11,429 | $9,006 | $10,878 | $11,004 |
| | Average annual total return | 14.29% | –3.43% | 1.70% | 1.82% |
| S&P 500 Index | Growth of $10,000 | $11,506 | $9,168 | $11,199 | $11,433 |
| | Average annual total return | 15.06% | –2.86% | 2.29% | 2.58% |

*The growth of $10,000 is cumulative.*

* *The Fund commenced offering Class B shares on April 30, 2002. Index returns began on April 30, 2002.*

** *The Fund commenced offering Class B2 shares on September 16, 2005. Index returns began on September 30, 2005.*

# Information About Your Fund's Expenses

As an investor of the Fund, you incur two types of costs: ongoing expenses and transaction costs. Ongoing expenses include management fees, distribution and service (12b-1) fees and other Fund expenses. Examples of transaction costs include contract charges, redemption fees and account maintenance fees, which are not shown in this section. The following tables are intended to help you understand your ongoing expenses (in dollars) of investing in the Fund and to help you compare these expenses with the ongoing expenses of investing in other mutual funds. The example in the table is based on an investment of $1,000 invested at the beginning of the six-month period and held for the entire period (July 1, 2010 to December 31, 2010).

The tables illustrate your Fund's expenses in two ways:

- **Actual Fund Return.** This helps you estimate the actual dollar amount of ongoing expenses (but not transaction costs) paid on a $1,000 investment in the Fund using the Fund's actual return during the period. To estimate the expenses you paid over the period, simply divide your account value by $1,000 (for example, an $8,600 account value divided by $1,000 = 8.6), then multiply the result by the number in the "Expenses Paid per $1,000" line under the share class you hold.
- **Hypothetical 5% Fund Return.** This helps you to compare your Fund's ongoing expenses (but not transaction costs) with those of other mutual funds using the Fund's actual expense ratio and a hypothetical rate of return of 5% per year before expenses. Examples using a 5% hypothetical Fund return may be found in the shareholder reports of other mutual funds. The hypothetical account values and expenses may not be used to estimate the actual ending account balance or expenses you paid for the period.

Please note that the expenses shown in these tables are meant to highlight your ongoing expenses only and do not reflect any transaction costs. The "Expenses Paid per $1,000" line of the tables is useful in comparing ongoing expenses only and will not help you determine the relative total expense of owning different funds. If these transaction costs had been included, your costs would have been higher.

**Expenses and Value of a $1,000 Investment** for the six months ended December 31, 2010

| Actual Fund Return | Class A | Class B | Class B2 |
|---|---|---|---|
| Beginning Account Value 7/1/10 | $1,000.00 | $1,000.00 | $1,000.00 |
| Ending Account Value 12/31/10 | $1,230.80 | $1,229.70 | $1,227.80 |
| Expenses Paid per $1,000* | $ 1.86 | $ 3.26 | $ 4.10 |

| Hypothetical 5% Fund Return | Class A | Class B | Class B2 |
|---|---|---|---|
| Beginning Account Value 7/1/10 | $1,000.00 | $1,000.00 | $1,000.00 |
| Ending Account Value 12/31/10 | $1,023.54 | $1,022.28 | $1,021.53 |
| Expenses Paid per $1,000* | $ 1.68 | $ 2.96 | $ 3.72 |

* *Expenses are equal to the Fund's annualized expense ratio for each share class, multiplied by the average account value over the period, multiplied by the number of days in the most recent six-month period, then divided by 365.*

| Annualized Expense Ratios | Class A | Class B | Class B2 |
|---|---|---|---|
| DWS Equity 500 Index VIP | .33% | .58% | .73% |

For more information, please refer to the Fund's prospectus.

These tables do not reflect charges and fees ("contract charges") associated with the separate account that invests in the Fund or any variable life insurance policy or variable annuity contract for which the Fund is an investment option.

## Management Summary

December 31, 2010

Although concerns about the outlook for economic growth periodically weighed on investor sentiment during the past 12 months, the Standard & Poor's 500® (S&P 500) Index finished the period with a healthy gain of 15.06%, thanks to three important trends. First, the US economy moved to a firmer footing than where it stood one year ago, causing investor fears of a "double-dip" recession to fade gradually into the background. Second, stock prices were energized by the overall health of US corporations, as demonstrated by strong corporate earnings results, cash-rich balance sheets and — in many cases — attractive dividend yields relative to bonds. The monetary policy of the US Federal Reserve Board (the Fed) was a third pillar of positive stock market performance. The Fed kept rates near zero for the full 12-month period and initiated its policy of "quantitative easing" in order to boost growth. Together, these favorable developments helped stocks continue their long climb off of the crisis lows of March 2009.

The Fund returned 14.70% during 2010 (Class A shares, unadjusted for contract charges). Since the Fund's investment strategy is to replicate the performance of the S&P 500 Index as closely as possible before the deduction of expenses, the Fund's return is normally close to the return of the index.

Heightened investor risk appetites and hopes for improving growth translated into outperformance for the higher-beta and economically sensitive areas of the market during 2010.[1] The top-performing market segment was the consumer discretionary sector, which delivered a return nearly double that of the market as a whole. The improving outlook for economic growth, particularly in the latter part of the period, fueled gains of over 20% in numerous restaurant and retail stocks. The environment of expanding global growth and rising commodity prices also boosted stocks in the industrials, materials and energy sectors.

The weakest-performing areas of the stock market were generally those seen as being most defensive and least sensitive to economic trends, such as consumer staples, health care and utilities. Technology stocks, while providing a double-digit return, also trailed the overall market. Large-cap tech stocks such as Microsoft Corp., Cisco Systems, Inc. and Intel Corp., among others, underperformed due to concerns about their future growth potential. Similarly, financial stocks gained 10%-plus as a group but fell short of the benchmark return. Many stocks in the sector remained under pressure from regulatory concerns and difficulties relating to the slow recovery from the housing and mortgage crisis of 2008.

We continue to follow a passive strategy designed to provide returns that approximate those of the benchmark.

Brent Reeder
Senior Vice President, Northern Trust Investments, Inc., Subadvisor to the Fund

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### Risk Considerations

Investing in derivatives entails special risks relating to liquidity, leverage and credit that may reduce returns and/or increase volatility. Various factors, including costs, cash flows and security selection, may cause the Fund's performance to differ from that of the index. Any decline in value of a fund security that is out on loan by the Fund will adversely affect performance. Financial failure of the borrower may mean a delay in recovery or loss of rights in the collateral. Stocks may decline in value. See the prospectus for details.

*The Standard & Poor's 500 (S&P 500) Index is an unmanaged, capitalization-weighted index of 500 stocks. The index is designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries.*

*"Standard & Poor's," "S&P," "S&P 500," "Standard & Poor's 500" and "500" are trademarks of The McGraw-Hill Companies, Inc., and have been licensed for use by the Fund's advisor. DWS Equity 500 Index VIP is not sponsored, endorsed, sold, nor promoted by Standard & Poor's, and Standard & Poor's makes no representation regarding the advisability of investing in the Fund. There is no guarantee that the Fund will be able to mirror the S&P 500 index closely enough to track its performance.*

*Index returns assume reinvestment of dividends and, unlike fund returns, do not reflect any fees or expenses. It is not possible to invest directly into an index.*

1 *Beta is a measure of volatility, or systematic risk, of a security or a portfolio in comparison to the market as a whole.*

*Portfolio management market commentary is as of December 31, 2010, and may not come to pass. This information is subject to change at any time based on market and other conditions and should not be construed as a recommendation. Past performance does not guarantee future results. Current and future portfolio holdings are subject to risk.*

# Portfolio Summary

| **Asset Allocation** (As a % of Investment Portfolio excluding Securities Lending Collateral) | **12/31/10** | **12/31/09** |
|---|---|---|
| Common Stocks | 99% | 98% |
| Cash Equivalents* | 1% | 2% |
| | 100% | 100% |

| **Sector Diversification** (As a % of Common Stocks) | **12/31/10** | **12/31/09** |
|---|---|---|
| Information Technology | 19% | 20% |
| Financials | 16% | 14% |
| Energy | 12% | 11% |
| Industrials | 11% | 10% |
| Health Care | 11% | 13% |
| Consumer Staples | 11% | 11% |
| Consumer Discretionary | 10% | 10% |
| Materials | 4% | 4% |
| Utilities | 3% | 4% |
| Telecommunication Services | 3% | 3% |
| | 100% | 100% |

| **Ten Largest Equity Holdings** (18.3% of Net Assets) | |
|---|---|
| 1. **Exxon Mobil Corp.**<br>Explorer and producer of oil and gas | **3.2%** |
| 2. **Apple, Inc.**<br>Manufacturer of personal computers and communication solutions | **2.5%** |
| 3. **Microsoft Corp.**<br>Developer of computer software | **1.8%** |
| 4. **General Electric Co.**<br>A diversified company provider of services to the technology, media and financial industries | **1.7%** |
| 5. **Chevron Corp.**<br>Operator of petroleum exploration, delivery and refining facilities | **1.6%** |
| 6. **International Business Machines Corp.**<br>Manufacturer of computers and provider of information processing services | **1.6%** |
| 7. **Procter & Gamble Co.**<br>Manufacturer of diversified consumer products | **1.5%** |
| 8. **AT&T, Inc.**<br>Provider of communications services | **1.5%** |
| 9. **Johnson & Johnson**<br>Provider of health care products | **1.5%** |
| 10. **JPMorgan Chase & Co.**<br>Provider of global financial services | **1.4%** |

*Asset allocation, sector diversification, and holdings are subject to change.*

* *In order to keep cash on hand to meet shareholder redemptions or other needs while maintaining exposure to the market, the Fund invests in futures contracts.*

*For more complete details about the Fund's investment portfolio, see page 7.*

Following the Fund's fiscal first and third quarter-end, a complete portfolio holdings listing is filed with the SEC on Form N-Q. The form will be available on the SEC's Web site at www.sec.gov, and it also may be reviewed and copied at the SEC's Public Reference Room in Washington, D.C. Information on the operation of the SEC's Public Reference Room may be obtained by calling (800) SEC-0330. The Fund's portfolio holdings are also posted on www.dws-investments.com from time to time. Please see the Fund's current prospectus for more information.

# Investment Portfolio

December 31, 2010

| | Shares | Value ($) |
|---|---|---|
| **Common Stocks 98.5%** | | |
| **Consumer Discretionary 10.5%** | | |
| **Auto Components 0.3%** | | |
| Goodyear Tire & Rubber Co.* | 16,251 | 192,575 |
| Johnson Controls, Inc. | 44,891 | 1,714,836 |
| | | **1,907,411** |
| **Automobiles 0.6%** | | |
| Ford Motor Co.* (a) | 249,604 | 4,190,851 |
| Harley-Davidson, Inc. | 15,811 | 548,168 |
| | | **4,739,019** |
| **Distributors 0.1%** | | |
| Genuine Parts Co. | 10,263 | **526,902** |
| **Diversified Consumer Services 0.1%** | | |
| Apollo Group, Inc. "A"* | 8,558 | 337,956 |
| DeVry, Inc. | 4,136 | 198,445 |
| H&R Block, Inc. | 20,413 | 243,119 |
| | | **779,520** |
| **Hotels Restaurants & Leisure 1.7%** | | |
| Carnival Corp. (Units) | 28,525 | 1,315,288 |
| Darden Restaurants, Inc. | 9,308 | 432,263 |
| International Game Technology | 19,874 | 351,571 |
| Marriott International, Inc. "A" (a) | 18,896 | 784,940 |
| McDonald's Corp. | 70,514 | 5,412,655 |
| Starbucks Corp. (a) | 49,114 | 1,578,033 |
| Starwood Hotels & Resorts Worldwide, Inc. (a) | 12,542 | 762,303 |
| Wyndham Worldwide Corp. | 11,793 | 353,318 |
| Wynn Resorts Ltd. | 5,057 | 525,119 |
| Yum! Brands, Inc. | 31,161 | 1,528,447 |
| | | **13,043,937** |
| **Household Durables 0.4%** | | |
| D.R. Horton, Inc. | 19,022 | 226,932 |
| Fortune Brands, Inc. | 10,247 | 617,382 |
| Harman International Industries, Inc.* | 4,700 | 217,610 |
| Leggett & Platt, Inc. | 10,054 | 228,829 |
| Lennar Corp. "A" (a) | 10,645 | 199,594 |
| Newell Rubbermaid, Inc. | 19,486 | 354,256 |
| Pulte Group, Inc.* (a) | 22,422 | 168,613 |
| Stanley Black & Decker, Inc. | 11,139 | 744,865 |
| Whirlpool Corp. (a) | 5,118 | 454,632 |
| | | **3,212,713** |
| **Internet & Catalog Retail 0.8%** | | |
| Amazon.com, Inc.* | 23,630 | 4,253,400 |
| Expedia, Inc. | 13,574 | 340,572 |
| Netflix, Inc.* | 2,924 | 513,747 |
| Priceline.com, Inc.* | 3,255 | 1,300,535 |
| | | **6,408,254** |
| **Leisure Equipment & Products 0.1%** | | |
| Hasbro, Inc. | 9,186 | 433,395 |
| Mattel, Inc. (a) | 23,458 | 596,537 |
| | | **1,029,932** |
| **Media 3.1%** | | |
| Cablevision Systems Corp. (New York Group) "A" | 16,183 | 547,633 |
| CBS Corp. "B" (a) | 45,758 | 871,690 |
| Comcast Corp. "A" | 185,861 | 4,083,366 |
| DIRECTV "A"* | 55,556 | 2,218,351 |
| Discovery Communications, Inc. "A"* (a) | 19,148 | 798,472 |
| Gannett Co., Inc. | 15,768 | 237,939 |
| Interpublic Group of Companies, Inc.* | 32,753 | 347,837 |
| McGraw-Hill Companies, Inc. | 20,122 | 732,642 |
| Meredith Corp. (a) | 2,488 | 86,209 |
| News Corp. "A" | 152,058 | 2,213,964 |
| Omnicom Group, Inc. | 19,883 | 910,641 |
| Scripps Networks Interactive "A" | 5,962 | 308,533 |
| Time Warner Cable, Inc. | 23,619 | 1,559,563 |
| Time Warner, Inc. | 73,978 | 2,379,872 |
| Viacom, Inc. "B" | 40,249 | 1,594,263 |
| Walt Disney Co. | 126,205 | 4,733,950 |
| Washington Post Co. "B" (a) | 372 | 163,494 |
| | | **23,788,419** |
| **Multiline Retail 0.8%** | | |
| Big Lots, Inc.* | 5,059 | 154,097 |
| Family Dollar Stores, Inc. | 8,430 | 419,055 |
| J.C. Penney Co., Inc. | 15,832 | 511,532 |
| Kohl's Corp.* | 19,320 | 1,049,849 |
| Macy's, Inc. | 28,452 | 719,835 |
| Nordstrom, Inc. (a) | 11,306 | 479,148 |
| Sears Holdings Corp.* (a) | 2,909 | 214,539 |
| Target Corp. | 47,167 | 2,836,152 |
| | | **6,384,207** |
| **Specialty Retail 1.9%** | | |
| Abercrombie & Fitch Co. "A" | 5,818 | 335,291 |
| AutoNation, Inc.* | 4,318 | 121,768 |
| AutoZone, Inc.* | 1,787 | 487,118 |
| Bed Bath & Beyond, Inc.* | 17,129 | 841,890 |
| Best Buy Co., Inc. | 22,219 | 761,889 |
| CarMax, Inc.* | 15,084 | 480,878 |
| GameStop Corp. "A"* (a) | 10,351 | 236,831 |
| Home Depot, Inc. (a) | 109,283 | 3,831,462 |
| Limited Brands, Inc. (a) | 17,798 | 546,933 |
| Lowe's Companies, Inc. | 91,996 | 2,307,260 |
| O'Reilly Automotive, Inc.* | 9,168 | 553,931 |
| RadioShack Corp. (a) | 7,420 | 137,196 |
| Ross Stores, Inc. | 8,145 | 515,171 |
| Staples, Inc. | 47,780 | 1,087,951 |
| The Gap, Inc. (a) | 28,828 | 638,252 |
| Tiffany & Co. | 8,483 | 528,236 |
| TJX Companies, Inc. | 26,214 | 1,163,639 |
| Urban Outfitters, Inc.* | 8,600 | 307,966 |
| | | **14,883,662** |
| **Textiles, Apparel & Luxury Goods 0.6%** | | |
| Coach, Inc. | 19,627 | 1,085,569 |
| NIKE, Inc. "B" (a) | 25,402 | 2,169,839 |
| Polo Ralph Lauren Corp. | 4,347 | 482,169 |
| VF Corp. (a) | 5,864 | 505,360 |
| | | **4,242,937** |
| **Consumer Staples 10.5%** | | |
| **Beverages 2.5%** | | |
| Brown-Forman Corp. "B" (a) | 6,998 | 487,201 |
| Coca-Cola Co. | 154,811 | 10,181,919 |
| Coca-Cola Enterprises, Inc. | 22,852 | 571,986 |
| Constellation Brands, Inc. "A"* | 11,807 | 261,525 |
| Dr. Pepper Snapple Group, Inc. | 15,273 | 536,999 |

*The accompanying notes are an integral part of the financial statements.*

| | Shares | Value ($) |
|---|---|---|
| Molson Coors Brewing Co. "B" (a) | 10,675 | 535,778 |
| PepsiCo, Inc. | 105,707 | 6,905,838 |
| | | **19,481,246** |
| **Food & Staples Retailing 2.3%** | | |
| Costco Wholesale Corp. | 28,806 | 2,080,081 |
| CVS Caremark Corp. | 90,604 | 3,150,301 |
| Kroger Co. | 42,160 | 942,698 |
| Safeway, Inc. | 25,024 | 562,790 |
| SUPERVALU, Inc. (a) | 13,849 | 133,366 |
| Sysco Corp. (a) | 38,731 | 1,138,691 |
| Wal-Mart Stores, Inc. | 130,750 | 7,051,348 |
| Walgreen Co. | 61,745 | 2,405,585 |
| Whole Foods Market, Inc.* | 9,843 | 497,957 |
| | | **17,962,817** |
| **Food Products 1.7%** | | |
| Archer-Daniels-Midland Co. | 42,295 | 1,272,234 |
| Campbell Soup Co. (a) | 12,940 | 449,665 |
| ConAgra Foods, Inc. | 29,633 | 669,113 |
| Dean Foods Co.* (a) | 11,939 | 105,541 |
| General Mills, Inc. | 42,651 | 1,517,949 |
| H.J. Heinz Co. (a) | 21,250 | 1,051,025 |
| Hormel Foods Corp. | 4,717 | 241,793 |
| Kellogg Co. | 16,732 | 854,671 |
| Kraft Foods, Inc. "A" | 116,386 | 3,667,323 |
| McCormick & Co., Inc. (a) | 8,856 | 412,070 |
| Mead Johnson Nutrition Co. | 13,769 | 857,120 |
| Sara Lee Corp. | 42,929 | 751,687 |
| The Hershey Co. (a) | 10,410 | 490,831 |
| The J.M. Smucker Co. (a) | 8,073 | 529,992 |
| Tyson Foods, Inc. "A" | 19,942 | 343,401 |
| | | **13,214,415** |
| **Household Products 2.2%** | | |
| Clorox Co. | 9,432 | 596,857 |
| Colgate-Palmolive Co. (a) | 32,159 | 2,584,619 |
| Kimberly-Clark Corp. | 27,140 | 1,710,906 |
| Procter & Gamble Co. | 186,615 | 12,004,943 |
| | | **16,897,325** |
| **Personal Products 0.2%** | | |
| Avon Products, Inc. (a) | 28,835 | 837,945 |
| Estee Lauder Companies, Inc. "A" (a) | 7,600 | 613,320 |
| | | **1,451,265** |
| **Tobacco 1.6%** | | |
| Altria Group, Inc. | 139,126 | 3,425,282 |
| Lorillard, Inc. | 9,871 | 810,014 |
| Philip Morris International, Inc. | 121,018 | 7,083,184 |
| Reynolds American, Inc. | 22,656 | 739,039 |
| | | **12,057,519** |
| **Energy 11.8%** | | |
| **Energy Equipment & Services 2.1%** | | |
| Baker Hughes, Inc. | 28,666 | 1,638,835 |
| Cameron International Corp.* | 15,965 | 809,904 |
| Diamond Offshore Drilling, Inc. | 4,672 | 312,417 |
| FMC Technologies, Inc.* (a) | 7,842 | 697,232 |
| Halliburton Co. | 60,708 | 2,478,708 |
| Helmerich & Payne, Inc. (a) | 7,177 | 347,941 |
| Nabors Industries Ltd.* | 19,072 | 447,429 |
| National Oilwell Varco, Inc. | 27,934 | 1,878,562 |
| Rowan Companies, Inc.* | 8,524 | 297,573 |
| Schlumberger Ltd. | 91,060 | 7,603,510 |
| | | **16,512,111** |

| | Shares | Value ($) |
|---|---|---|
| **Oil, Gas & Consumable Fuels 9.7%** | | |
| Anadarko Petroleum Corp. | 33,013 | 2,514,270 |
| Apache Corp. | 25,486 | 3,038,696 |
| Cabot Oil & Gas Corp. | 6,971 | 263,852 |
| Chesapeake Energy Corp. | 43,465 | 1,126,178 |
| Chevron Corp. | 134,213 | 12,246,936 |
| ConocoPhillips | 97,955 | 6,670,736 |
| CONSOL Energy, Inc. | 14,814 | 722,034 |
| Denbury Resources, Inc.* | 26,922 | 513,941 |
| Devon Energy Corp. | 28,790 | 2,260,303 |
| El Paso Corp. | 47,299 | 650,834 |
| EOG Resources, Inc. (a) | 16,931 | 1,547,663 |
| EQT Corp. (a) | 9,982 | 447,593 |
| Exxon Mobil Corp. | 336,268 | 24,587,916 |
| Hess Corp. | 19,938 | 1,526,055 |
| Marathon Oil Corp. | 47,230 | 1,748,927 |
| Massey Energy Co. | 6,864 | 368,254 |
| Murphy Oil Corp. | 12,702 | 946,934 |
| Newfield Exploration Co.* | 8,748 | 630,818 |
| Noble Energy, Inc. | 11,558 | 994,913 |
| Occidental Petroleum Corp. | 54,193 | 5,316,333 |
| Peabody Energy Corp. (a) | 17,868 | 1,143,195 |
| Pioneer Natural Resources Co. | 7,788 | 676,154 |
| QEP Resources, Inc. | 11,777 | 427,623 |
| Range Resources Corp. | 10,732 | 482,725 |
| Southwestern Energy Co.* | 23,248 | 870,173 |
| Spectra Energy Corp. (a) | 42,965 | 1,073,695 |
| Sunoco, Inc. | 8,065 | 325,100 |
| Tesoro Corp.* | 9,218 | 170,902 |
| Valero Energy Corp. | 38,112 | 881,149 |
| Williams Companies, Inc. | 39,350 | 972,732 |
| | | **75,146,634** |
| **Financials 15.8%** | | |
| **Capital Markets 2.5%** | | |
| Ameriprise Financial, Inc. | 16,648 | 958,092 |
| Bank of New York Mellon Corp. | 82,591 | 2,494,248 |
| Charles Schwab Corp. | 65,660 | 1,123,443 |
| E*TRADE Financial Corp.* | 13,066 | 209,056 |
| Federated Investors, Inc. "B" (a) | 6,350 | 166,179 |
| Franklin Resources, Inc. | 9,781 | 1,087,745 |
| Invesco Ltd. | 31,130 | 748,988 |
| Janus Capital Group, Inc. | 12,271 | 159,155 |
| Legg Mason, Inc. (a) | 10,300 | 373,581 |
| Morgan Stanley | 100,832 | 2,743,639 |
| Northern Trust Corp. | 17,197 | 952,886 |
| State Street Corp. | 33,352 | 1,545,532 |
| T. Rowe Price Group, Inc. | 16,975 | 1,095,566 |
| The Goldman Sachs Group, Inc. | 34,085 | 5,731,734 |
| | | **19,389,844** |
| **Commercial Banks 2.9%** | | |
| BB&T Corp. (a) | 45,658 | 1,200,349 |
| Comerica, Inc. (a) | 11,858 | 500,882 |
| Fifth Third Bancorp. | 53,466 | 784,881 |
| First Horizon National Corp. | 15,830 | 186,480 |
| Huntington Bancshares, Inc. | 58,144 | 399,449 |
| KeyCorp | 58,749 | 519,929 |
| M&T Bank Corp. | 8,027 | 698,750 |
| Marshall & Ilsley Corp. | 35,932 | 248,650 |
| PNC Financial Services Group, Inc. | 34,985 | 2,124,289 |
| Regions Financial Corp. | 83,546 | 584,822 |
| SunTrust Banks, Inc. (a) | 32,910 | 971,174 |
| US Bancorp. | 127,688 | 3,443,745 |

*The accompanying notes are an integral part of the financial statements.*

| | Shares | Value ($) |
|---|---|---|
| Wells Fargo & Co. (a) | 349,745 | 10,838,598 |
| Zions Bancorp. | 11,943 | 289,379 |
| | | **22,791,377** |
| **Consumer Finance 0.7%** | | |
| American Express Co. | 69,706 | 2,991,781 |
| Capital One Financial Corp. | 30,342 | 1,291,356 |
| Discover Financial Services | 36,615 | 678,476 |
| SLM Corp.* | 33,035 | 415,911 |
| | | **5,377,524** |
| **Diversified Financial Services 4.2%** | | |
| Bank of America Corp. | 672,112 | 8,965,974 |
| Citigroup, Inc.* | 1,935,779 | 9,156,235 |
| CME Group, Inc. | 4,449 | 1,431,466 |
| IntercontinentalExchange, Inc.* | 4,942 | 588,839 |
| JPMorgan Chase & Co. | 260,543 | 11,052,234 |
| Leucadia National Corp. | 13,272 | 387,277 |
| Moody's Corp. (a) | 13,692 | 363,386 |
| NYSE Euronext | 17,581 | 527,078 |
| The NASDAQ OMX Group, Inc.* | 9,330 | 221,214 |
| | | **32,693,703** |
| **Insurance 3.8%** | | |
| ACE Ltd. | 22,531 | 1,402,555 |
| Aflac, Inc. | 31,254 | 1,763,663 |
| Allstate Corp. | 35,611 | 1,135,279 |
| American International Group, Inc.* (a) | 9,419 | 542,723 |
| Aon Corp. | 22,235 | 1,023,032 |
| Assurant, Inc. | 7,087 | 272,991 |
| Berkshire Hathaway, Inc. "B"* | 115,372 | 9,242,451 |
| Chubb Corp. | 20,204 | 1,204,967 |
| Cincinnati Financial Corp. (a) | 10,538 | 333,949 |
| Genworth Financial, Inc. "A"* | 33,226 | 436,590 |
| Hartford Financial Services Group, Inc. | 29,864 | 791,097 |
| Lincoln National Corp. (a) | 21,263 | 591,324 |
| Loews Corp. | 20,898 | 813,141 |
| Marsh & McLennan Companies, Inc. (a) | 36,047 | 985,525 |
| MetLife, Inc. | 60,238 | 2,676,977 |
| Principal Financial Group, Inc. (a) | 21,554 | 701,798 |
| Progressive Corp. | 44,392 | 882,069 |
| Prudential Financial, Inc. | 32,289 | 1,895,687 |
| The Travelers Companies, Inc. (a) | 30,563 | 1,702,665 |
| Torchmark Corp. (a) | 5,374 | 321,043 |
| Unum Group | 21,316 | 516,273 |
| XL Group PLC | 21,826 | 476,243 |
| | | **29,712,042** |
| **Real Estate Investment Trusts 1.5%** | | |
| Apartment Investment & Management Co. "A" (REIT) | 7,725 | 199,614 |
| AvalonBay Communities, Inc. (REIT) (a) | 5,757 | 647,950 |
| Boston Properties, Inc. (REIT) (a) | 9,245 | 795,994 |
| Equity Residential (REIT) (a) | 19,185 | 996,661 |
| HCP, Inc. (REIT) (a) | 24,540 | 902,827 |
| Health Care REIT, Inc. (REIT) (a) | 9,425 | 449,007 |
| Host Hotels & Resorts, Inc. (REIT) (a) | 44,396 | 793,356 |
| Kimco Realty Corp. (REIT) (a) | 27,311 | 492,690 |
| Plum Creek Timber Co., Inc. (REIT) (a) | 10,835 | 405,771 |
| ProLogis (REIT) (a) | 38,254 | 552,388 |
| Public Storage (REIT) (a) | 9,236 | 936,715 |

| | Shares | Value ($) |
|---|---|---|
| Simon Property Group, Inc. (REIT) | 19,445 | 1,934,583 |
| Ventas, Inc. (REIT) | 10,500 | 551,040 |
| Vornado Realty Trust (REIT) (a) | 10,736 | 894,631 |
| Weyerhaeuser Co. (REIT) | 36,062 | 682,654 |
| | | **11,235,881** |
| **Real Estate Management & Development 0.1%** | | |
| CB Richard Ellis Group, Inc. "A"* | 19,406 | **397,435** |
| **Thrifts & Mortgage Finance 0.1%** | | |
| Hudson City Bancorp., Inc. (a) | 33,890 | 431,758 |
| People's United Financial, Inc. (a) | 23,677 | 331,715 |
| | | **763,473** |

## Health Care 10.7%

| | Shares | Value ($) |
|---|---|---|
| **Biotechnology 1.3%** | | |
| Amgen, Inc.* (a) | 62,927 | 3,454,692 |
| Biogen Idec, Inc.* (a) | 15,985 | 1,071,794 |
| Celgene Corp.* (a) | 31,309 | 1,851,614 |
| Cephalon, Inc.* (a) | 5,021 | 309,896 |
| Genzyme Corp.* | 17,380 | 1,237,456 |
| Gilead Sciences, Inc.* | 54,040 | 1,958,410 |
| | | **9,883,862** |
| **Health Care Equipment & Supplies 1.5%** | | |
| Baxter International, Inc. | 38,825 | 1,965,322 |
| Becton, Dickinson & Co. | 15,282 | 1,291,635 |
| Boston Scientific Corp.* | 101,955 | 771,799 |
| C.R. Bard, Inc. (a) | 6,278 | 576,132 |
| CareFusion Corp.* | 14,868 | 382,108 |
| DENTSPLY International, Inc. (a) | 9,495 | 324,444 |
| Intuitive Surgical, Inc.* (a) | 2,639 | 680,202 |
| Medtronic, Inc. | 72,047 | 2,672,223 |
| St. Jude Medical, Inc.* | 22,629 | 967,390 |
| Stryker Corp. (a) | 22,672 | 1,217,486 |
| Varian Medical Systems, Inc.* (a) | 8,037 | 556,803 |
| Zimmer Holdings, Inc.* (a) | 12,985 | 697,035 |
| | | **12,102,579** |
| **Health Care Providers & Services 1.9%** | | |
| Aetna, Inc. | 26,910 | 821,024 |
| AmerisourceBergen Corp. | 18,101 | 617,606 |
| Cardinal Health, Inc. | 23,028 | 882,203 |
| CIGNA Corp. | 18,229 | 668,275 |
| Coventry Health Care, Inc.* | 9,905 | 261,492 |
| DaVita, Inc.* | 6,342 | 440,706 |
| Express Scripts, Inc.* | 35,092 | 1,896,723 |
| Humana, Inc.* | 11,265 | 616,646 |
| Laboratory Corp. of America Holdings* (a) | 6,865 | 603,571 |
| McKesson Corp. | 16,788 | 1,181,539 |
| Medco Health Solutions, Inc.* | 28,234 | 1,729,897 |
| Patterson Companies, Inc. (a) | 6,474 | 198,299 |
| Quest Diagnostics, Inc. | 9,529 | 514,280 |
| Tenet Healthcare Corp.* | 32,273 | 215,906 |
| UnitedHealth Group, Inc. | 73,257 | 2,645,310 |
| WellPoint, Inc.* | 26,159 | 1,487,401 |
| | | **14,780,878** |
| **Health Care Technology 0.1%** | | |
| Cerner Corp.* (a) | 4,836 | **458,163** |
| **Life Sciences Tools & Services 0.5%** | | |
| Agilent Technologies, Inc.* | 22,841 | 946,303 |
| Life Technologies Corp.* | 12,613 | 700,021 |
| PerkinElmer, Inc. (a) | 7,891 | 203,746 |
| Thermo Fisher Scientific, Inc.* | 26,400 | 1,461,504 |
| Waters Corp.* | 6,131 | 476,440 |
| | | **3,788,014** |

*The accompanying notes are an integral part of the financial statements.*

| | Shares | Value ($) |
|---|---|---|
| **Pharmaceuticals 5.4%** | | |
| Abbott Laboratories | 103,187 | 4,943,689 |
| Allergan, Inc. | 20,408 | 1,401,417 |
| Bristol-Myers Squibb Co. | 113,988 | 3,018,402 |
| Eli Lilly & Co. (a) | 67,775 | 2,374,836 |
| Forest Laboratories, Inc.* | 18,743 | 599,401 |
| Hospira, Inc.* | 10,979 | 611,421 |
| Johnson & Johnson | 183,185 | 11,329,992 |
| King Pharmaceuticals, Inc.* | 6,039 | 84,848 |
| Merck & Co., Inc. | 205,546 | 7,407,878 |
| Mylan, Inc.* | 28,721 | 606,875 |
| Pfizer, Inc. | 534,231 | 9,354,385 |
| Watson Pharmaceuticals, Inc.* | 8,199 | 423,478 |
| | | **42,156,622** |
| **Industrials 10.8%** | | |
| **Aerospace & Defense 2.6%** | | |
| Boeing Co. | 48,883 | 3,190,105 |
| General Dynamics Corp. | 25,168 | 1,785,921 |
| Goodrich Corp. | 8,426 | 742,078 |
| Honeywell International, Inc. | 52,029 | 2,765,862 |
| ITT Corp. (a) | 12,377 | 644,965 |
| L-3 Communications Holdings, Inc. | 7,621 | 537,204 |
| Lockheed Martin Corp. (a) | 19,705 | 1,377,577 |
| Northrop Grumman Corp. | 19,432 | 1,258,805 |
| Precision Castparts Corp. | 9,470 | 1,318,319 |
| Raytheon Co. | 24,110 | 1,117,257 |
| Rockwell Collins, Inc. | 10,515 | 612,604 |
| United Technologies Corp. | 61,652 | 4,853,245 |
| | | **20,203,942** |
| **Air Freight & Logistics 1.1%** | | |
| C.H. Robinson Worldwide, Inc. | 10,943 | 877,519 |
| Expeditors International of Washington, Inc. | 14,320 | 781,872 |
| FedEx Corp. | 20,944 | 1,948,002 |
| United Parcel Service, Inc. "B" | 65,973 | 4,788,320 |
| | | **8,395,713** |
| **Airlines 0.1%** | | |
| Southwest Airlines Co. | 49,916 | **647,910** |
| **Building Products 0.0%** | | |
| Masco Corp. | 23,791 | **301,194** |
| **Commercial Services & Supplies 0.5%** | | |
| Avery Dennison Corp. | 7,306 | 309,336 |
| Cintas Corp. (a) | 8,566 | 239,505 |
| Iron Mountain, Inc. (a) | 13,483 | 337,210 |
| Pitney Bowes, Inc. (a) | 13,829 | 334,385 |
| R.R. Donnelley & Sons Co. | 14,037 | 245,227 |
| Republic Services, Inc. | 20,670 | 617,206 |
| Stericycle, Inc.* (a) | 5,753 | 465,533 |
| Waste Management, Inc. (a) | 31,668 | 1,167,599 |
| | | **3,716,001** |
| **Construction & Engineering 0.2%** | | |
| Fluor Corp. | 11,731 | 777,296 |
| Jacobs Engineering Group, Inc.* | 8,371 | 383,810 |
| Quanta Services, Inc.* | 14,683 | 292,486 |
| | | **1,453,592** |
| **Electrical Equipment 0.5%** | | |
| Emerson Electric Co. | 50,194 | 2,869,591 |
| Rockwell Automation, Inc. | 9,316 | 668,050 |
| Roper Industries, Inc. | 6,408 | 489,764 |
| | | **4,027,405** |

| | Shares | Value ($) |
|---|---|---|
| **Industrial Conglomerates 2.4%** | | |
| 3M Co. | 47,738 | 4,119,789 |
| General Electric Co. | 710,273 | 12,990,893 |
| Textron, Inc. (a) | 18,416 | 435,354 |
| Tyco International Ltd. | 32,520 | 1,347,629 |
| | | **18,893,665** |
| **Machinery 2.3%** | | |
| Caterpillar, Inc. | 42,307 | 3,962,474 |
| Cummins, Inc. | 13,122 | 1,443,551 |
| Danaher Corp. | 35,654 | 1,681,799 |
| Deere & Co. | 28,251 | 2,346,246 |
| Dover Corp. (a) | 12,580 | 735,301 |
| Eaton Corp. | 11,134 | 1,130,212 |
| Flowserve Corp. | 3,779 | 450,532 |
| Illinois Tool Works, Inc. | 33,070 | 1,765,938 |
| Ingersoll-Rand PLC (a) | 21,386 | 1,007,067 |
| PACCAR, Inc. (a) | 24,291 | 1,394,789 |
| Pall Corp. | 7,739 | 383,700 |
| Parker Hannifin Corp. | 10,626 | 917,024 |
| Snap-on, Inc. | 3,844 | 217,493 |
| | | **17,436,126** |
| **Professional Services 0.1%** | | |
| Dun & Bradstreet Corp. | 3,376 | 277,136 |
| Equifax, Inc. | 8,324 | 296,334 |
| Robert Half International, Inc. (a) | 9,808 | 300,125 |
| | | **873,595** |
| **Road & Rail 0.8%** | | |
| CSX Corp. | 24,871 | 1,606,915 |
| Norfolk Southern Corp. | 24,168 | 1,518,234 |
| Ryder System, Inc. | 3,482 | 183,293 |
| Union Pacific Corp. | 32,911 | 3,049,533 |
| | | **6,357,975** |
| **Trading Companies & Distributors 0.2%** | | |
| Fastenal Co. (a) | 9,911 | 593,768 |
| W.W. Grainger, Inc. | 3,783 | 522,470 |
| | | **1,116,238** |
| **Information Technology 18.4%** | | |
| **Communications Equipment 2.2%** | | |
| Cisco Systems, Inc.* | 369,545 | 7,475,895 |
| F5 Networks, Inc.* | 5,302 | 690,108 |
| Harris Corp. | 8,680 | 393,204 |
| JDS Uniphase Corp.* | 15,065 | 218,141 |
| Juniper Networks, Inc.* | 34,672 | 1,280,090 |
| Motorola, Inc.* | 155,908 | 1,414,086 |
| QUALCOMM, Inc. | 107,918 | 5,340,862 |
| Tellabs, Inc. | 24,419 | 165,561 |
| | | **16,977,947** |
| **Computers & Peripherals 4.4%** | | |
| Apple, Inc.* | 61,155 | 19,726,157 |
| Dell, Inc.* (a) | 111,648 | 1,512,830 |
| EMC Corp.* | 137,344 | 3,145,178 |
| Hewlett-Packard Co. | 151,262 | 6,368,130 |
| Lexmark International, Inc. "A"* | 5,414 | 188,516 |
| NetApp, Inc.* | 23,943 | 1,315,907 |
| QLogic Corp.* | 6,798 | 115,702 |
| SanDisk Corp.* | 15,788 | 787,190 |
| Western Digital Corp.* | 15,450 | 523,755 |
| | | **33,683,365** |

*The accompanying notes are an integral part of the financial statements.*

| | Shares | Value ($) |
|---|---|---|
| **Electronic Equipment, Instruments & Components 0.4%** | | |
| Amphenol Corp. "A" | 11,718 | 618,476 |
| Corning, Inc. | 104,153 | 2,012,236 |
| FLIR Systems, Inc.* (a) | 10,533 | 313,357 |
| Jabil Circuit, Inc. | 13,089 | 262,958 |
| Molex, Inc. (a) | 9,270 | 210,614 |
| | | **3,417,641** |
| **Internet Software & Services 1.9%** | | |
| Akamai Technologies, Inc.* | 12,258 | 576,739 |
| eBay, Inc.* | 76,424 | 2,126,880 |
| Google, Inc. "A"* | 16,630 | 9,877,721 |
| Monster Worldwide, Inc.* (a) | 8,668 | 204,825 |
| VeriSign, Inc. (a) | 11,610 | 379,298 |
| Yahoo!, Inc.* | 86,587 | 1,439,942 |
| | | **14,605,405** |
| **IT Services 3.0%** | | |
| Automatic Data Processing, Inc. | 32,822 | 1,519,002 |
| Cognizant Technology Solutions Corp. "A"* | 20,148 | 1,476,647 |
| Computer Sciences Corp. | 10,337 | 512,715 |
| Fidelity National Information Services, Inc. | 17,913 | 490,637 |
| Fiserv, Inc.* (a) | 10,036 | 587,708 |
| International Business Machines Corp. (a) | 82,865 | 12,161,268 |
| MasterCard, Inc. "A" | 6,436 | 1,442,372 |
| Paychex, Inc. | 21,046 | 650,532 |
| SAIC, Inc.* | 19,685 | 312,204 |
| Teradata Corp.* | 11,230 | 462,227 |
| Total System Services, Inc. | 10,827 | 166,519 |
| Visa, Inc. "A" (a) | 32,460 | 2,284,535 |
| Western Union Co. (a) | 44,126 | 819,420 |
| | | **22,885,786** |
| **Office Electronics 0.1%** | | |
| Xerox Corp. | 91,693 | **1,056,303** |
| **Semiconductors & Semiconductor Equipment 2.5%** | | |
| Advanced Micro Devices, Inc.* | 38,427 | 314,333 |
| Altera Corp. (a) | 20,988 | 746,753 |
| Analog Devices, Inc. | 20,041 | 754,944 |
| Applied Materials, Inc. (a) | 89,024 | 1,250,787 |
| Broadcom Corp. "A" | 30,138 | 1,312,510 |
| First Solar, Inc.* (a) | 3,632 | 472,668 |
| Intel Corp. | 372,050 | 7,824,212 |
| KLA-Tencor Corp. (a) | 11,230 | 433,927 |
| Linear Technology Corp. (a) | 14,790 | 511,586 |
| LSI Corp.* | 42,126 | 252,335 |
| MEMC Electronic Materials, Inc.* | 15,124 | 170,296 |
| Microchip Technology, Inc. (a) | 12,100 | 413,941 |
| Micron Technology, Inc.* (a) | 55,740 | 447,035 |
| National Semiconductor Corp. (a) | 16,528 | 227,425 |
| Novellus Systems, Inc.* | 6,031 | 194,922 |
| NVIDIA Corp.* | 38,990 | 600,446 |
| Teradyne, Inc.* (a) | 12,134 | 170,361 |
| Texas Instruments, Inc. (a) | 78,309 | 2,545,043 |
| Xilinx, Inc. | 17,365 | 503,238 |
| | | **19,146,762** |
| **Software 3.9%** | | |
| Adobe Systems, Inc.* | 33,564 | 1,033,100 |
| Autodesk, Inc.* (a) | 15,270 | 583,314 |
| BMC Software, Inc.* | 11,944 | 563,040 |
| CA, Inc. | 25,829 | 631,261 |
| Citrix Systems, Inc.* | 12,614 | 862,924 |
| Compuware Corp.* | 14,854 | 173,346 |
| Electronic Arts, Inc.* | 22,239 | 364,275 |
| Intuit, Inc.* | 18,700 | 921,910 |
| McAfee, Inc.* | 10,014 | 463,748 |
| Microsoft Corp. | 501,985 | 14,015,421 |
| Novell, Inc.* | 23,846 | 141,168 |
| Oracle Corp. | 258,005 | 8,075,557 |
| Red Hat, Inc.* | 12,731 | 581,170 |
| Salesforce.com, Inc.* | 7,798 | 1,029,336 |
| Symantec Corp.* | 51,254 | 857,992 |
| | | **30,297,562** |
| **Materials 3.7%** | | |
| **Chemicals 2.1%** | | |
| Air Products & Chemicals, Inc. | 14,220 | 1,293,309 |
| Airgas, Inc. | 4,968 | 310,301 |
| CF Industries Holdings, Inc. | 4,780 | 646,017 |
| Dow Chemical Co. | 77,356 | 2,640,934 |
| E.I. du Pont de Nemours & Co. (a) | 60,853 | 3,035,348 |
| Eastman Chemical Co. | 4,848 | 407,620 |
| Ecolab, Inc. | 15,348 | 773,846 |
| FMC Corp. (a) | 4,928 | 393,698 |
| International Flavors & Fragrances, Inc. | 5,362 | 298,074 |
| Monsanto Co. | 35,756 | 2,490,048 |
| PPG Industries, Inc. | 10,734 | 902,407 |
| Praxair, Inc. (a) | 20,438 | 1,951,216 |
| Sigma-Aldrich Corp. | 7,904 | 526,090 |
| The Sherwin-Williams Co. | 6,048 | 506,520 |
| | | **16,175,428** |
| **Construction Materials 0.1%** | | |
| Vulcan Materials Co. (a) | 8,646 | **383,536** |
| **Containers & Packaging 0.2%** | | |
| Ball Corp. | 6,004 | 408,572 |
| Bemis Co., Inc. | 7,229 | 236,099 |
| Owens-Illinois, Inc.* | 10,889 | 334,293 |
| Sealed Air Corp. | 10,958 | 278,881 |
| | | **1,257,845** |
| **Metals & Mining 1.2%** | | |
| AK Steel Holding Corp. (a) | 7,385 | 120,893 |
| Alcoa, Inc. | 67,580 | 1,040,056 |
| Allegheny Technologies, Inc. (a) | 6,565 | 362,257 |
| Cliffs Natural Resources, Inc. | 9,134 | 712,543 |
| Freeport-McMoRan Copper & Gold, Inc. | 31,421 | 3,773,348 |
| Newmont Mining Corp. | 32,789 | 2,014,228 |
| Nucor Corp. (a) | 20,873 | 914,655 |
| Titanium Metals Corp.* | 6,057 | 104,059 |
| United States Steel Corp. (a) | 9,671 | 564,980 |
| | | **9,607,019** |
| **Paper & Forest Products 0.1%** | | |
| International Paper Co. | 28,750 | 783,150 |
| MeadWestvaco Corp. | 11,220 | 293,515 |
| | | **1,076,665** |
| **Telecommunication Services 3.1%** | | |
| **Diversified Telecommunication Services 2.8%** | | |
| AT&T, Inc. | 393,944 | 11,574,075 |
| CenturyLink, Inc. (a) | 20,027 | 924,647 |
| Frontier Communications Corp. | 66,817 | 650,129 |
| Qwest Communications International, Inc. | 117,077 | 890,956 |

*The accompanying notes are an integral part of the financial statements.*

| | Shares | Value ($) |
|---|---|---|
| Verizon Communications, Inc. | 188,289 | 6,736,980 |
| Windstream Corp. | 32,607 | 454,542 |
| | | **21,231,329** |
| **Wireless Telecommunication Services 0.3%** | | |
| American Tower Corp. "A"* | 26,565 | 1,371,817 |
| MetroPCS Communications, Inc.* (a) | 17,388 | 219,610 |
| Sprint Nextel Corp.* (a) | 200,650 | 848,749 |
| | | **2,440,176** |
| **Utilities 3.2%** | | |
| **Electric Utilities 1.7%** | | |
| Allegheny Energy, Inc. | 11,335 | 274,761 |
| American Electric Power Co., Inc. | 31,858 | 1,146,251 |
| Duke Energy Corp. (a) | 88,146 | 1,569,880 |
| Edison International | 21,524 | 830,827 |
| Entergy Corp. | 11,957 | 846,914 |
| Exelon Corp. (a) | 44,013 | 1,832,701 |
| FirstEnergy Corp. (a) | 20,054 | 742,399 |
| NextEra Energy, Inc. | 27,569 | 1,433,312 |
| Northeast Utilities | 11,856 | 377,969 |
| Pepco Holdings, Inc. | 14,968 | 273,166 |
| Pinnacle West Capital Corp. | 7,333 | 303,953 |
| PPL Corp. | 32,434 | 853,663 |
| Progress Energy, Inc. | 19,334 | 840,642 |
| Southern Co. (a) | 56,027 | 2,141,912 |
| | | **13,468,350** |
| **Gas Utilities 0.1%** | | |
| Nicor, Inc. (a) | 2,902 | 144,867 |
| ONEOK, Inc. (a) | 7,177 | 398,108 |
| | | **542,975** |
| **Independent Power Producers & Energy Traders 0.1%** | | |
| AES Corp.* | 44,360 | 540,305 |
| Constellation Energy Group, Inc. | 13,438 | 411,606 |
| NRG Energy, Inc.* (a) | 16,637 | 325,087 |
| | | **1,276,998** |
| **Multi-Utilities 1.3%** | | |
| Ameren Corp. | 16,278 | 458,877 |
| CenterPoint Energy, Inc. | 28,412 | 446,637 |
| CMS Energy Corp. | 16,559 | 307,997 |
| Consolidated Edison, Inc. (a) | 19,217 | 952,587 |
| Dominion Resources, Inc. | 39,126 | 1,671,463 |
| DTE Energy Co. | 11,384 | 515,923 |
| Integrys Energy Group, Inc. | 5,205 | 252,494 |
| NiSource, Inc. | 18,623 | 328,137 |
| PG&E Corp. | 26,033 | 1,245,419 |
| Public Service Enterprise Group, Inc. | 33,476 | 1,064,871 |
| SCANA Corp. | 7,561 | 306,977 |
| Sempra Energy | 16,170 | 848,601 |
| TECO Energy, Inc. (a) | 14,226 | 253,223 |
| Wisconsin Energy Corp. | 7,858 | 462,522 |
| Xcel Energy, Inc. | 30,144 | 709,892 |
| | | **9,825,620** |
| **Total Common Stocks** (Cost $686,052,402) | | **761,981,710** |

| | Principal Amount ($) | Value ($) |
|---|---|---|
| **Government & Agency Obligation 0.2%** | | |
| **US Treasury Obligation** | | |
| US Treasury Bill, 0.175%**, 5/5/2011 (b) (Cost $1,354,167) | 1,355,000 | **1,354,325** |

| | Shares | Value ($) |
|---|---|---|
| **Securities Lending Collateral 10.5%** | | |
| Daily Assets Fund Institutional, 0.27% (c) (d) (Cost $80,919,416) | 80,919,416 | **80,919,416** |
| **Cash Equivalents 1.2%** | | |
| Central Cash Management Fund, 0.19% (c) (Cost $9,353,550) | 9,353,550 | **9,353,550** |

| | % of Net Assets | Value ($) |
|---|---|---|
| **Total Investment Portfolio** (Cost $777,679,535)† | 110.4 | **853,609,001** |
| **Other Assets and Liabilities, Net** | (10.4) | **(80,501,113)** |
| **Net Assets** | 100.0 | **773,107,888** |

* *Non-income producing security.*

** *Annualized yield at time of purchase; not a coupon rate.*

† *The cost for federal income tax purposes was $806,292,197. At December 31, 2010, net unrealized appreciation for all securities based on tax cost was $47,316,804. This consisted of aggregate gross unrealized appreciation for all securities in which there was an excess of value over tax cost of $174,402,944 and aggregate gross unrealized depreciation for all securities in which there was an excess of tax cost over value of $127,086,140.*

(a) *All or a portion of these securities were on loan (see Notes to Financial Statements). The value of all securities loaned at December 31, 2010 amounted to $78,984,238, which is 10.2% of net assets.*

(b) *At December 31, 2010, this security has been pledged, in whole or in part, to cover initial margin requirements for open futures contracts.*

(c) *Affiliated fund managed by Deutsche Investment Management Americas Inc. The rate shown is the annualized seven-day yield at period end.*

(d) *Represents collateral held in connection with securities lending. Income earned by the Fund is net of borrower rebates.*

*REIT: Real Estate Investment Trust*

*The accompanying notes are an integral part of the financial statements.*

*At December 31, 2010, open futures contracts purchased were as follows:*

| Futures | Currency | Expiration Date | Contracts | Notional Value ($) | Unrealized Appreciation ($) |
|---|---|---|---|---|---|
| S&P 500 Index | USD | 3/17/2011 | 38 | 11,903,500 | **329,093** |

| **Currency Abbreviation** | |
|---|---|
| USD | United States Dollar |

*For information on the Fund's policy and additional disclosures regarding futures contracts, please refer to Note B in the accompanying Notes to Financial Statements.*

## Fair Value Measurements

*Various inputs are used in determining the value of the Fund's investments. These inputs are summarized in three broad levels. Level 1 includes quoted prices in active markets for identical securities. Level 2 includes other significant observable inputs (including quoted prices for similar securities, interest rates, prepayment speeds, and credit risk). Level 3 includes significant unobservable inputs (including the Fund's own assumptions in determining the fair value of investments). The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities.*

*The following is a summary of the inputs used as of December 31, 2010 in valuing the Fund's investments. For information on the Fund's policy regarding the valuation of investments, please refer to the Security Valuation section of Note A in the accompanying Notes to Financial Statements.*

| Assets | Level 1 | Level 2 | Level 3 | Total |
|---|---|---|---|---|
| Common Stocks (e) | $ 761,981,710 | $ — | $ — | $ 761,981,710 |
| Short-Term Investments (e) | 90,272,966 | 1,354,325 | — | 91,627,291 |
| Derivatives (f) | 329,093 | — | — | 329,093 |
| **Total** | **$ 852,583,769** | **$ 1,354,325** | **$ —** | **$ 853,938,094** |

*There have been no significant transfers in and out of Level 1 and Level 2 fair value measurements during the year ended December 31, 2010.*

(e) *See Investment Portfolio for additional detailed categorizations.*

(f) *Derivatives include unrealized appreciation (depreciation) on open futures contracts.*

*The accompanying notes are an integral part of the financial statements.*

# Statement of Assets and Liabilities

as of December 31, 2010

| | | |
|---|---|---|
| **Assets** | | |
| Investments: | | |
| Investments in securities, at value (cost $687,406,569) — including $78,984,238 of securities loaned | $ | 763,336,035 |
| Investment in Daily Assets Fund Institutional (cost $80,919,416)* | | 80,919,416 |
| Investment in Central Cash Management Fund (cost $9,353,550) | | 9,353,550 |
| Total investments, at value (cost $777,679,535) | | 853,609,001 |
| Dividends receivable | | 905,340 |
| Interest receivable | | 11,514 |
| Receivable for investments sold | | 132,610 |
| Receivable for Fund shares sold | | 18,534 |
| Other assets | | 11,139 |
| Total assets | | 854,688,138 |
| **Liabilities** | | |
| Payable upon return of securities loaned | | 80,919,416 |
| Payable for Fund shares redeemed | | 330,914 |
| Payable for daily variation margin on open futures contracts | | 14,250 |
| Accrued management fee | | 132,346 |
| Accrued expenses and payables | | 183,324 |
| Total liabilities | | 81,580,250 |
| **Net assets, at value** | **$** | **773,107,888** |
| **Net Assets Consist of** | | |
| Undistributed net investment income | | 12,292,276 |
| Net unrealized appreciation (depreciation) on: | | |
| Investments | | 75,929,466 |
| Futures | | 329,093 |
| Accumulated net realized gain (loss) | | (40,506,095) |
| Paid-in capital | | 725,063,148 |
| **Net assets, at value** | **$** | **773,107,888** |
| **Class A** | | |
| **Net Asset Value,** offering and redemption price per share ($699,436,429 ÷ 53,096,781 outstanding shares of beneficial interest, $.001 par value, unlimited number of shares authorized) | **$** | **13.17** |
| **Class B** | | |
| **Net Asset Value,** offering and redemption price per share ($53,454,033 ÷ 4,060,194 outstanding shares of beneficial interest, $.001 par value, unlimited number of shares authorized) | **$** | **13.17** |
| **Class B2** | | |
| **Net Asset Value,** offering and redemption price per share ($20,217,426 ÷ 1,536,957 outstanding shares of beneficial interest, $.001 par value, unlimited number of shares authorized) | **$** | **13.15** |

* *Represents collateral on securities loaned.*

# Statement of Operations

for the year ended December 31, 2010

| | | |
|---|---|---|
| **Investment Income** | | |
| Income: | | |
| Dividends | $ | 15,008,552 |
| Interest | | 3,106 |
| Income distributions — Central Cash Management Fund | | 16,332 |
| Securities lending income, including income from Daily Assets Fund Institutional, net of borrower rebates | | 149,097 |
| Total income | | 15,177,087 |
| Expenses: | | |
| Management fee | | 1,469,763 |
| Administration fee | | 734,882 |
| Custodian fee | | 31,458 |
| Distribution service fees (Class B and Class B2) | | 173,648 |
| Recordkeeping fee (Class B2) | | 29,375 |
| Services to shareholders | | 18,881 |
| Professional fees | | 60,574 |
| Trustees' fees and expenses | | 26,484 |
| Reports to shareholders | | 32,764 |
| Other | | 51,508 |
| Total expenses | | 2,629,337 |
| **Net investment income (loss)** | | **12,547,750** |
| **Realized and Unrealized Gain (Loss)** | | |
| Net realized gain (loss) from: | | |
| Investments | | 10,067,953 |
| Futures | | 1,508,246 |
| | | 11,576,199 |
| Change in net unrealized appreciation (depreciation) on: | | |
| Investments | | 78,005,617 |
| Futures | | 143,053 |
| | | 78,148,670 |
| **Net gain (loss)** | | **89,724,869** |
| **Net increase (decrease) in net assets resulting from operations** | **$** | **102,272,619** |

*The accompanying notes are an integral part of the financial statements.*

# Statement of Changes in Net Assets

| Increase (Decrease) in Net Assets | Years Ended December 31, 2010 | 2009 |
|---|---|---|
| Operations: | | |
| Net investment income (loss) | $ 12,547,750 | $ 13,727,808 |
| Net realized gain (loss) | 11,576,199 | (8,316,684) |
| Change in net unrealized appreciation (depreciation) | 78,148,670 | 156,866,272 |
| Net increase (decrease) in net assets resulting from operations | 102,272,619 | 162,277,396 |
| Distributions to shareholders from: | | |
| Net investment income: | | |
| Class A | (12,705,478) | (17,327,332) |
| Class B | (822,134) | (1,082,916) |
| Class B2 | (300,774) | (464,083) |
| Total distributions | (13,828,386) | (18,874,331) |
| Fund share transactions: | | |
| **Class A** | | |
| Proceeds from shares sold | 34,225,993 | 51,508,341 |
| Reinvestment of distributions | 12,705,478 | 17,327,332 |
| Cost of shares redeemed | (105,618,602) | (105,596,818) |
| Net increase (decrease) in net assets from Class A share transactions | (58,687,131) | (36,761,145) |
| **Class B** | | |
| Proceeds from shares sold | 3,731,491 | 5,682,280 |
| Reinvestment of distributions | 822,134 | 1,082,916 |
| Cost of shares redeemed | (6,731,217) | (6,955,518) |
| Net increase (decrease) in net assets from Class B share transactions | (2,177,592) | (190,322) |
| **Class B2** | | |
| Proceeds from shares sold | 559,322 | 312,854 |
| Reinvestment of distributions | 300,774 | 464,083 |
| Cost of shares redeemed | (3,426,496) | (3,073,750) |
| Net increase (decrease) in net assets from Class B2 share transactions | (2,566,400) | (2,296,813) |
| **Increase (decrease) in net assets** | 25,013,110 | 104,154,785 |
| Net assets at beginning of period | 748,094,778 | 643,939,993 |
| Net assets at end of period (including undistributed net investment income of $12,292,276 and $13,582,034, respectively) | **$ 773,107,888** | **$ 748,094,778** |

| Increase (Decrease) in Net Assets | Years Ended December 31, 2010 | 2009 |
|---|---|---|
| **Class A** | | |
| Shares outstanding at beginning of period | 58,025,792 | 61,222,579 |
| Shares sold | 2,918,830 | 5,559,660 |
| Shares issued to shareholders in reinvestment of distributions | 1,017,252 | 1,969,015 |
| Shares redeemed | (8,865,093) | (10,725,462) |
| Net increase (decrease) in Class A shares | (4,929,011) | (3,196,787) |
| Shares outstanding at end of period | **53,096,781** | **58,025,792** |
| **Class B** | | |
| Shares outstanding at beginning of period | 4,245,476 | 4,244,481 |
| Shares sold | 314,546 | 581,990 |
| Shares issued to shareholders in reinvestment of distributions | 65,771 | 122,919 |
| Shares redeemed | (565,599) | (703,914) |
| Net increase (decrease) in Class B shares | (185,282) | 995 |
| Shares outstanding at end of period | **4,060,194** | **4,245,476** |
| **Class B2** | | |
| Shares outstanding at beginning of period | 1,758,162 | 1,992,383 |
| Shares sold | 46,908 | 32,417 |
| Shares issued to shareholders in reinvestment of distributions | 24,042 | 52,617 |
| Shares redeemed | (292,155) | (319,255) |
| Net increase (decrease) in Class B2 shares | (221,205) | (234,221) |
| Shares outstanding at end of period | **1,536,957** | **1,758,162** |

*The accompanying notes are an integral part of the financial statements.*

# Financial Highlights

## Class A

| Years Ended December 31, | 2010 | 2009 | 2008 | 2007 | 2006 |
|---|---|---|---|---|---|
| **Selected Per Share Data** | | | | | |
| **Net asset value, beginning of period** | **$11.68** | **$ 9.55** | **$15.53** | **$14.97** | **$13.11** |
| *Income (loss) from investment operations:* | | | | | |
| Net investment income (loss)[a] | .21 | .21 | .27 | .27 | .24 |
| Net realized and unrealized gain (loss) | 1.51 | 2.20 | (5.93) | .52 | 1.78 |
| **Total from investment operations** | 1.72 | 2.41 | (5.66) | .79 | 2.02 |
| *Less distributions from:* | | | | | |
| Net investment income | (.23) | (.28) | (.32) | (.23) | (.16) |
| **Net asset value, end of period** | **$13.17** | **$11.68** | **$ 9.55** | **$15.53** | **$14.97** |
| Total Return (%) | 14.70 | 26.32[b] | (37.15)[b] | 5.30[b] | 15.52[b] |
| **Ratios to Average Net Assets and Supplemental Data** | | | | | |
| Net assets, end of period ($ millions) | 699 | 678 | 584 | 1,046 | 1,412 |
| Ratio of expenses before expense reductions (%) | .33 | .34 | .33 | .33 | .28 |
| Ratio of expenses after expense reductions (%) | .33 | .32 | .28 | .30 | .27 |
| Ratio of net investment income (loss) (%) | 1.74 | 2.10 | 2.07 | 1.71 | 1.73 |
| Portfolio turnover rate (%) | 5 | 8 | 6 | 7[c] | 9 |

[a] *Based on average shares outstanding during the period.*

[b] *Total return would have been lower had certain expenses not been reduced.*

[c] *Excludes portfolio securities delivered as a result of processing redemption in-kind transactions.*

## Class B

| Years Ended December 31, | 2010 | 2009 | 2008 | 2007 | 2006 |
|---|---|---|---|---|---|
| **Selected Per Share Data** | | | | | |
| **Net asset value, beginning of period** | **$11.68** | **$ 9.54** | **$15.52** | **$14.96** | **$13.10** |
| *Income (loss) from investment operations:* | | | | | |
| Net investment income (loss)[a] | .18 | .18 | .24 | .23 | .21 |
| Net realized and unrealized gain (loss) | 1.51 | 2.22 | (5.94) | .52 | 1.78 |
| **Total from investment operations** | 1.69 | 2.40 | (5.70) | .75 | 1.99 |
| *Less distributions from:* | | | | | |
| Net investment income | (.20) | (.26) | (.28) | (.19) | (.13) |
| **Net asset value, end of period** | **$13.17** | **$11.68** | **$ 9.54** | **$15.52** | **$14.96** |
| Total Return (%) | 14.52 | 26.03[b] | (37.34)[b] | 5.03[b] | 15.24[b] |
| **Ratios to Average Net Assets and Supplemental Data** | | | | | |
| Net assets, end of period ($ millions) | 53 | 50 | 40 | 65 | 84 |
| Ratio of expenses before expense reductions (%) | .58 | .59 | .58 | .58 | .53 |
| Ratio of expenses after expense reductions (%) | .58 | .57 | .53 | .55 | .52 |
| Ratio of net investment income (loss) (%) | 1.49 | 1.85 | 1.82 | 1.46 | 1.48 |
| Portfolio turnover rate (%) | 5 | 8 | 6 | 7[c] | 9 |

[a] *Based on average shares outstanding during the period.*

[b] *Total return would have been lower had certain expenses not been reduced.*

[c] *Excludes portfolio securities delivered as a result of processing redemption in-kind transactions.*

## Class B2

| Years Ended December 31, | 2010 | 2009 | 2008 | 2007 | 2006 |
|---|---|---|---|---|---|
| **Selected Per Share Data** | | | | | |
| **Net asset value, beginning of period** | **$11.67** | **$ 9.54** | **$15.51** | **$14.96** | **$13.09** |
| *Income (loss) from investment operations:* | | | | | |
| Net investment income (loss)[a] | .16 | .17 | .22 | .21 | .19 |
| Net realized and unrealized gain (loss) | 1.50 | 2.21 | (5.93) | .52 | 1.79 |
| **Total from investment operations** | 1.66 | 2.38 | (5.71) | .73 | 1.98 |
| *Less distributions from:* | | | | | |
| Net investment income | (.18) | (.25) | (.26) | (.18) | (.11) |
| **Net asset value, end of period** | **$13.15** | **$11.67** | **$ 9.54** | **$15.51** | **$14.96** |
| Total Return (%) | 14.29 | 25.79[b] | (37.36)[b] | 4.85[b] | 15.20[b] |
| **Ratios to Average Net Assets and Supplemental Data** | | | | | |
| Net assets, end of period ($ millions) | 20 | 21 | 19 | 48 | 57 |
| Ratio of expenses before expense reductions (%) | .73 | .74 | .72 | .72 | .67 |
| Ratio of expenses after expense reductions (%) | .73 | .70 | .63 | .65 | .63 |
| Ratio of net investment income (loss) (%) | 1.34 | 1.72 | 1.72 | 1.36 | 1.37 |
| Portfolio turnover rate (%) | 5 | 8 | 6 | 7[c] | 9 |

[a] *Based on average shares outstanding during the period.*

[b] *Total return would have been lower had certain expenses not been reduced.*

[c] *Excludes portfolio securities delivered as a result of processing redemption in-kind transactions.*

# Notes to Financial Statements

## A. Organization and Significant Accounting Policies

DWS Investments VIT Funds (the "Trust") is registered under the Investment Company Act of 1940 as amended, (the "1940 Act"), as an open-end management investment company. The Trust is organized as a Massachusetts business trust. The Trust is comprised of two series. DWS Equity 500 Index VIP (the "Fund") is a diversified series of the Trust offered to investors. The Fund is an underlying investment vehicle for variable annuity contracts and variable life insurance policies to be offered by the separate accounts of certain life insurance companies ("Participating Insurance Companies").

**Multiple Classes of Shares of Beneficial Interest.** The Fund offers three classes of shares to investors: Class A shares, Class B shares and Class B2 shares. Class B and Class B2 shares are subject to Rule 12b-1 distribution fees under the 1940 Act and record keeping fees equal to an annual rate up to 0.25% and 0.15%, respectively, of Class B and Class B2 shares average daily net assets. Class A shares are not subject to such fees.

Investment income, realized and unrealized gains and losses, and certain Fund-level expenses and expense reductions, if any, are borne pro rata on the basis of relative net assets by the holders of all classes of shares, except that each class bears certain expenses unique to that class (including the applicable 12b-1 distribution fees and record keeping fees). Differences in class-level expenses may result in payment of different per share dividends by class. All shares have equal rights with respect to voting subject to class-specific arrangements.

The Fund's financial statements are prepared in accordance with accounting principles generally accepted in the United States of America which require the use of management estimates. Actual results could differ from those estimates. The policies described below are followed consistently by the Fund in the preparation of its financial statements.

**Security Valuation.** Investments are stated at value determined as of the close of regular trading on the New York Stock Exchange on each day the exchange is open for trading.

Various inputs are used in determining the value of the Fund's investments. These inputs are summarized in three broad levels. Level 1 includes quoted prices in active markets for identical securities. Level 2 includes other significant observable inputs (including quoted prices for similar securities, interest rates, prepayment speeds, and credit risk). Level 3 includes significant unobservable inputs (including the Fund's own assumptions in determining the fair value of investments). The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities.

Equity securities are valued at the most recent sale price or official closing price reported on the exchange (US or foreign) or over-the-counter market on which they trade and are categorized as Level 1 securities. Securities for which no sales are reported are valued at the calculated mean between the most recent bid and asked quotations on the relevant market or, if a mean cannot be determined, at the most recent bid quotation.

Debt securities are valued by independent pricing services approved by the Fund's Board. If the pricing services are unable to provide valuations, securities are valued at the most recent bid quotation or evaluated price, as applicable, obtained from one or more broker-dealers. Such services may use various pricing techniques which take into account appropriate factors such as yield, quality, coupon rate, maturity, type of issue, trading characteristics and other data, as well as broker quotes. These securities are generally categorized as Level 2.

Futures contracts are generally valued at the settlement prices established each day on the exchange on which they are traded and are categorized as Level 1.

Money market instruments purchased with an original or remaining maturity of sixty days or less, maturing at par, are valued at amortized cost, which approximates value, and are categorized as Level 2. Investments in open-end investment companies are valued at their net asset value each business day and are categorized as Level 1.

Securities and other assets for which market quotations are not readily available or for which the above valuation procedures are deemed not to reflect fair value are valued in a manner that is intended to reflect their fair value as determined in accordance with procedures approved by the Board and are generally categorized as Level 3. In accordance with the Fund's valuation procedures, factors used in determining value may include, but are not limited to, the type of the security; the size of the holding; the initial cost of the security; the existence of any contractual restrictions on the security's disposition; the price and extent of public trading in similar securities of the issuer or of comparable companies; quotations or evaluated prices from broker-dealers and/or pricing services; information obtained from the issuer, analysts, and/or the appropriate stock exchange (for exchange-traded securities); an analysis of the company's or issuer's financial statements; an evaluation of the forces that influence the issuer and the market(s) in which the security is purchased and sold and with respect to debt securities; the maturity, coupon, creditworthiness, currency denomination and the movement of the market

in which the security is normally traded. The value determined under these procedures may differ from published values for the same securities.

Disclosure about the classification of fair value measurements is included in a table following the Fund's Investment Portfolio.

**Securities Lending.** The Fund lends securities to certain financial institutions. The Fund retains beneficial ownership of the securities it has loaned and continues to receive interest and dividends paid by the issuer of securities and to participate in any changes in their market value. The Fund requires the borrowers of the securities to maintain collateral with the Fund consisting of either cash or liquid, unencumbered assets having a value at least equal to the value of the securities loaned. When the collateral falls below specified amounts, the lending agent will use its best effort to obtain additional collateral on the next business day to meet required amounts under the security lending agreement. The Fund may invest the cash collateral into a joint trading account in an affiliated money market fund pursuant to Exemptive Orders issued by the SEC. The Fund receives compensation for lending its securities either in the form of fees or by earning interest on invested cash collateral net of borrower rebates and fees paid to a lending agent. Either the Fund or the borrower may terminate the loan. There may be risks of delay and costs in recovery of securities or even loss of rights in the collateral should the borrower of the securities fail financially. The Fund is also subject to all investment risks associated with the reinvestment of any cash collateral received, including, but not limited to, interest rate, credit and liquidity risk associated with such investments.

**Federal Income Taxes.** The Fund's policy is to comply with the requirements of the Internal Revenue Code, as amended, which are applicable to regulated investment companies, and to distribute all of its taxable and tax-exempt income to its shareholders.

At December 31, 2010, the Fund had a net tax basis capital loss carryforward of approximately $11,647,000, including $1,072,000 inherited from its merger with an affiliated fund in fiscal year 2005, which may be applied against any realized net taxable capital gains of each succeeding year until fully utilized or until December 31, 2012 ($1,072,000) and December 31, 2017 ($10,575,000), the respective expiration dates, whichever occurs first, subject to certain limitations under Sections 382–384 of the Internal Revenue Code.

During the year ended December 31, 2010, the Fund utilized $15,534,000 of prior year capital losss carryforward.

The Fund has reviewed the tax positions for the open tax years as of December 31, 2010 and has determined that no provision for income tax is required in the Fund's financial statements. The Fund's federal tax returns for the prior three fiscal years remain open subject to examination by the Internal Revenue Service.

**Distribution of Income and Gains.** Net investment income of the Fund, if any, is declared and distributed to shareholders annually. Net realized gains from investment transactions, in excess of available capital loss carryforwards, would be taxable to the Fund if not distributed, and, therefore, will be distributed to shareholders at least annually.

The timing and characterization of certain income and capital gains distributions are determined annually in accordance with federal tax regulations, which may differ from accounting principles generally accepted in the United States of America. These differences primarily relate to investments in futures contracts and certain securities sold at a loss. As a result, net investment income (loss) and net realized gain (loss) on investment transactions for a reporting period may differ significantly from distributions during such period. Accordingly, the Fund may periodically make reclassifications among certain of its capital accounts without impacting the net asset value of the Fund.

At December 31, 2010, the Fund's components of distributable earnings (accumulated gains) on a tax basis were as follows:

| | |
|---|---|
| Undistributed ordinary income | $ 12,292,276 |
| Capital loss carryforwards | $ (11,647,000) |
| Unrealized appreciation (depreciation) on investments | $ 47,316,804 |

In addition, the tax character of distributions paid to shareholders by the Fund is summarized as follows:

| | **Years Ended December 31,** | |
|---|---|---|
| | **2010** | **2009** |
| Distributions from ordinary income | $ 13,828,386 | $ 18,874,331 |

**Contingencies.** In the normal course of business, the Fund may enter into contracts with service providers that contain general indemnification clauses. The Fund's maximum exposure under these arrangements is unknown as this would involve future claims that may be made against the Fund that have not yet been made. However, based on experience, the Fund expects the risk of loss to be remote.

**Expenses.** Expenses of the Trust arising in connection with a specific Fund are allocated to that Fund. Other Trust expenses which cannot be directly attributed to a fund are apportioned among the funds in the Trust.

**Other.** Investment transactions are accounted for on a trade date plus one basis for daily net asset valuation calculations. However, for financial reporting purposes, investment transactions are reported on trade date. Interest income is recorded on the accrual basis. Dividend income is recorded on the ex-dividend date. Realized gains and losses from investment transactions are recorded on an identified cost basis.

## B. Derivative Instruments

**Futures Contracts.** A futures contract is an agreement between a buyer or seller and an established futures exchange or its clearinghouse in which the buyer or seller agrees to take or make a delivery of a specific amount of a financial instrument at a specified price on a specific date (settlement date). For the year ended December 31, 2010, the Fund invested in futures to keep cash on hand to meet shareholder redemptions or other needs while maintaining exposure to the stock market.

Futures contracts are valued at the most recent settlement price. Upon entering into a futures contract, the Fund is required to deposit with a financial intermediary cash or securities ("initial margin") in an amount equal to a certain percentage of the face value indicated in the futures contract. Subsequent payments ("variation margin") are made or received by the Fund dependent upon the daily fluctuations in the value and are recorded for financial reporting purposes as unrealized gains or losses by the Fund. Gains or losses are realized when the contract expires or is closed. Since all futures contracts are exchange traded, counterparty risk is minimized as the exchange's clearinghouse acts as the counterparty, and guarantees the futures against default. Upon a futures contract close out or expiration, realized gain or loss is recognized.

Certain risks may arise upon entering into futures contracts, including the risk that an illiquid market will limit the Fund's ability to close out a futures contract prior to the settlement date and that a change in the value of a futures contract may not correlate exactly with the changes in the value of the underlying hedged security, index or currency. Risk of loss may exceed amounts recognized in the Statement of Assets and Liabilities.

A summary of the open futures contracts as of December 31, 2010 is included in a table following the Fund's Investment Portfolio. For the year ended December 31, 2010, the investment in futures contracts purchased had a total notional value generally indicative of a range from approximately $11,036,000 to $15,914,000.

The following tables summarize the value of the Fund's derivative instruments held as of December 31, 2010 and the related location in the accompanying Statement of Assets and Liabilities, presented by primary underlying risk exposure:

| Liability Derivatives | Futures Contracts |
|---|---|
| Equity Contracts (a) | $ 329,093 |

*The above derivative is located in the following Statement of Assets and Liabilities account:*

(a) *Net unrealized appreciation (depreciation) on futures. Liability of payable for daily variation margin on open futures contracts reflects unsettled variation margin.*

Additionally, the amount of unrealized and realized gains and losses on derivative instruments recognized in Fund earnings during the year ended December 31, 2010 and the related location in the accompanying Statement of Operations is summarized in the following tables by primary underlying risk exposure:

| Realized Gain (Loss) | Futures Contracts |
|---|---|
| Equity Contracts (a) | $ 1,508,246 |

*The above derivative is located in the following Statement of Operations account:*

(a) *Net realized gain (loss) from futures*

| Change in Net Unrealized Appreciation (Depreciation) | Futures Contracts |
|---|---|
| Equity Contracts (a) | $ 143,053 |

*The above derivative is located in the following Statement of Operations account:*

(a) *Change in net unrealized appreciation (depreciation) on futures*

## C. Purchases and Sales of Securities

During the year ended December 31, 2010, purchases and sales of investment securities (excluding short-term investments) aggregated $38,190,141 and $98,705,787, respectively.

## D. Related Parties

**Management Agreement.** Under the Investment Management Agreement with Deutsche Investment Management Americas Inc. ("DIMA" or the "Advisor"), an indirect, wholly owned subsidiary of Deutsche Bank AG, the Advisor determines the securities, instruments and other contracts relating to investments to be purchased, sold, or entered into by the Fund or delegates such responsibility to the Fund's sub-advisor. Pursuant to the Investment Management Agreement with the Advisor, the Fund pays an annual management fee based on the Fund's average daily net assets, computed and accrued daily and payable monthly, at the following annual rates:

| | |
|---|---|
| First $1 billion of the Fund's average daily net assets | .200% |
| Next $1 billion of such net assets | .175% |
| Over $2 billion of such net assets | .150% |

Accordingly, for the year ended December 31, 2010, the fee pursuant to the management agreement was equivalent to an annual effective rate of 0.20% of the Fund's average daily net assets.

Northern Trust Investments, Inc. ("NTI") acts as investment sub-advisor for the Fund. As the Fund's investment sub-advisor, NTI makes the Fund's investment decisions. It buys and sells securities for the Fund and conducts the research that leads to these purchase and sale decisions. NTI is paid by the Advisor for its services.

**Administration Fee.** Pursuant to the Administrative Services Agreement, DIMA provides most administrative services to the Fund. For all services provided under the Administrative Services Agreement, the Fund pays DIMA an annual fee ("Administration Fee") of 0.10% of the Fund's average daily net assets, computed and accrued daily and payable monthly. For the year ended December 31, 2010, the Administration Fee was $734,882, of which $65,511 is unpaid.

**Distribution Service Agreement.** DWS Investments Distributors, Inc. ("DIDI"), an affiliate of the Advisor, is the Fund's distributor. In accordance with the Distribution Plan, DIDI receives 12b-1 fees of 0.25% of average daily net assets of Class B and B2 shares. For the year ended December 31, 2010, the Distribution Service Fees were as follows:

| **Distribution Service Fees** | **Total Aggregated** | **Unpaid at December 31, 2010** |
|---|---|---|
| Class B | $ 124,689 | $ 11,214 |
| Class B2 | 48,959 | 4,260 |
| | **$ 173,648** | **$ 15,474** |

**Service Provider Fees.** DWS Investments Service Company ("DISC"), an affiliate of the Advisor, is the transfer agent, dividend-paying agent and shareholder service agent of the Fund. Pursuant to a sub-transfer agency agreement among DISC and DST Systems, Inc. ("DST"), DISC has delegated certain transfer agent, dividend-paying agent and shareholder service agent functions to DST. DISC compensates DST out of the shareholder servicing fee they receive from the Fund. For the year ended December 31, 2010, the amounts charged to the Fund by DISC were as follows:

| **Services to Shareholders** | **Total Aggregated** | **Unpaid at December 31, 2010** |
|---|---|---|
| Class A | $ 706 | $ 175 |
| Class B | 101 | 24 |
| Class B2 | 48 | 12 |
| | **$ 855** | **$ 211** |

**Typesetting and Filing Service Fees.** Under an agreement with DIMA, DIMA is compensated for providing typesetting and certain regulatory filing services to the Fund. For the year ended December 31, 2010, the amount charged to the Fund by DIMA included in the Statement of Operations under "reports to shareholders" aggregated $20,402, of which $7,585 is unpaid.

**Trustees' Fees and Expenses.** The Fund paid each Trustee not affiliated with the Advisor retainer fees plus specified amounts for various committee services and for the Board Chairperson.

**Affiliated Cash Management Vehicles.** The Fund may invest uninvested cash balances in Central Cash Management Fund, which is managed by the Advisor. The Fund indirectly bears its proportionate share of the expenses of the underlying money market funds. Central Cash Management Fund does not pay the Advisor an investment management fee. Central Cash Management Fund seeks a high level of current income consistent with liquidity and the preservation of capital.

## E. Line of Credit

The Fund and other affiliated funds (the "Participants") share in a $450 million revolving credit facility provided by a syndication of banks. The Fund may borrow for temporary or emergency purposes, including the meeting of redemption requests that otherwise might require the untimely disposition of securities. The Participants are charged an annual commitment fee which is allocated based on net assets, among each of the Participants. Interest is calculated at a rate per annum equal to the sum of the Federal Funds Rate plus 1.25 percent plus if LIBOR exceeds the Federal Funds Rate the amount of such excess. The Fund may borrow up to a maximum of 33 percent of its net assets under the agreement.

## F. Ownership of the Fund

At December 31, 2010, two participating insurance companies were beneficial owners of record of 10% or more of the total outstanding Class A shares of the Fund, each owning 61% and 11%, respectively. At December 31, 2010, one participating insurance company was a beneficial owner of record of 10% or more of the total outstanding Class B shares of the Fund, owning 87%. At December 31, 2010, one participating insurance company was a beneficial owner of record of 100% of the total outstanding Class B2 shares of the Fund.

# Report of Independent Registered Public Accounting Firm

**To the Trustees of DWS Investments VIT Funds and the Shareholders of DWS Equity 500 Index VIP:**

In our opinion, the accompanying statement of assets and liabilities, including the investment portfolio, and the related statements of operations and of changes in net assets and the financial highlights present fairly, in all material respects, the financial position of DWS Equity 500 Index VIP (the "Fund") at December 31, 2010, and the results of its operations, the changes in its net assets and the financial highlights for each of the periods indicated therein, in conformity with accounting principles generally accepted in the United States of America. These financial statements and financial highlights (hereafter referred to as "financial statements") are the responsibility of the Fund's management. Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these financial statements in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits, which included confirmation of securities at December 31, 2010 by correspondence with the custodian and brokers, provide a reasonable basis for our opinion.

Boston, Massachusetts
February 11, 2011

PricewaterhouseCoopers LLP

## Tax Information **(Unaudited)**

For corporate shareholders, 100% of the income dividends paid during the Fund's fiscal year ended December 31, 2010 qualified as a dividends received deduction.

Please consult a tax advisor if you have questions about federal or state income tax laws, or on how to prepare your tax returns. If you have specific questions about your account, please contact your insurance provider.

## Proxy Voting

The Fund's policies and procedures for voting proxies for portfolio securities and information about how the Fund voted proxies related to its portfolio securities during the 12-month period ended June 30 are available on our Web site — www.dws-investments.com (click on "proxy voting" at the bottom of the page) — or on the SEC's Web site — www.sec.gov. To obtain a written copy of the Fund's policies and procedures without charge, upon request, call us toll free at (800) 728-3337.

# Investment Management Agreement Approval

The Board of Trustees, including the Independent Trustees, approved the renewal of your Fund's investment management agreement (the "Agreement") with Deutsche Investment Management Americas Inc. ("DWS") and sub-advisory agreement (the "Sub-Advisory Agreement," and together with the Agreement, the "Agreements") between DWS and Northern Trust Investments, Inc. ("NTI") in September 2010.

In terms of the process that the Board followed prior to approving the Agreements, shareholders should know that:

- In September 2010, all of the Fund's Trustees were independent of DWS and its affiliates.
- The Trustees meet frequently to discuss fund matters. Each year, the Trustees dedicate substantial time to contract review matters. Over the course of several months, the Board's Contract Committee, in coordination with the Board's Equity Oversight Committee, reviewed comprehensive materials received from DWS, independent third parties and independent counsel. These materials included an analysis of the Fund's performance, fees and expenses, and profitability compiled by the Fund's independent fee consultant. The Board also received extensive information throughout the year regarding performance of the Fund.
- The Independent Trustees regularly meet privately with their independent counsel to discuss contract review and other matters. In addition, the Independent Trustees were also advised by the Fund's independent fee consultant in the course of their review of the Fund's contractual arrangements and considered a comprehensive report prepared by the independent fee consultant in connection with their deliberations (the "IFC Report").
- In connection with reviewing the Agreements, the Board also reviewed the terms of the Fund's Rule 12b-1 Plan, distribution agreement, administrative services agreement, transfer agency agreement and other material service agreements.
- Based on its evaluation of the information provided, the Contract Committee presented its findings and recommendations to the Independent Trustees as a group. The Independent Trustees reviewed the Contract Committee's findings and recommendations and presented their recommendations to the full Board.

In connection with the contract review process, the Contract Committee and the Board considered the factors discussed below, among others. The Board also considered that DWS and its predecessors have managed the Fund since its inception, and the Board believes that a long-term relationship with a capable, conscientious advisor is in the best interests of the Fund. The Board considered, generally, that shareholders chose to invest or remain invested in the Fund knowing that DWS managed the Fund, and that the Agreements were approved by the Fund's shareholders. DWS is part of Deutsche Bank, a major global banking institution that is engaged in a wide range of financial services. The Board believes that there are significant advantages to being part of a global asset management business that offers a wide range of investing expertise and resources, including hundreds of portfolio managers and analysts with research capabilities in many countries throughout the world.

While shareholders may focus primarily on fund performance and fees, the Fund's Board considers these and many other factors, including the quality and integrity of DWS's and NTI's personnel and such other issues as back-office operations, fund valuations, and compliance policies and procedures.

**Nature, Quality and Extent of Services.** The Board considered the terms of the Agreements, including the scope of advisory services provided under the Agreements. The Board noted that, under the Agreements, DWS and NTI provide portfolio management services to the Fund and that, pursuant to a separate administrative services agreement, DWS provides administrative services to the Fund. The Board considered the experience and skills of senior management and investment personnel, the resources made available to such personnel, the ability of DWS to attract and retain high-quality personnel, and the organizational depth and stability of DWS. The Board reviewed the Fund's performance over short-term and long-term periods and compared those returns to various agreed-upon performance measures, including market indices and a peer universe compiled by the independent fee consultant using information supplied by Lipper Inc. ("Lipper"). The Board also noted that it has put into place a process of identifying "Focus Funds" (e.g., funds performing poorly relative to their benchmark or a peer universe compiled by Lipper), and receives more frequent reporting and information from DWS regarding such funds, along with DWS's remedial plans to address underperformance. The Board believes this process is an effective manner of identifying and addressing underperforming funds. Based on the information provided, the Board noted that for the one-, three- and five-year periods ended December 31, 2009, the Fund's performance (Class A shares) was in the 1st quartile of the applicable Lipper universe (the 1st quartile being the best performers and the 4th quartile being the worst performers).

On the basis of this evaluation and the ongoing review of investment results by the Board, the Board concluded that the nature, quality and extent of services provided by DWS and NTI historically have been and continue to be satisfactory.

**Fees and Expenses.** The Board considered the Fund's investment management fee schedule, sub-advisory fee schedule, operating expenses, and total expense ratios, and comparative information provided by Lipper and the independent fee consultant regarding investment management fee rates paid to other investment advisors by similar funds (1st quartile being the most favorable and 4th quartile being the least favorable). With respect to management fees paid to other investment advisors by similar funds, the Board noted that the contractual fee rates paid by the Fund, which include the 0.10% fee paid to DWS under the Fund's administrative services agreement, were at the median (2nd quartile) of the applicable Lipper peer group (based on Lipper data provided as of December 31, 2009). With respect to the sub-advisory fee paid to NTI, the Board noted that the fee is paid by DWS out of its fee and not directly by the Fund. The Board noted that the Fund's Class A shares total (net) operating expenses were expected to be higher than the median (3rd quartile) of the applicable Lipper expense universe (based on Lipper data provided as of December 31, 2009, and analyzing Lipper expense universe Class A expenses less any applicable 12b-1 fees) ("Lipper Universe Expenses"). The Board also reviewed data comparing each share class's total (net) operating expenses to the applicable Lipper Universe Expenses. The Board considered the Fund's management fee rate as compared to fees charged by DWS and certain of its affiliates for comparable mutual funds and considered differences in fund and fee structures between the DWS Funds. The Board also considered how the Fund's total (net) operating expenses compared to the total (net) operating expenses of a more customized peer group selected by Lipper (based on factors as asset size).

The information considered by the Board as part of its review of management fees included information regarding fees charged by DWS and its affiliates to similar institutional accounts and to similar funds offered primarily to European investors ("DWS Europe funds"), in each case as applicable. The Board observed that advisory fee rates for institutional accounts generally were lower than the management fees charged by similarly managed DWS US mutual funds ("DWS Funds"), but also took note of the differences in services provided to DWS Funds as compared to institutional accounts. In the case of DWS Europe funds, the Board observed that fee rates for DWS Europe funds generally were higher than for similarly managed DWS Funds, but noted that differences in the types of services provided to DWS Funds relative to DWS Europe funds made it difficult to compare such fees.

On the basis of the information provided, the Board concluded that management fees were reasonable and appropriate in light of the nature, quality and extent of services provided by DWS and NTI.

**Profitability.** The Board reviewed detailed information regarding revenues received by DWS under the Agreement. The Board considered the estimated costs and pre-tax profits realized by DWS from advising the DWS Funds, as well as estimates of the pre-tax profits attributable to managing the Fund in particular. The Board also received information regarding the estimated enterprise-wide profitability of DWS and its affiliates with respect to all fund services in totality and by fund. The Board reviewed DWS's methodology in allocating its costs to the management of the Fund. Based on the information provided, the Board concluded that the pre-tax profits realized by DWS in connection with the management of the Fund were not unreasonable. The Board also reviewed information regarding the profitability of certain similar investment management firms. The Board noted that while information regarding the profitability of such firms is limited (and in some cases is not necessarily prepared on a comparable basis), DWS and its affiliates' overall profitability with respect to the DWS fund complex (after taking into account distribution and other services provided to the funds by DWS and its affiliates) was lower than the overall profitability levels of many comparable firms for which such data was available. The Board did not consider the profitability of NTI with respect to the Fund. The Board noted that DWS pays NTI's fee out of its management fee, and its understanding that the Fund's sub-advisory fee schedule was the product of an arm's length negotiation with DWS.

**Economies of Scale.** The Board considered whether there are economies of scale with respect to the management of the Fund and whether the Fund benefits from any economies of scale. The Board noted that the Fund's management fee schedule includes fee breakpoints. The Board concluded that the Fund's fee schedule represents an appropriate sharing between the Fund and DWS of such economies of scale as may exist in the management of the Fund at current asset levels.

**Other Benefits to DWS and NTI and Their Affiliates.** The Board also considered the character and amount of other incidental benefits received by DWS and NTI and their affiliates, including any fees received by DWS for administrative services provided to the Fund and any fees received by an affiliate of DWS for distribution services. The Board also considered benefits to DWS and NTI related to brokerage and soft-dollar allocations, including allocating brokerage to pay for research generated by parties other than the executing broker dealers, which pertain primarily to funds investing in equity securities, along with the incidental public relations benefits to DWS and NTI related to DWS Funds advertising and cross-selling opportunities among DWS products and services. The Board concluded that management fees were reasonable in light of these fallout benefits.

**Compliance.** The Board considered the significant attention and resources dedicated by DWS to documenting and enhancing its compliance processes in recent years. The Board noted in particular (i) the experience and seniority of both DWS's chief compliance officer and the Fund's chief compliance officer; (ii) the large number of DWS compliance personnel; and (iii) the substantial commitment of resources by DWS and its affiliates to compliance matters. The Board also considered the attention and resources dedicated by DWS to the oversight of the investment sub-advisor's compliance program and compliance with the applicable fund policies and procedures.

Based on all of the information considered and the conclusions reached, the Board unanimously determined that the continuation of the Agreements is in the best interests of the Fund. In making this determination, the Board did not give particular weight to any single factor identified above. The Board considered these factors over the course of numerous meetings, certain of which were in executive session with only the Independent Trustees and their counsel present. It is possible that individual Trustees may have weighed these factors differently in reaching their individual decisions to approve the continuation of the Agreements.

# Summary of Management Fee Evaluation by Independent Fee Consultant

October 3, 2010

Pursuant to an Order entered into by Deutsche Investment Management Americas and affiliates (collectively, "DeAM") with the Attorney General of New York, I, Thomas H. Mack, have been appointed the Independent Fee Consultant for the DWS Funds (formerly the DWS Scudder Funds). My duties include preparing an annual written evaluation of the management fees DeAM charges the Funds, considering among other factors the management fees charged by other mutual fund companies for like services, management fees DeAM charges other clients for like services, DeAM's costs of supplying services under the management agreements and related profit margins, possible economies of scale if a Fund grows larger, and the nature and quality of DeAM's services, including fund performance. This report summarizes my evaluation for 2010, including my qualifications, the evaluation process for each of the DWS Funds, consideration of certain complex-level factors, and my conclusions. I served in substantially the same capacity in 2007, 2008, and 2009.

## Qualifications

For more than 35 years I have served in various professional capacities within the investment management business. I have held investment analysis and advisory positions, including securities analyst, portfolio strategist and director of investment policy with a large investment firm. I have also performed business management functions, including business development, financial management and marketing research and analysis.

Since 1991, I have been an independent consultant within the asset management industry. I have provided services to over 125 client organizations, including investment managers, mutual fund boards, product distributors and related organizations. Over the past ten years I have completed a number of assignments for mutual fund boards, specifically including assisting boards with management contract renewal.

I hold a Master of Business Administration degree, with highest honors, from Harvard University and Master of Science and Bachelor of Science (highest honors) degrees from the University of California at Berkeley. I am an independent director and audit committee financial expert for two closed-end mutual funds and have served in various leadership and financial oversight capacities with non-profit organizations.

## Evaluation of Fees for each DWS Fund

My work focused primarily on evaluating, fund-by-fund, the fees charged to each of the 118 publicly offered Fund portfolios in the DWS Fund family. For each Fund, I considered each of the key factors mentioned above, as well as any other relevant information. In doing so I worked closely with the Funds' Independent Directors in their annual contract renewal process, as well as in their approval of contracts for several new funds (documented separately).

In evaluating each Fund's fees, I reviewed comprehensive materials provided by or on behalf of DeAM, including expense information prepared by Lipper Analytical, comparative performance information, profitability data, manager histories, and other materials. I also accessed certain additional information from the Lipper and Morningstar databases and drew on my industry knowledge and experience.

To facilitate evaluating this considerable body of information, I prepared for each Fund a document summarizing the key data elements in each area as well as additional analytics discussed below. This made it possible to consider each key data element in the context of the others.

In the course of contract renewal, DeAM agreed to implement a number of fee and expense adjustments requested by the Independent Directors which will favorably impact future fees and expenses, and my evaluation includes the effects of these changes.

### Fees and Expenses Compared with Other Funds

The competitive fee and expense evaluation for each fund focused on two primary comparisons:

- The Fund's contractual management fee (the advisory fee plus the administration fee where applicable) compared with those of a group of typically 12–15 funds in the same Lipper investment category (e.g. Large Capitalization Growth) having similar distribution arrangements and being of similar size.
- The Fund's total expenses compared with a broader universe of funds from the same Lipper investment category and having similar distribution arrangements.

These two comparisons provide a view of not only the level of the fee compared with funds of similar scale but also the total expense the Fund bears for all the services it receives, in comparison with the investment choices available in the Fund's investment category and distribution channel. The principal figure-of-merit used in these comparisons was the subject Fund's percentile ranking against peers.

### DeAM's Fees for Similar Services to Others

DeAM provided management fee schedules for all of its US domiciled fund and non-fund investment management accounts in any of the investment categories where there is a DWS Fund. These similar products included the other DWS Funds, non-fund pooled accounts, institutional accounts and sub-advisory accounts. Using this information, I calculated for each Fund the fee that would be charged to each similar product, at the subject Fund's asset level.

Evaluating information regarding non-fund products is difficult because there are varying levels of services required for different types of accounts, with mutual funds generally requiring considerably more regulatory and administrative types of service as well as having more frequent cash flows than other types of accounts. Also, while mutual fund fees for similar fund products can be expected to be similar, there will be some differences due to different pricing conditions in different distribution channels (e.g. retail funds versus those used in variable insurance products), differences in underlying investment processes and other factors.

**Costs and Profit Margins**

DeAM provided a detailed profitability analysis for each Fund. After making some adjustments so that the presentation would be more comparable to the available industry figures, I reviewed profit margins from investment management alone, from investment management plus other fund services (excluding distribution) provided to the Funds by DeAM (principally shareholder services), and DeAM profits from all sources, including distribution. A later section comments on overall profitability.

**Economies of Scale**

Economies of scale — an expected decline in management cost per dollar of fund assets as fund assets grow — are very rarely quantified and documented because of inherent difficulties in collecting and analyzing relevant data. However, in virtually every investment category that I reviewed, larger funds tend to have lower fees and lower total expenses than smaller funds. To see how each DWS Fund compares with this industry observation, I reviewed:

- The trend in Fund assets over the last five years and the accompanying trend in total expenses. This shows if the Fund has grown and, if so, whether total expense (management fees as well as other expenses) have declined as a percent of assets.
- Whether the Fund has break-points in its management fee schedule, the extent of the fee reduction built into the schedule and the asset levels where the breaks take effect, and in the case of a sub-advised Fund how the Fund's break-points compare with those of the sub-advisory fee schedule.
- How the Fund's contractual fee schedule compares with trends in the industry data. To accomplish this, I constructed a chart showing how actual latest-fiscal-year contractual fees of the Fund and of other similar funds relate to average fund assets, with the subject Fund's contractual fee schedule superimposed.

**Quality of Service — Performance**

The quality-of-service evaluation focused on investment performance, which is the principal result of the investment management service. Each Fund's performance was reviewed over the past 1, 3, 5 and 10 years, as applicable, and compared with that of other funds in the same investment category and with a suitable market index.

In addition, I calculated and reviewed risk-adjusted returns relative to an index of similar mutual funds' returns and a suitable market index. The risk-adjusted returns analysis provides a way of determining the extent to which the Fund's return comparisons are mainly the product of investment value-added (or lack thereof) or alternatively taking considerably more or less risk than is typical in its investment category.

I also received and considered the history of portfolio manager changes for each Fund, as this provided an important context for evaluating the performance results.

## Complex-Level Considerations

While this evaluation was conducted mainly at the individual fund level, there are some issues relating to the reasonableness of fees that can alternatively be considered across the whole fund complex:

- I reviewed DeAM's profitability analysis for all DWS Funds, with a view toward determining if the allocation procedures used were reasonable and how profit levels compared with public data for other investment managers.
- I considered whether DeAM and affiliates receive any significant ancillary or "fall-out" benefits that should be considered in interpreting the direct profitability results. These would be situations where serving as the investment manager of the Funds is beneficial to another part of the Deutsche Bank organization.
- I considered how aggregated DWS Fund expenses had varied over the years, by asset class and in the context of trends in asset levels.
- I reviewed the structure of the DeAM organization, trends in staffing levels, and information on compensation of investment management and other professionals compared with industry data.

## Findings

Based on the process and analysis discussed above, which included reviewing a wide range of information from management and external data sources and considering among other factors the fees DeAM charges other clients, the fees charged by other fund managers, DeAM's costs and profits associated with managing the Funds, economies of scale, possible fall-out benefits, and the nature and quality of services provided, in my opinion the management fees charged the DWS Funds are reasonable.

Thomas H. Mack

Thomas H. Mack

# Board Members and Officers

The following table presents certain information regarding the Board Members and Officers of the Trust as of December 31, 2010. Each Board Member's year of birth is set forth in parentheses after his or her name. Unless otherwise noted, (i) each Board Member has engaged in the principal occupation(s) noted in the table for at least the most recent five years, although not necessarily in the same capacity; and (ii) the address of each Independent Board Member is c/o Paul K. Freeman, Independent Chairman, DWS Funds, PO Box 101833, Denver, CO 80250-1833. Except as otherwise noted below, the term of office for each Board Member is until the election and qualification of a successor, or until such Board Member sooner dies, resigns, is removed or as otherwise provided in the governing documents of the fund. Because the fund does not hold an annual meeting of shareholders, each Board Member will hold office for an indeterminate period. The Board Members may also serve in similar capacities with other funds in the fund complex. The Length of Time Served represents the year in which the Board Member joined the board of one or more DWS funds now overseen by the Board.

### Independent Board Members

| Name, Year of Birth, Position with the Fund and Length of Time Served[1] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Paul K. Freeman (1950)<br>Chairperson since 2009<br>Board Member since 1993 | Consultant, World Bank/Inter-American Development Bank; Executive and Governing Council of the Independent Directors Council (education committees); formerly, Project Leader, International Institute for Applied Systems Analysis (1998–2001); Chief Executive Officer, The Eric Group, Inc. (environmental insurance) (1986–1998) | 122 |
| John W. Ballantine (1946)<br>Board Member since 1999 | Retired; formerly, Executive Vice President and Chief Risk Management Officer, First Chicago NBD Corporation/The First National Bank of Chicago (1996–1998); Executive Vice President and Head of International Banking (1995–1996). Directorships: Healthways, Inc. (provider of disease and care management services); Portland General Electric (utility company); Stockwell Capital Investments PLC (private equity). Former Directorships: First Oak Brook Bancshares, Inc. and Oak Brook Bank; Prisma Energy International | 122 |
| Henry P. Becton, Jr. (1943)<br>Board Member since 1990 | Vice Chair and former President, WGBH Educational Foundation. Directorships: Association of Public Television Stations; Lead Director, Becton Dickinson and Company[3] (medical technology company); Lead Director, Belo Corporation[3] (media company); Public Radio International; Public Radio Exchange (PRX); The PBS Foundation. Former Directorships: Boston Museum of Science; American Public Television; Concord Academy; New England Aquarium; Mass. Corporation for Educational Telecommunications; Committee for Economic Development; Public Broadcasting Service | 122 |
| Dawn-Marie Driscoll (1946)<br>Board Member since 1987 | President, Driscoll Associates (consulting firm); Executive Fellow, Center for Business Ethics, Bentley University; formerly, Partner, Palmer & Dodge (1988–1990); Vice President of Corporate Affairs and General Counsel, Filene's (1978–1988). Directorships: Trustee of 22 open-end mutual funds managed by Sun Capital Advisers, Inc. (since 2007); Director of ICI Mutual Insurance Company (since 2007); Advisory Board, Center for Business Ethics, Bentley University; Trustee, Southwest Florida Community Foundation (charitable organization). Former Directorships: Investment Company Institute (audit, executive, nominating committees) and Independent Directors Council (governance, executive committees) | 122 |
| Keith R. Fox (1954)<br>Board Member since 1996 | Managing General Partner, Exeter Capital Partners (a series of private investment funds). Directorships: Progressive International Corporation (kitchen goods importer and distributor); BoxTop Media Inc. (advertising); The Kennel Shop (retailer); former Chairman, National Association of Small Business Investment Companies | 122 |
| Kenneth C. Froewiss (1945)<br>Board Member since 2001 | Adjunct Professor of Finance, NYU Stern School of Business (September 2009–present; Clinical Professor from 1997–September 2009); Member, Finance Committee, Association for Asian Studies (2002–present); Director, Mitsui Sumitomo Insurance Group (US) (2004–present); prior thereto, Managing Director, J.P. Morgan (investment banking firm) (until 1996) | 122 |
| Richard J. Herring (1946)<br>Board Member since 1990 | Jacob Safra Professor of International Banking and Professor, Finance Department, The Wharton School, University of Pennsylvania (since July 1972); Co-Director, Wharton Financial Institutions Center (since July 2000); Co-Chair, U.S. Shadow Financial Regulatory Committee; Executive Director, Financial Economists Roundtable; Director, Japan Equity Fund, Inc. (since September 2007), Thai Capital Fund, Inc. (since September 2007), Singapore Fund, Inc. (since September 2007); Independent Director of Barclays Bank Delaware (since September 2010). Formerly, Vice Dean and Director, Wharton Undergraduate Division (July 1995–June 2000); Director, Lauder Institute of International Management Studies (July 2000–June 2006) | 122 |
| William McClayton (1944)<br>Board Member since 2004+ | Private equity investor (since October 2009); previously, Managing Director, Diamond Management & Technology Consultants, Inc. (global consulting firm) (2001–2009); Directorship: Board of Managers, YMCA of Metropolitan Chicago; formerly: Senior Partner, Arthur Andersen LLP (accounting) (1966–2001); Trustee, Ravinia Festival | 122 |

| Name, Year of Birth, Position with the Fund and Length of Time Served[1] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Rebecca W. Rimel (1951)<br>Board Member since 1995 | President and Chief Executive Officer, The Pew Charitable Trusts (charitable organization) (1994 to present); Trustee, Thomas Jefferson Foundation (charitable organization) (1994 to present); Trustee, Executive Committee, Philadelphia Chamber of Commerce (2001–2007); Director, CardioNet, Inc.[2] (2009–present) (health care). Formerly, Executive Vice President, The Glenmede Trust Company (investment trust and wealth management) (1983–2004); Board Member, Investor Education (charitable organization) (2004–2005); Director, Viasys Health Care[2] (January 2007–June 2007); Trustee, Pro Publica (charitable organization) (2007–2010) | 122 |
| William N. Searcy, Jr. (1946)<br>Board Member since 1993 | Private investor since October 2003; Trustee of 22 open-end mutual funds managed by Sun Capital Advisers, Inc. (since October 1998). Formerly, Pension & Savings Trust Officer, Sprint Corporation[2] (telecommunications) (November 1989–September 2003) | 122 |
| Jean Gleason Stromberg (1943)<br>Board Member since 1997 | Retired. Formerly, Consultant (1997–2001); Director, Financial Markets US Government Accountability Office (1996–1997); Partner, Fulbright & Jaworski, L.L.P. (law firm) (1978–1996). Directorships: The William and Flora Hewlett Foundation. Former Directorships: Service Source, Inc., Mutual Fund Directors Forum (2002–2004), American Bar Retirement Association (funding vehicle for retirement plans) (1987–1990 and 1994–1996) | 122 |
| Robert H. Wadsworth (1940)<br>Board Member since 1999 | President, Robert H. Wadsworth & Associates, Inc. (consulting firm) (1983 to present); Director, The Phoenix Boys Choir Association | 125 |

## Officers[4]

| Name, Year of Birth, Position with the Fund and Length of Time Served[5] | Principal Occupation(s) During Past 5 Years and Other Directorships Held |
|---|---|
| Michael G. Clark[6] (1965)<br>President, 2006–present | Managing Director[3], Deutsche Asset Management (2006–present); President of DWS family of funds; Director, ICI Mutual Insurance Company (since October 2007); formerly, Director of Fund Board Relations (2004–2006) and Director of Product Development (2000–2004), Merrill Lynch Investment Managers; Senior Vice President Operations, Merrill Lynch Asset Management (1999–2000) |
| Ingo Gefeke[7] (1967)<br>Executive Vice President since 2010 | Managing Director[3], Deutsche Asset Management; Global Head of Distribution and Product Management, DWS Global Head of Trading and Securities Lending. Member of the Board of Directors of DWS Investment GmbH Frankfurt (since July 2009) and DWS Holding & Service GmbH Frankfurt (since January 2010); formerly, Global Chief Administrative Officer, Deutsche Asset Management (2004–2009); Global Chief Operating Officer, Global Transaction Banking, Deutsche Bank AG, New York (2001–2004); Chief Operating Officer, Global Banking Division Americas, Deutsche Bank AG, New York (1999–2001); Central Management, Global Banking Services, Deutsche Bank AG, Frankfurt (1998–1999); Relationship Management, Deutsche Bank AG, Tokyo, Japan (1997–1998) |
| John Millette[8] (1962)<br>Vice President and Secretary, 1999–present | Director[3], Deutsche Asset Management |
| Paul H. Schubert[6] (1963)<br>Chief Financial Officer, 2004–present<br>Treasurer, 2005–present | Managing Director[3], Deutsche Asset Management (since July 2004); formerly, Executive Director, Head of Mutual Fund Services and Treasurer for UBS Family of Funds (1998–2004); Vice President and Director of Mutual Fund Finance at UBS Global Asset Management (1994–1998) |
| Caroline Pearson[8] (1962)<br>Chief Legal Officer, April 2010–present | Managing Director[3], Deutsche Asset Management; formerly, Assistant Secretary for DWS family of funds (1997–2010) |
| Rita Rubin[9] (1970)<br>Assistant Secretary, 2009–present | Vice President and Counsel, Deutsche Asset Management (since October 2007); formerly, Vice President, Morgan Stanley Investment Management (2004–2007) |
| Paul Antosca[8] (1957)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management (since 2006); Vice President, The Manufacturers Life Insurance Company (U.S.A.) (1990–2006) |
| Jack Clark[8] (1967)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management (since 2007); formerly, Vice President, State Street Corporation (2002–2007) |
| Diane Kenneally[8] (1966)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management |
| John Caruso[9] (1965)<br>Anti-Money Laundering Compliance Officer, 2010–present | Managing Director[3], Deutsche Asset Management |

| Name, Year of Birth, Position with the Fund and Length of Time Served[5] | Principal Occupation(s) During Past 5 Years and Other Directorships Held |
|---|---|
| Robert Kloby[9] (1962)<br>Chief Compliance Officer, 2006–present | Managing Director[3], Deutsche Asset Management |

1 *The length of time served represents the year in which the Board Member joined the board of one or more DWS funds currently overseen by the Board.*

2 *A publicly held company with securities registered pursuant to Section 12 of the Securities Exchange Act of 1934.*

3 *Executive title, not a board directorship.*

4 *As a result of their respective positions held with the Advisor, these individuals are considered "interested persons" of the Advisor within the meaning of the 1940 Act. Interested persons receive no compensation from the fund.*

5 *The length of time served represents the year in which the officer was first elected in such capacity for one or more DWS funds.*

6 *Address: 100 Plaza One, Jersey City, NJ 07311.*

7 *Effective January 11, 2011, Mr. Gefeke, Executive Vice President, resigned as an officer of the fund.*

*The mailing address of Mr. Gefeke is 345 Park Avenue, New York, New York 10154. Mr. Gefeke was an interested Board Member of certain DWS funds by virtue of his positions with Deutsche Asset Management. As an interested person, Mr. Gefeke received no compensation from the fund.*

8 *Address: One Beacon Street, Boston, MA 02108.*

9 *Address: 60 Wall Street, New York, New York 10005.*

*The fund's Statement of Additional Information ("SAI") includes additional information about the Board Members. The SAI is available, without charge, upon request. If you would like to request a copy of the SAI, you may do so by calling the following toll-free number: (800) 728-3337.*

# Notes

Deutsche Investment Management Americas Inc. ("DIMA"), an indirect, wholly owned subsidiary of Deutsche Bank AG, is the Fund's Advisor.

DWS Investments is part of Deutsche Bank's Asset Management division and, within the US, represents the retail asset management activities of Deutsche Bank AG, Deutsche Bank Trust Company Americas, Deutsche Investment Management Americas Inc. and DWS Trust Company.

The views expressed in this report reflect those of the portfolio managers only through the end of the period of the report as stated on the cover. The managers' views are subject to change at any time based on market and other conditions and should not be construed as a recommendation.

This information must be preceded or accompanied by a current prospectus.

Portfolio changes should not be considered recommendations for action by individual investors.

DWS Investments Distributors, Inc.
222 South Riverside Plaza
Chicago, IL 60606
(800) 621-1148

vit-equ500-2 (R-20600-1 2/11)

DWS INVESTMENTS
Deutsche Bank Group

DECEMBER 31, 2010

# ANNUAL REPORT

## DWS VARIABLE SERIES I

## DWS Bond VIP

**This report must be preceded or accompanied by a prospectus. To obtain an additional prospectus or summary prospectus, if available, call (800) 728-3337 or your financial representative. We advise you to consider the Fund's objectives, risks, charges and expenses carefully before investing. The summary prospectus and prospectus contain this and other important information about the Fund. Please read the prospectus carefully before you invest.**

*Investments in variable insurance portfolios (VIPs) involve risk. Stocks may decline in value. Bond investments are subject to interest-rate and credit risks. When interest rates rise, bond prices generally fall. Credit risk refers to the ability of an issuer to make timely payments of principal and interest. Investing in derivatives entails special risks relating to liquidity, leverage and credit that may reduce returns and/or increased volatility. Investing in foreign securities, particularly those of emerging markets, presents certain risks, such as currency fluctuations, political and economic changes, and market risks. There are additional risks associated with investing in commodities, high-yield bonds, aggressive growth stocks, non-diversified/ concentrated funds and small- and mid-cap stocks which are more fully explained in the prospectuses. Please read the prospectus for more information.*

*DWS Investments is part of Deutsche Bank's Asset Management division and, within the US, represents the retail asset management activities of Deutsche Bank AG, Deutsche Bank Trust Company Americas, Deutsche Investment Management Americas Inc. and DWS Trust Company.*

*NOT FDIC/NCUA INSURED    NO BANK GUARANTEE    MAY LOSE VALUE    NOT A DEPOSIT*
*NOT INSURED BY ANY FEDERAL GOVERNMENT AGENCY*

DWS INVESTMENTS
Deutsche Bank Group

# Performance Summary
**December 31, 2010**

## DWS Bond VIP

**All performance shown is historical, assumes reinvestment of all dividend and capital gain distributions, and does not guarantee future results. Investment return and principal value fluctuate with changing market conditions so that, when redeemed, shares may be worth more or less than their original cost. Current performance may be lower or higher than the performance data quoted. Please contact your participating insurance company for the Fund's most recent month-end performance. Performance doesn't reflect charges and fees ("contract charges") associated with the separate account that invests in the Fund or any variable life insurance policy or variable annuity contract for which the Fund is an investment option. These charges and fees will reduce returns.**

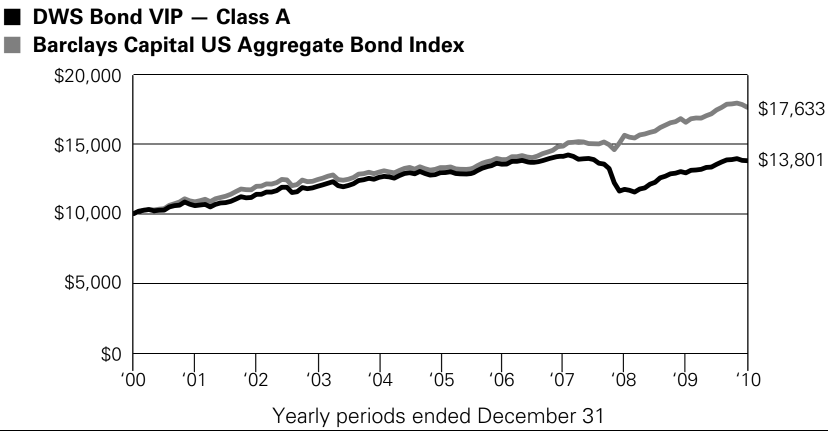
**The gross expense ratio of the Fund, as stated in the fee table of the prospectus dated May 1, 2010 is 0.59% for Class A shares and may differ from the expense ratio disclosed in the Financial Highlights table in this report.**

Fund returns during 5-year and 10-year periods shown reflect a fee waiver and/or expense reimbursement. Without this waiver/reimbursement, returns would have been lower.

### Risk Considerations

Bond investments are subject to interest-rate and credit risks. When interest rates rise, bond prices generally fall. Credit risk refers to the ability of an issuer to make timely payments of principal and interest. Investments in lower-quality and non-rated securities present greater risk of loss than investments in higher-quality securities. Investing in foreign securities, particularly those of emerging markets, presents certain risks, such as currency fluctuations, political and economic changes, and market risks. See the prospectus for details.

### Growth of an Assumed $10,000 Investment




*The Barclays Capital US Aggregate Bond Index is an unmanaged, market-value-weighted measure of Treasury issues, agency issues, corporate bond issues and mortgage securities.*

*Index returns, unlike fund returns, do not reflect any fees or expenses. It is not possible to invest directly into an index.*

### Comparative Results

| DWS Bond VIP | | 1-Year | 3-Year | 5-Year | 10-Year |
|---|---|---|---|---|---|
| **Class A** | Growth of $10,000 | $10,679 | $9,783 | $10,672 | $13,801 |
| | Average annual total return | 6.79% | –.73% | 1.31% | 3.27% |
| Barclays Capital US Aggregate Bond Index | Growth of $10,000 | $10,654 | $11,877 | $13,255 | $17,633 |
| | Average annual total return | 6.54% | 5.90% | 5.80% | 5.84% |

*The growth of $10,000 is cumulative.*

# Information About Your Fund's Expenses

## DWS Bond VIP

As an investor of the Fund, you incur two types of costs: ongoing expenses and transaction costs. Ongoing expenses include management fees, distribution and service (12b-1) fees and other Fund expenses. Examples of transaction costs include contract charges, redemption fees and account maintenance fees, which are not shown in this section. The following tables are intended to help you understand your ongoing expenses (in dollars) of investing in the Fund and to help you compare these expenses with the ongoing expenses of investing in other mutual funds. The example in the table is based on an investment of $1,000 invested at the beginning of the six-month period and held for the entire period (July 1, 2010 to December 31, 2010).

The tables illustrate your Fund's expenses in two ways:

- **Actual Fund Return.** This helps you estimate the actual dollar amount of ongoing expenses (but not transaction costs) paid on a $1,000 investment in the Fund using the Fund's actual return during the period. To estimate the expenses you paid over the period, simply divide your account value by $1,000 (for example, an $8,600 account value divided by $1,000 = 8.6), then multiply the result by the number in the "Expenses Paid per $1,000" line under the share class you hold.
- **Hypothetical 5% Fund Return.** This helps you to compare your Fund's ongoing expenses (but not transaction costs) with those of other mutual funds using the Fund's actual expense ratio and a hypothetical rate of return of 5% per year before expenses. Examples using a 5% hypothetical Fund return may be found in the shareholder reports of other mutual funds. The hypothetical account values and expenses may not be used to estimate the actual ending account balance or expenses you paid for the period.

Please note that the expenses shown in these tables are meant to highlight your ongoing expenses only and do not reflect any transaction costs. The "Expenses Paid per $1,000" line of the tables is useful in comparing ongoing expenses only and will not help you determine the relative total expense of owning different funds. If these transaction costs had been included, your costs would have been higher.

**Expenses and Value of a $1,000 Investment** for the six months ended December 31, 2010

| **Actual Fund Return** | **Class A** |
|---|---|
| Beginning Account Value 7/1/10 | $1,000.00 |
| Ending Account Value 12/31/10 | $1,019.80 |
| Expenses Paid per $1,000* | $ 2.95 |
| **Hypothetical 5% Fund Return** | **Class A** |
| Beginning Account Value 7/1/10 | $1,000.00 |
| Ending Account Value 12/31/10 | $1,022.28 |
| Expenses Paid per $1,000* | $ 2.96 |

* *Expenses are equal to the Fund's annualized expense ratio for each share class, multiplied by the average account value over the period, multiplied by the number of days in the most recent six-month period, then divided by 365.*

| **Annualized Expense Ratio** | **Class A** |
|---|---|
| DWS Variable Series I — DWS Bond VIP | .58% |

For more information, please refer to the Fund's prospectus.

These tables do not reflect charges and fees ("contract charges") associated with the separate account that invests in the Fund or any variable life insurance policy or variable annuity contract for which the Fund is an investment option.

## DWS Bond VIP

During the 12-month period ended December 31, 2010, the US Federal Reserve Board (the Fed) maintained the benchmark federal funds rate at near-zero levels and engaged in bond purchases designed to lower longer-term interest rates as it sought to stimulate economic growth.[1] Treasury yields fell for most of the year, before rising in the fourth quarter as market participants reacted to better economic data and the extension of Bush-era tax cuts. For the year, credit-sensitive sectors outperformed as investors sought yield in an environment of low interest rates. Corporate bonds benefited as corporate profits and balance sheets displayed strength throughout the period, with below-investment-grade issues leading returns. Among other credit sectors, commercial mortgage-backed securities were standout performers despite an ongoing soft leasing environment in many markets.[2]

During the 12-month period, the Fund provided a total return of 6.79% (Class A shares, unadjusted for contract charges), compared with the 6.54% return of its benchmark, the Barclays Capital US Aggregate Bond Index. (Past performance is no guarantee of future results.)

The Fund's performance versus the benchmark continued to be driven principally by exposure to more credit-sensitive fixed-income sectors. Our overweight in investment-grade corporate bonds was the leading contributor to returns, while our high-yield corporate and emerging-market holdings added to performance as well.[3] Currency weightings also added to performance, in particular our exposure to the Australian and Canadian dollars. On the downside, our underweighting early in the period of commercial mortgage-backed securities constrained returns. In addition, our positions in the bonds of a pair of Irish banks suffered as the crisis with respect to European sovereign debt played out over the period. The Fund's positioning with respect to overall duration and interest rate exposure was essentially a neutral factor for performance.[4] During the period, we maintained a somewhat conservative stance with respect to interest rate exposure as we monitored the impact of Fed bond purchases on inflation expectations and rates. In addition, we closely watched economic data which appeared to indicate that the recovery is taking hold, a trend that we believe could bode well for continued outperformance by credit-oriented sectors.

Kenneth R. Bowling, CFA
Jamie Guenther, CFA
John Brennan
Bruce Harley, CFA, CEBS
J. Richard Robben, CFA
David Vignolo, CFA
J. Kevin Horsley, CFA, CPA
Stephen Willer, CFA
William Chepolis, CFA *(joined the Fund on 2/1/2011)*
*Portfolio Managers*

*The Barclays Capital US Aggregate Bond Index is an unmanaged, market-value-weighted measure of Treasury issues, agency issues, corporate bond issues and mortgage securities.*

*Index returns, unlike fund returns, do not reflect any fees or expenses. It is not possible to invest directly into an index.*

1 *The federal funds rate is the interest rate, set by the US Federal Reserve Board, at which banks lend money to each other, usually on an overnight basis.*

2 *Commercial mortgage-backed securities (CMBS) are secured by loans on a commercial property.*

3 *"Overweight" means the Fund holds a higher weighting in a given sector or security than the benchmark. "Underweight" means the Fund holds a lower weighting.*

4 *Effective duration is an approximate measure of the Fund's sensitivity to interest rate changes taking into consideration any maturity shortening features.*

*Portfolio management market commentary is as of December 31, 2010, and may not come to pass. This information is subject to change at any time based on market and other conditions. Past performance does not guarantee future results. Current and future portfolio holdings are subject to risk.*

# Portfolio Summary

## DWS Bond VIP

| **Asset Allocation** (As a % of Investment Portfolio excluding Securities Lending Collateral) | **12/31/10** | **12/31/09** |
|---|---|---|
| Corporate Bonds | 31% | 24% |
| Mortgage-Backed Securities Pass-Throughs | 28% | 32% |
| Government & Agency Obligations | 21% | 24% |
| Commercial Mortgage-Backed Securities | 9% | 3% |
| Municipal Bonds and Notes | 5% | 3% |
| Collateralized Mortgage Obligations | 4% | 3% |
| Cash Equivalents | 2% | 10% |
| Asset-Backed | — | 1% |
| | 100% | 100% |

| **Quality** (Excludes Cash Equivalents and Securities Lending Collateral) | **12/31/10** | **12/31/09** |
|---|---|---|
| US Government & Treasury Obligations | 47% | 59% |
| AAA | 5% | 3% |
| AA | 5% | 6% |
| A | 10% | 9% |
| BBB | 17% | 15% |
| BB or Below | 14% | 7% |
| Not Rated | 2% | 1% |
| | 100% | 100% |

| **Interest Rate Sensitivity** | **12/31/10** | **12/31/09** |
|---|---|---|
| Effective Maturity | 7.30 years | 7.88 years |
| Effective Duration | 4.91 years | 4.65 years |

*Effective maturity is the weighted average of the bonds held by the Fund taking into consideration any maturity shortening features.*

*Effective duration is an approximate measure of the Fund's sensitivity to interest rate changes taking into consideration any maturity shortening features.*

*Asset allocation, quality and interest rate sensitivity are subject to change.*

*The quality ratings represent the lower of Moody's Investors Service, Inc. ("Moody's") or Standard & Poor's Corporation ("S&P") credit ratings. The ratings of Moody's and S&P represent their opinions as to the quality of the securities they rate. Ratings are relative and subjective and are not absolute standards of quality. The Fund's credit quality does not remove market risk.*

*For more complete details about the Fund's investment portfolio, see page 6.*

Following the Fund's fiscal first and third quarter-end, a complete portfolio holdings listing is filed with the SEC on Form N-Q. The form will be available on the SEC's Web site at www.sec.gov, and it also may be reviewed and copied at the SEC's Public Reference Room in Washington, D.C. Information on the operation of the SEC's Public Reference Room may be obtained by calling (800) SEC-0330. The Fund's portfolio holdings are also posted on www.dws-investments.com from time to time. Please see the Fund's current prospectus for more information.

## DWS Bond VIP

| | Principal Amount ($) (a) | Value ($) |
|---|---|---|
| **Corporate Bonds 37.3%** | | |
| **Consumer Discretionary 10.7%** | | |
| AMC Entertainment, Inc., 8.75%, 6/1/2019 | 1,200,000 | 1,281,000 |
| Cablevision Systems Corp., 8.625%, 9/15/2017 | 1,500,000 | 1,633,125 |
| CBS Corp., 5.9%, 10/15/2040 | 600,000 | 577,966 |
| Comcast Corp., 5.15%, 3/1/2020 | 450,000 | 472,655 |
| DIRECTV Holdings LLC, 6.35%, 3/15/2040 | 815,000 | 857,355 |
| Expedia, Inc.: | | |
| 5.95%, 8/15/2020 | 2,075,000 | 2,085,375 |
| 7.456%, 8/15/2018 | 1,150,000 | 1,311,000 |
| Home Depot, Inc., 5.4%, 9/15/2040 | 420,000 | 407,870 |
| JC Penney Co., Inc., 5.65%, 6/1/2020 | 1,500,000 | 1,436,250 |
| Levi Strauss & Co., 7.625%, 5/15/2020 | 1,700,000 | 1,755,250 |
| Lowe's Companies, Inc.: | | |
| 2.125%, 4/15/2016 | 250,000 | 244,490 |
| 3.75%, 4/15/2021 | 500,000 | 483,405 |
| MGM Resorts International, 144A, 9.0%, 3/15/2020 | 750,000 | 825,000 |
| NBC Universal, Inc., 144A, 5.95%, 4/1/2041 | 500,000 | 499,949 |
| Norcraft Companies LP, 10.5%, 12/15/2015 | 100,000 | 106,250 |
| Royal Caribbean Cruises Ltd., 7.25%, 6/15/2016 | 1,100,000 | 1,185,250 |
| Time Warner Cable, Inc., 7.3%, 7/1/2038 | 40,000 | 46,772 |
| Time Warner, Inc.: | | |
| 6.2%, 3/15/2040 | 400,000 | 425,222 |
| 7.625%, 4/15/2031 | 400,000 | 486,273 |
| Yum! Brands, Inc.: | | |
| 3.875%, 11/1/2020 | 465,000 | 444,208 |
| 5.3%, 9/15/2019 | 135,000 | 142,988 |
| | | **16,707,653** |
| **Consumer Staples 2.3%** | | |
| Anheuser-Busch InBev Worldwide, Inc., 144A, 7.75%, 1/15/2019 | 750,000 | 933,261 |
| CVS Caremark Corp.: | | |
| 6.125%, 9/15/2039 | 500,000 | 534,229 |
| 6.25%, 6/1/2027 | 332,000 | 365,103 |
| Kraft Foods, Inc., 5.375%, 2/10/2020 | 1,335,000 | 1,436,819 |
| Kroger Co., 5.4%, 7/15/2040 | 375,000 | 355,431 |
| | | **3,624,843** |
| **Energy 4.9%** | | |
| Chesapeake Energy Corp., 9.5%, 2/15/2015 | 550,000 | 620,125 |
| DCP Midstream LLC, 144A, 9.75%, 3/15/2019 | 980,000 | 1,266,474 |
| Enterprise Products Operating LLC, 6.125%, 10/15/2039 | 460,000 | 478,772 |

| | | Principal Amount ($) (a) | Value ($) |
|---|---|---|---|
| Kinder Morgan Energy Partners LP: | | | |
| 6.5%, 9/1/2039 | | 500,000 | 516,517 |
| 6.95%, 1/15/2038 | | 510,000 | 554,166 |
| ONEOK Partners LP, 6.15%, 10/1/2016 | | 482,000 | 541,702 |
| Plains All American Pipeline LP, 8.75%, 5/1/2019 | | 1,200,000 | 1,489,194 |
| Reliance Holdings USA, Inc., 144A, 4.5%, 10/19/2020 | | 650,000 | 620,199 |
| Weatherford International Ltd., 5.125%, 9/15/2020 | | 1,000,000 | 995,032 |
| Williams Partners LP, 4.125%, 11/15/2020 | | 570,000 | 539,898 |
| | | | **7,622,079** |
| **Financials 10.0%** | | | |
| American Express Co., 7.0%, 3/19/2018 | | 1,138,000 | 1,325,512 |
| Bank of America Corp.: | | | |
| 5.75%, 12/1/2017 | | 710,000 | 738,844 |
| 6.5%, 8/1/2016 | | 175,000 | 189,891 |
| Citigroup, Inc., 5.375%, 8/9/2020 | | 1,500,000 | 1,558,511 |
| Discover Bank, 8.7%, 11/18/2019 | | 710,000 | 835,751 |
| Fifth Third Bancorp., 5.45%, 1/15/2017 | | 651,000 | 665,428 |
| Ford Motor Credit Co., LLC: | | | |
| 7.0%, 4/15/2015 | | 900,000 | 967,151 |
| 8.0%, 6/1/2014 | | 1,500,000 | 1,652,560 |
| Hartford Financial Services Group, Inc., 5.95%, 10/15/2036 | | 300,000 | 283,030 |
| JPMorgan Chase & Co., 5.125%, 9/15/2014 | | 1,500,000 | 1,596,106 |
| KeyBank NA, 5.7%, 11/1/2017 | | 800,000 | 814,681 |
| Lincoln National Corp., 8.75%, 7/1/2019 | | 500,000 | 625,424 |
| MetLife, Inc., Series A, 6.817%, 8/15/2018 | | 400,000 | 466,353 |
| Morgan Stanley: | | | |
| 3.45%, 11/2/2015 | | 170,000 | 165,743 |
| Series F, 6.625%, 4/1/2018 | | 475,000 | 515,265 |
| PNC Bank NA, 6.875%, 4/1/2018 | | 200,000 | 228,612 |
| Prudential Financial, Inc.: | | | |
| Series B, 5.1%, 9/20/2014 | | 150,000 | 161,125 |
| 6.2%, 1/15/2015 | | 100,000 | 110,281 |
| 7.375%, 6/15/2019 | | 120,000 | 141,485 |
| Qtel International Finance Ltd., 144A, 5.0%, 10/19/2025 | | 935,000 | 846,390 |
| Red Arrow International Leasing PLC, "A", 8.375%, 6/30/2012 | RUB | 1,076,482 | 35,240 |
| The Goldman Sachs Group, Inc., 6.0%, 6/15/2020 | | 800,000 | 864,531 |
| Toll Brothers Finance Corp., 8.91%, 10/15/2017 | | 350,000 | 412,950 |
| Travelers Companies, Inc., 5.35%, 11/1/2040 | | 280,000 | 275,873 |
| | | | **15,476,737** |

*The accompanying notes are an integral part of the financial statements.*

| | Principal Amount ($) (a) | Value ($) |
|---|---|---|
| **Health Care 2.2%** | | |
| Express Scripts, Inc.: | | |
| 6.25%, 6/15/2014 | 385,000 | 430,415 |
| 7.25%, 6/15/2019 | 720,000 | 852,208 |
| HCA, Inc., 9.25%, 11/15/2016 | 725,000 | 773,485 |
| Laboratory Corp. of America Holdings, 4.625%, 11/15/2020 | 455,000 | 450,896 |
| Medco Health Solutions, Inc., 7.125%, 3/15/2018 | 715,000 | 839,050 |
| | | **3,346,054** |
| **Industrials 0.9%** | | |
| CSX Corp.: | | |
| 6.15%, 5/1/2037 | 400,000 | 430,065 |
| 6.25%, 3/15/2018 | 800,000 | 917,729 |
| | | **1,347,794** |
| **Materials 2.5%** | | |
| ArcelorMittal, 6.125%, 6/1/2018 | 500,000 | 532,743 |
| Corporacion Nacional del Cobre — Codelco, REG S, 7.5%, 1/15/2019 | 600,000 | 730,404 |
| Dow Chemical Co., 4.25%, 11/15/2020 | 455,000 | 435,844 |
| Exopack Holding Corp., 11.25%, 2/1/2014 | 420,000 | 435,750 |
| International Paper Co., 7.3%, 11/15/2039 | 770,000 | 877,371 |
| United States Steel Corp., 7.375%, 4/1/2020 | 800,000 | 820,000 |
| | | **3,832,112** |
| **Telecommunication Services 2.5%** | | |
| American Tower Corp., 5.05%, 9/1/2020 | 1,200,000 | 1,180,121 |
| Frontier Communications Corp., 8.125%, 10/1/2018 | 1,000,000 | 1,097,500 |
| Qwest Communications International, Inc., 8.0%, 10/1/2015 | 750,000 | 806,250 |
| Windstream Corp., 8.625%, 8/1/2016 | 775,000 | 815,687 |
| | | **3,899,558** |
| **Utilities 1.3%** | | |
| CMS Energy Corp., 5.05%, 2/15/2018 | 500,000 | 494,392 |
| DTE Energy Co., 7.625%, 5/15/2014 | 152,000 | 175,199 |
| Energy Future Competitive Holdings Co., 7.48%, 1/1/2017 | 26,811 | 22,709 |
| FirstEnergy Solutions Corp., 6.8%, 8/15/2039 | 517,000 | 501,077 |
| Majapahit Holding BV, REG S, 7.75%, 10/17/2016 | 100,000 | 115,679 |
| Sempra Energy, 6.5%, 6/1/2016 | 650,000 | 754,592 |
| | | **2,063,648** |
| **Total Corporate Bonds** (Cost $55,757,794) | | **57,920,478** |

## Mortgage-Backed Securities Pass-Throughs 34.3%

| | Principal Amount ($) (a) | Value ($) |
|---|---|---|
| Federal Home Loan Mortgage Corp.: | | |
| 4.5%, 12/1/2034 | 775,838 | 800,265 |
| 5.5%, with various maturities from 10/1/2023 until 8/1/2024 | 379,240 | 407,623 |
| 5.508%**, 2/1/2038 | 453,527 | 476,403 |
| 6.5%, 3/1/2026 | 755,865 | 841,826 |
| 7.0%, 1/1/2038 | 138,275 | 155,014 |
| Federal National Mortgage Association: | | |
| 3.274%**, 8/1/2037 | 118,346 | 123,960 |
| 3.5%, 7/1/2025 (b) | 7,500,000 | 7,553,906 |
| 4.0%, with various maturities from 9/1/2039 until 9/1/2040 (b) | 9,694,996 | 9,650,741 |
| 4.5%, 6/1/2034 | 708,667 | 732,004 |
| 5.0%, with various maturities from 2/1/2021 until 8/1/2040 | 3,158,126 | 3,329,400 |
| 5.152%**, 9/1/2038 | 207,642 | 220,428 |
| 5.39%**, 1/1/2038 | 528,565 | 555,702 |
| 5.5%, with various maturities from 12/1/2032 until 4/1/2037 (b) | 11,703,856 | 12,535,844 |
| 6.0%, with various maturities from 4/1/2024 until 8/1/2035 (b) | 7,535,326 | 8,203,130 |
| 6.5%, with various maturities from 3/1/2017 until 1/1/2036 (b) | 2,376,536 | 2,641,875 |
| 8.0%, 9/1/2015 | 15,745 | 17,070 |
| Government National Mortgage Association: | | |
| 4.5%, 6/1/2039 (b) | 1,600,000 | 1,661,375 |
| 5.0%, 4/1/2038 (b) | 1,600,000 | 1,701,125 |
| 5.5%, 3/1/2036 (b) | 1,600,000 | 1,729,125 |
| **Total Mortgage-Backed Securities Pass-Throughs** (Cost $52,686,995) | | **53,336,816** |

## Commercial Mortgage-Backed Securities 10.5%

| | Principal Amount ($) (a) | Value ($) |
|---|---|---|
| Banc of America Commercial Mortgage, Inc., "A4", Series 2007-4, 5.742%**, 2/10/2051 | 600,000 | 639,110 |
| Bear Stearns Commercial Mortgage Securities, Inc., "A4", Series 2007-PW18, 5.7%, 6/13/2050 | 1,738,000 | 1,810,887 |
| Citigroup/Deutsche Bank Commercial Mortgage Trust, "A4", Series 2006-CD2, 5.347%**, 1/15/2046 | 1,850,000 | 1,985,417 |
| Greenwich Capital Commercial Funding Corp., "A4", Series 2006-GG7, 5.883%**, 7/10/2038 | 2,375,000 | 2,591,122 |
| GS Mortgage Securities Corp. II: | | |
| "J", Series 2007-GG10, 144A, 5.807%**, 8/10/2045* | 1,096,000 | 9,316 |
| "K", Series 2007-GG10, 144A, 5.807%**, 8/10/2045* | 767,000 | 4,602 |
| JPMorgan Chase Commercial Mortgage Securities Corp.: | | |
| "A4", Series 2005-CB12, 4.895%, 9/12/2037 | 1,500,000 | 1,588,678 |
| "A4", Series 2006-CB16, 5.552%, 5/12/2045 | 640,000 | 683,772 |
| "E", Series 2007-LD11, 5.817%**, 6/15/2049 | 590,000 | 78,486 |
| "F", Series 2007-LD11, 5.817%**, 6/15/2049 | 650,000 | 52,710 |
| "G", Series 2007-LD11, 144A, 5.817%**, 6/15/2049 | 760,000 | 51,987 |

*The accompanying notes are an integral part of the financial statements.*

| | Principal Amount ($) (a) | Value ($) |
|---|---|---|
| "H", Series 2007-LD11, 144A, 5.817%**, 6/15/2049 | 460,000 | 13,800 |
| "A4", Series 2006-LDP7, 5.872%**, 4/15/2045 | 1,500,000 | 1,640,413 |
| "A4", Series 2007-LD12, 5.882%, 2/15/2051 | 1,380,000 | 1,461,081 |
| LB-UBS Commercial Mortgage Trust: | | |
| "A3", Series 2006-C7, 5.347%, 11/15/2038 | 1,750,000 | 1,850,204 |
| "A4", Series 2007-C6, 5.858%, 7/15/2040 | 1,000,000 | 1,050,670 |
| Merrill Lynch Mortgage Trust, "ASB", Series 2007-C1, 5.826%**, 6/12/2050 | 590,000 | 634,212 |
| Wachovia Bank Commercial Mortgage Trust, "H", Series 2007-C32, 144A, 5.744%**, 6/15/2049 | 770,000 | 99,366 |
| **Total Commercial Mortgage-Backed Securities** (Cost $19,898,506) | | **16,245,833** |

## Collateralized Mortgage Obligations 5.4%

| | Principal Amount ($) (a) | Value ($) |
|---|---|---|
| Countrywide Home Loans, "A2", Series 2006-1, 6.0%, 3/25/2036 | 641,046 | 555,359 |
| CS First Boston Mortgage Securities Corp., "10A3", Series 2005-10, 6.0%, 11/25/2035 | 159,455 | 101,141 |
| FDIC Structured Sale Guaranteed Notes, "1A", Series 2010-S1, 144A, 0.811%**, 2/25/2048 | 1,731,716 | 1,734,435 |
| Federal Home Loan Mortgage Corp.: | | |
| "PD", Series 2774, 5.0%, 8/15/2032 | 1,010,000 | 1,070,640 |
| "PE", Series 2898, 5.0%, 5/15/2033 | 335,000 | 358,212 |
| "KG", Series 2987, 5.0%, 12/15/2034 | 1,470,000 | 1,575,346 |
| Federal National Mortgage Association: | | |
| "IO", Series 2010-143, Interest Only, 5.0%, 12/25/2025 | 5,832,053 | 536,170 |
| "EG", Series 2005-22, 5.0%, 11/25/2033 | 750,000 | 803,109 |
| "TC", Series 2007-77, 5.5%, 9/25/2034 | 370,000 | 395,535 |
| Government National Mortgage Association: | | |
| "IP", Series 2010-79, Interest Only, 4.5%, 5/20/2039 | 2,338,103 | 397,549 |
| "KI", Series 2010-130, Interest Only, 5.5%, 9/16/2040 | 480,000 | 73,333 |
| MASTR Alternative Loans Trust, "8A1", Series 2004-3, 7.0%, 4/25/2034 | 12,467 | 11,822 |
| NCUA Guaranteed Notes, "1A", Series 2010-R1, 0.716%**, 10/7/2020 | 776,434 | 775,463 |
| Structured Asset Securities Corp., "2A1", Series 2003-1, 6.0%, 2/25/2018 | 1,979 | 2,030 |
| **Total Collateralized Mortgage Obligations** (Cost $8,330,639) | | **8,390,144** |

## Government & Agency Obligations 25.1%

### Sovereign Bonds 4.8%

| | | Principal Amount ($) (a) | Value ($) |
|---|---|---|---|
| Kingdom of Morocco, REG S, 4.5%, 10/5/2020 | EUR | 625,000 | 799,065 |
| Republic of Argentina: | | | |
| GDP Linked Note, Zero Coupon, 12/15/2035 (g) | | 410,000 | 62,115 |
| 8.28%, 12/31/2033 | | 650,476 | 603,316 |
| Republic of Egypt, 9.1%, 9/20/2012 | EGP | 230,000 | 39,673 |
| Republic of El Salvador, REG S, 8.25%, 4/10/2032 | | 40,000 | 44,400 |
| Republic of Lithuania, REG S, 5.125%, 9/14/2017 | | 200,000 | 196,500 |
| Republic of Panama: | | | |
| 5.2%, 1/30/2020 | | 425,000 | 450,500 |
| 7.125%, 1/29/2026 | | 220,000 | 264,550 |
| 7.25%, 3/15/2015 | | 80,000 | 92,400 |
| Republic of Peru, 7.125%, 3/30/2019 | | 600,000 | 717,000 |
| Republic of Poland, 6.375%, 7/15/2019 | | 560,000 | 627,318 |
| Republic of Serbia, REG S, 6.75%, 11/1/2024 | | 480,667 | 470,573 |
| Republic of Sri Lanka, 144A, 6.25%, 10/4/2020 | | 825,000 | 836,344 |
| Russian Federation, 144A, 5.0%, 4/29/2020 | | 2,200,000 | 2,200,000 |
| | | | **7,403,754** |

### US Government Sponsored Agency 0.8%

| | Principal Amount ($) (a) | Value ($) |
|---|---|---|
| Federal National Mortgage Association, 6.625%, 11/15/2030 | 950,000 | **1,198,680** |

### US Treasury Obligations 19.5%

| | Principal Amount ($) (a) | Value ($) |
|---|---|---|
| US Treasury Bills, 0.185%***, 3/17/2011 (c) | 969,000 | 968,784 |
| US Treasury Bond, 4.75%, 2/15/2037 (d) | 3,600,000 | 3,868,877 |
| US Treasury Note, 1.75%, 1/31/2014 (d) | 25,000,000 | 25,523,450 |
| | | **30,361,111** |
| **Total Government & Agency Obligations** (Cost $38,267,988) | | **38,963,545** |

## Loan Participations and Assignments 0.2%

### Sovereign Loans

| | Principal Amount ($) (a) | Value ($) |
|---|---|---|
| Gazprom, 144A, 8.125%, 7/31/2014 | 205,000 | 231,650 |
| Russian Agricultural Bank, REG S, 7.75%, 5/29/2018 | 100,000 | 108,250 |
| **Total Loan Participations and Assignments** (Cost $302,745) | | **339,900** |

## Municipal Bonds and Notes 6.2%

| | Principal Amount ($) (a) | Value ($) |
|---|---|---|
| California, University Revenues, Build America Bonds, 5.946%, 5/15/2045 | 420,000 | 391,885 |
| Gwinnett County, GA, Development Authority Revenue, Gwinnett Stadium Project, 6.4%, 1/1/2028 | 655,000 | 729,441 |

*The accompanying notes are an integral part of the financial statements.*

| | Principal Amount ($) (a) | Value ($) |
|---|---|---|
| Jicarilla, NM, Sales & Special Tax Revenue, Apache Nation Revenue, 144A, 5.2%, 12/1/2013 | 410,000 | 405,957 |
| Kentucky, Asset/Liability Commission, General Fund Revenue, 3.165%, 4/1/2018 | 1,800,000 | 1,759,248 |
| Los Angeles, CA, Community Development Agency Tax Allocation Revenue, Adelante Eastside Project, Series C, 6.49%, 9/1/2037 INS: Radian | 315,000 | 256,684 |
| Louisville & Jefferson County, KY, Metropolitan Sewer District & Drain Systems, Build America Bonds, 6.25%, 5/15/2043 | 400,000 | 402,744 |
| Nashville & Davidson County, TN, Metropolitan Government, Convention Center Authority Revenue, Build America Bonds, Series B, 6.731%, 7/1/2043 | 400,000 | 400,632 |
| New Jersey, Economic Development Authority Revenue, Series B, 6.5%, 11/1/2013 INS: AGC | 860,000 | 959,975 |
| Pennsylvania, State General Obligation, First Series, 5.25%, 2/1/2014 INS: NATL | 625,000 | 700,944 |
| Port Authority New York & New Jersey, One Hundred Fiftieth Series, 4.75%, 9/15/2016 | 930,000 | 975,961 |
| Rhode Island, Convention Center Authority Revenue, Civic Center, Series A, 6.06%, 5/15/2035 INS: AGMC | 515,000 | 491,233 |
| Virgin Islands, Port Authority Marine Revenue, Series B, 5.08%, 9/1/2013 INS: AGMC | 895,000 | 910,126 |
| Virginia, College Building Authority, Educational Facilities Revenue, 21st Century College, Series B, 5.0%, 2/1/2014 | 930,000 | 1,034,197 |
| Washington, Central Puget Sound Regional Transit Authority, Sales & Use Tax Revenue, Series A, 5.0%, 11/1/2036 | 285,000 | 284,364 |
| **Total Municipal Bonds and Notes** (Cost $9,625,860) | | **9,703,391** |

| | Shares | Value ($) |
|---|---|---|
| **Securities Lending Collateral 17.9%** | | |
| Daily Assets Fund Institutional, 0.27% (e) (f) (Cost $27,864,495) | 27,864,495 | **27,864,495** |
| **Cash Equivalents 2.0%** | | |
| Central Cash Management Fund, 0.19% (e) (Cost $3,051,609) | 3,051,609 | **3,051,609** |

| | % of Net Assets | Value ($) |
|---|---|---|
| **Total Investment Portfolio** (Cost $215,786,631)† | 138.9 | **215,816,211** |
| **Other Assets and Liabilities, Net** | (38.9) | **(60,438,518)** |
| **Net Assets** | 100.0 | **155,377,693** |

* *Non-income producing security.*

** *These securities are shown at their current rate as of December 31, 2010. Floating rate securities' yields vary with a designated market index or market rate, such as the coupon-equivalent of the US Treasury bill rate.*

*** *Annualized yield at time of purchase; not a coupon rate.*

† *The cost for federal income tax purposes was $215,805,423. At December 31, 2010, net unrealized appreciation for all securities based on tax cost was $10,788. This consisted of aggregate gross unrealized appreciation for all securities in which there was an excess of value over tax cost of $5,609,966 and aggregate gross unrealized depreciation for all securities in which there was an excess of tax cost over value of $5,599,178.*

(a) *Principal amount stated in US dollars unless otherwise noted.*

(b) *When-issued or delayed delivery security included.*

(c) *At December 31, 2010, this security has been pledged, in whole or in part, to cover initial margin requirements for open futures contracts.*

(d) *All or a portion of these securities were on loan (see Notes to Financial Statements). The value of all securities loaned at December 31, 2010 amounted to $27,157,007, which is 17.5% of net assets.*

(e) *Affiliated fund managed by Deutsche Investment Management Americas Inc. The rate shown is the annualized seven-day yield at period end.*

(f) *Represents collateral held in connection with securities lending. Income earned by the Fund is net of borrower rebates.*

(g) *Security is linked to Argentine Republic Gross Domestic Product (GDP). Security does not pay principal over life of security or at expiration. Payments are based on growth of Argentina GDP, subject to certain conditions.*

*144A: Security exempt from registration under Rule 144A of the Securities Act of 1933. These securities may be resold in transactions exempt from registration, normally to qualified institutional buyers.*

*AGC: Assured Guaranty Corp.*

*AGMC: Assured Guaranty Municipal Corp.*

*FDIC: Federal Deposit Insurance Corp.*

*GDP: Gross Domestic Product*

*INS: Insured*

*Interest Only: Interest Only (IO) bonds represent the "interest only" portion of payments on a pool of underlying mortgages or mortgage-backed securities. IO securities are subject to prepayment risk of the pool of underlying mortgages.*

*NATL: National Public Finance Guaranty Corp.*

*Radian: Radian Asset Assurance, Inc.*

*REG S: Securities sold under Regulation S may not be offered, sold or delivered within the United States or to, or for the account or benefit of, US persons, except pursuant to an exemption from, or in a transaction not subject to, the registration requirements of the Securities Act of 1933.*

*The accompanying notes are an integral part of the financial statements.*

*Included in the Fund are investments in mortgage- or asset-backed securities which are interests in separate pools of mortgages or assets. Effective maturities of these investments may be shorter than stated maturities due to prepayments. Some separate investments in the Federal Home Loan Mortgage Corp. and Federal National Mortgage Association issues have similar coupon rates and have been aggregated for presentation purposes in the investment portfolio.*

*At December 31, 2010, open futures contracts sold were as follows:*

| Futures | Currency | Expiration Date | Contracts | Notional Value ($) | Unrealized Appreciation (Depreciation) ($) |
|---|---|---|---|---|---|
| 10 Year US Treasury Note | USD | 3/22/2011 | 280 | 33,722,500 | 884,109 |
| British Pound Currency | USD | 3/14/2011 | 33 | 3,213,581 | 36,094 |
| Japanese Yen Currency | USD | 3/14/2011 | 14 | 2,157,400 | (59,484) |
| Ultra Long Term US Treasury Bond | USD | 3/22/2011 | 8 | 1,016,750 | 27,937 |
| **Total net unrealized appreciation** | | | | | **888,656** |

*As of December 31, 2010, the Fund had the following open forward foreign currency exchange contracts:*

| Contracts to Deliver | | In Exchange For | | Settlement Date | Unrealized Appreciation ($) | Counterparty |
|---|---|---|---|---|---|---|
| USD | 359,989 | EUR | 275,000 | 2/4/2011 | 7,468 | HSBC Bank USA |
| EUR | 900,000 | USD | 1,244,133 | 2/4/2011 | 41,548 | HSBC Bank USA |
| **Total net unrealized appreciation** | | | | | **49,016** | |

*As of December 31, 2010, the Fund had the following open forward foreign currency exchange contracts:*

| Contracts to Deliver | | In Exchange For | | Settlement Date | Unrealized Depreciation ($) | Counterparty |
|---|---|---|---|---|---|---|
| RUB | 3,600,000 | USD | 116,522 | 2/4/2011 | **(990)** | JPMorgan Chase Securities, Inc. |

| **Currency Abbreviations** | | | |
|---|---|---|---|
| EGP | Egyptian Pound | RUB | Russian Ruble |
| EUR | Euro | USD | United States Dollar |

*For information on the Fund's policy and additional disclosures regarding futures contracts and forward foreign currency exchange contracts, please refer to Note B in the accompanying Notes to Financial Statements.*

## Fair Value Measurements

*Various inputs are used in determining the value of the Fund's investments. These inputs are summarized in three broad levels. Level 1 includes quoted prices in active markets for identical securities. Level 2 includes other significant observable inputs (including quoted prices for similar securities, interest rates, prepayment speeds, and credit risk). Level 3 includes significant unobservable inputs (including the Fund's own assumptions in determining the fair value of investments). The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities.*

*The following is a summary of the inputs used as of December 31, 2010 in valuing the Fund's investments. For information on the Fund's policy regarding the valuation of investments, please refer to the Security Valuation section of Note A in the accompanying Notes to Financial Statements.*

| Assets | Level 1 | Level 2 | Level 3 | Total |
|---|---|---|---|---|
| Fixed Income Investments (h) | | | | |
| Corporate Bonds | $ — | $ 57,920,478 | $ — | $ 57,920,478 |
| Mortgage-Backed Securities Pass-Throughs | — | 53,336,816 | — | 53,336,816 |
| Commercial Mortgage-Backed Securities | — | 16,245,833 | — | 16,245,833 |
| Collateralized Mortgage Obligations | — | 8,390,144 | — | 8,390,144 |
| Government & Agency Obligations | — | 38,963,545 | — | 38,963,545 |
| Loan Participations and Assignments | — | 339,900 | — | 339,900 |
| Municipal Bonds and Notes | — | 9,703,391 | — | 9,703,391 |
| Short-Term Investments (h) | 30,916,104 | — | — | 30,916,104 |
| Derivatives (i) | 888,656 | 49,016 | — | 937,672 |
| **Total** | **$ 31,804,760** | **$ 184,949,123** | **$ —** | **$ 216,753,883** |
| **Liabilities** | | | | |
| Derivatives (i) | $ — | $ (990) | $ — | $ (990) |
| **Total** | **$ —** | **$ (990)** | **$ —** | **$ (990)** |

*There have been no significant transfers in and out of Level 1 and Level 2 fair value measurements during the year ended December 31, 2010.*

(h) *See Investment Portfolio for additional detailed categorizations.*

(i) *Derivatives include unrealized appreciation (depreciation) on open futures contracts and forward foreign currency exchange contracts.*

*The accompanying notes are an integral part of the financial statements.*

## Level 3 Reconciliation

*The following is a reconciliation of the Fund's Level 3 investments for which significant unobservable inputs were used in determining value:*

| | Government & Agency Obligations |
|---|---|
| **Balance as of December 31, 2009** | $ 41,830 |
| Realized gains (loss) | — |
| Change in unrealized appreciation (depreciation) | — |
| Amortization premium/discount | — |
| Net purchases (sales) | — |
| Transfers into of Level 3 | — |
| Transfers (out) of Level 3 | (41,830) (j) |
| **Balance as of December 31, 2010** | **$ —** |
| **Net change in unrealized appreciation (depreciation) from investments still held as of December 31, 2010** | **$ —** |

*Transfers between price levels are recognized at the beginning of the reporting period.*

(j) *The investment was transferred from Level 3 to Level 2 as a result of the availability of a pricing source supported by observable inputs.*

*The accompanying notes are an integral part of the financial statements.*

# Statement of Assets and Liabilities

as of December 31, 2010

| | |
|---|---|
| **Assets** | |
| Investments: | |
| Investments in securities, at value (cost $184,870,527), including $27,157,007 of securities loaned | $ 184,900,107 |
| Investment in Daily Assets Fund Institutional (cost $27,864,495)* | 27,864,495 |
| Investment in Central Cash Management Fund (cost $3,051,609) | 3,051,609 |
| Total investments, at value (cost $215,786,631) | 215,816,211 |
| Cash | 68,563 |
| Foreign currency, at value (cost $56,665) | 55,198 |
| Receivable for Fund shares sold | 117,035 |
| Interest receivable | 1,710,134 |
| Unrealized appreciation on open forward foreign currency exchange contracts | 49,016 |
| Foreign taxes recoverable | 1,177 |
| Other assets | 898 |
| Total assets | 217,818,232 |
| **Liabilities** | |
| Payable upon return of securities loaned | 27,864,495 |
| Payable for Investments purchased | 8,062 |
| Payable for investments purchased — when-issued/delayed delivery securities | 34,176,235 |
| Payable for Fund shares redeemed | 61,489 |
| Payable for daily variation margin on open futures contracts | 185,468 |
| Unrealized depreciation on open forward foreign currency exchange contracts | 990 |
| Accrued management fee | 48,171 |
| Other accrued expenses and payables | 95,629 |
| Total liabilities | 62,440,539 |
| **Net assets, at value** | **$ 155,377,693** |
| **Net Assets Consist of** | |
| Undistributed net investment income | 4,830,117 |
| Net unrealized appreciation (depreciation) on: | |
| Investments | 29,580 |
| Futures | 888,656 |
| Foreign currency | 46,460 |
| Accumulated net realized gain (loss) | (38,064,434) |
| Paid-in capital | 187,647,314 |
| **Net assets, at value** | **$ 155,377,693** |
| **Class A** | |
| **Net Asset Value,** offering and redemption price per share ($155,377,693 ÷ 27,458,970 outstanding shares of beneficial interest, $.01 par value, unlimited number of shares authorized) | **$ 5.66** |

* *Represents collateral on securities loaned.*

# Statement of Operations

for the year ended December 31, 2010

| | |
|---|---|
| **Investment Income** | |
| Income: | |
| Interest | $ 6,336,947 |
| Dividends | 2,496 |
| Income distributions — Central Cash Management Fund | 54,930 |
| Securities lending income, including income from Daily Assets Fund Institutional, net of borrower rebates | 15,190 |
| Total income | 6,409,563 |
| Expenses: | |
| Management fee | 623,165 |
| Administration fee | 159,786 |
| Services to shareholders | 6,328 |
| Custodian fee | 23,438 |
| Professional fees | 57,501 |
| Trustees' fees and expenses | 8,721 |
| Reports to shareholders | 46,313 |
| Other | 23,323 |
| Total expenses | 948,575 |
| **Net investment income** | **5,460,988** |
| **Realized and Unrealized Gain (Loss)** | |
| Net realized gain (loss) from: | |
| Investments | 6,379,975 |
| Futures | (1,314,321) |
| Foreign currency | (58,246) |
| Payments by affiliates (see Note H) | 7,050 |
| | 5,014,458 |
| Change in net unrealized appreciation (depreciation) on: | |
| Investments | (372,242) |
| Futures | 332,060 |
| Foreign currency | 43,683 |
| | 3,501 |
| **Net gain (loss)** | **5,017,959** |
| **Net increase (decrease) in net assets resulting from operations** | **$ 10,478,947** |

*The accompanying notes are an integral part of the financial statements.*

# Statement of Changes in Net Assets

| Increase (Decrease) in Net Assets | Years Ended December 31, 2010 | 2009 |
|---|---|---|
| Operations: | | |
| Net investment income | $ 5,460,988 | $ 7,096,250 |
| Net realized gain (loss) | 5,014,458 | (22,284,758) |
| Change in net unrealized appreciation (depreciation) | 3,501 | 29,440,278 |
| Net increase (decrease) in net assets resulting from operations | 10,478,947 | 14,251,770 |
| Distributions to shareholders from: | | |
| Net investment income: | | |
| Class A | (6,962,542) | (11,985,798) |
| Fund share transactions: | | |
| **Class A** | | |
| Proceeds from shares sold | 16,049,365 | 21,968,991 |
| Reinvestment of distributions | 6,962,542 | 11,985,798 |
| Cost of shares redeemed | (29,824,695) | (32,370,197) |
| Net increase (decrease) in net assets from Class A share transactions | (6,812,788) | 1,584,592 |
| **Increase (decrease) in net assets** | (3,296,383) | 3,850,564 |
| Net assets at beginning of period | 158,674,076 | 154,823,512 |
| Net assets at end of period (including undistributed net investment income of $4,830,117 and $6,639,923, respectively) | **$ 155,377,693** | **$ 158,674,076** |

| Other Information | | |
|---|---|---|
| **Class A** | | |
| Shares outstanding at beginning of period | 28,638,100 | 28,147,936 |
| Shares sold | 2,857,267 | 4,088,614 |
| Shares issued to shareholders in reinvestment of distributions | 1,277,530 | 2,364,063 |
| Shares redeemed | (5,313,927) | (5,962,513) |
| Net increase (decrease) in Class A shares | (1,179,130) | 490,164 |
| Shares outstanding at end of period | **27,458,970** | **28,638,100** |

*The accompanying notes are an integral part of the financial statements.*

# Financial Highlights

## Class A

| Years Ended December 31, | 2010 | 2009 | 2008 | 2007 | 2006 |
|---|---|---|---|---|---|
| **Selected Per Share Data** | | | | | |
| **Net asset value, beginning of period** | **$ 5.54** | **$ 5.50** | **$ 6.98** | **$ 7.03** | **$ 6.99** |
| *Income (loss) from investment operations:* | | | | | |
| Net investment income[a] | .19 | .25 | .37 | .35 | .33 |
| Net realized and unrealized gain (loss) | .18 | .26 | (1.48) | (.06) | (.01) |
| **Total from investment operations** | .37 | .51 | (1.11) | .29 | .32 |
| *Less distributions from:* | | | | | |
| Net investment income | (.25) | (.47) | (.37) | (.34) | (.27) |
| Net realized gains | — | — | — | — | (.01) |
| **Total distributions** | (.25) | (.47) | (.37) | (.34) | (.28) |
| **Net asset value, end of period** | **$ 5.66** | **$ 5.54** | **$ 5.50** | **$ 6.98** | **$ 7.03** |
| Total Return (%) | 6.79 | 10.07 | (16.77) | 4.18 | 4.72[b] |
| **Ratios to Average Net Assets and Supplemental Data** | | | | | |
| Net assets, end of period ($ millions) | 155 | 159 | 155 | 229 | 218 |
| Ratio of expenses before expense reductions (%) | .59 | .59 | .59 | .61 | .66 |
| Ratio of expenses after expense reductions (%) | .59 | .59 | .59 | .61 | .62 |
| Ratio of net investment income (%) | 3.42 | 4.68 | 5.76 | 5.03 | 4.82 |
| Portfolio turnover rate (%) | 357 | 284 | 196 | 185 | 186 |

a *Based on average shares outstanding during the period.*

b *Total return would have been lower had certain expenses not been reduced.*

# Notes to Financial Statements

## A. Organization and Significant Accounting Policies

DWS Variable Series I (the "Series") is registered under the Investment Company Act of 1940, as amended (the "1940 Act"), as an open-end, registered management investment company organized as a Massachusetts business trust. The Series consists of six diversified funds: DWS Bond VIP, DWS Growth & Income VIP, DWS Capital Growth VIP, DWS Global Opportunities VIP, DWS International VIP and DWS Health Care VIP (individually or collectively hereinafter referred to as a "Fund" or the "Funds"). These financial statements report on DWS Bond VIP. The Series is intended to be the underlying investment vehicle for variable annuity contracts and variable life insurance policies to be offered by the separate accounts of certain life insurance companies ("Participating Insurance Companies").

The Series' financial statements are prepared in accordance with accounting principles generally accepted in the United States of America, which require the use of management estimates. Actual results could differ from those estimates. The policies described below are followed consistently by the Series in the preparation of the financial statements for its Funds.

**Security Valuation.** Investments are stated at value determined as of the close of regular trading on the New York Stock Exchange on each day the exchange is open for trading.

Various inputs are used in determining the value of the Fund's investments. These inputs are summarized in three broad levels. Level 1 includes quoted prices in active markets for identical securities. Level 2 includes other significant observable inputs (including quoted prices for similar securities, interest rates, prepayment speeds, and credit risk). Level 3 includes significant unobservable inputs (including the Fund's own assumptions in determining the fair value of investments). The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities.

Debt securities are valued by independent pricing services approved by the Trustees of the Series. If the pricing services are unable to provide valuations, securities are valued at the most recent bid quotation or evaluated price, as applicable, obtained from one or more broker-dealers. Such services may use various pricing techniques which take into account appropriate factors such as yield, quality, coupon rate, maturity, type of issue, trading characteristics and other data, as well as broker quotes. These securities are generally categorized as Level 2.

Futures contracts are generally valued at the settlement prices established each day on the exchange on which they are traded and are categorized as Level 1.

Forward currency contracts are valued at the prevailing forward exchange rate of the underlying currencies and are categorized as Level 2.

Money market instruments purchased with an original or remaining maturity of sixty days or less, maturing at par, are valued at amortized cost, which approximates value, and are categorized as Level 2. Investments in open-end investment companies are valued at their net asset value each business day and are categorized as Level 1.

Securities and other assets for which market quotations are not readily available or for which the above valuation procedures are deemed not to reflect fair value are valued in a manner that is intended to reflect their fair value as determined in accordance with procedures approved by the Trustees and are generally categorized as Level 3. In accordance with the Fund's valuation procedures, factors used in determining value may include, but are not limited to, the type of the security; the size of the holding; the initial cost of the security; the existence of any contractual restrictions on the security's disposition; the price and extent of public trading in similar securities of the issuer or of comparable companies; quotations or evaluated prices from broker-dealers and/or pricing services; information obtained from the issuer, analysts, and/or the appropriate stock exchange (for exchange-traded securities); an analysis of the company's or issuer's financial statements; an evaluation of the forces that influence the issuer and the market(s) in which the security is purchased and sold and with respect to debt securities; the maturity, coupon, creditworthiness, currency denomination and the movement of the market in which the security is normally traded. The value determined under these procedures may differ from published values for the same securities.

Disclosure about the classification of fair value measurements is included in a table following the Fund's Investment Portfolio.

**Securities Lending.** The Fund lends securities to certain financial institutions. The Fund retains beneficial ownership of the securities it has loaned and continues to receive interest and dividends paid by the issuer of securities and to participate in any changes in their market value. The Fund requires the borrowers of the securities to maintain collateral with the Fund consisting of either cash or liquid, unencumbered assets having a value at least equal to the value of the securities loaned. When the collateral falls below specified amounts, the lending agent will use its best effort to obtain additional collateral on the next business day to meet required amounts under the security lending agreement. The Fund may invest the cash collateral into a joint trading account in an affiliated money market fund pursuant to Exemptive Orders issued by the SEC. The Fund receives compensation for lending its securities either in the form of fees or by earning interest on invested cash collateral net of borrower rebates and fees paid to a lending agent. Either the Fund or the borrower may terminate the loan. There may be risks of delay and costs in recovery of securities or even loss of rights in the collateral should the borrower of the securities fail financially. The Fund is also subject to all investment risks associated with the reinvestment of any cash collateral received, including, but not limited to, interest rate, credit and liquidity risk associated with such investments.

**Foreign Currency Translations.** The books and records of the Fund are maintained in US dollars. Investment securities and other assets and liabilities denominated in a foreign currency are translated into US dollars at the prevailing exchange rates at period end. Purchases and sales of investment securities, income and expenses are translated into US dollars at the prevailing exchange rates on the respective dates of the transactions.

Net realized and unrealized gains and losses on foreign currency transactions represent net gains and losses between trade and settlement dates on securities transactions, the disposition of forward foreign currency exchange contracts and foreign currencies, and the difference between the amount of net investment income accrued and the US dollar amount actually received. That portion of both realized and unrealized gains and losses on investments that results from fluctuations in foreign currency exchange rates is not separately disclosed but is included with net realized and unrealized gain/appreciation and loss/depreciation on investments.

**Mortgage Dollar Rolls.** The Fund may enter into mortgage dollar rolls in which the Fund sells to a bank or broker/dealer (the "counterparty") mortgage-backed securities for delivery in the current month and simultaneously contracts to repurchase similar, but not identical, securities on a fixed date. The counterparty receives all principal and interest payments, including prepayments, made on the security while it is the holder. The Fund receives compensation as consideration for entering into the commitment to repurchase. The compensation is paid in the form of a lower price for the security upon its repurchase, or alternatively, a fee. Mortgage dollar rolls may be renewed with a new sale and repurchase price and a cash settlement made at each renewal without physical delivery of the securities subject to the contract.

Certain risks may arise upon entering into mortgage dollar rolls from the potential inability of counterparties to meet the terms of their commitments. Additionally, the value of such securities may change adversely before the Fund is able to repurchase them. There can be no assurance that the Fund's use of the cash that it receives from a mortgage dollar roll will provide a return that exceeds its costs.

**When-Issued/Delayed Securities.** The Fund may purchase securities with delivery or payment to occur at a later date beyond the normal settlement period. At the time the Fund enters into a commitment to purchase a security, the transaction is recorded and the value of the security is reflected in the net asset value. The price of such security and the date when the security will be delivered and paid for are fixed at the time the transaction is negotiated. The value of the security may vary with market fluctuations. No interest accrues to the Fund until payment takes place. At the time the Fund enters into this type of transaction it is required to segregate cash or other liquid assets at least equal to the amount of the commitment.

Certain risks may arise upon entering into when-issued or delayed delivery securities from the potential inability of counterparties to meet the terms of their contracts or if the issuer does not issue the securities due to political, economic, or other factors. Additionally, losses may arise due to changes in the value of the underlying securities.

**Taxes.** The Fund is treated as a separate taxpayer as provided for in the Internal Revenue Code, as amended. It is the Fund's policy to comply with the requirements of the Internal Revenue Code, as amended, which are applicable to regulated investment companies, and to distribute all of its taxable income to the separate accounts of the Participating Insurance Companies which hold its shares.

At December 31, 2010, the Fund had an approximate net tax basis capital loss carryforward which may be applied against any realized net taxable capital gains of each succeeding year until fully utilized or until the following expiration date, whichever occurs first:

| Fund | Capital Loss Carryforwards ($) | Expiration Date | Capital Loss Carryfowards Utilized ($) |
|---|---|---|---|
| DWS Bond VIP | 37,157,000 | 12/31/2017 | 5,674,000 |

The Fund has reviewed the tax positions for the open tax years as of December 31, 2010 and has determined that no provision for income tax is required in the Fund's financial statements. The Fund's federal tax returns for the prior three fiscal years remain open subject to examination by the Internal Revenue Service.

**Distribution of Income and Gains.** The Fund will declare and distribute dividends from its net investment income, if any, annually, although additional distributions may be made if necessary. Net realized gains from investment transactions, in excess of available capital loss carryforwards, would be taxable to the Fund if not distributed, and, therefore, will be distributed to shareholders at least annually.

The timing and characterization of certain income and capital gains distributions are determined annually in accordance with federal tax regulations which may differ from accounting principles generally accepted in the United States of America. These differences primarily relate to investments in foreign denominated investments, investments in forward foreign currency exchange contracts and certain securities sold at a loss. As a result, net investment income (loss) and net realized gain (loss) on investment transactions for a reporting period may differ significantly from distributions during such period. Accordingly, the Fund may periodically make reclassifications among certain of its capital accounts without impacting the net asset value of the Fund.

At December 31, 2010, the Fund's components of distributable earnings (accumulated losses) on a tax-basis are as follows:

| Fund | Undistributed Ordinary Income ($)* | Capital Loss Carryforwards ($) | Net Unrealized Gain (Loss) on Investments ($) |
|---|---|---|---|
| DWS Bond VIP | 4,878,143 | (37,157,000) | 10,788 |

In addition, the tax character of distributions paid to shareholders by the Fund is summarized as follows:

| Fund | Distributions from Ordinary Income ($)* Years Ended December 31, 2010 | 2009 |
|---|---|---|
| DWS Bond VIP | 6,962,542 | 11,985,798 |

* *For tax purposes, short-term capital gains distributions are considered ordinary income distributions.*

**Expenses.** Expenses of the Series arising in connection with a specific Fund are allocated to that Fund. Other Series expenses which cannot be directly attributed to a Fund are apportioned among the Funds in the Series.

**Contingencies.** In the normal course of business, the Fund may enter into contracts with service providers that contain general indemnification clauses. The Fund's maximum exposure under these arrangements is unknown as this would involve future claims that may be made against the Fund that have not yet been made. However, based on experience, the Fund expects the risk of loss to be remote.

**Other.** Investment transactions are accounted for on a trade date plus one basis for daily net asset value calculations. However, for financial reporting purposes, investment transactions are reported on trade date. Interest income is recorded on the accrual basis net of foreign withholding taxes. Dividend income is recorded on the ex-dividend date net of foreign withholding taxes. Certain dividends from foreign securities may be recorded subsequent to the ex-dividend date as soon as the Fund is informed of such dividends. Realized gains and losses from investment transactions are recorded on an identified cost basis. All discounts and premiums are accreted/amortized for both tax and financial reporting purposes.

## B. Derivative Instruments

**Futures Contracts.** A futures contract is an agreement between a buyer or seller and an established futures exchange or its clearinghouse in which the buyer or seller agrees to take or make a delivery of a specific amount of a financial instrument at a specified price on a specific date (settlement date). For the year ended December 31, 2010, the Fund invested in interest rate futures to gain exposure to different parts of the yield curve while managing the overall duration. The Fund also entered into currency futures contracts for non-hedging purposes to seek to enhance potential gains.

Futures contracts are valued at the most recent settlement price. Upon entering into a futures contract, the Fund is required to deposit with a financial intermediary cash or securities ("initial margin") in an amount equal to a certain percentage of the face value indicated in the futures contract. Subsequent payments ("variation margin") are made or received by the Fund dependent upon the daily fluctuations in the value and are recorded for financial reporting purposes as unrealized gains or losses by the Fund. Gains or losses are realized when the contract expires or is closed. Since all futures contracts are exchange traded, counterparty risk is minimized as the exchange's clearinghouse acts as the counterparty, and guarantees the futures against default.

Certain risks may arise upon entering into futures contracts, including the risk that an illiquid market will limit the Fund's ability to close out a futures contract prior to the settlement date and that a change in the value of a futures contract may not correlate exactly with the changes in the value of the underlying hedged security, index or currency. Risk of loss may exceed amounts recognized in the Statement of Assets and Liabilities.

A summary of the open futures contracts as of December 31, 2010, is included in a table following the Fund's Investment Portfolio. For the year ended December 31, 2010, the Fund's investment in futures contracts purchased had a total notional value generally indicative of a range from $0 to approximately $9,400,000 and the investment in futures contracts sold had a total notional value generally indicative of a range from approximately $26,111,000 to $43,275,000.

**Forward Foreign Currency Exchange Contracts.** A forward foreign currency exchange contract ("forward currency contract") is a commitment to purchase or sell a foreign currency at the settlement date at a negotiated rate. The Fund is subject to foreign exchange rate risk in its securities denominated in foreign currencies. Changes in exchange rates between foreign currencies and the US dollar may affect the US dollar value of foreign securities or the income or gains received on these securities. To reduce the effect of currency fluctuations, the Fund may enter into forward foreign currency exchange contracts. For the year ended December 31, 2010, the Fund invested in forward foreign currency contracts to hedge its exposure to changes in foreign currency exchange rates on its foreign currency denominated securities.

Forward currency contracts are valued at the prevailing forward exchange rate of the underlying currencies and unrealized gain (loss) is recorded daily. On the settlement date of the forward currency contract, the Fund records a realized gain or loss equal to the difference between the value of the contract at the time it was opened and the value of the contract at the time it was closed. Certain risks may arise upon entering into forward currency contracts from the potential inability of counterparties to meet the terms of their contracts. The maximum counterparty credit risk to the Fund is measured by the unrealized gain on appreciated contracts. Additionally, when utilizing forward currency contracts to hedge, the Fund gives up the opportunity to profit from favorable exchange rate movements during the term of the contract.

A summary of the open forward currency contracts as of December 31, 2010, is included in a table following the Fund's Investment Portfolio. For the year ended December 31, 2010, the investment in forward currency contracts US dollars purchased had a total contract value generally indicative of a range from approximately $113,000 to $1,361,000 and the investment in forward currency contracts US dollars sold had a total contract value generally indicative of a range from $0 to approximately $360,000.

The following tables summarize the value of the Fund's derivative instruments held as of December 31, 2010 and the related location in the accompanying Statement of Assets and Liabilities, presented by primary underlying risk exposure:

| **Asset Derivative** | **Forward Contracts** |
|---|---|
| Foreign Exchange Contracts (a) | **$ 49,016** |

*The above derivative is located in the following Statement of Assets and Liabilities account:*

(a) *Unrealized appreciation on open forward foreign currency exchange contracts*

| **Liability Derivatives** | **Forward Contracts** | **Futures Contracts** | **Total** |
|---|---|---|---|
| Foreign Exchange Contracts (a) (b) | $ (990) | $ (23,390) | $ (24,380) |
| Interest Rate Contracts (b) | $ — | 912,046 | 912,046 |
| | **$ (990)** | **$ 888,656** | **$ 887,666** |

*Each of the above derivatives is located in the following Statement of Assets and Liabilities accounts:*

(a) *Unrealized depreciation on open forward foreign currency exchange contracts*

(b) *Net unrealized appreciation (depreciation) on futures. Liability of Payable for daily variation margin on open futures contracts reflects unsettled variation margin.*

Additionally, the amount of unrealized and realized gains and losses on derivative instruments recognized in Fund earnings during the year ended December 31, 2010 and the related location in the accompanying Statement of Operations is summarized in the following tables by primary underlying risk exposure:

| **Realized Gain (Loss)** | **Forward Contracts** | **Futures Contracts** | **Total** |
|---|---|---|---|
| Foreign Exchange Contracts (a) (b) | $ (10,064) | $ 285,798 | $ 275,734 |
| Interest Rate Contracts (b) | — | (1,600,119) | (1,600,119) |
| | **$ (10,064)** | **$ (1,314,321)** | **$ (1,324,385)** |

*Each of the above derivatives is located in the following Statement of Operations accounts:*

(a) *Net realized gain (loss) from foreign currency (Statement of Operations includes both forward currency contracts and foreign currency transactions)*

(b) *Net realized gain (loss) from futures*

| Change in Net Unrealized Appreciation (Depreciation) | Forward Contracts | Futures Contracts | Total |
|---|---|---|---|
| Foreign Exchange Contracts (a) (b) | $ 46,185 | $ (118,805) | $ (72,620) |
| Interest Rate Contracts (b) | — | 450,865 | 450,865 |
| | **$ 46,185** | **$ 332,060** | **$ 378,245** |

*Each of the above derivatives is located in the following Statement of Operations accounts:*

(a) *Change in net unrealized appreciation (depreciation) on foreign currency (Statement of Operations includes both forward currency contracts and foreign currency transactions)*

(b) *Change in net unrealized appreciation (depreciation) on futures*

## C. Purchases and Sales of Securities

During the year ended December 31, 2010, purchases and sales of investment securities (excluding short-term investments) were as follows:

| Fund | Purchases ($) | Sales ($) |
|---|---|---|
| DWS Bond VIP excluding US Treasury Obligations | 488,452,938 | 484,940,995 |
| US Treasury Obligations | 85,194,891 | 82,519,882 |

## D. Related Parties

Under the Investment Management Agreement with Deutsche Investment Management Americas Inc. ("DIMA" or the "Advisor"), an indirect, wholly owned subsidiary of Deutsche Bank AG, the Advisor directs the investments of the Fund in accordance with its investment objectives, policies and restrictions. The Advisor determines the securities, instruments and other contracts relating to investments to be purchased, sold or entered into by the Fund.

Under the Investment Management Agreement with the Advisor, the Fund pays a monthly management fee, based on the average daily net assets of the Fund, computed and accrued daily and payable monthly, at the annual rates shown below:

| Fund | Annual Management Fee Rate |
|---|---|
| DWS Bond VIP first $250 million of average daily net assets | .390% |
| next $750 million of average daily net assets | .365% |
| over $1 billion of average daily net assets | .340% |

For the year ended December 31, 2010, the total management fee and effective management fee rate are as follows:

| Fund | Total Aggregated ($) | Annual Effective Rate |
|---|---|---|
| DWS Bond VIP | 623,165 | .39% |

**Administration Fee.** Pursuant to an Administrative Services Agreement, DIMA provides most administrative services to the Series. For all services provided under the Administrative Services Agreement, the Fund pays the Advisor an annual fee ("Administration Fee") of 0.10% of the Fund's average daily net assets, computed and accrued daily and payable monthly. For the year ended December 31, 2010, the Administration Fee was as follows:

| Fund | Total Aggregated ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS Bond VIP | 159,786 | 13,159 |

**Service Provider Fees.** DWS Investments Service Company ("DISC"), an affiliate of the Advisor, is the transfer agent, dividend-paying agent and shareholder service agent for the Series. Pursuant to a sub-transfer agency agreement between DISC and DST Systems, Inc. ("DST"), DISC has delegated certain transfer agent, dividend-paying agent and shareholder service agent functions to DST. DISC compensates DST out of the shareholder servicing fee it receives from the Fund. For the year ended December 31, 2010, the amounts charged to the Fund by DISC were as follows:

| Fund | Total Aggregated ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS Bond VIP Class A | 730 | 186 |

**Typesetting and Filing Service Fees.** Under an agreement with DIMA, DIMA is compensated for providing typesetting and certain regulatory filing services to the Fund. For the year ended December 31, 2010, the amount charged to the Fund by DIMA included in the Statement of Operations under "reports to shareholders" was as follows:

| Fund | Total Aggregated ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS Bond VIP | 13,045 | 3,334 |

**Trustees' Fees and Expenses.** The Fund paid each Trustee not affiliated with the Advisor retainer fees plus specified amounts for various committee services and for the Board Chairperson.

**Affiliated Cash Management Vehicles.** The Fund may invest uninvested cash balances in Central Cash Management Fund, which is managed by the Advisor. The Fund indirectly bears its proportionate share of the expenses of the underlying money market funds. Central Cash Management Fund does not pay the Advisor an investment management fee. Central Cash Management Fund seeks a high level of current income consistent with liquidity and the preservation of capital.

## E. Investing in Emerging Markets

Investing in emerging markets may involve special risks and considerations not typically associated with investing in developed markets. These risks include revaluation of currencies, high rates of inflation or deflation, repatriation restrictions on income and capital, and future adverse political, social and economic developments. Moreover, securities issued in these markets may be less liquid, subject to government ownership controls or delayed settlements and may have prices more volatile or less easily assessed than those of comparable securities of issuers in developed markets.

## F. Ownership of the Fund

One participating insurance company was an owner of record of 10% or more of the total outstanding Class A shares of the Fund, owning 61%.

## G. Line of Credit

The Series and other affiliated funds (the "Participants") share in a $450 million revolving credit facility provided by a syndication of banks. The Fund may borrow for temporary or emergency purposes, including the meeting of redemption requests that otherwise might require the untimely disposition of securities. The Participants are charged an annual commitment fee which is allocated based on net assets, among each of the Participants. Interest is calculated at a rate per annum equal to the sum of the Federal Funds Rate plus 1.25 percent plus if LIBOR exceeds the Federal Funds Rate the amount of such excess. The Fund may borrow up to a maximum of 33 percent of its net assets under the agreement.

## H. Payments Made by Affiliates

During the year ended December 31, 2010, the Advisor fully reimbursed the Fund $7,050 for losses incurred on trades executed incorrectly. The amount reimbursed was less than 0.01% of the Fund's average net assets.

# Report of Independent Registered Public Accounting Firm

**To the Trustees of DWS Variable Series I and the Shareholders of DWS Bond VIP:**

In our opinion, the accompanying statement of assets and liabilities, including the investment portfolio, and the related statements of operations and of changes in net assets and the financial highlights present fairly, in all material respects, the financial position of DWS Bond VIP (the "Fund") at December 31, 2010 and the results of its operations, the changes in its net assets, and the financial highlights for the periods indicated therein, in conformity with accounting principles generally accepted in the United States of America. These financial statements and financial highlights (hereafter referred to as "financial statements") are the responsibility of the Fund's management. Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these financial statements in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits, which included confirmation of securities at December 31, 2010 by correspondence with the custodians and brokers, provide a reasonable basis for our opinion.

Boston, Massachusetts
February 11, 2011

PricewaterhouseCoopers LLP

# Tax Information

**(Unaudited)**

Please consult a tax advisor if you have questions about federal or state income tax laws, or on how to prepare your tax returns. If you have specific questions about your account, please contact your insurance provider.

# Proxy Voting

The Series' policies and procedures for voting proxies for portfolio securities and information about how the Series voted proxies related to its portfolio securities during the 12-month period ended June 30 are available on our Web site — www.dws-investments.com (click on "proxy voting"at the bottom of the page) — or on the SEC's Web site — www.sec.gov. To obtain a written copy of the Series' policies and procedures without charge, upon request, call us toll free at (800) 728-3337.

# Investment Management Agreement Approval

The Board of Trustees, including the Independent Trustees, approved the renewal of your Fund's investment management agreement (the "Agreement") with Deutsche Investment Management Americas Inc. ("DWS") in September 2010.

In terms of the process that the Board followed prior to approving the Agreement, shareholders should know that:

- In September 2010, all of the Fund's Trustees were independent of DWS and its affiliates.
- The Trustees meet frequently to discuss fund matters. Each year, the Trustees dedicate substantial time to contract review matters. Over the course of several months, the Board's Contract Committee, in coordination with the Board's Fixed Income and Quant Oversight Committee, reviewed comprehensive materials received from DWS, independent third parties and independent counsel. These materials included an analysis of the Fund's performance, fees and expenses, and profitability compiled by the Fund's independent fee consultant. The Board also received extensive information throughout the year regarding performance of the Fund.
- The Independent Trustees regularly meet privately with their independent counsel to discuss contract review and other matters. In addition, the Independent Trustees were also advised by the Fund's independent fee consultant in the course of their review of the Fund's contractual arrangements and considered a comprehensive report prepared by the independent fee consultant in connection with their deliberations (the "IFC Report").
- In connection with reviewing the Agreement, the Board also reviewed the terms of the Fund's distribution agreement, administrative services agreement, transfer agency agreement and other material service agreements.
- Based on its evaluation of the information provided, the Contract Committee presented its findings and recommendations to the Independent Trustees as a group. The Independent Trustees reviewed the Contract Committee's findings and recommendations and presented their recommendations to the full Board.

In connection with the contract review process, the Contract Committee and the Board considered the factors discussed below, among others. The Board also considered that DWS and its predecessors have managed the Fund since its inception, and the Board believes that a long-term relationship with a capable, conscientious advisor is in the best interests of the Fund. The Board considered, generally, that shareholders chose to invest or remain invested in the Fund knowing that DWS managed the Fund, and that the Agreement was approved by the Fund's shareholders. DWS is part of Deutsche Bank, a major global banking institution that is engaged in a wide range of financial services. The Board believes that there are significant advantages to being part of a global asset management business that offers a wide range of investing expertise and resources, including hundreds of portfolio managers and analysts with research capabilities in many countries throughout the world.

While shareholders may focus primarily on fund performance and fees, the Fund's Board considers these and many other factors, including the quality and integrity of DWS's personnel and such other issues as back-office operations, fund valuations, and compliance policies and procedures.

**Nature, Quality and Extent of Services.** The Board considered the terms of the Agreement, including the scope of advisory services provided under the Agreement. The Board noted that, under the Agreement, DWS provides portfolio management services to the Fund and that, pursuant to a separate administrative services agreement, DWS provides administrative services to the Fund. The Board considered the experience and skills of senior management and investment personnel, the resources made available to such personnel, the ability of DWS to attract and retain high-quality personnel, and the organizational depth and stability of DWS. The Board reviewed the Fund's performance over short-term and long-term periods and compared those returns to various agreed-upon performance measures, including market indices and a peer universe compiled by the independent fee consultant using information supplied by Lipper Inc. ("Lipper"). The Board also noted that it has put into place a process of identifying "Focus Funds" (e.g., funds performing poorly relative to their benchmark or a peer universe compiled by Lipper), and receives more frequent reporting and information from DWS regarding such funds, along with DWS's remedial plans to address underperformance. The Board believes this process is an effective manner of identifying and addressing underperforming funds. Based on the information provided, the Board noted that for the one-, three- and five-year periods ended December 31, 2009, the Fund's performance (Class A shares) was in the 3rd quartile, 4th quartile and 4th quartile, respectively, of the applicable Lipper universe (the 1st quartile being the best performers and the 4th quartile being the worst performers). The Board also observed that the Fund has outperformed its benchmark in the one-year period and has underperformed its benchmark in the three- and five-year periods ended December 31, 2009.

On the basis of this evaluation and the ongoing review of investment results by the Board, the Board concluded that the nature, quality and extent of services provided by DWS historically have been and continue to be satisfactory.

**Fees and Expenses.** The Board considered the Fund's investment management fee schedule, operating expenses and total expense ratios, and comparative information provided by Lipper and the independent fee consultant regarding investment management fee rates paid to other investment advisors by similar funds (1st quartile being the most favorable and 4th quartile being the least favorable). With respect to management fees paid to other investment advisors by similar funds, the Board noted that the contractual fee rates paid by the Fund, which include a 0.10% fee paid to DWS under the Fund's administrative services agreement, were lower than the median (2nd quartile) of the applicable Lipper peer group (based on Lipper data provided as of December 31, 2009). The Board noted that the Fund's Class A shares total (net) operating expenses were expected to be higher than the median (3rd quartile) of the applicable Lipper expense universe (based on Lipper data provided as of December 31, 2009) ("Lipper Universe Expenses").

The information considered by the Board as part of its review of management fees included information regarding fees charged by DWS and its affiliates to similar institutional accounts and to similar funds offered primarily to European investors ("DWS Europe funds"), in each case as applicable. The Board observed that advisory fee rates for institutional accounts generally were lower than the management fees charged by similarly managed DWS US mutual funds ("DWS Funds"), but also took note of the differences in services provided to DWS Funds as compared to institutional accounts. In the case of DWS Europe funds, the Board observed that fee rates for DWS Europe funds generally were higher than for similarly managed DWS Funds, but noted that differences in the types of services provided to DWS Funds relative to DWS Europe funds made it difficult to compare such fees.

On the basis of the information provided, the Board concluded that management fees were reasonable and appropriate in light of the nature, quality and extent of services provided by DWS.

**Profitability**. The Board reviewed detailed information regarding revenues received by DWS under the Agreement. The Board considered the estimated costs and pre-tax profits realized by DWS from advising the DWS Funds, as well as estimates of the pre-tax profits attributable to managing the Fund in particular. The Board also received information regarding the estimated enterprise-wide profitability of DWS and its affiliates with respect to all fund services in totality and by fund. The Board reviewed DWS's methodology in allocating its costs to the management of the Fund. Based on the information provided, the Board concluded that the pre-tax profits realized by DWS in connection with the management of the Fund were not unreasonable. The Board also reviewed information regarding the profitability of certain similar investment management firms. The Board noted that while information regarding the profitability of such firms is limited (and in some cases is not necessarily prepared on a comparable basis), DWS and its affiliates' overall profitability with respect to the DWS fund complex (after taking into account distribution and other services provided to the funds by DWS and its affiliates) was lower than the overall profitability levels of many comparable firms for which such data was available.

**Economies of Scale.** The Board considered whether there are economies of scale with respect to the management of the Fund and whether the Fund benefits from any economies of scale. The Board noted that the Fund's management fee schedule includes fee breakpoints. The Board concluded that the Fund's fee schedule represents an appropriate sharing between the Fund and DWS of such economies of scale as may exist in the management of the Fund at current asset levels.

**Other Benefits to DWS and Its Affiliates.** The Board also considered the character and amount of other incidental benefits received by DWS and its affiliates, including any fees received by DWS for administrative services provided to the Fund and any fees received by an affiliate of DWS for distribution services. The Board also considered benefits to DWS related to brokerage and soft-dollar allocations, including allocating brokerage to pay for research generated by parties other than the executing broker dealers, which pertain primarily to funds investing in equity securities, along with the incidental public relations benefits to DWS related to DWS Funds advertising and cross-selling opportunities among DWS products and services. The Board concluded that management fees were reasonable in light of these fallout benefits.

**Compliance.** The Board considered the significant attention and resources dedicated by DWS to documenting and enhancing its compliance processes in recent years. The Board noted in particular (i) the experience and seniority of both DWS's chief compliance officer and the Fund's chief compliance officer; (ii) the large number of DWS compliance personnel; and (iii) the substantial commitment of resources by DWS and its affiliates to compliance matters.

Based on all of the information considered and the conclusions reached, the Board unanimously determined that the continuation of the Agreement is in the best interests of the Fund. In making this determination, the Board did not give particular weight to any single factor identified above. The Board considered these factors over the course of numerous meetings, certain of which were in executive session with only the Independent Trustees and their counsel present. It is possible that individual Trustees may have weighed these factors differently in reaching their individual decisions to approve the continuation of the Agreement.

# Summary of Management Fee Evaluation by Independent Fee Consultant

October 3, 2010

Pursuant to an Order entered into by Deutsche Investment Management Americas and affiliates (collectively, "DeAM") with the Attorney General of New York, I, Thomas H. Mack, have been appointed the Independent Fee Consultant for the DWS Funds (formerly the DWS Scudder Funds). My duties include preparing an annual written evaluation of the management fees DeAM charges the Funds, considering among other factors the management fees charged by other mutual fund companies for like services, management fees DeAM charges other clients for like services, DeAM's costs of supplying services under the management agreements and related profit margins, possible economies of scale if a Fund grows larger, and the nature and quality of DeAM's services, including fund performance. This report summarizes my evaluation for 2010, including my qualifications, the evaluation process for each of the DWS Funds, consideration of certain complex-level factors, and my conclusions. I served in substantially the same capacity in 2007, 2008, and 2009.

## Qualifications

For more than 35 years I have served in various professional capacities within the investment management business. I have held investment analysis and advisory positions, including securities analyst, portfolio strategist and director of investment policy with a large investment firm. I have also performed business management functions, including business development, financial management and marketing research and analysis.

Since 1991, I have been an independent consultant within the asset management industry. I have provided services to over 125 client organizations, including investment managers, mutual fund boards, product distributors and related organizations. Over the past ten years I have completed a number of assignments for mutual fund boards, specifically including assisting boards with management contract renewal.

I hold a Master of Business Administration degree, with highest honors, from Harvard University and Master of Science and Bachelor of Science (highest honors) degrees from the University of California at Berkeley. I am an independent director and audit committee financial expert for two closed-end mutual funds and have served in various leadership and financial oversight capacities with non-profit organizations.

## Evaluation of Fees for each DWS Fund

My work focused primarily on evaluating, fund-by-fund, the fees charged to each of the 118 publicly offered Fund portfolios in the DWS Fund family. For each Fund, I considered each of the key factors mentioned above, as well as any other relevant information. In doing so I worked closely with the Funds' Independent Directors in their annual contract renewal process, as well as in their approval of contracts for several new funds (documented separately).

In evaluating each Fund's fees, I reviewed comprehensive materials provided by or on behalf of DeAM, including expense information prepared by Lipper Analytical, comparative performance information, profitability data, manager histories, and other materials. I also accessed certain additional information from the Lipper and Morningstar databases and drew on my industry knowledge and experience.

To facilitate evaluating this considerable body of information, I prepared for each Fund a document summarizing the key data elements in each area as well as additional analytics discussed below. This made it possible to consider each key data element in the context of the others.

In the course of contract renewal, DeAM agreed to implement a number of fee and expense adjustments requested by the Independent Directors which will favorably impact future fees and expenses, and my evaluation includes the effects of these changes.

### Fees and Expenses Compared with Other Funds

The competitive fee and expense evaluation for each fund focused on two primary comparisons:

- The Fund's contractual management fee (the advisory fee plus the administration fee where applicable) compared with those of a group of typically 12–15 funds in the same Lipper investment category (e.g. Large Capitalization Growth) having similar distribution arrangements and being of similar size.
- The Fund's total expenses compared with a broader universe of funds from the same Lipper investment category and having similar distribution arrangements.

These two comparisons provide a view of not only the level of the fee compared with funds of similar scale but also the total expense the Fund bears for all the services it receives, in comparison with the investment choices available in the Fund's investment category and distribution channel. The principal figure-of-merit used in these comparisons was the subject Fund's percentile ranking against peers.

### DeAM's Fees for Similar Services to Others

DeAM provided management fee schedules for all of its US domiciled fund and non-fund investment management accounts in any of the investment categories where there is a DWS Fund. These similar products included the other DWS Funds, non-fund pooled accounts, institutional accounts and sub-advisory accounts. Using this information, I calculated for each Fund the fee that would be charged to each similar product, at the subject Fund's asset level.

Evaluating information regarding non-fund products is difficult because there are varying levels of services required for different types of accounts, with mutual funds generally requiring considerably more regulatory and administrative types of service as well as having more frequent cash flows than other types of accounts. Also, while mutual fund fees for similar fund products can be expected to be similar, there will be some differences due to different pricing conditions in different distribution channels (e.g. retail funds versus those used in variable insurance products), differences in underlying investment processes and other factors.

**Costs and Profit Margins**

DeAM provided a detailed profitability analysis for each Fund. After making some adjustments so that the presentation would be more comparable to the available industry figures, I reviewed profit margins from investment management alone, from investment management plus other fund services (excluding distribution) provided to the Funds by DeAM (principally shareholder services), and DeAM profits from all sources, including distribution. A later section comments on overall profitability.

**Economies of Scale**

Economies of scale — an expected decline in management cost per dollar of fund assets as fund assets grow — are very rarely quantified and documented because of inherent difficulties in collecting and analyzing relevant data. However, in virtually every investment category that I reviewed, larger funds tend to have lower fees and lower total expenses than smaller funds. To see how each DWS Fund compares with this industry observation, I reviewed:

- The trend in Fund assets over the last five years and the accompanying trend in total expenses. This shows if the Fund has grown and, if so, whether total expense (management fees as well as other expenses) have declined as a percent of assets.
- Whether the Fund has break-points in its management fee schedule, the extent of the fee reduction built into the schedule and the asset levels where the breaks take effect, and in the case of a sub-advised Fund how the Fund's break-points compare with those of the sub-advisory fee schedule.
- How the Fund's contractual fee schedule compares with trends in the industry data. To accomplish this, I constructed a chart showing how actual latest-fiscal-year contractual fees of the Fund and of other similar funds relate to average fund assets, with the subject Fund's contractual fee schedule superimposed.

**Quality of Service — Performance**

The quality-of-service evaluation focused on investment performance, which is the principal result of the investment management service. Each Fund's performance was reviewed over the past 1, 3, 5 and 10 years, as applicable, and compared with that of other funds in the same investment category and with a suitable market index.

In addition, I calculated and reviewed risk-adjusted returns relative to an index of similar mutual funds' returns and a suitable market index. The risk-adjusted returns analysis provides a way of determining the extent to which the Fund's return comparisons are mainly the product of investment value-added (or lack thereof) or alternatively taking considerably more or less risk than is typical in its investment category.

I also received and considered the history of portfolio manager changes for each Fund, as this provided an important context for evaluating the performance results.

## Complex-Level Considerations

While this evaluation was conducted mainly at the individual fund level, there are some issues relating to the reasonableness of fees that can alternatively be considered across the whole fund complex:

- I reviewed DeAM's profitability analysis for all DWS Funds, with a view toward determining if the allocation procedures used were reasonable and how profit levels compared with public data for other investment managers.
- I considered whether DeAM and affiliates receive any significant ancillary or "fall-out" benefits that should be considered in interpreting the direct profitability results. These would be situations where serving as the investment manager of the Funds is beneficial to another part of the Deutsche Bank organization.
- I considered how aggregated DWS Fund expenses had varied over the years, by asset class and in the context of trends in asset levels.
- I reviewed the structure of the DeAM organization, trends in staffing levels, and information on compensation of investment management and other professionals compared with industry data.

## Findings

Based on the process and analysis discussed above, which included reviewing a wide range of information from management and external data sources and considering among other factors the fees DeAM charges other clients, the fees charged by other fund managers, DeAM's costs and profits associated with managing the Funds, economies of scale, possible fall-out benefits, and the nature and quality of services provided, in my opinion the management fees charged the DWS Funds are reasonable.

Thomas H. Mack

Thomas H. Mack

# Board Members and Officers

The following table presents certain information regarding the Board Members and Officers of the Trust as of December 31, 2010. Each Board Member's year of birth is set forth in parentheses after his or her name. Unless otherwise noted, (i) each Board Member has engaged in the principal occupation(s) noted in the table for at least the most recent five years, although not necessarily in the same capacity; and (ii) the address of each Independent Board Member is c/o Paul K. Freeman, Independent Chairman, DWS Funds, PO Box 101833, Denver, CO 80250-1833. Except as otherwise noted below, the term of office for each Board Member is until the election and qualification of a successor, or until such Board Member sooner dies, resigns, is removed or as otherwise provided in the governing documents of the fund. Because the fund does not hold an annual meeting of shareholders, each Board Member will hold office for an indeterminate period. The Board Members may also serve in similar capacities with other funds in the fund complex. The Length of Time Served represents the year in which the Board Member joined the board of one or more DWS funds now overseen by the Board.

### Independent Board Members

| Name, Year of Birth, Position with the Fund and Length of Time Served[1] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Paul K. Freeman (1950)<br>Chairperson since 2009<br>Board Member since 1993 | Consultant, World Bank/Inter-American Development Bank; Executive and Governing Council of the Independent Directors Council (education committees); formerly, Project Leader, International Institute for Applied Systems Analysis (1998–2001); Chief Executive Officer, The Eric Group, Inc. (environmental insurance) (1986–1998) | 122 |
| John W. Ballantine (1946)<br>Board Member since 1999 | Retired; formerly, Executive Vice President and Chief Risk Management Officer, First Chicago NBD Corporation/The First National Bank of Chicago (1996–1998); Executive Vice President and Head of International Banking (1995–1996). Directorships: Healthways, Inc. (provider of disease and care management services); Portland General Electric (utility company); Stockwell Capital Investments PLC (private equity). Former Directorships: First Oak Brook Bancshares, Inc. and Oak Brook Bank; Prisma Energy International | 122 |
| Henry P. Becton, Jr. (1943)<br>Board Member since 1990 | Vice Chair and former President, WGBH Educational Foundation. Directorships: Association of Public Television Stations; Lead Director, Becton Dickinson and Company[3] (medical technology company); Lead Director, Belo Corporation[3] (media company); Public Radio International; Public Radio Exchange (PRX); The PBS Foundation. Former Directorships: Boston Museum of Science; American Public Television; Concord Academy; New England Aquarium; Mass. Corporation for Educational Telecommunications; Committee for Economic Development; Public Broadcasting Service | 122 |
| Dawn-Marie Driscoll (1946)<br>Board Member since 1987 | President, Driscoll Associates (consulting firm); Executive Fellow, Center for Business Ethics, Bentley University; formerly, Partner, Palmer & Dodge (1988–1990); Vice President of Corporate Affairs and General Counsel, Filene's (1978–1988). Directorships: Trustee of 22 open-end mutual funds managed by Sun Capital Advisers, Inc. (since 2007); Director of ICI Mutual Insurance Company (since 2007); Advisory Board, Center for Business Ethics, Bentley University; Trustee, Southwest Florida Community Foundation (charitable organization). Former Directorships: Investment Company Institute (audit, executive, nominating committees) and Independent Directors Council (governance, executive committees) | 122 |
| Keith R. Fox (1954)<br>Board Member since 1996 | Managing General Partner, Exeter Capital Partners (a series of private investment funds). Directorships: Progressive International Corporation (kitchen goods importer and distributor); BoxTop Media Inc. (advertising); The Kennel Shop (retailer); former Chairman, National Association of Small Business Investment Companies | 122 |
| Kenneth C. Froewiss (1945)<br>Board Member since 2001 | Adjunct Professor of Finance, NYU Stern School of Business (September 2009–present; Clinical Professor from 1997–September 2009); Member, Finance Committee, Association for Asian Studies (2002–present); Director, Mitsui Sumitomo Insurance Group (US) (2004–present); prior thereto, Managing Director, J.P. Morgan (investment banking firm) (until 1996) | 122 |
| Richard J. Herring (1946)<br>Board Member since 1990 | Jacob Safra Professor of International Banking and Professor, Finance Department, The Wharton School, University of Pennsylvania (since July 1972); Co-Director, Wharton Financial Institutions Center (since July 2000); Co-Chair, U.S. Shadow Financial Regulatory Committee; Executive Director, Financial Economists Roundtable; Director, Japan Equity Fund, Inc. (since September 2007), Thai Capital Fund, Inc. (since September 2007), Singapore Fund, Inc. (since September 2007); Independent Director of Barclays Bank Delaware (since September 2010). Formerly, Vice Dean and Director, Wharton Undergraduate Division (July 1995–June 2000); Director, Lauder Institute of International Management Studies (July 2000–June 2006) | 122 |
| William McClayton (1944)<br>Board Member since 2004+ | Private equity investor (since October 2009); previously, Managing Director, Diamond Management & Technology Consultants, Inc. (global consulting firm) (2001–2009); Directorship: Board of Managers, YMCA of Metropolitan Chicago; formerly: Senior Partner, Arthur Andersen LLP (accounting) (1966–2001); Trustee, Ravinia Festival | 122 |

| Name, Year of Birth, Position with the Fund and Length of Time Served[1] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Rebecca W. Rimel (1951)<br>Board Member since 1995 | President and Chief Executive Officer, The Pew Charitable Trusts (charitable organization) (1994 to present); Trustee, Thomas Jefferson Foundation (charitable organization) (1994 to present); Trustee, Executive Committee, Philadelphia Chamber of Commerce (2001–2007); Director, CardioNet, Inc.[2] (2009–present) (health care). Formerly, Executive Vice President, The Glenmede Trust Company (investment trust and wealth management) (1983–2004); Board Member, Investor Education (charitable organization) (2004–2005); Director, Viasys Health Care[2] (January 2007–June 2007); Trustee, Pro Publica (charitable organization) (2007–2010) | 122 |
| William N. Searcy, Jr. (1946)<br>Board Member since 1993 | Private investor since October 2003; Trustee of 22 open-end mutual funds managed by Sun Capital Advisers, Inc. (since October 1998). Formerly, Pension & Savings Trust Officer, Sprint Corporation[2] (telecommunications) (November 1989–September 2003) | 122 |
| Jean Gleason Stromberg (1943)<br>Board Member since 1997 | Retired. Formerly, Consultant (1997–2001); Director, Financial Markets US Government Accountability Office (1996–1997); Partner, Fulbright & Jaworski, L.L.P. (law firm) (1978–1996). Directorships: The William and Flora Hewlett Foundation. Former Directorships: Service Source, Inc., Mutual Fund Directors Forum (2002–2004), American Bar Retirement Association (funding vehicle for retirement plans) (1987–1990 and 1994–1996) | 122 |
| Robert H. Wadsworth (1940)<br>Board Member since 1999 | President, Robert H. Wadsworth & Associates, Inc. (consulting firm) (1983 to present); Director, The Phoenix Boys Choir Association | 125 |

## Officers[4]

| Name, Year of Birth, Position with the Fund and Length of Time Served[5] | Principal Occupation(s) During Past 5 Years and Other Directorships Held |
|---|---|
| Michael G. Clark[6] (1965)<br>President, 2006–present | Managing Director[3], Deutsche Asset Management (2006–present); President of DWS family of funds; Director, ICI Mutual Insurance Company (since October 2007); formerly, Director of Fund Board Relations (2004–2006) and Director of Product Development (2000–2004), Merrill Lynch Investment Managers; Senior Vice President Operations, Merrill Lynch Asset Management (1999–2000) |
| Ingo Gefeke[7] (1967)<br>Executive Vice President since 2010 | Managing Director[3], Deutsche Asset Management; Global Head of Distribution and Product Management, DWS Global Head of Trading and Securities Lending. Member of the Board of Directors of DWS Investment GmbH Frankfurt (since July 2009) and DWS Holding & Service GmbH Frankfurt (since January 2010); formerly, Global Chief Administrative Officer, Deutsche Asset Management (2004–2009); Global Chief Operating Officer, Global Transaction Banking, Deutsche Bank AG, New York (2001–2004); Chief Operating Officer, Global Banking Division Americas, Deutsche Bank AG, New York (1999–2001); Central Management, Global Banking Services, Deutsche Bank AG, Frankfurt (1998–1999); Relationship Management, Deutsche Bank AG, Tokyo, Japan (1997–1998) |
| John Millette[8] (1962)<br>Vice President and Secretary, 1999–present | Director[3], Deutsche Asset Management |
| Paul H. Schubert[6] (1963)<br>Chief Financial Officer, 2004–present<br>Treasurer, 2005–present | Managing Director[3], Deutsche Asset Management (since July 2004); formerly, Executive Director, Head of Mutual Fund Services and Treasurer for UBS Family of Funds (1998–2004); Vice President and Director of Mutual Fund Finance at UBS Global Asset Management (1994–1998) |
| Caroline Pearson[8] (1962)<br>Chief Legal Officer, April 2010–present | Managing Director[3], Deutsche Asset Management; formerly, Assistant Secretary for DWS family of funds (1997–2010) |
| Rita Rubin[9] (1970)<br>Assistant Secretary, 2009–present | Vice President and Counsel, Deutsche Asset Management (since October 2007); formerly, Vice President, Morgan Stanley Investment Management (2004–2007) |
| Paul Antosca[8] (1957)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management (since 2006); Vice President, The Manufacturers Life Insurance Company (U.S.A.) (1990–2006) |
| Jack Clark[8] (1967)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management (since 2007); formerly, Vice President, State Street Corporation (2002–2007) |
| Diane Kenneally[8] (1966)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management |
| John Caruso[9] (1965)<br>Anti-Money Laundering Compliance Officer, 2010–present | Managing Director[3], Deutsche Asset Management |

| Name, Year of Birth, Position with the Fund and Length of Time Served[5] | Principal Occupation(s) During Past 5 Years and Other Directorships Held |
|---|---|
| Robert Kloby[9] (1962)<br>Chief Compliance Officer, 2006–present | Managing Director[3], Deutsche Asset Management |

1 *The length of time served represents the year in which the Board Member joined the board of one or more DWS funds currently overseen by the Board.*

2 *A publicly held company with securities registered pursuant to Section 12 of the Securities Exchange Act of 1934.*

3 *Executive title, not a board directorship.*

4 *As a result of their respective positions held with the Advisor, these individuals are considered "interested persons" of the Advisor within the meaning of the 1940 Act. Interested persons receive no compensation from the fund.*

5 *The length of time served represents the year in which the officer was first elected in such capacity for one or more DWS funds.*

6 *Address: 100 Plaza One, Jersey City, NJ 07311.*

7 *Effective January 11, 2011, Mr. Gefeke, Executive Vice President, resigned as an officer of the fund.*

*The mailing address of Mr. Gefeke is 345 Park Avenue, New York, New York 10154. Mr. Gefeke was an interested Board Member of certain DWS funds by virtue of his positions with Deutsche Asset Management. As an interested person, Mr. Gefeke received no compensation from the fund.*

8 *Address: One Beacon Street, Boston, MA 02108.*

9 *Address: 60 Wall Street, New York, New York 10005.*

*The fund's Statement of Additional Information ("SAI") includes additional information about the Board Members. The SAI is available, without charge, upon request. If you would like to request a copy of the SAI, you may do so by calling the following toll-free number: (800) 728-3337.*

DWS Investments is part of Deutsche Bank's Asset Management division and, within the US, represents the retail asset management activities of Deutsche Bank AG, Deutsche Bank Trust Company Americas, Deutsche Investment Management Americas Inc. and DWS Trust Company.

The views expressed in this report reflect those of the portfolio managers only through the end of the period of the report as stated on the cover. The managers' views are subject to change at any time based on market and other conditions and should not be construed as a recommendation.

This information must be preceded or accompanied by a current prospectus.

Portfolio changes should not be considered recommendations for action by individual investors.

DWS Investments Distributors, Inc.
222 South Riverside Plaza
Chicago, IL 60606
(800) 621-1148

VS1bond-2 (2/11)

DWS INVESTMENTS
Deutsche Bank Group

DECEMBER 31, 2010

# ANNUAL REPORT

## DWS VARIABLE SERIES I

## DWS Capital Growth VIP

**This report must be preceded or accompanied by a prospectus. To obtain an additional prospectus or summary prospectus, if available, call (800) 728-3337 or your financial representative. We advise you to consider the Fund's objectives, risks, charges and expenses carefully before investing. The summary prospectus and prospectus contain this and other important information about the Fund. Please read the prospectus carefully before you invest.**

*Investments in variable insurance portfolios (VIPs) involve risk. Stocks may decline in value. Bond investments are subject to interest-rate and credit risks. When interest rates rise, bond prices generally fall. Credit risk refers to the ability of an issuer to make timely payments of principal and interest. Investing in derivatives entails special risks relating to liquidity, leverage and credit that may reduce returns and/or increased volatility. Investing in foreign securities, particularly those of emerging markets, presents certain risks, such as currency fluctuations, political and economic changes, and market risks. There are additional risks associated with investing in commodities, high-yield bonds, aggressive growth stocks, non-diversified/ concentrated funds and small- and mid-cap stocks which are more fully explained in the prospectuses. Please read the prospectus for more information.*

*DWS Investments is part of Deutsche Bank's Asset Management division and, within the US, represents the retail asset management activities of Deutsche Bank AG, Deutsche Bank Trust Company Americas, Deutsche Investment Management Americas Inc. and DWS Trust Company.*



DWS INVESTMENTS
Deutsche Bank Group

# Performance Summary

December 31, 2010

## DWS Capital Growth VIP

**All performance shown is historical, assumes reinvestment of all dividend and capital gain distributions, and does not guarantee future results. Investment return and principal value fluctuate with changing market conditions so that, when redeemed, shares may be worth more or less than their original cost. Current performance may be lower or higher than the performance data quoted. Please contact your participating insurance company for the Fund's most recent month-end performance. Performance doesn't reflect charges and fees ("contract charges") associated with the separate account that invests in the Fund or any variable life insurance policy or variable annuity contract for which the Fund is an investment option. These charges and fees will reduce returns. While all share classes have the same underlying portfolio, their performance will differ.**

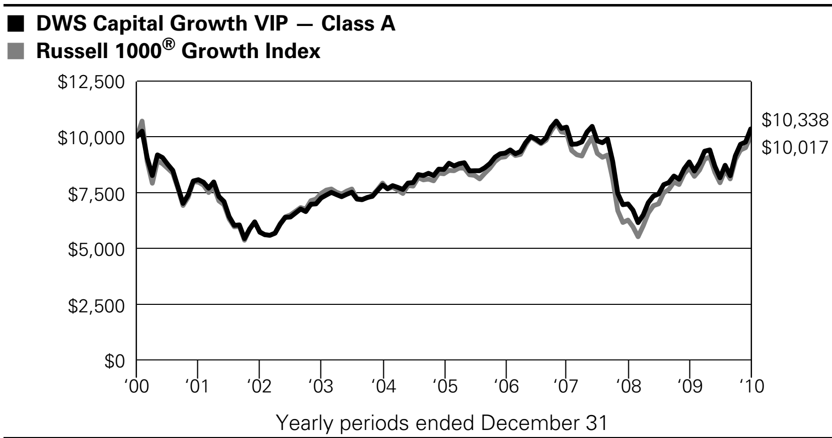
**The gross expense ratios of the Fund, as stated in the fee table of the prospectus dated May 1, 2010 are 0.51% and 0.85% for Class A and Class B shares, respectively, and may differ from the expense ratios disclosed in the Financial Highlights tables in this report.**

Fund returns during all periods shown reflect a fee waiver and/or expense reimbursement. Without this waiver/reimbursement, returns would have been lower.

### Risk Considerations

Stocks may decline in value. See the prospectus for details.

### Growth of an Assumed $10,000 Investment




*The Russell 1000® Growth Index is an unmanaged, capitalization-weighted index containing those securities in the Russell 1000 Index with higher price-to-book ratios and higher forecasted growth values.*

*Index returns assume the reinvestment of dividends and, unlike fund returns, do not reflect any fees or expenses. It is not possible to invest directly into an index.*

### Comparative Results

| DWS Capital Growth VIP | | 1-Year | 3-Year | 5-Year | 10-Year |
|---|---|---|---|---|---|
| **Class A** | Growth of $10,000 | $11,671 | $9,923 | $12,125 | $10,338 |
| | Average annual total return | 16.71% | –.26% | 3.93% | .33% |
| Russell 1000 Growth Index | Growth of $10,000 | $11,671 | $9,858 | $12,023 | $10,017 |
| | Average annual total return | 16.71% | –.47% | 3.75% | .02% |

| DWS Capital Growth VIP | | 1-Year | 3-Year | 5-Year | 10-Year |
|---|---|---|---|---|---|
| **Class B** | Growth of $10,000 | $11,633 | $9,828 | $11,926 | $9,995 |
| | Average annual total return | 16.33% | –.58% | 3.59% | –.01% |
| Russell 1000 Growth Index | Growth of $10,000 | $11,671 | $9,858 | $12,023 | $10,017 |
| | Average annual total return | 16.71% | –.47% | 3.75% | .02% |

*The growth of $10,000 is cumulative.*

# Information About Your Fund's Expenses

## DWS Capital Growth VIP

As an investor of the Fund, you incur two types of costs: ongoing expenses and transaction costs. Ongoing expenses include management fees, distribution and service (12b-1) fees and other Fund expenses. Examples of transaction costs include contract charges, redemption fees and account maintenance fees, which are not shown in this section. The following tables are intended to help you understand your ongoing expenses (in dollars) of investing in the Fund and to help you compare these expenses with the ongoing expenses of investing in other mutual funds. The example in the table is based on an investment of $1,000 invested at the beginning of the six-month period and held for the entire period (July 1, 2010 to December 31, 2010).

The tables illustrate your Fund's expenses in two ways:

- **Actual Fund Return.** This helps you estimate the actual dollar amount of ongoing expenses (but not transaction costs) paid on a $1,000 investment in the Fund using the Fund's actual return during the period. To estimate the expenses you paid over the period, simply divide your account value by $1,000 (for example, an $8,600 account value divided by $1,000 = 8.6), then multiply the result by the number in the "Expenses Paid per $1,000" line under the share class you hold.
- **Hypothetical 5% Fund Return.** This helps you to compare your Fund's ongoing expenses (but not transaction costs) with those of other mutual funds using the Fund's actual expense ratio and a hypothetical rate of return of 5% per year before expenses. Examples using a 5% hypothetical Fund return may be found in the shareholder reports of other mutual funds. The hypothetical account values and expenses may not be used to estimate the actual ending account balance or expenses you paid for the period.

Please note that the expenses shown in these tables are meant to highlight your ongoing expenses only and do not reflect any transaction costs. The "Expenses Paid per $1,000" line of the tables is useful in comparing ongoing expenses only and will not help you determine the relative total expense of owning different funds. If these transaction costs had been included, your costs would have been higher.

**Expenses and Value of a $1,000 Investment** for the six months ended December 31, 2010

| Actual Fund Return | Class A | Class B |
|---|---|---|
| Beginning Account Value 7/1/10 | $1,000.00 | $1,000.00 |
| Ending Account Value 12/31/10 | $1,268.00 | $1,266.10 |
| Expenses Paid per $1,000* | $ 2.92 | $ 4.86 |
| **Hypothetical 5% Fund Return** | **Class A** | **Class B** |
| Beginning Account Value 7/1/10 | $1,000.00 | $1,000.00 |
| Ending Account Value 12/31/10 | $1,022.63 | $1,020.92 |
| Expenses Paid per $1,000* | $ 2.60 | $ 4.33 |

* *Expenses are equal to the Fund's annualized expense ratio for each share class, multiplied by the average account value over the period, multiplied by the number of days in the most recent six-month period, then divided by 365.*

| Annualized Expense Ratios | Class A | Class B |
|---|---|---|
| DWS Variable Series I — DWS Capital Growth VIP | .51% | .85% |

For more information, please refer to the Fund's prospectus.

These tables do not reflect charges and fees ("contract charges") associated with the separate account that invests in the Fund or any variable life insurance policy or variable annuity contract for which the Fund is an investment option.

## DWS Capital Growth VIP

Coming into 2010, we began to see the gradual withdrawal of government stimulus in response to the recession and increasing worry by market watchers that the recovery might falter as a result. The fiscal crisis in Europe also spurred market turbulence, though austerity pledges by a number of European governments (and central bank intervention there) eased fears of a possible European economic "contagion." In the third quarter, stocks benefited from a robust September rally spurred in part by news that the US Federal Reserve Board (the Fed) would take additional policy measures if needed in order to prevent the US economy from regressing. In the closing months of 2010, positive economic news, including stronger manufacturing reports, continued improvement for US gross domestic product (GDP), and an upturn in consumer confidence, sparked a number of market rallies over the quarter.[1] Lastly, investors largely welcomed the congressional compromise where lawmakers extended the Bush-era tax cuts as well as unemployment benefits, as these actions provide some additional economic certainty for 2011.

For the 12 months ended December 31, 2010, the Fund returned 16.71% (Class A shares, unadjusted for contract charges), matching the 16.71% return of the Russell 1000® Growth Index. (Past performance is no guarantee of future results.)

During the period, stock selection was slightly positive offsetting the slightly negative sector allocation. The largest contribution to performance came from a surprising source, consumer discretionary stocks, considering the low expectations for consumer spending entering 2010. However, specialty retail stocks — which have strongly benefited from robust emerging-market consumer demand for specialty/luxury items, along with demand for automobiles globally — boosted the consumer discretionary sector. The Fund's overweight to industrials also contributed, based on improving manufacturing reports and several industrial firms' ability to exceed pessimistic earnings forecasts.[2] In contrast, the Fund's slight overweight and stock selection in health care detracted from returns as several holdings proved disappointing. In addition, stock selection within information technology detracted.

Owen Fitzpatrick, CFA
*Lead Portfolio Manager*

Thomas M. Hynes, Jr., CFA
Brendan O'Neill, CFA
*Portfolio Managers*

*The Russell 1000® Growth Index is an unmanaged, capitalization-weighted index containing those securities in the Russell 1000® Index with higher price-to-book ratios and higher forecasted growth values.*

*Index returns assume reinvestment of dividends and, unlike fund returns, do not reflect any fees or expenses. It is not possible to invest directly into an index.*

1 *Gross domestic product is the value of goods and services produced in an economy.*

2 *"Overweight" means the Fund holds a higher weighting in a given sector or security than the benchmark. "Underweight" means the Fund holds a lower weighting.*

*Portfolio management market commentary is as of December 31, 2010, and may not come to pass. This information is subject to change at any time based on market and other conditions. Past performance does not guarantee future results. Current and future portfolio holdings are subject to risk.*

# Portfolio Summary

## DWS Capital Growth VIP

| **Asset Allocation** (As a % of Investment Portfolio excluding Securities Lending Collateral) | **12/31/10** | **12/31/09** |
|---|---|---|
| Common Stocks | 100% | 99% |
| Cash Equivalents | — | 1% |
| | 100% | 100% |

| **Sector Diversification** (As a % of Common Stocks) | **12/31/10** | **12/31/09** |
|---|---|---|
| Information Technology | 31% | 34% |
| Consumer Discretionary | 16% | 11% |
| Industrials | 14% | 12% |
| Energy | 12% | 6% |
| Health Care | 10% | 17% |
| Materials | 6% | 5% |
| Consumer Staples | 5% | 8% |
| Financials | 5% | 4% |
| Telecommunication Services | 1% | 2% |
| Utilities | — | 1% |
| | 100% | 100% |

*Asset allocation and sector diversification are subject to change.*

*For more complete details about the Fund's investment portfolio, see page 6.*

Following the Fund's fiscal first and third quarter-end, a complete portfolio holdings listing is filed with the SEC on Form N-Q. The form will be available on the SEC's Web site at www.sec.gov, and it also may be reviewed and copied at the SEC's Public Reference Room in Washington, D.C. Information on the operation of the SEC's Public Reference Room may be obtained by calling (800) SEC-0330. The Fund's portfolio holdings are also posted on www.dws-investments.com from time to time. Please see the Fund's current prospectus for more information.

# Investment Portfolio

December 31, 2010

## DWS Capital Growth VIP

| | Shares | Value ($) |
|---|---|---|
| **Common Stocks 99.8%** | | |
| **Consumer Discretionary 15.5%** | | |
| **Auto Components 3.0%** | | |
| Autoliv, Inc. (a) | 78,450 | 6,192,843 |
| BorgWarner, Inc.* (a) | 216,840 | 15,690,542 |
| | | **21,883,385** |
| **Hotels Restaurants & Leisure 3.5%** | | |
| Darden Restaurants, Inc. (a) | 195,460 | 9,077,162 |
| Marriott International, Inc. "A" (a) | 276,401 | 11,481,698 |
| McDonald's Corp. | 69,100 | 5,304,116 |
| | | **25,862,976** |
| **Media 1.8%** | | |
| Scripps Networks Interactive "A" (a) | 257,300 | **13,315,275** |
| **Multiline Retail 2.7%** | | |
| Dollar General Corp.* (a) | 133,130 | 4,083,097 |
| Kohl's Corp.* | 160,670 | 8,730,808 |
| Nordstrom, Inc. (a) | 178,060 | 7,546,183 |
| | | **20,360,088** |
| **Specialty Retail 2.6%** | | |
| Dick's Sporting Goods, Inc.* (a) | 176,470 | 6,617,625 |
| Limited Brands, Inc. (a) | 415,870 | 12,779,685 |
| | | **19,397,310** |
| **Textiles, Apparel & Luxury Goods 1.9%** | | |
| NIKE, Inc. "B" (a) | 167,735 | **14,327,924** |
| **Consumer Staples 5.1%** | | |
| **Beverages 1.4%** | | |
| PepsiCo, Inc. | 162,575 | **10,621,025** |
| **Food & Staples Retailing 1.8%** | | |
| Sysco Corp. (a) | 260,880 | 7,669,872 |
| Wal-Mart Stores, Inc. (a) | 98,264 | 5,299,377 |
| | | **12,969,249** |
| **Household Products 1.9%** | | |
| Church & Dwight Co., Inc. (a) | 100,164 | 6,913,319 |
| Colgate-Palmolive Co. (a) | 86,840 | 6,979,331 |
| | | **13,892,650** |
| **Energy 12.0%** | | |
| **Energy Equipment & Services 3.5%** | | |
| National Oilwell Varco, Inc. | 191,783 | 12,897,407 |
| Schlumberger Ltd. (a) | 157,380 | 13,141,230 |
| | | **26,038,637** |
| **Oil, Gas & Consumable Fuels 8.5%** | | |
| Alpha Natural Resources, Inc.* | 222,900 | 13,380,687 |
| Anadarko Petroleum Corp. (a) | 174,580 | 13,296,013 |
| EOG Resources, Inc. (a) | 87,490 | 7,997,461 |
| Exxon Mobil Corp. (a) | 202,420 | 14,800,950 |
| Occidental Petroleum Corp. | 134,320 | 13,176,792 |
| | | **62,651,903** |
| **Financials 4.9%** | | |
| **Capital Markets 4.2%** | | |
| Charles Schwab Corp. (a) | 352,250 | 6,026,997 |
| Morgan Stanley | 310,490 | 8,448,433 |
| T. Rowe Price Group, Inc. (a) | 253,620 | 16,368,635 |
| | | **30,844,065** |

| | Shares | Value ($) |
|---|---|---|
| **Insurance 0.7%** | | |
| MetLife, Inc. | 114,040 | **5,067,938** |
| **Health Care 9.8%** | | |
| **Biotechnology 4.5%** | | |
| Amgen, Inc.* | 97,292 | 5,341,331 |
| Celgene Corp.* | 324,380 | 19,183,833 |
| Gilead Sciences, Inc.* | 239,705 | 8,686,909 |
| | | **33,212,073** |
| **Health Care Equipment & Supplies 1.7%** | | |
| Edwards Lifesciences Corp.* (a) | 89,831 | 7,261,938 |
| Thoratec Corp.* (a) | 189,990 | 5,380,517 |
| | | **12,642,455** |
| **Health Care Providers & Services 3.6%** | | |
| Express Scripts, Inc.* (a) | 297,570 | 16,083,658 |
| McKesson Corp. | 147,960 | 10,413,425 |
| | | **26,497,083** |
| **Industrials 14.5%** | | |
| **Aerospace & Defense 2.9%** | | |
| TransDigm Group, Inc.* | 110,160 | 7,932,622 |
| United Technologies Corp. | 169,220 | 13,320,998 |
| | | **21,253,620** |
| **Commercial Services & Supplies 1.0%** | | |
| Stericycle, Inc.* (a) | 95,250 | **7,707,630** |
| **Electrical Equipment 4.3%** | | |
| AMETEK, Inc. | 463,500 | 18,192,375 |
| Roper Industries, Inc. (a) | 181,940 | 13,905,674 |
| | | **32,098,049** |
| **Machinery 4.1%** | | |
| Navistar International Corp.* (a) | 218,657 | 12,662,427 |
| Parker Hannifin Corp. (a) | 202,120 | 17,442,956 |
| | | **30,105,383** |
| **Road & Rail 2.2%** | | |
| Norfolk Southern Corp. (a) | 261,180 | **16,407,328** |
| **Information Technology 30.6%** | | |
| **Communications Equipment 4.7%** | | |
| Cisco Systems, Inc.* | 1,089,685 | 22,044,327 |
| QUALCOMM, Inc. | 267,010 | 13,214,325 |
| | | **35,258,652** |
| **Computers & Peripherals 8.7%** | | |
| Apple, Inc.* | 128,904 | 41,579,274 |
| EMC Corp.* (a) | 650,015 | 14,885,343 |
| Hewlett-Packard Co. | 185,785 | 7,821,549 |
| | | **64,286,166** |
| **Internet Software & Services 3.2%** | | |
| Akamai Technologies, Inc.* (a) | 165,840 | 7,802,772 |
| Google, Inc. "A"* | 27,175 | 16,141,135 |
| | | **23,943,907** |
| **IT Services 3.0%** | | |
| Accenture PLC "A" | 117,220 | 5,683,998 |
| International Business Machines Corp. | 61,160 | 8,975,841 |
| VeriFone Systems, Inc.* | 134,069 | 5,169,701 |
| Visa, Inc. "A" (a) | 37,490 | 2,638,546 |
| | | **22,468,086** |

*The accompanying notes are an integral part of the financial statements.*

| | Shares | Value ($) |
|---|---|---|
| **Semiconductors & Semiconductor Equipment 1.6%** | | |
| Intel Corp. | 551,870 | **11,605,826** |
| **Software 9.4%** | | |
| Adobe Systems, Inc.* | 123,880 | 3,813,027 |
| Check Point Software Technologies Ltd.* (a) | 151,620 | 7,013,941 |
| Concur Technologies, Inc.* (a) | 187,410 | 9,732,201 |
| Microsoft Corp. | 664,300 | 18,547,256 |
| Oracle Corp. | 690,925 | 21,625,953 |
| Solera Holdings, Inc. (a) | 170,810 | 8,765,969 |
| | | **69,498,347** |
| **Materials 6.3%** | | |
| **Chemicals 2.2%** | | |
| Huntsman Corp. (a) | 452,407 | 7,062,073 |
| The Mosaic Co. | 121,521 | 9,279,344 |
| | | **16,341,417** |
| **Containers & Packaging 1.6%** | | |
| Owens-Illinois, Inc.* (a) | 380,480 | **11,680,736** |
| **Metals & Mining 2.5%** | | |
| Freeport-McMoRan Copper & Gold, Inc. (a) | 157,290 | **18,888,956** |
| **Telecommunication Services 1.1%** | | |
| **Wireless Telecommunication Services** | | |
| American Tower Corp. "A"* | 160,070 | **8,266,015** |
| **Total Common Stocks** (Cost $494,685,918) | | **739,394,154** |
| **Securities Lending Collateral 35.7%** | | |
| Daily Assets Fund Institutional, 0.27% (b) (c) (Cost $264,201,382) | 264,201,382 | **264,201,382** |
| **Cash Equivalents 0.2%** | | |
| Central Cash Management Fund, 0.19% (b) (Cost $1,727,407) | 1,727,407 | **1,727,407** |

| | % of Net Assets | Value ($) |
|---|---|---|
| **Total Investment Portfolio** (Cost $760,614,707)† | 135.7 | **1,005,322,943** |
| **Other Assets and Liabilities, Net** | (35.7) | **(264,266,883)** |
| **Net Assets** | 100.0 | **741,056,060** |

* *Non-income producing security.*

† *The cost for federal income tax purposes was $763,567,179. At December 31, 2010, net unrealized appreciation for all securities based on tax cost was $241,755,764. This consisted of aggregate gross unrealized appreciation for all securities in which there was an excess of value over tax cost of $250,498,317 and aggregate gross unrealized depreciation for all securities in which there was an excess of tax cost over value of $8,742,553.*

(a) *All or a portion of these securities were on loan (see Notes to Financial Statements). The value of all securities loaned at December 31, 2010 amounted to $257,619,904, which is 34.8% of net assets.*

(b) *Affiliated fund managed by Deutsche Investment Management Americas Inc. The rate shown is the annualized seven-day yield at period end.*

(c) *Represents collateral held in connection with securities lending. Income earned by the Fund is net of borrower rebates.*

## Fair Value Measurements

*Various inputs are used in determining the value of the Fund's investments. These inputs are summarized in three broad levels. Level 1 includes quoted prices in active markets for identical securities. Level 2 includes other significant observable inputs (including quoted prices for similar securities, interest rates, prepayment speeds, and credit risk). Level 3 includes significant unobservable inputs (including the Fund's own assumptions in determining the fair value of investments). The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities.*

*The following is a summary of the inputs used as of December 31, 2010 in valuing the Fund's investments. For information on the Fund's policy regarding the valuation of investments, please refer to the Security Valuation section of Note A in the accompanying Notes to Financial Statements.*

| Assets | Level 1 | Level 2 | Level 3 | Total |
|---|---|---|---|---|
| Common Stocks (d) | $ 739,394,154 | $ — | $ — | $ 739,394,154 |
| Short-Term Investments (d) | 265,928,789 | — | — | 265,928,789 |
| **Total** | **$ 1,005,322,943** | **$ —** | **$ —** | **$ 1,005,322,943** |

*There have been no significant transfers in and out of Level 1 and Level 2 fair value measurements during the year ended December 31, 2010.*

(d) *See Investment Portfolio for additional detailed categorizations.*

*The accompanying notes are an integral part of the financial statements.*

# Statement of Assets and Liabilities

as of December 31, 2010

| | |
|---|---|
| **Assets** | |
| Investments: | |
| Investments in securities, at value (cost $494,685,918), including $257,619,904 of securities loaned | $ 739,394,154 |
| Investment in Daily Assets Fund Institutional (cost $264,201,382)* | 264,201,382 |
| Investment in Central Cash Management Fund (cost $1,727,407) | 1,727,407 |
| Total investments, at value (cost $760,614,707) | 1,005,322,943 |
| Foreign currency, at value (cost $1,221) | 1,344 |
| Receivable for Fund shares sold | 540,106 |
| Interest receivable | 10,846 |
| Dividends receivable | 242,213 |
| Foreign taxes recoverable | 21,609 |
| Due from Advisor | 242 |
| Other assets | 3,845 |
| Total assets | 1,006,143,148 |
| **Liabilities** | |
| Payable upon return of securities loaned | 264,201,382 |
| Payable for Fund shares redeemed | 464,639 |
| Accrued management fee | 202,542 |
| Accrued distribution service fee (Class B) | 1,890 |
| Other accrued expenses and payables | 216,635 |
| Total liabilities | 265,087,088 |
| **Net assets, at value** | **$ 741,056,060** |
| **Net Assets Consist of** | |
| Undistributed net investment income | 5,191,902 |
| Net unrealized appreciation (depreciation) on: | |
| Investments | 244,708,236 |
| Foreign currency | 4,323 |
| Accumulated net realized gain (loss) | (166,155,788) |
| Paid-in capital | 657,307,387 |
| **Net assets, at value** | **$ 741,056,060** |
| **Class A** | |
| **Net Asset Value,** offering and redemption price per share ($728,888,149 ÷ 37,210,167 outstanding shares of beneficial interest, $.01 par value, unlimited number of shares authorized) | **$ 19.59** |
| **Class B** | |
| **Net Asset Value,** offering and redemption price per share ($12,167,911 ÷ 623,731 outstanding shares of beneficial interest, $.01 par value, unlimited number of shares authorized) | **$ 19.51** |

* *Represents collateral on securities loaned.*

# Statement of Operations

for the year ended December 31, 2010

| | |
|---|---|
| **Investment Income** | |
| Income: | |
| Dividends | $ 8,829,123 |
| Income distributions — Central Cash Management Fund | 11,380 |
| Securities lending income, including income from Daily Assets Fund Institutional, net of borrower rebates | 178,797 |
| Total income | 9,019,300 |
| Expenses: | |
| Management fee | 2,618,221 |
| Administration fee | 700,197 |
| Services to shareholders | 13,779 |
| Record keeping fee (Class B) | 10,220 |
| Custodian fee | 65,859 |
| Distribution service fee (Class B) | 29,332 |
| Professional fees | 54,954 |
| Trustees' fees and expenses | 21,391 |
| Reports to shareholders | 84,105 |
| Other | 34,298 |
| Total expenses before expense reductions | 3,632,356 |
| Expense reductions | (53,321) |
| Total expenses after expense reductions | 3,579,035 |
| **Net investment income (loss)** | **5,440,265** |
| **Realized and Unrealized Gain (Loss)** | |
| Net realized gain (loss) from: | |
| Investments | 56,925,932 |
| Foreign currency | 13,620 |
| | 56,939,552 |
| Change in net unrealized appreciation (depreciation) on: | |
| Investments | 46,075,809 |
| Foreign currency | (12,815) |
| | 46,062,994 |
| **Net gain (loss)** | **103,002,546** |
| **Net increase (decrease) in net assets resulting from operations** | **$ 108,442,811** |

*The accompanying notes are an integral part of the financial statements.*

# Statement of Changes in Net Assets

| Increase (Decrease) in Net Assets | Years Ended December 31, 2010 | 2009 |
|---|---|---|
| Operations: | | |
| Net investment income (loss) | $ 5,440,265 | $ 6,299,270 |
| Net realized gain (loss) | 56,939,552 | (29,080,095) |
| Change in net unrealized appreciation (depreciation) | 46,062,994 | 184,141,634 |
| Net increase (decrease) in net assets resulting from operations | 108,442,811 | 161,360,809 |
| Distributions to shareholders from: | | |
| Net investment income: | | |
| Class A | (6,317,623) | (7,997,037) |
| Class B | (67,783) | (116,634) |
| Total distributions | (6,385,406) | (8,113,671) |
| Fund share transactions: | | |
| **Class A** | | |
| Proceeds from shares sold | 12,396,402 | 18,231,110 |
| Net assets acquired in tax-free reorganization | — | 66,828,943 |
| Reinvestment of distributions | 6,317,623 | 7,997,037 |
| Cost of shares redeemed | (105,101,955) | (122,840,820) |
| Net increase (decrease) in net assets from Class A share transactions | (86,387,930) | (29,783,730) |
| **Class B** | | |
| Proceeds from shares sold | 1,077,251 | 1,745,917 |
| Reinvestment of distributions | 67,783 | 116,634 |
| Cost of shares redeemed | (2,881,286) | (2,624,791) |
| Net increase (decrease) in net assets from Class B share transactions | (1,736,252) | (762,240) |
| **Increase (decrease) in net assets** | 13,933,223 | 122,701,168 |
| Net assets at beginning of period | 727,122,837 | 604,421,669 |
| Net assets at end of period (including undistributed net investment income of $5,191,902 and $6,123,423, respectively) | **$ 741,056,060** | **$ 727,122,837** |

| Other Information | | |
|---|---|---|
| **Class A** | | |
| Shares outstanding at beginning of period | 42,229,316 | 43,844,542 |
| Shares sold | 714,318 | 1,329,558 |
| Shares issued in tax-free reorganization | — | 5,009,687 |
| Shares issued to shareholders in reinvestment of distributions | 348,655 | 644,923 |
| Shares redeemed | (6,082,122) | (8,599,394) |
| Net increase (decrease) in Class A shares | (5,019,149) | (1,615,226) |
| Shares outstanding at end of period | **37,210,167** | **42,229,316** |
| **Class B** | | |
| Shares outstanding at beginning of period | 725,636 | 777,803 |
| Shares sold | 62,186 | 124,580 |
| Shares issued to shareholders in reinvestment of distributions | 3,749 | 9,421 |
| Shares redeemed | (167,840) | (186,168) |
| Net increase (decrease) in Class B shares | (101,905) | (52,167) |
| Shares outstanding at end of period | **623,731** | **725,636** |

*The accompanying notes are an integral part of the financial statements.*

# Financial Highlights

## Class A

| Years Ended December 31, | 2010 | 2009 | 2008 | 2007 | 2006 |
|---|---|---|---|---|---|
| **Selected Per Share Data** | | | | | |
| **Net asset value, beginning of period** | **$16.93** | **$13.55** | **$20.41** | **$18.24** | **$16.90** |
| *Income (loss) from investment operations:* | | | | | |
| Net investment income (loss)[a] | .14[d] | .14 | .16 | .17[d] | .13[c] |
| Net realized and unrealized gain (loss) | 2.68 | 3.43 | (6.83) | 2.12 | 1.31 |
| **Total from investment operations** | 2.82 | 3.57 | (6.67) | 2.29 | 1.44 |
| *Less distributions from:* | | | | | |
| Net investment income | (.16) | (.19) | (.19) | (.12) | (.10) |
| **Net asset value, end of period** | **$19.59** | **$16.93** | **$13.55** | **$20.41** | **$18.24** |
| Total Return (%)[b] | 16.71 | 26.87 | (32.98) | 12.59 | 8.53[c] |
| **Ratios to Average Net Assets and Supplemental Data** | | | | | |
| Net assets, end of period ($ millions) | 729 | 715 | 594 | 1,058 | 1,131 |
| Ratio of expenses before expense reductions (%) | .51 | .51 | .50 | .53 | .52 |
| Ratio of expenses after expense reductions (%) | .51 | .49 | .49 | .52 | .49 |
| Ratio of net investment income (loss) (%) | .78[d] | .98 | .89 | .86[d] | .73[c] |
| Portfolio turnover rate (%) | 42 | 76 | 21 | 30 | 16 |

a *Based on average shares outstanding during the period.*

b *Total return would have been lower had certain expenses not been reduced.*

c *Includes non-recurring income from the Advisor recorded as a result of an administrative proceeding regarding disclosure of brokerage allocation practices in connection with sales of DWS Funds. The non-recurring income resulted in an increase in net investment income of $0.007 per share and an increase in the ratio of net investment income of 0.04%. Excluding this non-recurring income, total return would have been 0.03% lower.*

d *Net investment income per share and ratio of net investment income include non-recurring dividend income amounting to $0.05 and $0.03 per share and 0.28% and 0.17% of average daily net assets for the years ended December 31, 2010 and 2007, respectively.*

## Class B

| Years Ended December 31, | 2010 | 2009 | 2008 | 2007 | 2006 |
|---|---|---|---|---|---|
| **Selected Per Share Data** | | | | | |
| **Net asset value, beginning of period** | **$16.86** | **$13.49** | **$20.31** | **$18.15** | **$16.81** |
| *Income (loss) from investment operations:* | | | | | |
| Net investment income (loss)[a] | .08[d] | .09 | .10 | .09[d] | .06[c] |
| Net realized and unrealized gain (loss) | 2.67 | 3.43 | (6.81) | 2.12 | 1.31 |
| **Total from investment operations** | 2.75 | 3.52 | (6.71) | 2.21 | 1.37 |
| *Less distributions from:* | | | | | |
| Net investment income | (.10) | (.15) | (.11) | (.05) | (.03) |
| **Net asset value, end of period** | **$19.51** | **$16.86** | **$13.49** | **$20.31** | **$18.15** |
| Total Return (%)[b] | 16.33 | 26.49 | (33.20) | 12.18 | 8.17[c] |
| **Ratios to Average Net Assets and Supplemental Data** | | | | | |
| Net assets, end of period ($ millions) | 12 | 12 | 10 | 19 | 107 |
| Ratio of expenses before expense reductions (%) | .85 | .85 | .85 | .94 | .91 |
| Ratio of expenses after expense reductions (%) | .84 | .82 | .82 | .90 | .86 |
| Ratio of net investment income (loss) (%) | .45[d] | .65 | .56 | .48[d] | .36[c] |
| Portfolio turnover rate (%) | 42 | 76 | 21 | 30 | 16 |

a *Based on average shares outstanding during the period.*

b *Total return would have been lower had certain expenses not been reduced.*

c *Includes non-recurring income from the Advisor recorded as a result of an administrative proceeding regarding disclosure of brokerage allocation practices in connection with sales of DWS Funds. The non-recurring income resulted in an increase in net investment income of $0.007 per share and an increase in the ratio of net investment income of 0.04%. Excluding this non-recurring income, total return would have been 0.03% lower.*

d *Net investment income per share and ratio of net investment income include non-recurring dividend income amounting to $0.05 and $0.03 per share and $0.28% and 0.17% of average daily net assets for the years ended December 31, 2010 and 2007, respectively.*

# Notes to Financial Statements

## A. Organization and Significant Accounting Policies

DWS Variable Series I (the "Series") is registered under the Investment Company Act of 1940, as amended (the "1940 Act"), as an open-end, registered management investment company organized as a Massachusetts business trust. The Series consists of six diversified funds: DWS Bond VIP, DWS Growth & Income VIP, DWS Capital Growth VIP, DWS Global Opportunities VIP, DWS International VIP and DWS Health Care VIP (individually or collectively hereinafter referred to as a "Fund" or the "Funds"). These financial statements report on DWS Capital Growth VIP. The Series is intended to be the underlying investment vehicle for variable annuity contracts and variable life insurance policies to be offered by the separate accounts of certain life insurance companies ("Participating Insurance Companies").

**Multiple Classes of Shares of Beneficial Interest.** The Fund offers two classes of shares (Class A shares and Class B shares). Class B shares are subject to Rule 12b-1 distribution fees under the 1940 Act and record keeping fees equal to an annual rate of 0.25% and up to 0.15%, respectively, of the average daily net assets of the Class B shares of the Fund. Class A shares are not subject to such fees.

Investment income, realized and unrealized gains and losses, and certain fund-level expenses and expense reductions, if any, are borne pro rata on the basis of relative net assets by the holders of all classes of shares, except that each class bears certain expenses unique to that class (including the applicable 12b-1 distribution fees and record keeping fees). Differences in class-level expenses may result in payment of different per share dividends by class. All shares have equal rights with respect to voting subject to class-specific arrangements.

The Series' financial statements are prepared in accordance with accounting principles generally accepted in the United States of America, which require the use of management estimates. Actual results could differ from those estimates. The policies described below are followed consistently by the Series in the preparation of the financial statements for its Funds.

**Security Valuation.** Investments are stated at value determined as of the close of regular trading on the New York Stock Exchange on each day the exchange is open for trading.

Various inputs are used in determining the value of the Fund's investments. These inputs are summarized in three broad levels. Level 1 includes quoted prices in active markets for identical securities. Level 2 includes other significant observable inputs (including quoted prices for similar securities, interest rates, prepayment speeds, and credit risk). Level 3 includes significant unobservable inputs (including the Fund's own assumptions in determining the fair value of investments). The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities.

Equity securities are valued at the most recent sale price or official closing price reported on the exchange (US or foreign) or over-the-counter market on which they trade and are categorized as Level 1 securities. Securities for which no sales are reported are valued at the calculated mean between the most recent bid and asked quotations on the relevant market or, if a mean cannot be determined, at the most recent bid quotation.

Money market instruments purchased with an original or remaining maturity of sixty days or less, maturing at par, are valued at amortized cost, which approximates value, and are categorized as Level 2. Investments in open-end investment companies are valued at their net asset value each business day and are categorized as Level 1.

Securities and other assets for which market quotations are not readily available or for which the above valuation procedures are deemed not to reflect fair value are valued in a manner that is intended to reflect their fair value as determined in accordance with procedures approved by the Trustees and are generally categorized as Level 3. In accordance with the Fund's valuation procedures, factors used in determining value may include, but are not limited to, the type of the security; the size of the holding; the initial cost of the security; the existence of any contractual restrictions on the security's disposition; the price and extent of public trading in similar securities of the issuer or of comparable companies; quotations or evaluated prices from broker-dealers and/or pricing services; information obtained from the issuer, analysts, and/or the appropriate stock exchange (for exchange-traded securities); an analysis of the company's or issuer's financial statements; an evaluation of the forces that influence the issuer and the market(s) in which the security is purchased and sold and with respect to debt securities; the maturity, coupon, creditworthiness, currency denomination and the movement of the market in which the security is normally traded. The value determined under these procedures may differ from published values for the same securities.

Disclosure about the classification of fair value measurements is included in a table following the Fund's Investment Portfolio.

**Securities Lending.** The Fund lends securities to certain financial institutions. The Fund retains beneficial ownership of the securities it has loaned and continues to receive interest and dividends paid by the issuer of securities and to participate in any changes in their market value. The Fund requires the borrowers of the securities to maintain collateral with the Fund consisting of either cash or liquid, unencumbered assets having a value at least equal to the value of the securities loaned. When the collateral falls below specified amounts, the lending agent will use its best effort to obtain additional collateral on the next business day to meet required amounts under the security lending agreement. The Fund may invest the cash collateral into a joint trading account in an affiliated money market fund pursuant to Exemptive Orders issued by the SEC. The Fund receives compensation for lending its securities either in the form of fees or by earning interest on invested cash collateral net of borrower rebates and fees paid to a lending agent. Either the Fund or the borrower may terminate the loan. There may be risks of delay and costs in recovery of securities or even loss of rights in the collateral should the borrower of the securities fail financially. The Fund is also subject to all investment risks associated with the reinvestment of any cash collateral received, including, but not limited to, interest rate, credit and liquidity risk associated with such investments.

**Foreign Currency Translations.** The books and records of the Fund are maintained in US dollars. Investment securities and other assets and liabilities denominated in a foreign currency are translated into US dollars at the prevailing exchange rates at period end. Purchases and sales of investment securities, income and expenses are translated into US dollars at the prevailing exchange rates on the respective dates of the transactions.

Net realized and unrealized gains and losses on foreign currency transactions represent net gains and losses between trade and settlement dates on securities transactions, the disposition of forward foreign currency exchange contracts and foreign currencies, and the difference between the amount of net investment income accrued and the US dollar amount actually received. That portion of both realized and unrealized gains and losses on investments that results from fluctuations in foreign currency exchange rates is not separately disclosed but is included with net realized and unrealized gain/appreciation and loss/depreciation on investments.

**Taxes.** The Fund is treated as a separate taxpayer as provided for in the Internal Revenue Code, as amended. It is the Fund's policy to comply with the requirements of the Internal Revenue Code, as amended, which are applicable to regulated investment companies, and to distribute all of its taxable income to the separate accounts of the Participating Insurance Companies which hold its shares.

At December 31, 2010, the Fund had an approximate net tax basis capital loss carryforward which may be applied against any realized net taxable capital gains of each succeeding year until fully utilized or until the following expiration dates, whichever occurs first:

| Fund | Capital Loss Carryforwards ($) | Expiration Date | Capital Loss Carryfowards Utilized ($) | Capital Loss Carryfowards Expired ($) |
|---|---|---|---|---|
| DWS Capital Growth VIP | 163,203,000 | 12/31/2011–12/31/2017 | 57,103,000 | 36,274,000 |

At December 31, 2010, the Fund had a net tax basis capital loss carryforward of approximately $163,203,000, including $31,237,000 inherited from its mergers with affiliated funds in fiscal years 2005, 2006 and 2009 which may be applied against any realized net taxable capital gains of each succeeding year until fully utilized and which may be subject to certain limitations under Sections 382–384 of the Internal Revenue Code. Due to these limitations (under Sections 382–384 of the Internal Revenue Code), approximately $1,097,000 of the inherited capital loss carryforward cannot be used by the funds, and is not included in the capital loss carryforward of $163,203,000 disclosed above.

The Fund has reviewed the tax positions for the open tax years as of December 31, 2010 and has determined that no provision for income tax is required in the Fund's financial statements. The Fund's federal tax returns for the prior three fiscal years remain open subject to examination by the Internal Revenue Service.

**Distribution of Income and Gains.** The Fund will declare and distribute dividends from its net investment income, if any, annually, although additional distributions may be made if necessary. Net realized gains from investment transactions, in excess of available capital loss carryforwards, would be taxable to the Fund if not distributed, and, therefore, will be distributed to shareholders at least annually.

The timing and characterization of certain income and capital gains distributions are determined annually in accordance with federal tax regulations which may differ from accounting principles generally accepted in the United States of America. These differences primarily relate to certain securities sold at a loss. As a result, net investment income (loss) and net realized gain (loss) on investment transactions for a reporting period may differ significantly from distributions during such period. Accordingly, the Fund may periodically make reclassifications among certain of its capital accounts without impacting the net asset value of the Fund.

At December 31, 2010, the Fund's components of distributable earnings (accumulated losses) on a tax-basis are as follows:

| Fund | Undistributed Ordinary Income ($)* | Capital Loss Carryforwards ($) | Net Unrealized Gain (Loss) on Investments ($) |
|---|---|---|---|
| DWS Capital Growth VIP | 5,191,902 | (163,203,000) | 241,755,764 |

In addition, the tax character of distributions paid to shareholders by the Fund is summarized as follows:

| Fund | Distributions from Ordinary Income ($)* Years Ended December 31, 2010 | 2009 |
|---|---|---|
| DWS Capital Growth VIP | 6,385,406 | 8,113,671 |

* *For tax purposes, short-term capital gains distributions are considered ordinary income distributions.*

**Expenses.** Expenses of the Series arising in connection with a specific Fund are allocated to that Fund. Other Series expenses which cannot be directly attributed to a Fund are apportioned among the Funds in the Series.

**Contingencies.** In the normal course of business, the Fund may enter into contracts with service providers that contain general indemnification clauses. The Fund's maximum exposure under these arrangements is unknown as this would involve future claims that may be made against the Fund that have not yet been made. However, based on experience, the Fund expects the risk of loss to be remote.

**Other.** Investment transactions are accounted for on a trade date plus one basis for daily net asset value calculations. However, for financial reporting purposes, investment transactions are reported on trade date. Interest income is recorded on the accrual basis net of foreign withholding taxes. Dividend income is recorded on the ex-dividend date net of foreign withholding taxes. Certain dividends from foreign securities may be recorded subsequent to the ex-dividend date as soon as the Fund is informed of such dividends. Realized gains and losses from investment transactions are recorded on an identified cost basis.

## B. Purchases and Sales of Securities

During the year ended December 31, 2010, purchases and sales of investment securities (excluding short-term investments) were as follows:

| Fund | Purchases ($) | Sales ($) |
|---|---|---|
| DWS Capital Growth VIP | 285,882,039 | 369,248,095 |

## C. Related Parties

Under the Investment Management Agreement with Deutsche Investment Management Americas Inc. ("DIMA" or the "Advisor"), an indirect, wholly owned subsidiary of Deutsche Bank AG, the Advisor directs the investments of the Fund in accordance with its investment objectives, policies and restrictions. The Advisor determines the securities, instruments and other contracts relating to investments to be purchased, sold or entered into by the Fund.

Under the Investment Management Agreement with the Advisor, the Fund pays a monthly management fee, based on the average daily net assets of the Fund, computed and accrued daily and payable monthly, at the annual rates shown below:

| Fund | Annual Management Fee Rate |
|---|---|
| DWS Capital Growth VIP | |
| first $250 million of average daily net assets | .390% |
| next $750 million of average daily net assets | .365% |
| over $1 billion of average daily net assets | .340% |

For the period from January 1, 2010 through April 30, 2010, the Advisor, the underwriter and accounting agent contractually agreed to waive a portion of their fee to the extent necessary to maintain the operating expenses of each class (excluding certain expenses such as extraordinary expenses, taxes, brokerage and interest) as follows:

| Fund | Annual Rate |
|---|---|
| DWS Capital Growth VIP Class A | .49% |
| DWS Capital Growth VIP Class B | .82% |

Accordingly, for the year ended December 31, 2010, the total management fee, management fee waived and effective management fee rate are as follows:

| Fund | Total Aggregated ($) | Waived ($) | Annual Effective Rate |
|---|---|---|---|
| DWS Capital Growth VIP | 2,618,221 | 52,169 | .37% |

In addition, for the year ended December 31, 2010, the Advisor waived record keeping expenses of Class B shares of the Fund as follows:

| Fund | Waived ($) |
|---|---|
| DWS Capital Growth VIP | 232 |

**Administration Fee.** Pursuant to an Administrative Services Agreement, DIMA provides most administrative services to the Series. For all services provided under the Administrative Services Agreement, the Fund pays the Advisor an annual fee ("Administration Fee") of 0.10% of the Fund's average daily net assets, computed and accrued daily and payable monthly. For the year ended December 31, 2010, the Administration Fee was as follows:

| Fund | Total Aggregated ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS Capital Growth VIP | 700,197 | 62,425 |

**Service Provider Fees.** DWS Investments Service Company ("DISC"), an affiliate of the Advisor, is the transfer agent, dividend-paying agent and shareholder service agent for the Series. Pursuant to a sub-transfer agency agreement between DISC and DST Systems, Inc. ("DST"), DISC has delegated certain transfer agent, dividend-paying agent and shareholder service agent functions to DST. DISC compensates DST out of the shareholder servicing fee it receives from the Fund. For the year ended December 31, 2010, the amounts charged to the Fund by DISC were as follows:

| Fund | Total Aggregated ($) | Waived ($) |
|---|---|---|
| DWS Capital Growth VIP Class A | 814 | 814 |
| DWS Capital Growth VIP Class B | 106 | 106 |

DWS Investments Distributors, Inc. ("DIDI"), also an affiliate of the Advisor, is the Series' Distributor. In accordance with the Master Distribution Plan, DIDI receives 12b-1 fees of 0.25% of average daily net assets of Class B shares. Pursuant to the Master Distribution Plan, DIDI remits these fees to the Participating Insurance Companies for various costs incurred or paid by these companies in connection with marketing and distribution of Class B shares. These fees are detailed in the Fund's Statement of Operations.

**Typesetting and Filing Service Fees.** Under an agreement with DIMA, DIMA is compensated for providing typesetting and certain regulatory filing services to the Fund. For the year ended December 31, 2010, the amount charged to the Fund by DIMA included in the Statement of Operations under "reports to shareholders" was as follows:

| Fund | Total Aggregated ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS Capital Growth VIP | 11,562 | 2,182 |

**Trustees' Fees and Expenses.** The Fund paid each Trustee not affiliated with the Advisor retainer fees plus specified amounts for various committee services and for the Board Chairperson.

**Affiliated Cash Management Vehicles.** The Fund may invest uninvested cash balances in Central Cash Management Fund, which is managed by the Advisor. The Fund indirectly bears its proportionate share of the expenses of the underlying money market funds. Central Cash Management Fund does not pay the Advisor an investment management fee. Central Cash Management Fund seeks a high level of current income consistent with liquidity and the preservation of capital.

## D. Ownership of the Fund

Three participating insurance companies were owners of record of 10% or more of the total outstanding Class A shares of the Fund, each owning 43%, 22% and 12%. Two participating insurance companies were owners of record of 10% or more of the total outstanding Class B shares of the Fund, each owning 82% and 17%.

## E. Line of Credit

The Series and other affiliated funds (the "Participants") share in a $450 million revolving credit facility provided by a syndication of banks. The Fund may borrow for temporary or emergency purposes, including the meeting of redemption requests that otherwise might require the untimely disposition of securities. The Participants are charged an annual commitment fee which is allocated based on net assets, among each of the Participants. Interest is calculated at a rate per annum equal to the sum of the Federal Funds Rate plus 1.25 percent plus if LIBOR exceeds the Federal Funds Rate the amount of such excess. The Fund may borrow up to a maximum of 33 percent of its net assets under the agreement.

## F. Acquisition of Assets

On April 24, 2009, the Fund acquired all of the net assets of DWS Janus Growth & Income VIP pursuant to a plan of reorganization approved by shareholders on April 20, 2009. The purpose of the transaction was to combine two funds managed by DWS with comparable investment objectives and strategies. The acquisition was accomplished by a tax-free exchange of 9,556,588 Class A shares of DWS Janus Growth & Income VIP for 5,009,687 Class A shares of the Fund outstanding on April 24, 2009. DWS Janus Growth & Income VIP's net assets at that date, $66,828,943, including $510,610 of net unrealized appreciation, were combined with those of the Fund. The aggregate net assets of the Fund immediately before the acquisition were $572,408,860. The combined net assets of the Fund immediately following the acquisition were $639,237,803.

## G. Subsequent Events

On January 12, 2011, the Board of the following Acquired Funds approved, in principle, the merger of the Acquired Funds into the Acquiring Fund. Completion of the merger is subject to a number of conditions, including final approval by Acquired Funds Board and approval by the shareholders of the Acquired Funds at a shareholder meeting expected to be held during the month of April 2011. If shareholder approval is obtained, the mergers are expected to occur on or about May 1, 2011.

| Acquired Funds | Acquiring Fund |
|---|---|
| DWS Variable Series I — DWS Health Care VIP | DWS Variable Series I — DWS Capital Growth VIP |
| DWS Variable Series II — DWS Technology VIP | DWS Variable Series I — DWS Capital Growth VIP |

# Report of Independent Registered Public Accounting Firm

**To the Trustees of DWS Variable Series I and the Shareholders of DWS Capital Growth VIP:**

In our opinion, the accompanying statement of assets and liabilities, including the investment portfolio, and the related statements of operations and of changes in net assets and the financial highlights present fairly, in all material respects, the financial position of DWS Capital Growth VIP (the "Fund") at December 31, 2010 and the results of its operations, the changes in its net assets, and the financial highlights for the periods indicated therein, in conformity with accounting principles generally accepted in the United States of America. These financial statements and financial highlights (hereafter referred to as "financial statements") are the responsibility of the Fund's management. Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these financial statements in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits, which included confirmation of securities at December 31, 2010 by correspondence with the custodians and brokers, provide a reasonable basis for our opinion.

Boston, Massachusetts
February 11, 2011

PricewaterhouseCoopers LLP

## Tax Information

**(Unaudited)**

For corporate shareholders of the Fund, 100% of the ordinary dividends (i.e., income dividends plus short-term capital gains) paid during the Fund's fiscal year ended December 31, 2010 qualified for the dividends received deduction.

Please consult a tax advisor if you have questions about federal or state income tax laws, or on how to prepare your tax returns. If you have specific questions about your account, please contact your insurance provider.

## Proxy Voting

The Series' policies and procedures for voting proxies for portfolio securities and information about how the Series voted proxies related to its portfolio securities during the 12-month period ended June 30 are available on our Web site — www.dws-investments.com (click on "proxy voting"at the bottom of the page) — or on the SEC's Web site — www.sec.gov. To obtain a written copy of the Series' policies and procedures without charge, upon request, call us toll free at (800) 728-3337.

# Investment Management Agreement Approval

The Board of Trustees, including the Independent Trustees, approved the renewal of your Fund's investment management agreement (the "Agreement") with Deutsche Investment Management Americas Inc. ("DWS") in September 2010.

In terms of the process that the Board followed prior to approving the Agreement, shareholders should know that:

- In September 2010, all of the Fund's Trustees were independent of DWS and its affiliates.
- The Trustees meet frequently to discuss fund matters. Each year, the Trustees dedicate substantial time to contract review matters. Over the course of several months, the Board's Contract Committee, in coordination with the Board's Equity Oversight Committee, reviewed comprehensive materials received from DWS, independent third parties and independent counsel. These materials included an analysis of the Fund's performance, fees and expenses, and profitability compiled by the Fund's independent fee consultant. The Board also received extensive information throughout the year regarding performance of the Fund.
- The Independent Trustees regularly meet privately with their independent counsel to discuss contract review and other matters. In addition, the Independent Trustees were also advised by the Fund's independent fee consultant in the course of their review of the Fund's contractual arrangements and considered a comprehensive report prepared by the independent fee consultant in connection with their deliberations (the "IFC Report").
- In connection with reviewing the Agreement, the Board also reviewed the terms of the Fund's Rule 12b-1 plan, distribution agreement, administrative services agreement, transfer agency agreement and other material service agreements.
- Based on its evaluation of the information provided, the Contract Committee presented its findings and recommendations to the Independent Trustees as a group. The Independent Trustees reviewed the Contract Committee's findings and recommendations and presented their recommendations to the full Board.

In connection with the contract review process, the Contract Committee and the Board considered the factors discussed below, among others. The Board also considered that DWS and its predecessors have managed the Fund since its inception, and the Board believes that a long-term relationship with a capable, conscientious advisor is in the best interests of the Fund. The Board considered, generally, that shareholders chose to invest or remain invested in the Fund knowing that DWS managed the Fund, and that the Agreement was approved by the Fund's shareholders. DWS is part of Deutsche Bank, a major global banking institution that is engaged in a wide range of financial services. The Board believes that there are significant advantages to being part of a global asset management business that offers a wide range of investing expertise and resources, including hundreds of portfolio managers and analysts with research capabilities in many countries throughout the world.

While shareholders may focus primarily on fund performance and fees, the Fund's Board considers these and many other factors, including the quality and integrity of DWS's personnel and such other issues as back-office operations, fund valuations, and compliance policies and procedures.

**Nature, Quality and Extent of Services.** The Board considered the terms of the Agreement, including the scope of advisory services provided under the Agreement. The Board noted that, under the Agreement, DWS provides portfolio management services to the Fund and that, pursuant to a separate administrative services agreement, DWS provides administrative services to the Fund. The Board considered the experience and skills of senior management and investment personnel, the resources made available to such personnel, the ability of DWS to attract and retain high-quality personnel, and the organizational depth and stability of DWS. The Board reviewed the Fund's performance over short-term and long-term periods and compared those returns to various agreed-upon performance measures, including market indices and a peer universe compiled by the independent fee consultant using information supplied by Lipper Inc. ("Lipper"). The Board also noted that it has put into place a process of identifying "Focus Funds" (e.g., funds performing poorly relative to their benchmark or a peer universe compiled by Lipper), and receives more frequent reporting and information from DWS regarding such funds, along with DWS's remedial plans to address underperformance. The Board believes this process is an effective manner of identifying and addressing underperforming funds. Based on the information provided, the Board noted that for the one-, three- and five-year periods ended December 31, 2009, the Fund's performance (Class A shares) was in the 4th quartile, 2nd quartile and 1st quartile, respectively, of the applicable Lipper universe (the 1st quartile being the best performers and the 4th quartile being the worst performers). The Board also observed that the Fund has outperformed its benchmark in the three- and five-year periods and has underperformed its benchmark in the one-year period ended December 31, 2009. The Board noted the disappointing investment performance of the Fund in recent periods and continued to discuss with senior management of DWS the factors contributing to such underperformance and actions being taken to improve performance. The Board observed that the Fund had experienced improved relative performance during the first seven months of 2010.

On the basis of this evaluation and the ongoing review of investment results by the Board, the Board concluded that the nature, quality and extent of services provided by DWS historically have been and continue to be satisfactory.

**Fees and Expenses.** The Board considered the Fund's investment management fee schedule, operating expenses and total expense ratios, and comparative information provided by Lipper and the independent fee consultant regarding investment management fee rates paid to other investment advisors by similar funds (1st quartile being the most favorable and 4th quartile being the least favorable). With respect to management fees paid to other investment advisors by similar funds, the Board noted that the contractual fee rates paid by the Fund, which include a 0.10% fee paid to DWS under the Fund's administrative services agreement, were lower than the median (1st quartile) of the applicable Lipper peer group (based on Lipper data provided as of December 31, 2009). The Board noted that the Fund's Class A shares total (net) operating expenses were expected to be lower than the median (1st quartile) of the applicable Lipper expense universe (based on Lipper data provided as of December 31, 2009) ("Lipper Universe Expenses"). The Board also reviewed data comparing each share class's total (net) operating expenses to the applicable Lipper Universe Expenses. The Board considered the Fund's management fee rate as compared to fees charged by DWS and certain of its affiliates for comparable mutual funds and considered differences in fund and fee structures between the DWS Funds. The Board also considered how the Fund's total (net) operating expenses compared to the total (net) operating expenses of a more customized peer group selected by Lipper (based on such factors as asset size).

The information considered by the Board as part of its review of management fees included information regarding fees charged by DWS and its affiliates to similar institutional accounts and to similar funds offered primarily to European investors ("DWS Europe funds"), in each case as applicable. The Board observed that advisory fee rates for institutional accounts generally were lower than the management fees charged by similarly managed DWS US mutual funds ("DWS Funds"), but also took note of the differences in services provided to DWS Funds as compared to institutional accounts. In the case of DWS Europe funds, the Board observed that fee rates for DWS Europe funds generally were higher than for similarly managed DWS Funds, but noted that differences in the types of services provided to DWS Funds relative to DWS Europe funds made it difficult to compare such fees.

On the basis of the information provided, the Board concluded that management fees were reasonable and appropriate in light of the nature, quality and extent of services provided by DWS.

**Profitability.** The Board reviewed detailed information regarding revenues received by DWS under the Agreement. The Board considered the estimated costs and pre-tax profits realized by DWS from advising the DWS Funds, as well as estimates of the pre-tax profits attributable to managing the Fund in particular. The Board also received information regarding the estimated enterprise-wide profitability of DWS and its affiliates with respect to all fund services in totality and by fund. The Board reviewed DWS's methodology in allocating its costs to the management of the Fund. Based on the information provided, the Board concluded that the pre-tax profits realized by DWS in connection with the management of the Fund were not unreasonable. The Board also reviewed information regarding the profitability of certain similar investment management firms. The Board noted that while information regarding the profitability of such firms is limited (and in some cases is not necessarily prepared on a comparable basis), DWS and its affiliates' overall profitability with respect to the DWS fund complex (after taking into account distribution and other services provided to the funds by DWS and its affiliates) was lower than the overall profitability levels of many comparable firms for which such data was available.

**Economies of Scale.** The Board considered whether there are economies of scale with respect to the management of the Fund and whether the Fund benefits from any economies of scale. The Board noted that the Fund's management fee schedule includes fee breakpoints. The Board concluded that the Fund's fee schedule represents an appropriate sharing between the Fund and DWS of such economies of scale as may exist in the management of the Fund at current asset levels.

**Other Benefits to DWS and Its Affiliates.** The Board also considered the character and amount of other incidental benefits received by DWS and its affiliates, including any fees received by DWS for administrative services provided to the Fund and any fees received by an affiliate of DWS for distribution services. The Board also considered benefits to DWS related to brokerage and soft-dollar allocations, including allocating brokerage to pay for research generated by parties other than the executing broker dealers, which pertain primarily to funds investing in equity securities, along with the incidental public relations benefits to DWS related to DWS Funds advertising and cross-selling opportunities among DWS products and services. The Board concluded that management fees were reasonable in light of these fallout benefits.

**Compliance.** The Board considered the significant attention and resources dedicated by DWS to documenting and enhancing its compliance processes in recent years. The Board noted in particular (i) the experience and seniority of both DWS's chief compliance officer and the Fund's chief compliance officer; (ii) the large number of DWS compliance personnel; and (iii) the substantial commitment of resources by DWS and its affiliates to compliance matters.

Based on all of the information considered and the conclusions reached, the Board unanimously determined that the continuation of the Agreement is in the best interests of the Fund. In making this determination, the Board did not give particular weight to any single factor identified above. The Board considered these factors over the course of numerous meetings, certain of which were in executive session with only the Independent Trustees and their counsel present. It is possible that individual Trustees may have weighed these factors differently in reaching their individual decisions to approve the continuation of the Agreement.

# Summary of Management Fee Evaluation by Independent Fee Consultant

October 3, 2010

Pursuant to an Order entered into by Deutsche Investment Management Americas and affiliates (collectively, "DeAM") with the Attorney General of New York, I, Thomas H. Mack, have been appointed the Independent Fee Consultant for the DWS Funds (formerly the DWS Scudder Funds). My duties include preparing an annual written evaluation of the management fees DeAM charges the Funds, considering among other factors the management fees charged by other mutual fund companies for like services, management fees DeAM charges other clients for like services, DeAM's costs of supplying services under the management agreements and related profit margins, possible economies of scale if a Fund grows larger, and the nature and quality of DeAM's services, including fund performance. This report summarizes my evaluation for 2010, including my qualifications, the evaluation process for each of the DWS Funds, consideration of certain complex-level factors, and my conclusions. I served in substantially the same capacity in 2007, 2008, and 2009.

## Qualifications

For more than 35 years I have served in various professional capacities within the investment management business. I have held investment analysis and advisory positions, including securities analyst, portfolio strategist and director of investment policy with a large investment firm. I have also performed business management functions, including business development, financial management and marketing research and analysis.

Since 1991, I have been an independent consultant within the asset management industry. I have provided services to over 125 client organizations, including investment managers, mutual fund boards, product distributors and related organizations. Over the past ten years I have completed a number of assignments for mutual fund boards, specifically including assisting boards with management contract renewal.

I hold a Master of Business Administration degree, with highest honors, from Harvard University and Master of Science and Bachelor of Science (highest honors) degrees from the University of California at Berkeley. I am an independent director and audit committee financial expert for two closed-end mutual funds and have served in various leadership and financial oversight capacities with non-profit organizations.

## Evaluation of Fees for each DWS Fund

My work focused primarily on evaluating, fund-by-fund, the fees charged to each of the 118 publicly offered Fund portfolios in the DWS Fund family. For each Fund, I considered each of the key factors mentioned above, as well as any other relevant information. In doing so I worked closely with the Funds' Independent Directors in their annual contract renewal process, as well as in their approval of contracts for several new funds (documented separately).

In evaluating each Fund's fees, I reviewed comprehensive materials provided by or on behalf of DeAM, including expense information prepared by Lipper Analytical, comparative performance information, profitability data, manager histories, and other materials. I also accessed certain additional information from the Lipper and Morningstar databases and drew on my industry knowledge and experience.

To facilitate evaluating this considerable body of information, I prepared for each Fund a document summarizing the key data elements in each area as well as additional analytics discussed below. This made it possible to consider each key data element in the context of the others.

In the course of contract renewal, DeAM agreed to implement a number of fee and expense adjustments requested by the Independent Directors which will favorably impact future fees and expenses, and my evaluation includes the effects of these changes.

### Fees and Expenses Compared with Other Funds

The competitive fee and expense evaluation for each fund focused on two primary comparisons:

- The Fund's contractual management fee (the advisory fee plus the administration fee where applicable) compared with those of a group of typically 12–15 funds in the same Lipper investment category (e.g. Large Capitalization Growth) having similar distribution arrangements and being of similar size.
- The Fund's total expenses compared with a broader universe of funds from the same Lipper investment category and having similar distribution arrangements.

These two comparisons provide a view of not only the level of the fee compared with funds of similar scale but also the total expense the Fund bears for all the services it receives, in comparison with the investment choices available in the Fund's investment category and distribution channel. The principal figure-of-merit used in these comparisons was the subject Fund's percentile ranking against peers.

### DeAM's Fees for Similar Services to Others

DeAM provided management fee schedules for all of its US domiciled fund and non-fund investment management accounts in any of the investment categories where there is a DWS Fund. These similar products included the other DWS Funds, non-fund pooled accounts, institutional accounts and sub-advisory accounts. Using this information, I calculated for each Fund the fee that would be charged to each similar product, at the subject Fund's asset level.

Evaluating information regarding non-fund products is difficult because there are varying levels of services required for different types of accounts, with mutual funds generally requiring considerably more regulatory and administrative types of service as well as having more frequent cash flows than other types of accounts. Also, while mutual fund fees for similar fund products can be expected to be similar, there will be some differences due to different pricing conditions in different distribution channels (e.g. retail funds versus those used in variable insurance products), differences in underlying investment processes and other factors.

**Costs and Profit Margins**

DeAM provided a detailed profitability analysis for each Fund. After making some adjustments so that the presentation would be more comparable to the available industry figures, I reviewed profit margins from investment management alone, from investment management plus other fund services (excluding distribution) provided to the Funds by DeAM (principally shareholder services), and DeAM profits from all sources, including distribution. A later section comments on overall profitability.

**Economies of Scale**

Economies of scale — an expected decline in management cost per dollar of fund assets as fund assets grow — are very rarely quantified and documented because of inherent difficulties in collecting and analyzing relevant data. However, in virtually every investment category that I reviewed, larger funds tend to have lower fees and lower total expenses than smaller funds. To see how each DWS Fund compares with this industry observation, I reviewed:

- The trend in Fund assets over the last five years and the accompanying trend in total expenses. This shows if the Fund has grown and, if so, whether total expense (management fees as well as other expenses) have declined as a percent of assets.
- Whether the Fund has break-points in its management fee schedule, the extent of the fee reduction built into the schedule and the asset levels where the breaks take effect, and in the case of a sub-advised Fund how the Fund's break-points compare with those of the sub-advisory fee schedule.
- How the Fund's contractual fee schedule compares with trends in the industry data. To accomplish this, I constructed a chart showing how actual latest-fiscal-year contractual fees of the Fund and of other similar funds relate to average fund assets, with the subject Fund's contractual fee schedule superimposed.

**Quality of Service — Performance**

The quality-of-service evaluation focused on investment performance, which is the principal result of the investment management service. Each Fund's performance was reviewed over the past 1, 3, 5 and 10 years, as applicable, and compared with that of other funds in the same investment category and with a suitable market index.

In addition, I calculated and reviewed risk-adjusted returns relative to an index of similar mutual funds' returns and a suitable market index. The risk-adjusted returns analysis provides a way of determining the extent to which the Fund's return comparisons are mainly the product of investment value-added (or lack thereof) or alternatively taking considerably more or less risk than is typical in its investment category.

I also received and considered the history of portfolio manager changes for each Fund, as this provided an important context for evaluating the performance results.

## Complex-Level Considerations

While this evaluation was conducted mainly at the individual fund level, there are some issues relating to the reasonableness of fees that can alternatively be considered across the whole fund complex:

- I reviewed DeAM's profitability analysis for all DWS Funds, with a view toward determining if the allocation procedures used were reasonable and how profit levels compared with public data for other investment managers.
- I considered whether DeAM and affiliates receive any significant ancillary or "fall-out" benefits that should be considered in interpreting the direct profitability results. These would be situations where serving as the investment manager of the Funds is beneficial to another part of the Deutsche Bank organization.
- I considered how aggregated DWS Fund expenses had varied over the years, by asset class and in the context of trends in asset levels.
- I reviewed the structure of the DeAM organization, trends in staffing levels, and information on compensation of investment management and other professionals compared with industry data.

## Findings

Based on the process and analysis discussed above, which included reviewing a wide range of information from management and external data sources and considering among other factors the fees DeAM charges other clients, the fees charged by other fund managers, DeAM's costs and profits associated with managing the Funds, economies of scale, possible fall-out benefits, and the nature and quality of services provided, in my opinion the management fees charged the DWS Funds are reasonable.

Thomas H. Mack

Thomas H. Mack

# Board Members and Officers

The following table presents certain information regarding the Board Members and Officers of the Trust as of December 31, 2010. Each Board Member's year of birth is set forth in parentheses after his or her name. Unless otherwise noted, (i) each Board Member has engaged in the principal occupation(s) noted in the table for at least the most recent five years, although not necessarily in the same capacity; and (ii) the address of each Independent Board Member is c/o Paul K. Freeman, Independent Chairman, DWS Funds, PO Box 101833, Denver, CO 80250-1833. Except as otherwise noted below, the term of office for each Board Member is until the election and qualification of a successor, or until such Board Member sooner dies, resigns, is removed or as otherwise provided in the governing documents of the fund. Because the fund does not hold an annual meeting of shareholders, each Board Member will hold office for an indeterminate period. The Board Members may also serve in similar capacities with other funds in the fund complex. The Length of Time Served represents the year in which the Board Member joined the board of one or more DWS funds now overseen by the Board.

**Independent Board Members**

| Name, Year of Birth, Position with the Fund and Length of Time Served[1] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Paul K. Freeman (1950)<br>Chairperson since 2009<br>Board Member since 1993 | Consultant, World Bank/Inter-American Development Bank; Executive and Governing Council of the Independent Directors Council (education committees); formerly, Project Leader, International Institute for Applied Systems Analysis (1998–2001); Chief Executive Officer, The Eric Group, Inc. (environmental insurance) (1986–1998) | 122 |
| John W. Ballantine (1946)<br>Board Member since 1999 | Retired; formerly, Executive Vice President and Chief Risk Management Officer, First Chicago NBD Corporation/The First National Bank of Chicago (1996–1998); Executive Vice President and Head of International Banking (1995–1996). Directorships: Healthways, Inc. (provider of disease and care management services); Portland General Electric (utility company); Stockwell Capital Investments PLC (private equity). Former Directorships: First Oak Brook Bancshares, Inc. and Oak Brook Bank; Prisma Energy International | 122 |
| Henry P. Becton, Jr. (1943)<br>Board Member since 1990 | Vice Chair and former President, WGBH Educational Foundation. Directorships: Association of Public Television Stations; Lead Director, Becton Dickinson and Company[3] (medical technology company); Lead Director, Belo Corporation[3] (media company); Public Radio International; Public Radio Exchange (PRX); The PBS Foundation. Former Directorships: Boston Museum of Science; American Public Television; Concord Academy; New England Aquarium; Mass. Corporation for Educational Telecommunications; Committee for Economic Development; Public Broadcasting Service | 122 |
| Dawn-Marie Driscoll (1946)<br>Board Member since 1987 | President, Driscoll Associates (consulting firm); Executive Fellow, Center for Business Ethics, Bentley University; formerly, Partner, Palmer & Dodge (1988–1990); Vice President of Corporate Affairs and General Counsel, Filene's (1978–1988). Directorships: Trustee of 22 open-end mutual funds managed by Sun Capital Advisers, Inc. (since 2007); Director of ICI Mutual Insurance Company (since 2007); Advisory Board, Center for Business Ethics, Bentley University; Trustee, Southwest Florida Community Foundation (charitable organization). Former Directorships: Investment Company Institute (audit, executive, nominating committees) and Independent Directors Council (governance, executive committees) | 122 |
| Keith R. Fox (1954)<br>Board Member since 1996 | Managing General Partner, Exeter Capital Partners (a series of private investment funds). Directorships: Progressive International Corporation (kitchen goods importer and distributor); BoxTop Media Inc. (advertising); The Kennel Shop (retailer); former Chairman, National Association of Small Business Investment Companies | 122 |
| Kenneth C. Froewiss (1945)<br>Board Member since 2001 | Adjunct Professor of Finance, NYU Stern School of Business (September 2009–present; Clinical Professor from 1997–September 2009); Member, Finance Committee, Association for Asian Studies (2002–present); Director, Mitsui Sumitomo Insurance Group (US) (2004–present); prior thereto, Managing Director, J.P. Morgan (investment banking firm) (until 1996) | 122 |
| Richard J. Herring (1946)<br>Board Member since 1990 | Jacob Safra Professor of International Banking and Professor, Finance Department, The Wharton School, University of Pennsylvania (since July 1972); Co-Director, Wharton Financial Institutions Center (since July 2000); Co-Chair, U.S. Shadow Financial Regulatory Committee; Executive Director, Financial Economists Roundtable; Director, Japan Equity Fund, Inc. (since September 2007), Thai Capital Fund, Inc. (since September 2007), Singapore Fund, Inc. (since September 2007); Independent Director of Barclays Bank Delaware (since September 2010). Formerly, Vice Dean and Director, Wharton Undergraduate Division (July 1995–June 2000); Director, Lauder Institute of International Management Studies (July 2000–June 2006) | 122 |
| William McClayton (1944)<br>Board Member since 2004+ | Private equity investor (since October 2009); previously, Managing Director, Diamond Management & Technology Consultants, Inc. (global consulting firm) (2001–2009); Directorship: Board of Managers, YMCA of Metropolitan Chicago; formerly: Senior Partner, Arthur Andersen LLP (accounting) (1966–2001); Trustee, Ravinia Festival | 122 |

| Name, Year of Birth, Position with the Fund and Length of Time Served[1] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Rebecca W. Rimel (1951)<br>Board Member since 1995 | President and Chief Executive Officer, The Pew Charitable Trusts (charitable organization) (1994 to present); Trustee, Thomas Jefferson Foundation (charitable organization) (1994 to present); Trustee, Executive Committee, Philadelphia Chamber of Commerce (2001–2007); Director, CardioNet, Inc.[2] (2009–present) (health care). Formerly, Executive Vice President, The Glenmede Trust Company (investment trust and wealth management) (1983–2004); Board Member, Investor Education (charitable organization) (2004–2005); Director, Viasys Health Care[2] (January 2007–June 2007); Trustee, Pro Publica (charitable organization) (2007–2010) | 122 |
| William N. Searcy, Jr. (1946)<br>Board Member since 1993 | Private investor since October 2003; Trustee of 22 open-end mutual funds managed by Sun Capital Advisers, Inc. (since October 1998). Formerly, Pension & Savings Trust Officer, Sprint Corporation[2] (telecommunications) (November 1989–September 2003) | 122 |
| Jean Gleason Stromberg (1943)<br>Board Member since 1997 | Retired. Formerly, Consultant (1997–2001); Director, Financial Markets US Government Accountability Office (1996–1997); Partner, Fulbright & Jaworski, L.L.P. (law firm) (1978–1996). Directorships: The William and Flora Hewlett Foundation. Former Directorships: Service Source, Inc., Mutual Fund Directors Forum (2002–2004), American Bar Retirement Association (funding vehicle for retirement plans) (1987–1990 and 1994–1996) | 122 |
| Robert H. Wadsworth (1940)<br>Board Member since 1999 | President, Robert H. Wadsworth & Associates, Inc. (consulting firm) (1983 to present); Director, The Phoenix Boys Choir Association | 125 |

## Officers[4]

| Name, Year of Birth, Position with the Fund and Length of Time Served[5] | Principal Occupation(s) During Past 5 Years and Other Directorships Held |
|---|---|
| Michael G. Clark[6] (1965)<br>President, 2006–present | Managing Director[3], Deutsche Asset Management (2006–present); President of DWS family of funds; Director, ICI Mutual Insurance Company (since October 2007); formerly, Director of Fund Board Relations (2004–2006) and Director of Product Development (2000–2004), Merrill Lynch Investment Managers; Senior Vice President Operations, Merrill Lynch Asset Management (1999–2000) |
| Ingo Gefeke[7] (1967)<br>Executive Vice President since 2010 | Managing Director[3], Deutsche Asset Management; Global Head of Distribution and Product Management, DWS Global Head of Trading and Securities Lending. Member of the Board of Directors of DWS Investment GmbH Frankfurt (since July 2009) and DWS Holding & Service GmbH Frankfurt (since January 2010); formerly, Global Chief Administrative Officer, Deutsche Asset Management (2004–2009); Global Chief Operating Officer, Global Transaction Banking, Deutsche Bank AG, New York (2001–2004); Chief Operating Officer, Global Banking Division Americas, Deutsche Bank AG, New York (1999–2001); Central Management, Global Banking Services, Deutsche Bank AG, Frankfurt (1998–1999); Relationship Management, Deutsche Bank AG, Tokyo, Japan (1997–1998) |
| John Millette[8] (1962)<br>Vice President and Secretary, 1999–present | Director[3], Deutsche Asset Management |
| Paul H. Schubert[6] (1963)<br>Chief Financial Officer, 2004–present<br>Treasurer, 2005–present | Managing Director[3], Deutsche Asset Management (since July 2004); formerly, Executive Director, Head of Mutual Fund Services and Treasurer for UBS Family of Funds (1998–2004); Vice President and Director of Mutual Fund Finance at UBS Global Asset Management (1994–1998) |
| Caroline Pearson[8] (1962)<br>Chief Legal Officer, April 2010–present | Managing Director[3], Deutsche Asset Management; formerly, Assistant Secretary for DWS family of funds (1997–2010) |
| Rita Rubin[9] (1970)<br>Assistant Secretary, 2009–present | Vice President and Counsel, Deutsche Asset Management (since October 2007); formerly, Vice President, Morgan Stanley Investment Management (2004–2007) |
| Paul Antosca[8] (1957)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management (since 2006); Vice President, The Manufacturers Life Insurance Company (U.S.A.) (1990–2006) |
| Jack Clark[8] (1967)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management (since 2007); formerly, Vice President, State Street Corporation (2002–2007) |
| Diane Kenneally[8] (1966)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management |
| John Caruso[9] (1965)<br>Anti-Money Laundering Compliance Officer, 2010–present | Managing Director[3], Deutsche Asset Management |

| Name, Year of Birth, Position with the Fund and Length of Time Served[5] | Principal Occupation(s) During Past 5 Years and Other Directorships Held |
|---|---|
| Robert Kloby[9] (1962)<br>Chief Compliance Officer, 2006–present | Managing Director[3], Deutsche Asset Management |

1 *The length of time served represents the year in which the Board Member joined the board of one or more DWS funds currently overseen by the Board.*

2 *A publicly held company with securities registered pursuant to Section 12 of the Securities Exchange Act of 1934.*

3 *Executive title, not a board directorship.*

4 *As a result of their respective positions held with the Advisor, these individuals are considered "interested persons" of the Advisor within the meaning of the 1940 Act. Interested persons receive no compensation from the fund.*

5 *The length of time served represents the year in which the officer was first elected in such capacity for one or more DWS funds.*

6 *Address: 100 Plaza One, Jersey City, NJ 07311.*

7 *Effective January 11, 2011, Mr. Gefeke, Executive Vice President, resigned as an officer of the fund.*

*The mailing address of Mr. Gefeke is 345 Park Avenue, New York, New York 10154. Mr. Gefeke was an interested Board Member of certain DWS funds by virtue of his positions with Deutsche Asset Management. As an interested person, Mr. Gefeke received no compensation from the fund.*

8 *Address: One Beacon Street, Boston, MA 02108.*

9 *Address: 60 Wall Street, New York, New York 10005.*

*The fund's Statement of Additional Information ("SAI") includes additional information about the Board Members. The SAI is available, without charge, upon request. If you would like to request a copy of the SAI, you may do so by calling the following toll-free number: (800) 728-3337.*

DWS Investments is part of Deutsche Bank's Asset Management division and, within the US, represents the retail asset management activities of Deutsche Bank AG, Deutsche Bank Trust Company Americas, Deutsche Investment Management Americas Inc. and DWS Trust Company.

The views expressed in this report reflect those of the portfolio managers only through the end of the period of the report as stated on the cover. The managers' views are subject to change at any time based on market and other conditions and should not be construed as a recommendation.

This information must be preceded or accompanied by a current prospectus.

Portfolio changes should not be considered recommendations for action by individual investors.

DWS Investments Distributors, Inc.
222 South Riverside Plaza
Chicago, IL 60606
(800) 621-1148

VS1capgro-2 (2/11)

DWS INVESTMENTS
Deutsche Bank Group

DECEMBER 31, 2010

# ANNUAL REPORT

## DWS VARIABLE SERIES I

## DWS Global Opportunities VIP

**This report must be preceded or accompanied by a prospectus. To obtain an additional prospectus or summary prospectus, if available, call (800) 728-3337 or your financial representative. We advise you to consider the Fund's objectives, risks, charges and expenses carefully before investing. The summary prospectus and prospectus contain this and other important information about the Fund. Please read the prospectus carefully before you invest.**

*Investments in variable insurance portfolios (VIPs) involve risk. Stocks may decline in value. Bond investments are subject to interest-rate and credit risks. When interest rates rise, bond prices generally fall. Credit risk refers to the ability of an issuer to make timely payments of principal and interest. Investing in derivatives entails special risks relating to liquidity, leverage and credit that may reduce returns and/or increased volatility. Investing in foreign securities, particularly those of emerging markets, presents certain risks, such as currency fluctuations, political and economic changes, and market risks. There are additional risks associated with investing in commodities, high-yield bonds, aggressive growth stocks, non-diversified/ concentrated funds and small- and mid-cap stocks which are more fully explained in the prospectuses. Please read the prospectus for more information.*

*DWS Investments is part of Deutsche Bank's Asset Management division and, within the US, represents the retail asset management activities of Deutsche Bank AG, Deutsche Bank Trust Company Americas, Deutsche Investment Management Americas Inc. and DWS Trust Company.*

*NOT FDIC/NCUA INSURED    NO BANK GUARANTEE    MAY LOSE VALUE    NOT A DEPOSIT*
*NOT INSURED BY ANY FEDERAL GOVERNMENT AGENCY*

DWS INVESTMENTS
Deutsche Bank Group

# Performance Summary

December 31, 2010

## DWS Global Opportunities VIP

**All performance shown is historical, assumes reinvestment of all dividend and capital gain distributions, and does not guarantee future results. Investment return and principal value fluctuate with changing market conditions so that, when redeemed, shares may be worth more or less than their original cost. Current performance may be lower or higher than the performance data quoted. Please contact your participating insurance company for the Fund's most recent month-end performance. Performance doesn't reflect charges and fees ("contract charges") associated with the separate account that invests in the Fund or any variable life insurance policy or variable annuity contract for which the Fund is an investment option. These charges and fees will reduce returns. While all share classes have the same underlying portfolio, their performance will differ.**

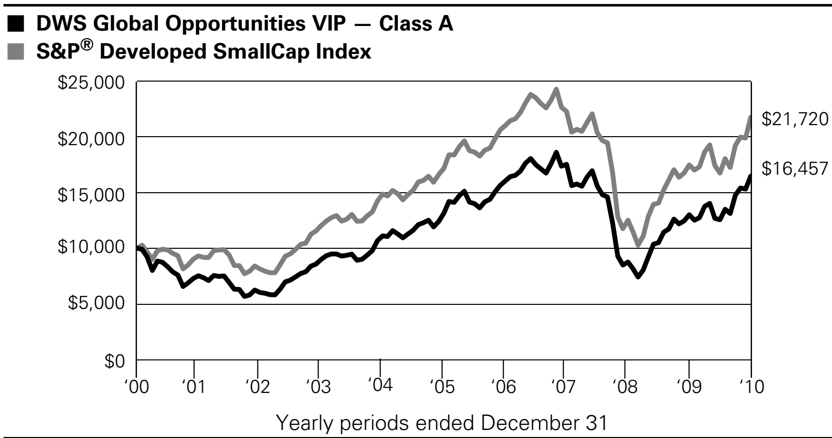
**The gross expense ratios of the Fund, as stated in the fee table of the prospectus dated May 1, 2010 are 1.11% and 1.42% for Class A and Class B shares, respectively, and may differ from the expense ratios disclosed in the Financial Highlights tables in this report.**

Fund returns during all periods shown reflect a fee waiver and/or reimbursement. Without this waiver/reimbursement, returns would have been lower.

### Risk Considerations

Investing in foreign securities, particularly those of emerging markets, presents certain risks, such as currency fluctuations, political and economic changes, and market risks. Stocks of smaller companies involve greater risk than securities of larger, more-established companies. Stocks may decline in value. See the prospectus for details.

### Growth of an Assumed $10,000 Investment




*The S&P® Developed SmallCap Index is an unmanaged index of small-capitalization stocks within 26 countries around the globe.*

*Index returns assume the reinvestment of dividends net of withholding tax and, unlike fund returns, do not reflect any fees or expenses. It is not possible to invest directly into an index.*

### Comparative Results

| DWS Global Opportunities VIP | | 1-Year | 3-Year | 5-Year | 10-Year |
|---|---|---|---|---|---|
| **Class A** | Growth of $10,000 | $12,664 | $9,391 | $12,534 | $16,457 |
| | Average annual total return | 26.64% | –2.07% | 4.62% | 5.11% |
| S&P Developed SmallCap Index | Growth of $10,000 | $12,442 | $9,759 | $12,666 | $21,720 |
| | Average annual total return | 24.42% | –.81% | 4.84% | 8.07% |

| DWS Global Opportunities VIP | | 1-Year | 3-Year | 5-Year | 10-Year |
|---|---|---|---|---|---|
| **Class B** | Growth of $10,000 | $12,638 | $9,301 | $12,346 | $16,015 |
| | Average annual total return | 26.38% | –2.39% | 4.31% | 4.82% |
| S&P Developed SmallCap Index | Growth of $10,000 | $12,442 | $9,759 | $12,666 | $21,720 |
| | Average annual total return | 24.42% | –.81% | 4.84% | 8.07% |

*The growth of $10,000 is cumulative.*

# Information About Your Fund's Expenses

## DWS Global Opportunities VIP

As an investor of the Fund, you incur two types of costs: ongoing expenses and transaction costs. Ongoing expenses include management fees, distribution and service (12b-1) fees and other Fund expenses. Examples of transaction costs include contract charges, redemption fees and account maintenance fees, which are not shown in this section. The following tables are intended to help you understand your ongoing expenses (in dollars) of investing in the Fund and to help you compare these expenses with the ongoing expenses of investing in other mutual funds. In the most recent six-month period, the Fund limited these expenses; had it not done so, expenses would have been higher. The example in the table is based on an investment of $1,000 invested at the beginning of the six-month period and held for the entire period (July 1, 2010 to December 31, 2010).

The tables illustrate your Fund's expenses in two ways:

- **Actual Fund Return.** This helps you estimate the actual dollar amount of ongoing expenses (but not transaction costs) paid on a $1,000 investment in the Fund using the Fund's actual return during the period. To estimate the expenses you paid over the period, simply divide your account value by $1,000 (for example, an $8,600 account value divided by $1,000 = 8.6), then multiply the result by the number in the "Expenses Paid per $1,000" line under the share class you hold.
- **Hypothetical 5% Fund Return.** This helps you to compare your Fund's ongoing expenses (but not transaction costs) with those of other mutual funds using the Fund's actual expense ratio and a hypothetical rate of return of 5% per year before expenses. Examples using a 5% hypothetical Fund return may be found in the shareholder reports of other mutual funds. The hypothetical account values and expenses may not be used to estimate the actual ending account balance or expenses you paid for the period.

Please note that the expenses shown in these tables are meant to highlight your ongoing expenses only and do not reflect any transaction costs. The "Expenses Paid per $1,000" line of the tables is useful in comparing ongoing expenses only and will not help you determine the relative total expense of owning different funds. If these transaction costs had been included, your costs would have been higher.

**Expenses and Value of a $1,000 Investment** for the six months ended December 31, 2010

| Actual Fund Return | Class A | Class B |
|---|---|---|
| Beginning Account Value 7/1/10 | $1,000.00 | $1,000.00 |
| Ending Account Value 12/31/10 | $1,310.10 | $1,308.80 |
| Expenses Paid per $1,000* | $ 6.00 | $ 7.39 |
| **Hypothetical 5% Fund Return** | **Class A** | **Class B** |
| Beginning Account Value 7/1/10 | $1,000.00 | $1,000.00 |
| Ending Account Value 12/31/10 | $1,020.01 | $1,018.80 |
| Expenses Paid per $1,000* | $ 5.24 | $ 6.46 |

* *Expenses are equal to the Fund's annualized expense ratio for each share class, multiplied by the average account value over the period, multiplied by the number of days in the most recent six-month period, then divided by 365.*

| Annualized Expense Ratios | Class A | Class B |
|---|---|---|
| DWS Variable Series I — DWS Global Opportunities VIP | 1.03% | 1.27% |

For more information, please refer to the Fund's prospectus.

These tables do not reflect charges and fees ("contract charges") associated with the separate account that invests in the Fund or any variable life insurance policy or variable annuity contract for which the Fund is an investment option.

## DWS Global Opportunities VIP

DWS Global Opportunities VIP returned 26.64% in 2010 (Class A shares, unadjusted for contract charges), outperforming the 24.42% return of its benchmark, the S&P® Developed SmallCap Index. (Past performance is no guarantee of future results.)

Our stock selection process was most effective in the information technology sector. Notable individual winners were ARM Holdings PLC, which licenses semiconductor designs to the makers of smartphones and other mobile devices, and two Chinese IT outsourcing companies, VanceInfo Technologies, Inc. and HiSoft Technology International.* Our stock picks also outperformed in the consumer staples sector, thanks in part to our investments in Diamond Foods, Inc. and SunOpta, Inc., and in financials, where our top holding was the Swiss private equity firm Partners Group Holding AG. On the negative side, we lost some ground through our underweight in materials and our stock selection in the industrials, energy and materials sectors.[1]

On a sector basis, our bottom-up approach led us to maintain overweight positions in information technology, health care and energy, and underweights in financials, materials and utilities. Our largest sector shift during the year was to increase the Fund's weightings in the technology and consumer sectors, both of which stand to benefit in a continuing environment of global economic recovery. We funded this increase by reducing the extent of our overweight in energy and industrials.

In terms of geographical weightings, our search for "cheap growth" prompted us to keep an underweight in North America in favor of overweights in Europe and Asia. We believe that during the period, the overseas markets were a better source of growth, in the case of non-Japan Asia, and valuation, in the case of Europe and Japan.

Joseph Axtell, CFA
*Portfolio Manager*

*The S&P Developed SmallCap Index is an unmanaged index of small-capitalization stocks within 26 countries around the globe.*

*Index returns assume the reinvestment of dividends net of withholding tax and, unlike fund returns, do not reflect any fees or expenses. It is not possible to invest directly into an index.*

1 *"Overweight" means the Fund holds a higher weighting in a given sector or security than the benchmark. "Underweight" means the Fund holds a lower weighting.*

* *Not held in the portfolio as of December 31, 2010.*

*Portfolio management market commentary is as of December 31, 2010, and may not come to pass. This information is subject to change at any time based on market and other conditions. Past performance does not guarantee future results. Current and future portfolio holdings are subject to risk.*

# Portfolio Summary

## DWS Global Opportunities VIP

| **Asset Allocation** (As a % of Investment Portfolio excluding Securities Lending Collateral) | **12/31/10** | **12/31/09** |
|---|---|---|
| Common Stocks | 99% | 97% |
| Cash Equivalents | 1% | 2% |
| Participatory Notes | — | 1% |
| | 100% | 100% |

| **Geographical Diversification** (As a % of Investment Portfolio excluding Cash Equivalents and Securities Lending Collateral) | **12/31/10** | **12/31/09** |
|---|---|---|
| United States | 40% | 40% |
| Continental Europe | 21% | 27% |
| Pacific Basin | 15% | 13% |
| United Kingdom | 9% | 7% |
| Japan | 8% | 8% |
| Australia | 2% | 1% |
| Canada | 2% | 2% |
| Latin America | 1% | 1% |
| Africa | — | — |
| Other | 2% | 1% |
| | 100% | 100% |

| **Sector Diversification** (As a % of Investment Portfolio excluding Cash Equivalents and Securities Lending Collateral) | **12/31/10** | **12/31/09** |
|---|---|---|
| Industrials | 22% | 18% |
| Consumer Discretionary | 18% | 16% |
| Information Technology | 15% | 16% |
| Health Care | 14% | 16% |
| Financials | 12% | 12% |
| Energy | 8% | 10% |
| Materials | 6% | 6% |
| Consumer Staples | 5% | 5% |
| Utilities | — | 1% |
| | 100% | 100% |

*Asset allocation, geographical diversification and sector diversification are subject to change.*

*For more complete details about the Fund's investment portfolio, see page 6.*

Following the Fund's fiscal first and third quarter-end, a complete portfolio holdings listing is filed with the SEC on Form N-Q. The form will be available on the SEC's Web site at www.sec.gov, and it also may be reviewed and copied at the SEC's Public Reference Room in Washington, D.C. Information on the operation of the SEC's Public Reference Room may be obtained by calling (800) SEC-0330. The Fund's portfolio holdings are also posted on www.dws-investments.com from time to time. Please see the Fund's current prospectus for more information.

# Investment Portfolio

December 31, 2010

## DWS Global Opportunities VIP

| | Shares | Value ($) |
|---|---|---|
| **Common Stocks 99.2%** | | |
| **Australia 2.2%** | | |
| Austal Ltd. | 317,365 | 1,132,857 |
| Lynas Corp., Ltd.* | 1,164,743 | 2,454,077 |
| (Cost $1,390,842) | | **3,586,934** |
| **Bermuda 0.7%** | | |
| Lazard Ltd. "A" (Cost $666,344) | 27,300 | **1,078,077** |
| **Brazil 1.5%** | | |
| Diagnosticos da America SA | 82,396 | 1,116,066 |
| Fleury SA | 81,302 | 1,305,308 |
| (Cost $1,328,722) | | **2,421,374** |
| **Canada 1.8%** | | |
| SunOpta, Inc.* | 234,000 | 1,829,880 |
| Thompson Creek Metals Co., Inc.* | 68,800 | 1,012,736 |
| (Cost $2,766,815) | | **2,842,616** |
| **Channel Islands 1.2%** | | |
| Charter International PLC | 70,502 | 928,271 |
| Randgold Resources Ltd. (ADR) (a) | 11,800 | 971,494 |
| (Cost $1,610,895) | | **1,899,765** |
| **China 2.3%** | | |
| Charm Communications, Inc. (ADR)* | 34,536 | 340,525 |
| Mecox Lane Ltd. (ADR)* | 49,544 | 367,121 |
| Minth Group Ltd. | 1,105,800 | 1,815,306 |
| VanceInfo Technologies, Inc. (ADR)* | 34,175 | 1,180,404 |
| (Cost $1,665,607) | | **3,703,356** |
| **Cyprus 0.5%** | | |
| ProSafe SE (b) (Cost $681,555) | 104,343 | **830,309** |
| **France 1.9%** | | |
| Flamel Technologies SA (ADR)* | 169,600 | 1,160,064 |
| JC Decaux SA* | 45,071 | 1,386,758 |
| Meetic | 19,827 | 430,541 |
| (Cost $3,646,705) | | **2,977,363** |
| **Germany 5.2%** | | |
| Fresenius Medical Care AG & Co. KGaA | 72,504 | 4,189,568 |
| M.A.X. Automation AG | 261,915 | 1,211,297 |
| Rational AG | 7,284 | 1,607,928 |
| United Internet AG (Registered) | 78,543 | 1,276,509 |
| (Cost $2,694,731) | | **8,285,302** |
| **Gibraltar 0.4%** | | |
| PartyGaming PLC* (Cost $887,555) | 214,906 | **688,548** |
| **Greece 0.2%** | | |
| Hellenic Exchanges SA (Cost $712,162) | 49,139 | **321,756** |
| **Hong Kong 6.6%** | | |
| Dah Sing Banking Group Ltd. | 555,740 | 946,634 |
| EVA Precision Industrial Holdings Ltd. (c) | 2,625,521 | 2,563,774 |
| K Wah International Holdings Ltd. | 2,552,501 | 955,612 |
| Kingboard Chemical Holdings Ltd. | 290,640 | 1,740,594 |
| Midland Holdings Ltd. | 1,049,268 | 861,251 |
| REXLot Holdings Ltd. (c) | 14,450,000 | 1,524,419 |
| Shui On Construction & Materials Ltd. | 658,000 | 761,888 |
| Wing Hang Bank Ltd. | 84,572 | 1,169,654 |
| (Cost $5,527,070) | | **10,523,826** |
| **India 0.3%** | | |
| Magma Fincorp Ltd. (Cost $467,151) | 307,555 | **493,505** |
| **Ireland 3.9%** | | |
| C&C Group PLC (d) | 149,879 | 677,959 |
| C&C Group PLC (d) | 185,737 | 839,662 |
| ICON PLC (ADR)* | 44,900 | 983,310 |
| Norkom Group PLC* | 292,633 | 586,568 |
| Paddy Power PLC | 39,555 | 1,622,720 |
| Ryanair Holdings PLC (d) | 2,200 | 11,024 |
| Ryanair Holdings PLC (d) | 312,536 | 1,574,510 |
| (Cost $4,121,744) | | **6,295,753** |
| **Italy 0.5%** | | |
| Prysmian SpA (Cost $837,686) | 46,571 | **793,091** |
| **Japan 8.0%** | | |
| Digital Garage, Inc.* | 647 | 1,604,463 |
| Hajime Construction Co., Ltd. | 24,859 | 853,268 |
| Internet Initiative Japan, Inc. | 398 | 1,129,886 |
| Kenedix, Inc.* | 3,738 | 1,136,685 |
| M3, Inc. | 147 | 738,373 |
| MISUMI Group, Inc. | 60,600 | 1,508,650 |
| Nidec Corp. | 14,811 | 1,493,463 |
| Nippon Seiki Co., Ltd. | 95,000 | 1,138,333 |
| Nitori Holdings Co., Ltd. | 11,600 | 1,014,358 |
| Universal Entertainment Corp.* | 77,200 | 2,254,833 |
| (Cost $8,219,088) | | **12,872,312** |
| **Korea 0.8%** | | |
| S&T Dynamics Co., Ltd.* (Cost $741,138) | 60,890 | **1,225,193** |
| **Luxembourg 0.5%** | | |
| L'Occitane International SA* (Cost $590,029) | 300,750 | **831,891** |
| **Netherlands 4.3%** | | |
| Brunel International NV | 23,026 | 907,397 |
| Chicago Bridge & Iron Co. NV (NY Registered Shares)* | 48,500 | 1,595,650 |
| Koninklijke Vopak NV | 32,153 | 1,518,850 |
| QIAGEN NV* | 62,600 | 1,224,420 |
| SBM Offshore NV | 74,639 | 1,672,143 |
| (Cost $3,760,925) | | **6,918,460** |
| **Philippines 0.4%** | | |
| Cebu Air, Inc.* (Cost $792,490) | 258,830 | **669,968** |
| **Singapore 2.4%** | | |
| Amtek Engineering Ltd.* | 1,907,000 | 1,604,831 |
| UOB-Kay Hian Holdings Ltd. | 587,000 | 809,592 |
| Venture Corp., Ltd. | 198,773 | 1,434,245 |
| (Cost $3,252,407) | | **3,848,668** |
| **South Africa 0.5%** | | |
| Northam Platinum Ltd. (Cost $734,867) | 108,524 | **746,283** |

*The accompanying notes are an integral part of the financial statements.*

| | Shares | Value ($) |
|---|---|---|
| **Spain 0.9%** | | |
| Tecnicas Reunidas SA | 14,090 | 897,087 |
| Telvent GIT SA (NY registered shares)* | 18,992 | 501,769 |
| (Cost $1,342,398) | | **1,398,856** |
| **Switzerland 1.1%** | | |
| Advanced Digital Broadcast Holdings SA (ADB Group) (Registered) | 5,140 | 168,200 |
| Partners Group Holding AG | 8,682 | 1,647,715 |
| (Cost $748,707) | | **1,815,915** |
| **Taiwan 1.0%** | | |
| E Ink Holdings, Inc.* (Cost $1,496,706) | 754,050 | **1,528,453** |
| **Thailand 0.7%** | | |
| Kiatnakin Bank PCL (Cost $769,666) | 913,600 | **1,181,967** |
| **United Arab Emirates 0.7%** | | |
| Lamprell PLC (Cost $670,976) | 220,696 | **1,106,240** |
| **United Kingdom 8.6%** | | |
| Aegis Group PLC | 277,722 | 608,360 |
| ARM Holdings PLC | 289,717 | 1,912,036 |
| Ashmore Group PLC | 317,788 | 1,660,297 |
| Babcock International Group PLC | 180,919 | 1,610,623 |
| Burberry Group PLC | 51,674 | 905,549 |
| Domino's Pizza UK & IRL PLC | 126,845 | 1,090,668 |
| ICAP PLC | 98,470 | 821,356 |
| John Wood Group PLC | 122,820 | 1,070,421 |
| Michael Page International PLC | 190,557 | 1,648,890 |
| Rotork PLC | 46,454 | 1,323,954 |
| Serco Group PLC | 120,037 | 1,039,616 |
| (Cost $8,099,191) | | **13,691,770** |
| **United States 40.1%** | | |
| Accuray, Inc.* | 125,840 | 849,420 |
| Advance Auto Parts, Inc. | 18,150 | 1,200,623 |
| Aecom Technology Corp.* | 48,468 | 1,355,650 |
| Aeropostale, Inc.* | 54,050 | 1,331,792 |
| Affiliated Managers Group, Inc.* | 10,000 | 992,200 |
| Alpha Natural Resources, Inc.* | 25,400 | 1,524,762 |
| Altra Holdings, Inc.* | 27,455 | 545,256 |
| BE Aerospace, Inc.* | 42,000 | 1,555,260 |
| BorgWarner, Inc.* | 23,700 | 1,714,932 |
| Cameron International Corp.* | 19,200 | 974,016 |
| Cardtronics, Inc.* | 72,000 | 1,274,400 |
| Central European Distribution Corp.* (e) | 31,300 | 716,770 |
| Cliffs Natural Resources, Inc. | 17,700 | 1,380,777 |
| Complete Production Services, Inc.* | 40,807 | 1,205,846 |
| Deckers Outdoor Corp.* | 29,992 | 2,391,562 |
| Diamond Foods, Inc. | 35,100 | 1,866,618 |
| Dresser-Rand Group, Inc.* | 27,800 | 1,184,002 |
| EnerNOC, Inc.* | 27,700 | 662,307 |
| ExamWorks Group, Inc.* | 27,150 | 501,732 |
| FleetCor Technologies, Inc.* | 8,745 | 270,395 |
| FSI International, Inc.* | 193,500 | 855,270 |
| FTI Consulting, Inc.* | 38,850 | 1,448,328 |
| Green Mountain Coffee Roasters, Inc.* | 39,564 | 1,300,073 |
| Guess?, Inc. | 30,700 | 1,452,724 |
| Harris Corp. | 23,500 | 1,064,550 |
| hhgregg, Inc.* | 46,900 | 982,555 |
| Huntington Bancshares, Inc. | 117,453 | 806,902 |
| iGATE Corp. | 53,535 | 1,055,175 |
| Itron, Inc.* | 26,900 | 1,491,605 |
| Jarden Corp. | 23,400 | 722,358 |
| Jefferies Group, Inc. | 56,400 | 1,501,932 |
| Joy Global, Inc. | 22,075 | 1,915,006 |
| Lam Research Corp.* | 20,300 | 1,051,134 |
| Life Technologies Corp.* | 30,200 | 1,676,100 |
| Metabolix, Inc.* | 45,800 | 557,386 |
| NIC, Inc. | 94,372 | 916,352 |
| Northern Oil & Gas, Inc.* | 52,400 | 1,425,804 |
| NxStage Medical, Inc.* | 92,419 | 2,299,385 |
| Onyx Pharmaceuticals, Inc.* | 22,453 | 827,842 |
| Prosperity Bancshares, Inc. | 25,700 | 1,009,496 |
| Questcor Pharmaceuticals, Inc.* | 115,704 | 1,704,320 |
| Rovi Corp.* | 23,300 | 1,444,833 |
| Schweitzer-Mauduit International, Inc. | 24,006 | 1,510,458 |
| Stericycle, Inc.* | 17,600 | 1,424,192 |
| STR Holdings, Inc.* | 39,764 | 795,280 |
| SXC Health Solutions Corp.* | 24,000 | 1,028,640 |
| Sycamore Networks, Inc. | 30,900 | 636,231 |
| Thoratec Corp.* | 57,200 | 1,619,904 |
| TiVo, Inc.* | 72,127 | 622,456 |
| Ultra Petroleum Corp.* | 29,400 | 1,404,438 |
| Urban Outfitters, Inc.* | 42,100 | 1,507,601 |
| VIVUS, Inc.* | 80,000 | 749,600 |
| Waddell & Reed Financial, Inc. "A" | 26,800 | 945,772 |
| Zions Bancorp. | 34,576 | 837,778 |
| (Cost $40,370,092) | | **64,089,800** |
| **Total Common Stocks** (Cost $100,594,264) | | **158,667,351** |

## Warrants 0.0%

| | Shares | Value ($) |
|---|---|---|
| **Hong Kong** | | |
| Kingboard Chemical Holdings Ltd. Expiration Date 10/31/2012* (Cost $0) | 39,014 | **41,409** |

## Cash Equivalents 0.9%

| | Shares | Value ($) |
|---|---|---|
| Central Cash Management Fund, 0.19% (f) (Cost $1,403,436) | 1,403,436 | **1,403,436** |

| | % of Net Assets | Value ($) |
|---|---|---|
| **Total Investment Portfolio** (Cost $101,997,700)† | 100.1 | **160,112,196** |
| **Other Assets and Liabilities, Net** | (0.1) | **(94,890)** |
| **Net Assets** | 100.0 | **160,017,306** |

* *Non-income producing security.*

† *The cost for federal income tax purposes was $104,651,714. At December 31, 2010, net unrealized appreciation for all securities based on tax cost was $55,460,482. This consisted of aggregate gross unrealized appreciation for all securities in which there was an excess of value over tax cost of $62,843,932 and aggregate gross unrealized depreciation for all securities in which there was an excess of tax cost over value of $7,383,450.*

(a) *Security is listed in country of domicile. Significant business activities of the company are in Africa.*

*The accompanying notes are an integral part of the financial statements.*

(b) *Security is listed in country of domicile. Significant business activities of the company are in Norway.*

(c) *Security is listed in country of domicile. Significant business activities of the company are in China.*

(d) *Securities with the same description are the same corporate entity but trade on different stock exchanges.*

(e) *Security is listed in country of domicile. Significant business activities of the company are in Poland.*

(f) *Affiliated fund managed by Deutsche Investment Management Americas Inc. The rate shown is the annualized seven-day yield at period end.*

*ADR: American Depositary Receipt*

## Fair Value Measurements

*Various inputs are used in determining the value of the Fund's investments. These inputs are summarized in three broad levels. Level 1 includes quoted prices in active markets for identical securities. Level 2 includes other significant observable inputs (including quoted prices for similar securities, interest rates, prepayment speeds, and credit risk). Level 3 includes significant unobservable inputs (including the Fund's own assumptions in determining the fair value of investments). The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities.*

*The following is a summary of the inputs used as of December 31, 2010 in valuing the Fund's investments. For information on the Fund's policy regarding the valuation of investments, please refer to the Security Valuation section of Note A in the accompanying Notes to Financial Statements.*

| **Assets** | **Level 1** | **Level 2** | **Level 3** | **Total** |
|---|---|---|---|---|
| Common Stocks & Warrants | | | | |
| Australia | $ — | $ 3,586,934 | $ — | $ 3,586,934 |
| Bermuda | 1,078,077 | — | — | 1,078,077 |
| Brazil | 2,421,374 | — | — | 2,421,374 |
| Canada | 2,842,616 | — | — | 2,842,616 |
| Channel Islands | 971,494 | 928,271 | — | 1,899,765 |
| China | 1,888,050 | 1,815,306 | — | 3,703,356 |
| Cyprus | — | 830,309 | — | 830,309 |
| France | 1,160,064 | 1,817,299 | — | 2,977,363 |
| Germany | — | 8,285,302 | — | 8,285,302 |
| Gibraltar | — | 688,548 | — | 688,548 |
| Greece | — | 321,756 | — | 321,756 |
| Hong Kong | — | 10,565,235 | — | 10,565,235 |
| India | — | 493,505 | — | 493,505 |
| Ireland | 983,310 | 5,312,443 | — | 6,295,753 |
| Italy | — | 793,091 | — | 793,091 |
| Japan | — | 12,872,312 | — | 12,872,312 |
| Korea | — | 1,225,193 | — | 1,225,193 |
| Luxembourg | — | 831,891 | — | 831,891 |
| Netherlands | 1,595,650 | 5,322,810 | — | 6,918,460 |
| Philippines | — | 669,968 | — | 669,968 |
| Singapore | — | 3,848,668 | — | 3,848,668 |
| South Africa | — | 746,283 | — | 746,283 |
| Spain | 501,769 | 897,087 | — | 1,398,856 |
| Switzerland | — | 1,815,915 | — | 1,815,915 |
| Taiwan | — | 1,528,453 | — | 1,528,453 |
| Thailand | — | 1,181,967 | — | 1,181,967 |
| United Arab Emirates | — | 1,106,240 | — | 1,106,240 |
| United Kingdom | — | 13,691,770 | — | 13,691,770 |
| United States | 64,089,800 | — | — | 64,089,800 |
| Short-Term Investments (g) | 1,403,436 | — | — | 1,403,436 |
| **Total** | **$ 78,935,640** | **$ 81,176,556** | **$ —** | **$ 160,112,196** |

*There have been no significant transfers in and out of Level 1 and Level 2 fair value measurements during the year ended December 31, 2010.*

(g) *See Investment Portfolio for additional detailed categorizations.*

*The accompanying notes are an integral part of the financial statements.*

## Statement of Assets and Liabilities

as of December 31, 2010

| Assets | | |
|---|---|---|
| Investments: | | |
| Investments in securities, at value (cost $100,594,264) | $ | 158,708,760 |
| Investment in Central Cash Management Fund (cost $1,403,436) | | 1,403,436 |
| Total investments, at value (cost $101,997,700) | | 160,112,196 |
| Foreign currency, at value (cost $124,556) | | 125,904 |
| Receivable for investments sold | | 45,967 |
| Receivable for Fund shares sold | | 3,742 |
| Interest receivable | | 332 |
| Dividends receivable | | 33,773 |
| Foreign taxes recoverable | | 36,680 |
| Due from Advisor | | 46 |
| Other assets | | 811 |
| Total assets | | 160,359,451 |

| Liabilities | | |
|---|---|---|
| Payable for Fund shares redeemed | | 155,006 |
| Accrued management fee | | 102,954 |
| Accrued distribution service fee (Class B) | | 480 |
| Deferred foreign taxes | | 664 |
| Other accrued expenses and payables | | 83,041 |
| Total liabilities | | 342,145 |
| **Net assets, at value** | **$** | **160,017,306** |

| Net Assets Consist of | | |
|---|---|---|
| Undistributed net investment income | | 768,378 |
| Net unrealized appreciation (depreciation) on: | | |
| Investments (net of deferred foreign taxes of $644) | | 58,113,832 |
| Foreign currency | | 6,670 |
| Accumulated net realized gain (loss) | | (10,334,679) |
| Paid-in capital | | 111,463,105 |
| **Net assets, at value** | **$** | **160,017,306** |
| **Class A** | | |
| **Net Asset Value,** offering and redemption price per share ($157,718,776 ÷ 11,043,518 outstanding shares of beneficial interest, $.01 par value, unlimited number of shares authorized) | **$** | **14.28** |
| **Class B** | | |
| **Net Asset Value,** offering and redemption price per share ($2,298,530 ÷ 163,772 outstanding shares of beneficial interest, $.01 par value, unlimited number of shares authorized) | **$** | **14.03** |

## Statement of Operations

for the year ended December 31, 2010

| Investment Income | | |
|---|---|---|
| Income: | | |
| Dividends (net of foreign taxes withheld of $106,757) | $ | 2,011,038 |
| Income distributions — Central Cash Management Fund | | 6,384 |
| Securities lending income, including income from Daily Assets Fund Institutional, net of borrower rebates | | 78,877 |
| Total income | | 2,096,299 |
| Expenses: | | |
| Management fee | | 1,278,032 |
| Administration fee | | 143,599 |
| Services to shareholders | | 5,559 |
| Custodian fee | | 43,249 |
| Distribution service fee (Class B) | | 8,866 |
| Professional fees | | 57,944 |
| Trustees' fees and expenses | | 7,645 |
| Reports to shareholders | | 31,043 |
| Other | | 35,596 |
| Total expenses before expense reductions | | 1,611,533 |
| Expense reductions | | (104,862) |
| Total expenses after expense reductions | | 1,506,671 |
| **Net investment income (loss)** | | **589,628** |

| Realized and Unrealized Gain (Loss) | | |
|---|---|---|
| Net realized gain (loss) from: | | |
| Investments | | 13,483,540 |
| Foreign currency | | (73,263) |
| Payments by affiliates (see Note G) | | 36 |
| | | 13,410,313 |
| Change in net unrealized appreciation (depreciation) on: | | |
| Investments (net of deferred foreign taxes of $644) | | 20,279,521 |
| Foreign currency | | 5,402 |
| | | 20,284,923 |
| **Net gain (loss)** | | **33,695,236** |
| **Net increase (decrease) in net assets resulting from operations** | **$** | **34,284,864** |

*The accompanying notes are an integral part of the financial statements.*

# Statement of Changes in Net Assets

| Increase (Decrease) in Net Assets | Years Ended December 31, 2010 | 2009 |
|---|---|---|
| Operations: | | |
| Net investment income (loss) | $ 589,628 | $ 582,620 |
| Net realized gain (loss) | 13,410,313 | (7,267,367) |
| Change in net unrealized appreciation (depreciation) | 20,284,923 | 55,600,054 |
| Net increase (decrease) in net assets resulting from operations | 34,284,864 | 48,915,307 |
| Distributions to shareholders from: | | |
| Net investment income: | | |
| Class A | (567,314) | (2,053,958) |
| Class B | (5,306) | (80,052) |
| Total distributions | (572,620) | (2,134,010) |
| Fund share transactions: | | |
| **Class A** | | |
| Proceeds from shares sold | 13,029,724 | 8,747,386 |
| Reinvestment of distributions | 567,314 | 2,053,958 |
| Cost of shares redeemed | (27,999,087) | (33,699,813) |
| Net increase (decrease) in net assets from Class A share transactions | (14,402,049) | (22,898,469) |
| **Class B** | | |
| Proceeds from shares sold | 260,167 | 692,203 |
| Reinvestment of distributions | 5,306 | 80,052 |
| Cost of shares redeemed | (5,280,324) | (1,476,946) |
| Net increase (decrease) in net assets from Class B share transactions | (5,014,851) | (704,691) |
| **Increase (decrease) in net assets** | 14,295,344 | 23,178,137 |
| Net assets at beginning of period | 145,721,962 | 122,543,825 |
| Net assets at end of period (including undistributed net investment income of $768,378 and $165,912, respectively) | **$ 160,017,306** | **$ 145,721,962** |

| Other Information | | |
|---|---|---|
| **Class A** | | |
| Shares outstanding at beginning of period | 12,301,988 | 15,069,861 |
| Shares sold | 1,052,936 | 905,526 |
| Shares issued to shareholders in reinvestment of distributions | 46,236 | 264,685 |
| Shares redeemed | (2,357,642) | (3,938,084) |
| Net increase (decrease) in Class A shares | (1,258,470) | (2,767,873) |
| Shares outstanding at end of period | **11,043,518** | **12,301,988** |
| **Class B** | | |
| Shares outstanding at beginning of period | 586,186 | 669,567 |
| Shares sold | 22,014 | 75,308 |
| Shares issued to shareholders in reinvestment of distributions | 439 | 10,492 |
| Shares redeemed | (444,867) | (169,181) |
| Net increase (decrease) in Class B shares | (422,414) | (83,381) |
| Shares outstanding at end of period | **163,772** | **586,186** |

*The accompanying notes are an integral part of the financial statements.*

# Financial Highlights

## Class A

| Years Ended December 31, | 2010 | 2009 | 2008 | 2007 | 2006 |
|---|---|---|---|---|---|
| **Selected Per Share Data** | | | | | |
| **Net asset value, beginning of period** | **$11.32** | **$ 7.79** | **$18.28** | **$18.15** | **$15.00** |
| *Income (loss) from investment operations:* | | | | | |
| Net investment income (loss)[a] | .05 | .04 | .20[d] | .08[d] | .03[c] |
| Net realized and unrealized gain (loss) | 2.96 | 3.64 | (8.18) | 1.61 | 3.28 |
| **Total from investment operations** | 3.01 | 3.68 | (7.98) | 1.69 | 3.31 |
| *Less distributions from:* | | | | | |
| Net investment income | (.05) | (.15) | (.04) | (.23) | (.16) |
| Net realized gains | — | — | (2.47) | (1.33) | — |
| **Total distributions** | (.05) | (.15) | (2.51) | (1.56) | (.16) |
| **Net asset value, end of period** | **$14.28** | **$11.32** | **$ 7.79** | **$18.28** | **$18.15** |
| Total Return (%) | 26.64[b] | 48.20[b] | (49.96)[b] | 9.33[b] | 22.08[c] |
| **Ratios to Average Net Assets and Supplemental Data** | | | | | |
| Net assets, end of period ($ millions) | 158 | 139 | 117 | 310 | 331 |
| Ratio of expenses before expense reductions (%) | 1.12 | 1.11 | 1.11 | 1.14 | 1.12 |
| Ratio of expenses after expense reductions (%) | 1.04 | .99 | .99 | 1.12 | 1.12 |
| Ratio of net investment income (loss) (%) | .42 | .47 | 1.53[d] | .45[d] | .16[c] |
| Portfolio turnover rate (%) | 39 | 53 | 21 | 19 | 28 |

a *Based on average shares outstanding during the period.*

b *Total return would have been lower had certain expenses not been reduced.*

c *Includes non-recurring income from the Advisor recorded as a result of an administrative proceeding regarding disclosure of brokerage allocation practices in connection with sales of DWS Funds. The non-recurring income resulted in an increase in net investment income of $0.002 per share and an increase in the ratio of net investment income of 0.01%. Excluding this non-recurring income, total return would have been 0.01% lower.*

d *Net investment income per share and the ratio of net investment income include non-recurring dividend income amounting to $0.05 and $0.02 per share and 0.37% and 0.09% of average daily net assets for the years ended December 31, 2008 and 2007, respectively.*

## Class B

| Years Ended December 31, | 2010 | 2009 | 2008 | 2007 | 2006 |
|---|---|---|---|---|---|
| **Selected Per Share Data** | | | | | |
| **Net asset value, beginning of period** | **$11.11** | **$ 7.65** | **$18.03** | **$17.93** | **$14.84** |
| *Income (loss) from investment operations:* | | | | | |
| Net investment income (loss)[a] | .03 | .02 | .16[e] | .01[e] | (.00)[b,d] |
| Net realized and unrealized gain (loss) | 2.90 | 3.57 | (8.07) | 1.61 | 3.24 |
| **Total from investment operations** | 2.93 | 3.59 | (7.91) | 1.62 | 3.24 |
| *Less distributions from:* | | | | | |
| Net investment income | (.01) | (.13) | — | (.19) | (.15) |
| Net realized gains | — | — | (2.47) | (1.33) | — |
| **Total distributions** | (.01) | (.13) | (2.47) | (1.52) | (.15) |
| **Net asset value, end of period** | **$14.03** | **$11.11** | **$ 7.65** | **$18.03** | **$17.93** |
| Total Return (%)[c] | 26.38 | 47.66 | (50.16) | 8.92 | 21.88[d] |
| **Ratios to Average Net Assets and Supplemental Data** | | | | | |
| Net assets, end of period ($ millions) | 2 | 7 | 5 | 12 | 37 |
| Ratio of expenses before expense reductions (%) | 1.34 | 1.42 | 1.42 | 1.53 | 1.51 |
| Ratio of expenses after expense reductions (%) | 1.26 | 1.30 | 1.30 | 1.50 | 1.31 |
| Ratio of net investment income (loss) (%) | .20 | .16 | 1.21[e] | .07[e] | (.03)[d] |
| Portfolio turnover rate (%) | 39 | 53 | 21 | 19 | 28 |

a *Based on average shares outstanding during the period.*

b *Amount is less than $.005.*

c *Total return would have been lower had certain expenses not been reduced.*

d *Includes non-recurring income from the Advisor recorded as a result of an administrative proceeding regarding disclosure of brokerage allocation practices in connection with sales of DWS Funds. The non-recurring income resulted in an increase in net investment income of $0.002 per share and an increase in the ratio of net investment income of 0.01%. Excluding this non-recurring income, total return would have been 0.01% lower.*

e *Net investment income per share and the ratio of net investment income include non-recurring dividend income amounting to $0.05 and $0.02 per share and 0.37% and 0.09% of average daily net assets for the years ended December 31, 2008 and 2007, respectively.*

# Notes to Financial Statements

## A. Organization and Significant Accounting Policies

DWS Variable Series I (the "Series") is registered under the Investment Company Act of 1940, as amended (the "1940 Act"), as an open-end, registered management investment company organized as a Massachusetts business trust. The Series consists of six diversified funds: DWS Bond VIP, DWS Growth & Income VIP, DWS Capital Growth VIP, DWS Global Opportunities VIP, DWS International VIP and DWS Health Care VIP (individually or collectively hereinafter referred to as a "Fund" or the "Funds"). These financial statements report on DWS Global Opportunities VIP. The Series is intended to be the underlying investment vehicle for variable annuity contracts and variable life insurance policies to be offered by the separate accounts of certain life insurance companies ("Participating Insurance Companies").

**Multiple Classes of Shares of Beneficial Interest.** The Fund offers two classes of shares (Class A shares and Class B shares). Class B shares are subject to Rule 12b-1 distribution fees under the 1940 Act and record keeping fees equal to an annual rate of 0.25% and up to 0.15%, respectively, of the average daily net assets of the Class B shares of the Fund. Class A shares are not subject to such fees.

Investment income, realized and unrealized gains and losses, and certain fund-level expenses and expense reductions, if any, are borne pro rata on the basis of relative net assets by the holders of all classes of shares, except that each class bears certain expenses unique to that class (including the applicable 12b-1 distribution fees and record keeping fees). Differences in class-level expenses may result in payment of different per share dividends by class. All shares have equal rights with respect to voting subject to class-specific arrangements.

The Series' financial statements are prepared in accordance with accounting principles generally accepted in the United States of America, which require the use of management estimates. Actual results could differ from those estimates. The policies described below are followed consistently by the Series in the preparation of the financial statements for its Funds.

**Security Valuation.** Investments are stated at value determined as of the close of regular trading on the New York Stock Exchange on each day the exchange is open for trading.

Various inputs are used in determining the value of the Fund's investments. These inputs are summarized in three broad levels. Level 1 includes quoted prices in active markets for identical securities. Level 2 includes other significant observable inputs (including quoted prices for similar securities, interest rates, prepayment speeds, and credit risk). Level 3 includes significant unobservable inputs (including the Fund's own assumptions in determining the fair value of investments). The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities.

Equity securities are valued at the most recent sale price or official closing price reported on the exchange (US or foreign) or over-the-counter market on which they trade and are categorized as Level 1 securities. Securities for which no sales are reported are valued at the calculated mean between the most recent bid and asked quotations on the relevant market or, if a mean cannot be determined, at the most recent bid quotation. For certain international equity securities, in order to adjust for events which may occur between the close of the foreign exchanges and the close of the New York Stock Exchange, a fair valuation model may be used. This fair valuation model takes into account comparisons to the valuation of American Depository Receipts (ADRs), exchange-traded funds, futures contracts and certain indices and these securities are categorized as Level 2.

Money market instruments purchased with an original or remaining maturity of sixty days or less, maturing at par, are valued at amortized cost, which approximates value, and are categorized as Level 2. Investments in open-end investment companies are valued at their net asset value each business day and are categorized as Level 1.

Securities and other assets for which market quotations are not readily available or for which the above valuation procedures are deemed not to reflect fair value are valued in a manner that is intended to reflect their fair value as determined in accordance with procedures approved by the Trustees and are generally categorized as Level 3. In accordance with the Fund's valuation procedures, factors used in determining value may include, but are not limited to, the type of the security; the size of the holding; the initial cost of the security; the existence of any contractual restrictions on the security's disposition; the price and extent of public trading in similar securities of the issuer or of comparable companies; quotations or evaluated prices from broker-dealers and/or pricing services; information obtained from the issuer, analysts, and/or the appropriate stock exchange (for exchange-traded securities); an analysis of the company's or issuer's financial statements; an evaluation of the forces that influence the issuer and the market(s) in which the security is purchased and sold and with respect to debt securities; the maturity, coupon, creditworthiness, currency denomination and the movement of the market in which the security is normally traded. The value determined under these procedures may differ from published values for the same securities.

Disclosure about the classification of fair value measurements is included in a table following the Fund's Investment Portfolio.

**Securities Lending.** The Fund lends securities to certain financial institutions. The Fund retains beneficial ownership of the securities it has loaned and continues to receive interest and dividends paid by the issuer of securities and to participate in any changes in their market value. The Fund requires the borrowers of the securities to maintain collateral with the Fund consisting of either cash or liquid, unencumbered assets having a value at least equal to the value of the securities loaned. When the collateral falls below specified amounts, the lending agent will use its best effort to obtain additional collateral on the next business day to meet required amounts under the security lending agreement. The Fund may invest the cash collateral into a joint trading account in an affiliated money market fund pursuant to Exemptive Orders issued by the SEC. The Fund receives compensation for lending its securities either in the form of fees or by earning interest on invested cash collateral net of borrower rebates and fees paid to a lending agent. Either the Fund or the borrower may terminate the loan. There may be risks of delay and costs in recovery of securities or even loss of rights in the collateral should the borrower of the securities fail financially. The Fund is also subject to all investment risks associated with the reinvestment of any cash collateral received, including, but not limited to, interest rate, credit and liquidity risk associated with such investments. The Fund had no securities on loan as of December 31, 2010.

**Foreign Currency Translations.** The books and records of the Fund are maintained in US dollars. Investment securities and other assets and liabilities denominated in a foreign currency are translated into US dollars at the prevailing exchange rates at period end. Purchases and sales of investment securities, income and expenses are translated into US dollars at the prevailing exchange rates on the respective dates of the transactions.

Net realized and unrealized gains and losses on foreign currency transactions represent net gains and losses between trade and settlement dates on securities transactions, the disposition of forward foreign currency exchange contracts and foreign currencies, and the difference between the amount of net investment income accrued and the US dollar amount actually received. That portion of both realized and unrealized gains and losses on investments that results from fluctuations in foreign currency exchange rates is not separately disclosed but is included with net realized and unrealized gain/appreciation and loss/depreciation on investments.

**Taxes.** The Fund is treated as a separate taxpayer as provided for in the Internal Revenue Code, as amended. It is the Fund's policy to comply with the requirements of the Internal Revenue Code, as amended, which are applicable to regulated investment companies, and to distribute all of its taxable income to the separate accounts of the Participating Insurance Companies which hold its shares.

Additionally, based on the Series' understanding of the tax rules and rates related to income, gains and transactions for the foreign jurisdictions in which the Fund invests, the Fund will provide for foreign taxes, and where appropriate, deferred foreign taxes.

At December 31, 2010, the Fund had an approximate net tax basis capital loss carryforward which may be applied against any realized net taxable capital gains of each succeeding year until fully utilized or until the following expiration date, whichever occurs first:

| Fund | Capital Loss Carryforwards ($) | Expiration Date | Capital Loss Carryfowards Utilized ($) |
|---|---|---|---|
| DWS Global Opportunities VIP | 9,364,000 | 12/31/2017 | 12,952,000 |

The Fund has reviewed the tax positions for the open tax years as of December 31, 2010 and has determined that no provision for income tax is required in the Fund's financial statements. The Fund's federal tax returns for the prior three fiscal years remain open subject to examination by the Internal Revenue Service.

**Distribution of Income and Gains.** The Fund will declare and distribute dividends from its net investment income, if any, annually, although additional distributions may be made if necessary. Net realized gains from investment transactions, in excess of available capital loss carryforwards, would be taxable to the Fund if not distributed, and, therefore, will be distributed to shareholders at least annually.

The timing and characterization of certain income and capital gains distributions are determined annually in accordance with federal tax regulations which may differ from accounting principles generally accepted in the United States of America. These differences primarily relate to investments in foreign denominated investments, passive foreign investment companies and certain securities sold at a loss. As a result, net investment income (loss) and net realized gain (loss) on investment transactions for a reporting period may differ significantly from distributions during such period. Accordingly, the Fund may periodically make reclassifications among certain of its capital accounts without impacting the net asset value of the Fund.

At December 31, 2010, the Fund's components of distributable earnings (accumulated losses) on a tax-basis are as follows:

| Fund | Undistributed Ordinary Income ($)* | Capital Loss Carryforwards ($) | Net Unrealized Gain (Loss) on Investments ($) |
|---|---|---|---|
| DWS Global Opportunities VIP | 2,437,828 | (9,364,000) | 55,460,482 |

In addition, the tax character of distributions paid to shareholders by the Fund is summarized as follows:

| | Distributions from Ordinary Income ($)* Years Ended December 31, | |
|---|---|---|
| Fund | 2010 | 2009 |
| DWS Global Opportunities VIP | 572,620 | 2,134,010 |

* *For tax purposes, short-term capital gains distributions are considered ordinary income distributions.*

**Expenses.** Expenses of the Series arising in connection with a specific Fund are allocated to that Fund. Other Series expenses which cannot be directly attributed to a Fund are apportioned among the Funds in the Series.

**Contingencies.** In the normal course of business, the Fund may enter into contracts with service providers that contain general indemnification clauses. The Fund's maximum exposure under these arrangements is unknown as this would involve future claims that may be made against the Fund that have not yet been made. However, based on experience, the Fund expects the risk of loss to be remote.

**Other.** Investment transactions are accounted for on a trade date plus one basis for daily net asset value calculations. However, for financial reporting purposes, investment transactions are reported on trade date. Interest income is recorded on the accrual basis net of foreign withholding taxes. Dividend income is recorded on the ex-dividend date net of foreign withholding taxes. Certain dividends from foreign securities may be recorded subsequent to the ex-dividend date as soon as the Fund is informed of such dividends. Realized gains and losses from investment transactions are recorded on an identified cost basis. All discounts and premiums are accreted/amortized for both tax and financial reporting purposes.

## B. Purchases and Sales of Securities

During the year ended December 31, 2010, purchases and sales of investment securities (excluding short-term investments) were as follows:

| Fund | Purchases ($) | Sales ($) |
|---|---|---|
| DWS Global Opportunities VIP | 55,347,620 | 73,032,042 |

## C. Related Parties

Under the Investment Management Agreement with Deutsche Investment Management Americas Inc. ("DIMA" or the "Advisor"), an indirect, wholly owned subsidiary of Deutsche Bank AG, the Advisor directs the investments of the Fund in accordance with its investment objectives, policies and restrictions. The Advisor determines the securities, instruments and other contracts relating to investments to be purchased, sold or entered into by the Fund.

Under the Investment Management Agreement with the Advisor, the Fund pays a monthly management fee, based on the average daily net assets of the Fund, computed and accrued daily and payable monthly, at the annual rates shown below:

| Fund | Annual Management Fee Rate |
|---|---|
| DWS Global Opportunities VIP | |
| first $500 million of average daily net assets | .890% |
| next $500 million of average daily net assets | .875% |
| next $1 billion of average daily net assets | .860% |
| over $2 billion of average daily net assets | .845% |

For the period from January 1, 2010 through September 30, 2010, the Advisor, the underwriter and accounting agent contractually agreed to waive a portion of their fee to the extent necessary to maintain the operating expenses of each class (excluding certain expenses such as extraordinary expenses, taxes, brokerage and interest) as follows:

| Fund | Annual Rate |
|---|---|
| DWS Global Opportunities VIP Class A | 1.06% |
| DWS Global Opportunities VIP Class B | 1.46% |

In addition, for the period from October 1, 2010 through September 30, 2011, the Advisor, the underwriter and accounting agent contractually agreed to waive a portion of their fee to the extent necessary to maintain the operating expenses of each class (excluding certain expenses such as extraordinary expenses, taxes, brokerage and interest) as follows:

| Fund | Annual Rate |
|---|---|
| DWS Global Opportunities VIP Class A | 1.00% |
| DWS Global Opportunities VIP Class B | 1.40% |

Accordingly, for the year ended December 31, 2010, the total management fee, management fee waived and effective management fee rate are as follows:

| Fund | Total Aggregated ($) | Waived ($) | Annual Effective Rate |
|---|---|---|---|
| DWS Global Opportunities VIP | 1,278,032 | 104,345 | .82% |

**Administration Fee.** Pursuant to an Administrative Services Agreement, DIMA provides most administrative services to the Series. For all services provided under the Administrative Services Agreement, the Fund pays the Advisor an annual fee ("Administration Fee") of 0.10% of the Fund's average daily net assets, computed and accrued daily and payable monthly. For the year ended December 31, 2010, the Administration Fee was as follows:

| Fund | Total Aggregated ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS Global Opportunities VIP | 143,599 | 13,299 |

**Service Provider Fees.** DWS Investments Service Company ("DISC"), an affiliate of the Advisor, is the transfer agent, dividend-paying agent and shareholder service agent for the Series. Pursuant to a sub-transfer agency agreement between DISC and DST Systems, Inc. ("DST"), DISC has delegated certain transfer agent, dividend-paying agent and shareholder service agent functions to DST. DISC compensates DST out of the shareholder servicing fee it receives from the Fund. For the year ended December 31, 2010, the amounts charged to the Fund by DISC were as follows:

| Fund | Total Aggregated ($) | Waived ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|---|
| DWS Global Opportunities VIP Class A | 517 | 517 | — |
| DWS Global Opportunities VIP Class B | 130 | — | 30 |

DWS Investments Distributors, Inc. ("DIDI"), also an affiliate of the Advisor, is the Series' Distributor. In accordance with the Master Distribution Plan, DIDI receives 12b-1 fees of 0.25% of average daily net assets of Class B shares. Pursuant to the Master Distribution Plan, DIDI remits these fees to the Participating Insurance Companies for various costs incurred or paid by these companies in connection with marketing and distribution of Class B shares. These fees are detailed in the Fund's Statement of Operations.

**Typesetting and Filing Service Fees.** Under an agreement with DIMA, DIMA is compensated for providing typesetting and certain regulatory filing services to the Fund. For the year ended December 31, 2010, the amount charged to the Fund by DIMA included in the Statement of Operations under "reports to shareholders" was as follows:

| Fund | Total Aggregated ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS Global Opportunities VIP | 12,386 | 2,153 |

**Trustees' Fees and Expenses.** The Fund paid each Trustee not affiliated with the Advisor retainer fees plus specified amounts for various committee services and for the Board Chairperson.

**Affiliated Cash Management Vehicles.** The Fund may invest uninvested cash balances in Central Cash Management Fund, which is managed by the Advisor. The Fund indirectly bears its proportionate share of the expenses of the underlying money market funds. Central Cash Management Fund does not pay the Advisor an investment management fee. Central Cash Management Fund seeks a high level of current income consistent with liquidity and the preservation of capital.

### D. Investing in Emerging Markets

Investing in emerging markets may involve special risks and considerations not typically associated with investing in developed markets. These risks include revaluation of currencies, high rates of inflation or deflation, repatriation restrictions on income and capital, and future adverse political, social and economic developments. Moreover, securities issued in these markets may be less liquid, subject to government ownership controls or delayed settlements and may have prices more volatile or less easily assessed than those of comparable securities of issuers in developed markets.

### E. Ownership of the Fund

Three participating insurance companies were owners of record of 10% or more of the total outstanding Class A shares of the Fund, each owning 47%,19% and 11%. One participating insurance company was an owner of record of 10% or more of the total outstanding Class B shares of the Fund, owning 92%.

### F. Line of Credit

The Series and other affiliated funds (the "Participants") share in a $450 million revolving credit facility provided by a syndication of banks. The Fund may borrow for temporary or emergency purposes, including the meeting of redemption requests that otherwise might require the untimely disposition of securities. The Participants are charged an annual commitment fee which is allocated based on net assets, among each of the Participants. Interest is calculated at a rate per annum equal to the sum of the Federal Funds Rate plus 1.25 percent plus if LIBOR exceeds the Federal Funds Rate the amount of such excess. The Fund may borrow up to a maximum of 33 percent of its net assets under the agreement.

### G. Payments Made by Affiliates

During the year ended December 31, 2010, the Advisor fully reimbursed the Fund $36 for losses incurred on trades executed incorrectly. The amount reimbursed was less than 0.01% of the Fund's average net assets.

### H. Subsequent Event

On January 12, 2011, the Board of Trustees approved changes to the name and investment strategy of the Fund. Effective on or about May 1, 2011, the name of the Fund will change from "DWS Global Opportunities VIP" to "DWS Global Small Cap Growth VIP." For a description of the new investment strategy, please see the supplement dated February 1, 2011 to the Fund's current prospectus posted on www.dws-investments.com.

# Report of Independent Registered Public Accounting Firm

**To the Trustees of DWS Variable Series I and the Shareholders of DWS Global Opportunities VIP:**

In our opinion, the accompanying statement of assets and liabilities, including the investment portfolio, and the related statements of operations and of changes in net assets and the financial highlights present fairly, in all material respects, the financial position of DWS Global Opportunities VIP (the "Fund") at December 31, 2010 and the results of its operations, the changes in its net assets, and the financial highlights for the periods indicated therein, in conformity with accounting principles generally accepted in the United States of America. These financial statements and financial highlights (hereafter referred to as "financial statements") are the responsibility of the Fund's management. Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these financial statements in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits, which included confirmation of securities at December 31, 2010 by correspondence with the custodians and brokers, provide a reasonable basis for our opinion.

Boston, Massachusetts
February 11, 2011

PricewaterhouseCoopers LLP

## Tax Information

**(Unaudited)**

For corporate shareholders of the Fund, 34% of the ordinary dividends (i.e., income dividends plus short-term capital gains) paid during the Fund's fiscal year ended December 31, 2010 qualified for the dividends received deduction.

The Fund paid foreign taxes of $91,853 and earned $1,063,242 of foreign source income during the year ended December 31, 2010. Pursuant to Section 853 of the Internal Revenue Code, the Fund designates $0.01 per share as foreign taxes paid and $0.10 per share as income earned from foreign sources for the year ended December 31, 2010.

Please consult a tax advisor if you have questions about federal or state income tax laws, or on how to prepare your tax returns. If you have specific questions about your account, please contact your insurance provider.

## Proxy Voting

The Series' policies and procedures for voting proxies for portfolio securities and information about how the Series voted proxies related to its portfolio securities during the 12-month period ended June 30 are available on our Web site — www.dws-investments.com (click on "proxy voting" at the bottom of the page) — or on the SEC's Web site — www.sec.gov. To obtain a written copy of the Series' policies and procedures without charge, upon request, call us toll free at (800) 728-3337.

# Investment Management Agreement Approval

The Board of Trustees, including the Independent Trustees, approved the renewal of your Fund's investment management agreement (the "Agreement") with Deutsche Investment Management Americas Inc. ("DWS") in September 2010.

In terms of the process that the Board followed prior to approving the Agreement, shareholders should know that:

- In September 2010, all of the Fund's Trustees were independent of DWS and its affiliates.
- The Trustees meet frequently to discuss fund matters. Each year, the Trustees dedicate substantial time to contract review matters. Over the course of several months, the Board's Contract Committee, in coordination with the Board's Equity Oversight Committee, reviewed comprehensive materials received from DWS, independent third parties and independent counsel. These materials included an analysis of the Fund's performance, fees and expenses, and profitability compiled by the Fund's independent fee consultant. The Board also received extensive information throughout the year regarding performance of the Fund.
- The Independent Trustees regularly meet privately with their independent counsel to discuss contract review and other matters. In addition, the Independent Trustees were also advised by the Fund's independent fee consultant in the course of their review of the Fund's contractual arrangements and considered a comprehensive report prepared by the independent fee consultant in connection with their deliberations (the "IFC Report").
- In connection with reviewing the Agreement, the Board also reviewed the terms of the Fund's Rule 12b-1 plan, distribution agreement, administrative services agreement, transfer agency agreement and other material service agreements.
- Based on its evaluation of the information provided, the Contract Committee presented its findings and recommendations to the Independent Trustees as a group. The Independent Trustees reviewed the Contract Committee's findings and recommendations and presented their recommendations to the full Board.

In connection with the contract review process, the Contract Committee and the Board considered the factors discussed below, among others. The Board also considered that DWS and its predecessors have managed the Fund since its inception, and the Board believes that a long-term relationship with a capable, conscientious advisor is in the best interests of the Fund. The Board considered, generally, that shareholders chose to invest or remain invested in the Fund knowing that DWS managed the Fund, and that the Agreement was approved by the Fund's shareholders. DWS is part of Deutsche Bank, a major global banking institution that is engaged in a wide range of financial services. The Board believes that there are significant advantages to being part of a global asset management business that offers a wide range of investing expertise and resources, including hundreds of portfolio managers and analysts with research capabilities in many countries throughout the world.

While shareholders may focus primarily on fund performance and fees, the Fund's Board considers these and many other factors, including the quality and integrity of DWS's personnel and such other issues as back-office operations, fund valuations, and compliance policies and procedures.

**Nature, Quality and Extent of Services.** The Board considered the terms of the Agreement, including the scope of advisory services provided under the Agreement. The Board noted that, under the Agreement, DWS provides portfolio management services to the Fund and that, pursuant to a separate administrative services agreement, DWS provides administrative services to the Fund. The Board considered the experience and skills of senior management and investment personnel, the resources made available to such personnel, the ability of DWS to attract and retain high-quality personnel, and the organizational depth and stability of DWS. The Board reviewed the Fund's performance over short-term and long-term periods and compared those returns to various agreed-upon performance measures, including market indices and a peer universe compiled by the independent fee consultant using information supplied by Lipper Inc. ("Lipper"). The Board also noted that it has put into place a process of identifying "Focus Funds" (e.g., funds performing poorly relative to their benchmark or a peer universe compiled by Lipper), and receives more frequent reporting and information from DWS regarding such funds, along with DWS's remedial plans to address underperformance. The Board believes this process is an effective manner of identifying and addressing underperforming funds. Based on the information provided, the Board noted that for the one-, three- and five-year periods ended December 31, 2009, the Fund's performance (Class A shares) was in the 1st quartile, 4th quartile and 3rd quartile, respectively, of the applicable Lipper universe (the 1st quartile being the best performers and the 4th quartile being the worst performers). The Board also observed that the Fund has outperformed its benchmark in the one-year period and has underperformed its benchmark in the three- and five-year periods ended December 31, 2009. The Board observed that there were significant limitations to the usefulness of the comparative data provided by Lipper, noting that the applicable Lipper universe for the Fund included funds that pursue substantially different investment programs as compared to that pursued by the Fund. As a result, the Board gave increased weight to the Fund's performance relative to its benchmark than some of the additional comparative data.

On the basis of this evaluation and the ongoing review of investment results by the Board, the Board concluded that the nature, quality and extent of services provided by DWS historically have been and continue to be satisfactory.

**Fees and Expenses.** The Board considered the Fund's investment management fee schedule, operating expenses and total expense ratios, and comparative information provided by Lipper and the independent fee consultant regarding investment management fee rates paid to other investment advisors by similar funds. With respect to management fees paid to other investment advisors by similar funds, the Board noted that the contractual fee rates paid by the Fund, which include a 0.10% fee paid to DWS under the Fund's administrative services agreement, were higher than the median of the applicable Lipper peer group (based on Lipper data provided as of December 31, 2009). The Board noted that the Fund's Class A shares total (net) operating expenses were expected to be higher than the median of the applicable Lipper expense universe (based on Lipper data provided as of December 31, 2009 ("Lipper Universe Expenses"). The Board also reviewed data comparing each share class's total (net) operating expenses to the applicable Lipper Universe Expenses. The Trustees also observed that the Lipper expense universe for the Fund included funds that pursue substantially different investment programs as compared to that pursued by the Fund. The Board considered the Fund's management fee rate as compared to fees charged by DWS and certain of its affiliates for comparable mutual funds and considered differences in fund and fee structures between the DWS Funds. The Board also considered how the Fund's total (net) operating expenses compared to the total (net) operating expenses of a more customized peer group selected by Lipper (based on such factors as asset size).

The Board also noted that the expense limitations agreed to by DWS helped to ensure that the Fund's total (net) operating expenses would remain competitive.

The information considered by the Board as part of its review of management fees included information regarding fees charged by DWS and its affiliates to similar institutional accounts and to similar funds offered primarily to European investors ("DWS Europe funds"), in each case as applicable. The Board observed that advisory fee rates for institutional accounts generally were lower than the management fees charged by similarly managed DWS US mutual funds ("DWS Funds"), but also took note of the differences in services provided to DWS Funds as compared to institutional accounts. In the case of DWS Europe funds, the Board observed that fee rates for DWS Europe funds generally were higher than for similarly managed DWS Funds, but noted that differences in the types of services provided to DWS Funds relative to DWS Europe funds made it difficult to compare such fees.

On the basis of the information provided, the Board concluded that management fees were reasonable and appropriate in light of the nature, quality and extent of services provided by DWS.

**Profitability.** The Board reviewed detailed information regarding revenues received by DWS under the Agreement. The Board considered the estimated costs and pre-tax profits realized by DWS from advising the DWS Funds, as well as estimates of the pre-tax profits attributable to managing the Fund in particular. The Board also received information regarding the estimated enterprise-wide profitability of DWS and its affiliates with respect to all fund services in totality and by fund. The Board reviewed DWS's methodology in allocating its costs to the management of the Fund. Based on the information provided, the Board concluded that the pre-tax profits realized by DWS in connection with the management of the Fund were not unreasonable. The Board also reviewed information regarding the profitability of certain similar investment management firms. The Board noted that while information regarding the profitability of such firms is limited (and in some cases is not necessarily prepared on a comparable basis), DWS and its affiliates' overall profitability with respect to the DWS fund complex (after taking into account distribution and other services provided to the funds by DWS and its affiliates) was lower than the overall profitability levels of many comparable firms for which such data was available.

**Economies of Scale.** The Board considered whether there are economies of scale with respect to the management of the Fund and whether the Fund benefits from any economies of scale. The Board noted that the Fund's management fee schedule includes fee breakpoints. The Board concluded that the Fund's fee schedule represents an appropriate sharing between the Fund and DWS of such economies of scale as may exist in the management of the Fund at current asset levels.

**Other Benefits to DWS and Its Affiliates.** The Board also considered the character and amount of other incidental benefits received by DWS and its affiliates, including any fees received by DWS for administrative services provided to the Fund and any fees received by an affiliate of DWS for distribution services. The Board also considered benefits to DWS related to brokerage and soft-dollar allocations, including allocating brokerage to pay for research generated by parties other than the executing broker dealers, which pertain primarily to funds investing in equity securities, along with the incidental public relations benefits to DWS related to DWS Funds

advertising and cross-selling opportunities among DWS products and services. The Board concluded that management fees were reasonable in light of these fallout benefits.

**Compliance.** The Board considered the significant attention and resources dedicated by DWS to documenting and enhancing its compliance processes in recent years. The Board noted in particular (i) the experience and seniority of both DWS's chief compliance officer and the Fund's chief compliance officer; (ii) the large number of DWS compliance personnel; and (iii) the substantial commitment of resources by DWS and its affiliates to compliance matters.

Based on all of the information considered and the conclusions reached, the Board unanimously determined that the continuation of the Agreement is in the best interests of the Fund. In making this determination, the Board did not give particular weight to any single factor identified above. The Board considered these factors over the course of numerous meetings, certain of which were in executive session with only the Independent Trustees and their counsel present. It is possible that individual Trustees may have weighed these factors differently in reaching their individual decisions to approve the continuation of the Agreement.

# Summary of Management Fee Evaluation by Independent Fee Consultant

October 3, 2010

Pursuant to an Order entered into by Deutsche Investment Management Americas and affiliates (collectively, "DeAM") with the Attorney General of New York, I, Thomas H. Mack, have been appointed the Independent Fee Consultant for the DWS Funds (formerly the DWS Scudder Funds). My duties include preparing an annual written evaluation of the management fees DeAM charges the Funds, considering among other factors the management fees charged by other mutual fund companies for like services, management fees DeAM charges other clients for like services, DeAM's costs of supplying services under the management agreements and related profit margins, possible economies of scale if a Fund grows larger, and the nature and quality of DeAM's services, including fund performance. This report summarizes my evaluation for 2010, including my qualifications, the evaluation process for each of the DWS Funds, consideration of certain complex-level factors, and my conclusions. I served in substantially the same capacity in 2007, 2008, and 2009.

## Qualifications

For more than 35 years I have served in various professional capacities within the investment management business. I have held investment analysis and advisory positions, including securities analyst, portfolio strategist and director of investment policy with a large investment firm. I have also performed business management functions, including business development, financial management and marketing research and analysis.

Since 1991, I have been an independent consultant within the asset management industry. I have provided services to over 125 client organizations, including investment managers, mutual fund boards, product distributors and related organizations. Over the past ten years I have completed a number of assignments for mutual fund boards, specifically including assisting boards with management contract renewal.

I hold a Master of Business Administration degree, with highest honors, from Harvard University and Master of Science and Bachelor of Science (highest honors) degrees from the University of California at Berkeley. I am an independent director and audit committee financial expert for two closed-end mutual funds and have served in various leadership and financial oversight capacities with non-profit organizations.

## Evaluation of Fees for each DWS Fund

My work focused primarily on evaluating, fund-by-fund, the fees charged to each of the 118 publicly offered Fund portfolios in the DWS Fund family. For each Fund, I considered each of the key factors mentioned above, as well as any other relevant information. In doing so I worked closely with the Funds' Independent Directors in their annual contract renewal process, as well as in their approval of contracts for several new funds (documented separately).

In evaluating each Fund's fees, I reviewed comprehensive materials provided by or on behalf of DeAM, including expense information prepared by Lipper Analytical, comparative performance information, profitability data, manager histories, and other materials. I also accessed certain additional information from the Lipper and Morningstar databases and drew on my industry knowledge and experience.

To facilitate evaluating this considerable body of information, I prepared for each Fund a document summarizing the key data elements in each area as well as additional analytics discussed below. This made it possible to consider each key data element in the context of the others.

In the course of contract renewal, DeAM agreed to implement a number of fee and expense adjustments requested by the Independent Directors which will favorably impact future fees and expenses, and my evaluation includes the effects of these changes.

### Fees and Expenses Compared with Other Funds

The competitive fee and expense evaluation for each fund focused on two primary comparisons:

- The Fund's contractual management fee (the advisory fee plus the administration fee where applicable) compared with those of a group of typically 12–15 funds in the same Lipper investment category (e.g. Large Capitalization Growth) having similar distribution arrangements and being of similar size.
- The Fund's total expenses compared with a broader universe of funds from the same Lipper investment category and having similar distribution arrangements.

These two comparisons provide a view of not only the level of the fee compared with funds of similar scale but also the total expense the Fund bears for all the services it receives, in comparison with the investment choices available in the Fund's investment category and distribution channel. The principal figure-of-merit used in these comparisons was the subject Fund's percentile ranking against peers.

### DeAM's Fees for Similar Services to Others

DeAM provided management fee schedules for all of its US domiciled fund and non-fund investment management accounts in any of the investment categories where there is a DWS Fund. These similar products included the other DWS Funds, non-fund pooled accounts, institutional accounts and sub-advisory accounts. Using this information, I calculated for each Fund the fee that would be charged to each similar product, at the subject Fund's asset level.

Evaluating information regarding non-fund products is difficult because there are varying levels of services required for different types of accounts, with mutual funds generally requiring considerably more regulatory and administrative types of service as well as having more frequent cash flows than other types of accounts. Also, while mutual fund fees for similar fund products can be expected to be similar, there will be some differences due to different pricing conditions in different distribution channels (e.g. retail funds versus those used in variable insurance products), differences in underlying investment processes and other factors.

**Costs and Profit Margins**

DeAM provided a detailed profitability analysis for each Fund. After making some adjustments so that the presentation would be more comparable to the available industry figures, I reviewed profit margins from investment management alone, from investment management plus other fund services (excluding distribution) provided to the Funds by DeAM (principally shareholder services), and DeAM profits from all sources, including distribution. A later section comments on overall profitability.

**Economies of Scale**

Economies of scale — an expected decline in management cost per dollar of fund assets as fund assets grow — are very rarely quantified and documented because of inherent difficulties in collecting and analyzing relevant data. However, in virtually every investment category that I reviewed, larger funds tend to have lower fees and lower total expenses than smaller funds. To see how each DWS Fund compares with this industry observation, I reviewed:

- The trend in Fund assets over the last five years and the accompanying trend in total expenses. This shows if the Fund has grown and, if so, whether total expense (management fees as well as other expenses) have declined as a percent of assets.
- Whether the Fund has break-points in its management fee schedule, the extent of the fee reduction built into the schedule and the asset levels where the breaks take effect, and in the case of a sub-advised Fund how the Fund's break-points compare with those of the sub-advisory fee schedule.
- How the Fund's contractual fee schedule compares with trends in the industry data. To accomplish this, I constructed a chart showing how actual latest-fiscal-year contractual fees of the Fund and of other similar funds relate to average fund assets, with the subject Fund's contractual fee schedule superimposed.

**Quality of Service — Performance**

The quality-of-service evaluation focused on investment performance, which is the principal result of the investment management service. Each Fund's performance was reviewed over the past 1, 3, 5 and 10 years, as applicable, and compared with that of other funds in the same investment category and with a suitable market index.

In addition, I calculated and reviewed risk-adjusted returns relative to an index of similar mutual funds' returns and a suitable market index. The risk-adjusted returns analysis provides a way of determining the extent to which the Fund's return comparisons are mainly the product of investment value-added (or lack thereof) or alternatively taking considerably more or less risk than is typical in its investment category.

I also received and considered the history of portfolio manager changes for each Fund, as this provided an important context for evaluating the performance results.

## Complex-Level Considerations

While this evaluation was conducted mainly at the individual fund level, there are some issues relating to the reasonableness of fees that can alternatively be considered across the whole fund complex:

- I reviewed DeAM's profitability analysis for all DWS Funds, with a view toward determining if the allocation procedures used were reasonable and how profit levels compared with public data for other investment managers.
- I considered whether DeAM and affiliates receive any significant ancillary or "fall-out" benefits that should be considered in interpreting the direct profitability results. These would be situations where serving as the investment manager of the Funds is beneficial to another part of the Deutsche Bank organization.
- I considered how aggregated DWS Fund expenses had varied over the years, by asset class and in the context of trends in asset levels.
- I reviewed the structure of the DeAM organization, trends in staffing levels, and information on compensation of investment management and other professionals compared with industry data.

## Findings

Based on the process and analysis discussed above, which included reviewing a wide range of information from management and external data sources and considering among other factors the fees DeAM charges other clients, the fees charged by other fund managers, DeAM's costs and profits associated with managing the Funds, economies of scale, possible fall-out benefits, and the nature and quality of services provided, in my opinion the management fees charged the DWS Funds are reasonable.

Thomas H. Mack

Thomas H. Mack

# Board Members and Officers

The following table presents certain information regarding the Board Members and Officers of the Trust as of December 31, 2010. Each Board Member's year of birth is set forth in parentheses after his or her name. Unless otherwise noted, (i) each Board Member has engaged in the principal occupation(s) noted in the table for at least the most recent five years, although not necessarily in the same capacity; and (ii) the address of each Independent Board Member is c/o Paul K. Freeman, Independent Chairman, DWS Funds, PO Box 101833, Denver, CO 80250-1833. Except as otherwise noted below, the term of office for each Board Member is until the election and qualification of a successor, or until such Board Member sooner dies, resigns, is removed or as otherwise provided in the governing documents of the fund. Because the fund does not hold an annual meeting of shareholders, each Board Member will hold office for an indeterminate period. The Board Members may also serve in similar capacities with other funds in the fund complex. The Length of Time Served represents the year in which the Board Member joined the board of one or more DWS funds now overseen by the Board.

### Independent Board Members

| Name, Year of Birth, Position with the Fund and Length of Time Served[1] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Paul K. Freeman (1950)<br>Chairperson since 2009<br>Board Member since 1993 | Consultant, World Bank/Inter-American Development Bank; Executive and Governing Council of the Independent Directors Council (education committees); formerly, Project Leader, International Institute for Applied Systems Analysis (1998–2001); Chief Executive Officer, The Eric Group, Inc. (environmental insurance) (1986–1998) | 122 |
| John W. Ballantine (1946)<br>Board Member since 1999 | Retired; formerly, Executive Vice President and Chief Risk Management Officer, First Chicago NBD Corporation/The First National Bank of Chicago (1996–1998); Executive Vice President and Head of International Banking (1995–1996). Directorships: Healthways, Inc. (provider of disease and care management services); Portland General Electric (utility company); Stockwell Capital Investments PLC (private equity). Former Directorships: First Oak Brook Bancshares, Inc. and Oak Brook Bank; Prisma Energy International | 122 |
| Henry P. Becton, Jr. (1943)<br>Board Member since 1990 | Vice Chair and former President, WGBH Educational Foundation. Directorships: Association of Public Television Stations; Lead Director, Becton Dickinson and Company[3] (medical technology company); Lead Director, Belo Corporation[3] (media company); Public Radio International; Public Radio Exchange (PRX); The PBS Foundation. Former Directorships: Boston Museum of Science; American Public Television; Concord Academy; New England Aquarium; Mass. Corporation for Educational Telecommunications; Committee for Economic Development; Public Broadcasting Service | 122 |
| Dawn-Marie Driscoll (1946)<br>Board Member since 1987 | President, Driscoll Associates (consulting firm); Executive Fellow, Center for Business Ethics, Bentley University; formerly, Partner, Palmer & Dodge (1988–1990); Vice President of Corporate Affairs and General Counsel, Filene's (1978–1988). Directorships: Trustee of 22 open-end mutual funds managed by Sun Capital Advisers, Inc. (since 2007); Director of ICI Mutual Insurance Company (since 2007); Advisory Board, Center for Business Ethics, Bentley University; Trustee, Southwest Florida Community Foundation (charitable organization). Former Directorships: Investment Company Institute (audit, executive, nominating committees) and Independent Directors Council (governance, executive committees) | 122 |
| Keith R. Fox (1954)<br>Board Member since 1996 | Managing General Partner, Exeter Capital Partners (a series of private investment funds). Directorships: Progressive International Corporation (kitchen goods importer and distributor); BoxTop Media Inc. (advertising); The Kennel Shop (retailer); former Chairman, National Association of Small Business Investment Companies | 122 |
| Kenneth C. Froewiss (1945)<br>Board Member since 2001 | Adjunct Professor of Finance, NYU Stern School of Business (September 2009–present; Clinical Professor from 1997–September 2009); Member, Finance Committee, Association for Asian Studies (2002–present); Director, Mitsui Sumitomo Insurance Group (US) (2004–present); prior thereto, Managing Director, J.P. Morgan (investment banking firm) (until 1996) | 122 |
| Richard J. Herring (1946)<br>Board Member since 1990 | Jacob Safra Professor of International Banking and Professor, Finance Department, The Wharton School, University of Pennsylvania (since July 1972); Co-Director, Wharton Financial Institutions Center (since July 2000); Co-Chair, U.S. Shadow Financial Regulatory Committee; Executive Director, Financial Economists Roundtable; Director, Japan Equity Fund, Inc. (since September 2007), Thai Capital Fund, Inc. (since September 2007), Singapore Fund, Inc. (since September 2007); Independent Director of Barclays Bank Delaware (since September 2010). Formerly, Vice Dean and Director, Wharton Undergraduate Division (July 1995–June 2000); Director, Lauder Institute of International Management Studies (July 2000–June 2006) | 122 |
| William McClayton (1944)<br>Board Member since 2004+ | Private equity investor (since October 2009); previously, Managing Director, Diamond Management & Technology Consultants, Inc. (global consulting firm) (2001–2009); Directorship: Board of Managers, YMCA of Metropolitan Chicago; formerly: Senior Partner, Arthur Andersen LLP (accounting) (1966–2001); Trustee, Ravinia Festival | 122 |

| Name, Year of Birth, Position with the Fund and Length of Time Served[1] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Rebecca W. Rimel (1951)<br>Board Member since 1995 | President and Chief Executive Officer, The Pew Charitable Trusts (charitable organization) (1994 to present); Trustee, Thomas Jefferson Foundation (charitable organization) (1994 to present); Trustee, Executive Committee, Philadelphia Chamber of Commerce (2001–2007); Director, CardioNet, Inc.[2] (2009–present) (health care). Formerly, Executive Vice President, The Glenmede Trust Company (investment trust and wealth management) (1983–2004); Board Member, Investor Education (charitable organization) (2004–2005); Director, Viasys Health Care[2] (January 2007–June 2007); Trustee, Pro Publica (charitable organization) (2007–2010) | 122 |
| William N. Searcy, Jr. (1946)<br>Board Member since 1993 | Private investor since October 2003; Trustee of 22 open-end mutual funds managed by Sun Capital Advisers, Inc. (since October 1998). Formerly, Pension & Savings Trust Officer, Sprint Corporation[2] (telecommunications) (November 1989–September 2003) | 122 |
| Jean Gleason Stromberg (1943)<br>Board Member since 1997 | Retired. Formerly, Consultant (1997–2001); Director, Financial Markets US Government Accountability Office (1996–1997); Partner, Fulbright & Jaworski, L.L.P. (law firm) (1978–1996). Directorships: The William and Flora Hewlett Foundation. Former Directorships: Service Source, Inc., Mutual Fund Directors Forum (2002–2004), American Bar Retirement Association (funding vehicle for retirement plans) (1987–1990 and 1994–1996) | 122 |
| Robert H. Wadsworth (1940)<br>Board Member since 1999 | President, Robert H. Wadsworth & Associates, Inc. (consulting firm) (1983 to present); Director, The Phoenix Boys Choir Association | 125 |

## Officers[4]

| Name, Year of Birth, Position with the Fund and Length of Time Served[5] | Principal Occupation(s) During Past 5 Years and Other Directorships Held |
|---|---|
| Michael G. Clark[6] (1965)<br>President, 2006–present | Managing Director[3], Deutsche Asset Management (2006–present); President of DWS family of funds; Director, ICI Mutual Insurance Company (since October 2007); formerly, Director of Fund Board Relations (2004–2006) and Director of Product Development (2000–2004), Merrill Lynch Investment Managers; Senior Vice President Operations, Merrill Lynch Asset Management (1999–2000) |
| Ingo Gefeke[7] (1967)<br>Executive Vice President since 2010 | Managing Director[3], Deutsche Asset Management; Global Head of Distribution and Product Management, DWS Global Head of Trading and Securities Lending. Member of the Board of Directors of DWS Investment GmbH Frankfurt (since July 2009) and DWS Holding & Service GmbH Frankfurt (since January 2010); formerly, Global Chief Administrative Officer, Deutsche Asset Management (2004–2009); Global Chief Operating Officer, Global Transaction Banking, Deutsche Bank AG, New York (2001–2004); Chief Operating Officer, Global Banking Division Americas, Deutsche Bank AG, New York (1999–2001); Central Management, Global Banking Services, Deutsche Bank AG, Frankfurt (1998–1999); Relationship Management, Deutsche Bank AG, Tokyo, Japan (1997–1998) |
| John Millette[8] (1962)<br>Vice President and Secretary, 1999–present | Director[3], Deutsche Asset Management |
| Paul H. Schubert[6] (1963)<br>Chief Financial Officer, 2004–present<br>Treasurer, 2005–present | Managing Director[3], Deutsche Asset Management (since July 2004); formerly, Executive Director, Head of Mutual Fund Services and Treasurer for UBS Family of Funds (1998–2004); Vice President and Director of Mutual Fund Finance at UBS Global Asset Management (1994–1998) |
| Caroline Pearson[8] (1962)<br>Chief Legal Officer, April 2010–present | Managing Director[3], Deutsche Asset Management; formerly, Assistant Secretary for DWS family of funds (1997–2010) |
| Rita Rubin[9] (1970)<br>Assistant Secretary, 2009–present | Vice President and Counsel, Deutsche Asset Management (since October 2007); formerly, Vice President, Morgan Stanley Investment Management (2004–2007) |
| Paul Antosca[8] (1957)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management (since 2006); Vice President, The Manufacturers Life Insurance Company (U.S.A.) (1990–2006) |
| Jack Clark[8] (1967)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management (since 2007); formerly, Vice President, State Street Corporation (2002–2007) |
| Diane Kenneally[8] (1966)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management |
| John Caruso[9] (1965)<br>Anti-Money Laundering Compliance Officer, 2010–present | Managing Director[3], Deutsche Asset Management |

| Name, Year of Birth, Position with the Fund and Length of Time Served[5] | Principal Occupation(s) During Past 5 Years and Other Directorships Held |
|---|---|
| Robert Kloby[9] (1962)<br>Chief Compliance Officer, 2006–present | Managing Director[3], Deutsche Asset Management |

1 *The length of time served represents the year in which the Board Member joined the board of one or more DWS funds currently overseen by the Board.*

2 *A publicly held company with securities registered pursuant to Section 12 of the Securities Exchange Act of 1934.*

3 *Executive title, not a board directorship.*

4 *As a result of their respective positions held with the Advisor, these individuals are considered "interested persons" of the Advisor within the meaning of the 1940 Act. Interested persons receive no compensation from the fund.*

5 *The length of time served represents the year in which the officer was first elected in such capacity for one or more DWS funds.*

6 *Address: 100 Plaza One, Jersey City, NJ 07311.*

7 *Effective January 11, 2011, Mr. Gefeke, Executive Vice President, resigned as an officer of the fund.*

*The mailing address of Mr. Gefeke is 345 Park Avenue, New York, New York 10154. Mr. Gefeke was an interested Board Member of certain DWS funds by virtue of his positions with Deutsche Asset Management. As an interested person, Mr. Gefeke received no compensation from the fund.*

8 *Address: One Beacon Street, Boston, MA 02108.*

9 *Address: 60 Wall Street, New York, New York 10005.*

*The fund's Statement of Additional Information ("SAI") includes additional information about the Board Members. The SAI is available, without charge, upon request. If you would like to request a copy of the SAI, you may do so by calling the following toll-free number: (800) 728-3337.*

# Notes

DWS Investments is part of Deutsche Bank's Asset Management division and, within the US, represents the retail asset management activities of Deutsche Bank AG, Deutsche Bank Trust Company Americas, Deutsche Investment Management Americas Inc. and DWS Trust Company.

The views expressed in this report reflect those of the portfolio managers only through the end of the period of the report as stated on the cover. The managers' views are subject to change at any time based on market and other conditions and should not be construed as a recommendation.

This information must be preceded or accompanied by a current prospectus.

Portfolio changes should not be considered recommendations for action by individual investors.

DWS Investments Distributors, Inc.
222 South Riverside Plaza
Chicago, IL 60606
(800) 621-1148

VS1gloopp-2 (2/11)

DWS INVESTMENTS
Deutsche Bank Group

DECEMBER 31, 2010

# ANNUAL REPORT

## DWS VARIABLE SERIES I

## DWS Growth & Income VIP

**This report must be preceded or accompanied by a prospectus. To obtain an additional prospectus or summary prospectus, if available, call (800) 728-3337 or your financial representative. We advise you to consider the Fund's objectives, risks, charges and expenses carefully before investing. The summary prospectus and prospectus contain this and other important information about the Fund. Please read the prospectus carefully before you invest.**

*Investments in variable insurance portfolios (VIPs) involve risk. Stocks may decline in value. Bond investments are subject to interest-rate and credit risks. When interest rates rise, bond prices generally fall. Credit risk refers to the ability of an issuer to make timely payments of principal and interest. Investing in derivatives entails special risks relating to liquidity, leverage and credit that may reduce returns and/or increased volatility. Investing in foreign securities, particularly those of emerging markets, presents certain risks, such as currency fluctuations, political and economic changes, and market risks. There are additional risks associated with investing in commodities, high-yield bonds, aggressive growth stocks, non-diversified/ concentrated funds and small- and mid-cap stocks which are more fully explained in the prospectuses. Please read the prospectus for more information.*

*DWS Investments is part of Deutsche Bank's Asset Management division and, within the US, represents the retail asset management activities of Deutsche Bank AG, Deutsche Bank Trust Company Americas, Deutsche Investment Management Americas Inc. and DWS Trust Company.*

*NOT FDIC/NCUA INSURED   NO BANK GUARANTEE   MAY LOSE VALUE   NOT A DEPOSIT*
*NOT INSURED BY ANY FEDERAL GOVERNMENT AGENCY*

DWS INVESTMENTS
Deutsche Bank Group

# Performance Summary

December 31, 2010

## DWS Growth & Income VIP

**All performance shown is historical, assumes reinvestment of all dividend and capital gain distributions, and does not guarantee future results. Investment return and principal value fluctuate with changing market conditions so that, when redeemed, shares may be worth more or less than their original cost. Current performance may be lower or higher than the performance data quoted. Please contact your participating insurance company for the Fund's most recent month-end performance. Performance doesn't reflect charges and fees ("contract charges") associated with the separate account that invests in the Fund or any variable life insurance policy or variable annuity contract for which the Fund is an investment option. These charges and fees will reduce returns. While all share classes have the same underlying portfolio, their performance will differ.**

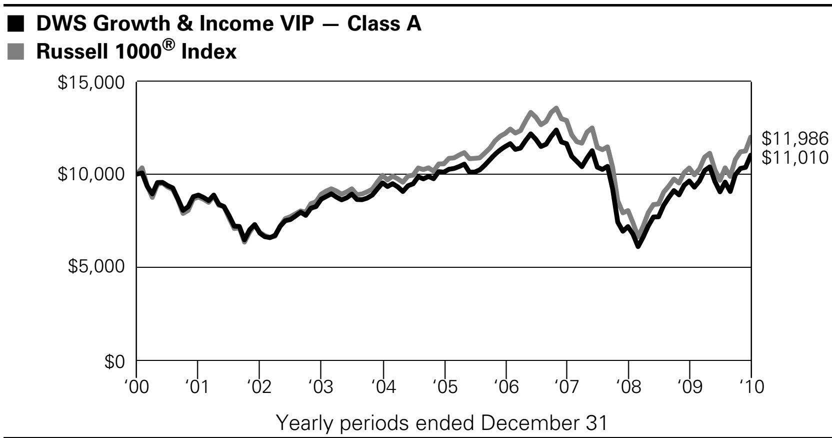
**The gross expense ratios of the Fund, as stated in the fee table of the prospectus dated May 1, 2010 are 0.63% and 0.89% for Class A and Class B shares, respectively, and may differ from the expense ratios disclosed in the Financial Highlights tables in this report.**

Fund returns during all periods shown reflect a fee waiver and/or expense reimbursement. Without this waiver/reimbursement, returns would have been lower.

### Risk Considerations

Portfolio management could be wrong in its analysis of industries, companies, economic trends and favor a security that underperforms the market. Stocks may decline in value. See the prospectus for details.

### Growth of an Assumed $10,000 Investment




*The Russell 1000® Index is an unmanaged index that measures the performance of the 1,000 largest companies in the Russell 3000 Index, which represents approximately 92% of the total market capitalization of the Russell 3000 Index.*

*Index returns assume the reinvestment of dividends and, unlike fund returns, do not reflect any fees or expenses. It is not possible to invest directly into an index.*

### Comparative Results

| DWS Growth & Income VIP | | 1-Year | 3-Year | 5-Year | 10-Year |
|---|---|---|---|---|---|
| **Class A** | Growth of $10,000 | $11,440 | $9,467 | $10,903 | $11,010 |
| | Average annual total return | 14.40% | –1.81% | 1.74% | 0.97% |
| Russell 1000 Index | Growth of $10,000 | $11,610 | $9,305 | $11,364 | $11,986 |
| | Average annual total return | 16.10% | –2.37% | 2.59% | 1.83% |

| DWS Growth & Income VIP | | 1-Year | 3-Year | 5-Year | 10-Year |
|---|---|---|---|---|---|
| **Class B** | Growth of $10,000 | $11,412 | $9,411 | $10,768 | $10,714 |
| | Average annual total return | 14.12% | –2.00% | 1.49% | 0.69% |
| Russell 1000 Index | Growth of $10,000 | $11,610 | $9,305 | $11,364 | $11,986 |
| | Average annual total return | 16.10% | –2.37% | 2.59% | 1.83% |

*The growth of $10,000 is cumulative.*

# Information About Your Fund's Expenses

## DWS Growth & Income VIP

As an investor of the Fund, you incur two types of costs: ongoing expenses and transaction costs. Ongoing expenses include management fees, distribution and service (12b-1) fees and other Fund expenses. Examples of transaction costs include contract charges, redemption fees and account maintenance fees, which are not shown in this section. The following tables are intended to help you understand your ongoing expenses (in dollars) of investing in the Fund and to help you compare these expenses with the ongoing expenses of investing in other mutual funds. The example in the table is based on an investment of $1,000 invested at the beginning of the six-month period and held for the entire period (July 1, 2010 to December 31, 2010).

The tables illustrate your Fund's expenses in two ways:

- **Actual Fund Return.** This helps you estimate the actual dollar amount of ongoing expenses (but not transaction costs) paid on a $1,000 investment in the Fund using the Fund's actual return during the period. To estimate the expenses you paid over the period, simply divide your account value by $1,000 (for example, an $8,600 account value divided by $1,000 = 8.6), then multiply the result by the number in the "Expenses Paid per $1,000" line under the share class you hold.
- **Hypothetical 5% Fund Return.** This helps you to compare your Fund's ongoing expenses (but not transaction costs) with those of other mutual funds using the Fund's actual expense ratio and a hypothetical rate of return of 5% per year before expenses. Examples using a 5% hypothetical Fund return may be found in the shareholder reports of other mutual funds. The hypothetical account values and expenses may not be used to estimate the actual ending account balance or expenses you paid for the period.

Please note that the expenses shown in these tables are meant to highlight your ongoing expenses only and do not reflect any transaction costs. The "Expenses Paid per $1,000" line of the tables is useful in comparing ongoing expenses only and will not help you determine the relative total expense of owning different funds. If these transaction costs had been included, your costs would have been higher.

**Expenses and Value of a $1,000 Investment** for the six months ended December 31, 2010

| Actual Fund Return | Class A | Class B |
|---|---|---|
| Beginning Account Value 7/1/10 | $1,000.00 | $1,000.00 |
| Ending Account Value 12/31/10 | $1,217.40 | $1,215.80 |
| Expenses Paid per $1,000* | $ 3.41 | $ 4.86 |
| **Hypothetical 5% Portfolio Return** | **Class A** | **Class B** |
| Beginning Account Value 7/1/10 | $1,000.00 | $1,000.00 |
| Ending Account Value 12/31/10 | $1,022.13 | $1,020.82 |
| Expenses Paid per $1,000* | $ 3.11 | $ 4.43 |

* *Expenses are equal to the Fund's annualized expense ratio for each share class, multiplied by the average account value over the period, multiplied by the number of days in the most recent six-month period, then divided by 365.*

| Annualized Expense Ratios | Class A | Class B |
|---|---|---|
| DWS Variable Series I — DWS Growth & Income VIP | .61% | .87% |

For more information, please refer to the Fund's prospectus.

These tables do not reflect charges and fees ("contract charges") associated with the separate account that invests in the Fund or any variable life insurance policy or variable annuity contract for which the Fund is an investment option.

# Management Summary

**December 31, 2010**

## DWS Growth & Income VIP

US equities performed very well during 2010, as investors were cheered by gradually improving economic data and surprisingly strong corporate profits. The Russell 1000® Index — the Fund's benchmark — gained 16.10% on the year, building on its 28.43% rally of 2009. The Fund, while also producing a positive return of 14.40% (Class A shares, unadjusted for contract charges), fell short of the benchmark. (Past performance is no guarantee of future results.)

Our approach to managing the Fund is disciplined and dynamic — disciplined in the sense that we use a quantitative approach that measures numerous factors related to growth, value, quality and market sentiment, and dynamic in that we can choose to give different weightings to these factors based on a rigorous analysis of the past that seeks to determine which periods are most like now. The Fund's sentiment factors employ a variety of factors to gauge the momentum of individual stock prices. The past year was a highly rotational year for style performance, with leadership changing several times — from growth to sentiment, then to quality, and then back to sentiment. The Fund's growth and sentiment factors performed relatively well over the full year, whereas the value and quality factors were mostly weak. We started the year with healthy weightings to sentiment and growth, which added value early in the year. However, our relatively large weighting toward value throughout the year more than offset this and proved to be the biggest drag on relative performance.

From a sector perspective, our stock selection process was least effective in the information technology segment, where our overweight positions in Microsoft Corp., Computer Sciences Corp. and the disk-drive maker Western Digital Corp.* weighed on performance.[1] The industrials sector was an additional area of underperformance, due in part to our overweights in Raytheon Co. and the truck manufacturer Oshkosh Corp. Our stock picks also fell short in the utilities and consumer staples sectors. On the plus side, we outperformed the benchmark by a wide margin in the energy sector. We generated strong performance by moving to overweight positions in stocks that plummeted sharply in the wake of the Gulf oil spill and then staged rebounds from undervalued levels, such as Transocean Ltd., Anadarko Petroleum Corp.* and National Oilwell Varco, Inc. We also performed very well within financials, thanks in part to our overweight positions in Berkshire Hathaway, Inc. and ACE Ltd.

Robert Wang
Russell Shtern, CFA
*Portfolio Managers, QS Investors, LLC, Subadvisor to the Fund*

*The Russell 1000 Index is an unmanaged index that measures the performance of the 1,000 largest companies in the Russell 3000® Index, which represents approximately 92% of the total market capitalization of the Russell 3000 Index.*

*Index returns assume the reinvestment of dividends and, unlike fund returns, do not reflect any fees or expenses. It is not possible to invest directly into an index.*

1 *"Overweight" means the Fund holds a higher weighting in a given sector or security than the benchmark. "Underweight" means the Fund holds a lower weighting.*

* *Not held in the portfolio as of December 31, 2010.*

*Portfolio management market commentary is as of December 31, 2010, and may not come to pass. This information is subject to change at any time based on market and other conditions. Past performance does not guarantee future results. Current and future portfolio holdings are subject to risk.*

# Portfolio Summary

## DWS Growth & Income VIP

| **Asset Allocation** (As a % of Investment Portfolio excluding Securities Lending Collateral) | **12/31/10** | **12/31/09** |
|---|---|---|
| Common Stocks | 99% | 98% |
| Cash Equivalents | 1% | 1% |
| Government & Agency Obligation | — | 1% |
| | 100% | 100% |

| **Sector Diversification** (As a % of Common Stocks) | **12/31/10** | **12/31/09** |
|---|---|---|
| Information Technology | 19% | 19% |
| Financials | 17% | 11% |
| Health Care | 14% | 14% |
| Industrials | 12% | 13% |
| Energy | 11% | 9% |
| Consumer Discretionary | 11% | 12% |
| Consumer Staples | 7% | 11% |
| Materials | 5% | 5% |
| Telecommunication Services | 2% | 4% |
| Utilities | 2% | 2% |
| | 100% | 100% |

*Asset allocation and sector diversification are subject to change.*

*For more complete details about the Fund's investment portfolio, see page 6.*

Following the Fund's fiscal first and third quarter-end, a complete portfolio holdings listing is filed with the SEC on Form N-Q. The form will be available on the SEC's Web site at www.sec.gov, and it also may be reviewed and copied at the SEC's Public Reference Room in Washington, D.C. Information on the operation of the SEC's Public Reference Room may be obtained by calling (800) SEC-0330. The Fund's portfolio holdings are also posted on www.dws-investments.com from time to time. Please see the Fund's current prospectus for more information.

# Investment Portfolio

December 31, 2010

## DWS Growth & Income VIP

| | Shares | Value ($) |
|---|---|---|
| **Common Stocks 99.0%** | | |
| **Consumer Discretionary 10.4%** | | |
| **Auto Components 0.1%** | | |
| Goodyear Tire & Rubber Co.* | 6,200 | **73,470** |
| **Diversified Consumer Services 0.5%** | | |
| Apollo Group, Inc. "A"* | 3,100 | 122,419 |
| Career Education Corp.* (a) | 9,000 | 186,570 |
| Coinstar, Inc.* | 1,600 | 90,304 |
| DeVry, Inc. | 1,500 | 71,970 |
| Sotheby's | 1,600 | 72,000 |
| | | **543,263** |
| **Hotels Restaurants & Leisure 1.0%** | | |
| Chipotle Mexican Grill, Inc.* (a) | 600 | 127,596 |
| McDonald's Corp. | 3,300 | 253,308 |
| Panera Bread Co. "A"* | 1,400 | 141,694 |
| Starbucks Corp. | 15,000 | 481,950 |
| | | **1,004,548** |
| **Household Durables 0.2%** | | |
| Garmin Ltd. (a) | 6,200 | **192,138** |
| **Internet & Catalog Retail 1.0%** | | |
| Liberty Media Corp. — Interactive "A"* | 32,500 | 512,525 |
| Priceline.com, Inc.* | 1,300 | 519,415 |
| | | **1,031,940** |
| **Media 2.8%** | | |
| CBS Corp. "B" | 8,400 | 160,020 |
| Comcast Corp. "A" (a) | 50,400 | 1,107,288 |
| Liberty Media-Starz "A"* | 1,800 | 119,664 |
| McGraw-Hill Companies, Inc. | 4,400 | 160,204 |
| News Corp. "A" | 9,100 | 132,496 |
| Time Warner, Inc. | 19,600 | 630,532 |
| Walt Disney Co. | 12,900 | 483,879 |
| | | **2,794,083** |
| **Multiline Retail 0.8%** | | |
| Dillard's, Inc. "A" (a) | 16,200 | 614,628 |
| Kohl's Corp.* | 4,300 | 233,662 |
| | | **848,290** |
| **Specialty Retail 2.6%** | | |
| Advance Auto Parts, Inc. | 7,000 | 463,050 |
| American Eagle Outfitters, Inc. | 9,500 | 138,985 |
| AnnTaylor Stores Corp.* | 2,700 | 73,953 |
| Barnes & Noble, Inc. (a) | 7,800 | 110,370 |
| Chico's FAS, Inc. | 5,700 | 68,571 |
| Guess?, Inc. | 2,300 | 108,836 |
| Rent-A-Center, Inc. | 3,600 | 116,208 |
| Ross Stores, Inc. | 2,500 | 158,125 |
| The Gap, Inc. | 36,300 | 803,682 |
| TJX Companies, Inc. | 13,000 | 577,070 |
| | | **2,618,850** |
| **Textiles, Apparel & Luxury Goods 1.4%** | | |
| Coach, Inc. | 6,700 | 370,577 |
| Deckers Outdoor Corp.* | 2,100 | 167,454 |
| NIKE, Inc. "B" (a) | 4,300 | 367,306 |
| VF Corp. | 5,500 | 473,990 |
| | | **1,379,327** |
| **Consumer Staples 6.9%** | | |
| **Beverages 0.2%** | | |
| Molson Coors Brewing Co. "B" | 3,900 | **195,741** |
| **Food & Staples Retailing 1.4%** | | |
| Wal-Mart Stores, Inc. | 24,700 | 1,332,071 |
| Whole Foods Market, Inc.* (a) | 800 | 40,472 |
| | | **1,372,543** |
| **Food Products 2.7%** | | |
| Archer-Daniels-Midland Co. | 14,500 | 436,160 |
| Corn Products International, Inc. | 4,400 | 202,400 |
| Fresh Del Monte Produce, Inc. | 5,700 | 142,215 |
| H.J. Heinz Co. | 5,500 | 272,030 |
| Hormel Foods Corp. | 2,100 | 107,646 |
| The Hershey Co. | 14,500 | 683,675 |
| Tyson Foods, Inc. "A" (a) | 47,700 | 821,394 |
| Unilever PLC (ADR) | 2,700 | 83,376 |
| | | **2,748,896** |
| **Household Products 0.6%** | | |
| Kimberly-Clark Corp. | 2,200 | 138,688 |
| Procter & Gamble Co. | 7,300 | 469,609 |
| | | **608,297** |
| **Personal Products 0.4%** | | |
| Estee Lauder Companies, Inc. "A" | 1,100 | 88,770 |
| Herbalife Ltd. | 5,100 | 348,687 |
| | | **437,457** |
| **Tobacco 1.6%** | | |
| Lorillard, Inc. | 8,200 | 672,892 |
| Philip Morris International, Inc. | 15,200 | 889,656 |
| | | **1,562,548** |
| **Energy 11.2%** | | |
| **Energy Equipment & Services 3.4%** | | |
| Complete Production Services, Inc.* | 10,300 | 304,365 |
| Diamond Offshore Drilling, Inc. | 3,000 | 200,610 |
| FMC Technologies, Inc.* | 1,200 | 106,692 |
| Helmerich & Payne, Inc. | 1,800 | 87,264 |
| Nabors Industries Ltd.* | 11,300 | 265,098 |
| National Oilwell Varco, Inc. | 15,100 | 1,015,475 |
| Noble Corp. (a) | 4,500 | 160,965 |
| Oceaneering International, Inc.* | 1,900 | 139,897 |
| Oil States International, Inc.* | 10,000 | 640,900 |
| Transocean Ltd.* (a) | 6,900 | 479,619 |
| | | **3,400,885** |
| **Oil, Gas & Consumable Fuels 7.8%** | | |
| Chevron Corp. | 12,000 | 1,095,000 |
| Cimarex Energy Co. | 1,400 | 123,942 |
| CNOOC Ltd. (ADR) | 400 | 95,348 |
| Devon Energy Corp. | 12,100 | 949,971 |
| Exxon Mobil Corp. | 27,800 | 2,032,736 |
| Hess Corp. | 8,300 | 635,282 |
| Murphy Oil Corp. | 9,500 | 708,225 |
| Newfield Exploration Co.* | 2,600 | 187,486 |
| Noble Energy, Inc. | 3,800 | 327,104 |
| Occidental Petroleum Corp. | 6,200 | 608,220 |
| Valero Energy Corp. | 45,100 | 1,042,712 |
| | | **7,806,026** |

*The accompanying notes are an integral part of the financial statements.*

| | Shares | Value ($) |
|---|---|---|
| **Financials 17.3%** | | |
| **Capital Markets 1.8%** | | |
| Ameriprise Financial, Inc. | 2,700 | 155,385 |
| BlackRock, Inc. | 1,700 | 323,986 |
| Janus Capital Group, Inc. | 5,400 | 70,038 |
| Legg Mason, Inc. | 4,400 | 159,588 |
| State Street Corp. | 5,000 | 231,700 |
| T. Rowe Price Group, Inc. | 4,500 | 290,430 |
| The Goldman Sachs Group, Inc. | 3,400 | 571,744 |
| | | **1,802,871** |
| **Commercial Banks 4.1%** | | |
| CIT Group, Inc.* (a) | 8,100 | 381,510 |
| Fifth Third Bancorp. (a) | 46,800 | 687,024 |
| Huntington Bancshares, Inc. | 33,500 | 230,145 |
| KeyCorp | 42,200 | 373,470 |
| M&T Bank Corp. (a) | 1,700 | 147,985 |
| PNC Financial Services Group, Inc. | 9,200 | 558,624 |
| SunTrust Banks, Inc. | 35,600 | 1,050,556 |
| Wells Fargo & Co. | 20,500 | 635,295 |
| | | **4,064,609** |
| **Consumer Finance 2.4%** | | |
| Capital One Financial Corp. (a) | 37,800 | 1,608,768 |
| Discover Financial Services | 42,800 | 793,084 |
| | | **2,401,852** |
| **Diversified Financial Services 2.8%** | | |
| Bank of America Corp. | 28,500 | 380,190 |
| Citigroup, Inc.* | 69,700 | 329,681 |
| CME Group, Inc. | 800 | 257,400 |
| JPMorgan Chase & Co. | 35,800 | 1,518,636 |
| PHH Corp.* (a) | 6,900 | 159,735 |
| The NASDAQ OMX Group, Inc.* (a) | 4,900 | 116,179 |
| | | **2,761,821** |
| **Insurance 5.8%** | | |
| ACE Ltd. | 20,300 | 1,263,675 |
| Aflac, Inc. | 5,000 | 282,150 |
| Allied World Assurance Co. Holdings Ltd. | 5,000 | 297,200 |
| Arch Capital Group Ltd.* | 1,800 | 158,490 |
| Aspen Insurance Holdings Ltd. | 3,900 | 111,618 |
| Assurant, Inc. | 3,100 | 119,412 |
| Axis Capital Holdings Ltd. | 3,000 | 107,640 |
| Berkshire Hathaway, Inc. "A"* | 2 | 240,900 |
| Berkshire Hathaway, Inc. "B"* | 2,100 | 168,231 |
| Chubb Corp. | 15,100 | 900,564 |
| Everest Re Group Ltd. | 1,800 | 152,676 |
| Hartford Financial Services Group, Inc. | 9,300 | 246,357 |
| Platinum Underwriters Holdings Ltd. | 2,200 | 98,934 |
| The Travelers Companies, Inc. | 30,600 | 1,704,726 |
| | | **5,852,573** |
| **Real Estate Investment Trusts 0.4%** | | |
| HCP, Inc. (REIT) | 5,100 | 187,629 |
| Public Storage (REIT) | 1,500 | 152,130 |
| SL Green Realty Corp. (REIT) | 1,500 | 101,265 |
| | | **441,024** |
| **Health Care 13.6%** | | |
| **Biotechnology 1.8%** | | |
| Biogen Idec, Inc.* | 7,500 | 502,875 |
| Celgene Corp.* | 5,300 | 313,442 |
| Cephalon, Inc.* (a) | 15,500 | 956,660 |
| | | **1,772,977** |

| | Shares | Value ($) |
|---|---|---|
| **Health Care Providers & Services 8.1%** | | |
| Aetna, Inc. | 19,300 | 588,843 |
| AmerisourceBergen Corp. | 40,500 | 1,381,860 |
| Cardinal Health, Inc. | 42,200 | 1,616,682 |
| Coventry Health Care, Inc.* | 26,200 | 691,680 |
| Health Net, Inc.* | 4,700 | 128,263 |
| Humana, Inc.* | 15,400 | 842,996 |
| UnitedHealth Group, Inc. | 47,600 | 1,718,836 |
| WellPoint, Inc.* | 19,900 | 1,131,514 |
| | | **8,100,674** |
| **Pharmaceuticals 3.7%** | | |
| Eli Lilly & Co. | 35,100 | 1,229,904 |
| Endo Pharmaceuticals Holdings, Inc.* | 12,700 | 453,517 |
| Forest Laboratories, Inc.* | 53,400 | 1,707,732 |
| Medicis Pharmaceutical Corp. "A" | 3,900 | 104,481 |
| Par Pharmaceutical Companies, Inc.* | 5,900 | 227,209 |
| | | **3,722,843** |
| **Industrials 11.5%** | | |
| **Aerospace & Defense 3.1%** | | |
| General Dynamics Corp. | 8,700 | 617,352 |
| Honeywell International, Inc. | 6,900 | 366,804 |
| Northrop Grumman Corp. (a) | 23,700 | 1,535,286 |
| Raytheon Co. | 12,300 | 569,982 |
| | | **3,089,424** |
| **Air Freight & Logistics 1.6%** | | |
| FedEx Corp. | 4,300 | 399,943 |
| United Parcel Service, Inc. "B" | 16,700 | 1,212,086 |
| | | **1,612,029** |
| **Airlines 0.2%** | | |
| Alaska Air Group, Inc.* | 2,700 | **153,063** |
| **Commercial Services & Supplies 0.4%** | | |
| Cintas | 4,400 | 123,024 |
| R.R. Donnelley & Sons Co. (a) | 15,400 | 269,038 |
| | | **392,062** |
| **Construction & Engineering 0.4%** | | |
| EMCOR Group, Inc.* | 9,400 | 272,412 |
| KBR, Inc. | 4,900 | 149,303 |
| | | **421,715** |
| **Electrical Equipment 0.2%** | | |
| Rockwell Automation, Inc. | 2,100 | **150,591** |
| **Industrial Conglomerates 1.1%** | | |
| 3M Co. | 13,100 | **1,130,530** |
| **Machinery 2.0%** | | |
| Danaher Corp. | 7,600 | 358,492 |
| Dover Corp. | 2,900 | 169,505 |
| Eaton Corp. | 4,800 | 487,248 |
| Ingersoll-Rand PLC (a) | 6,700 | 315,503 |
| Oshkosh Corp.* | 11,300 | 398,212 |
| Parker Hannifin Corp. | 1,800 | 155,340 |
| Trinity Industries, Inc. (a) | 6,000 | 159,660 |
| | | **2,043,960** |
| **Professional Services 0.3%** | | |
| Manpower, Inc. (a) | 4,300 | **269,868** |
| **Road & Rail 1.6%** | | |
| Norfolk Southern Corp. | 12,200 | 766,404 |
| Ryder System, Inc. | 16,700 | 879,088 |
| | | **1,645,492** |
| **Trading Companies & Distributors 0.6%** | | |
| W.W. Grainger, Inc. (a) | 4,500 | **621,495** |

*The accompanying notes are an integral part of the financial statements.*

| | Shares | Value ($) |
|---|---|---|
| **Information Technology 18.7%** | | |
| **Communications Equipment 1.6%** | | |
| F5 Networks, Inc.* | 4,100 | 533,656 |
| Nokia Corp. (ADR) (a) | 31,500 | 325,080 |
| Research In Motion Ltd.* (a) | 10,100 | 587,113 |
| Tellabs, Inc. | 19,100 | 129,498 |
| | | **1,575,347** |
| **Computers & Peripherals 0.7%** | | |
| Dell, Inc.* | 8,200 | 111,110 |
| Lexmark International, Inc. "A"* | 15,500 | 539,710 |
| | | **650,820** |
| **Electronic Equipment, Instruments & Components 3.9%** | | |
| Anixter International, Inc. | 1,600 | 95,568 |
| Arrow Electronics, Inc.* | 19,900 | 681,575 |
| Avnet, Inc.* | 17,000 | 561,510 |
| FLIR Systems, Inc.* | 2,400 | 71,400 |
| Ingram Micro, Inc. "A"* | 23,000 | 439,070 |
| Jabil Circuit, Inc. | 11,900 | 239,071 |
| Power-One, Inc.* (a) | 10,600 | 108,120 |
| Tech Data Corp.* | 10,700 | 471,014 |
| Tyco Electronics Ltd. | 25,600 | 906,240 |
| Vishay Intertechnology, Inc.* | 25,900 | 380,212 |
| | | **3,953,780** |
| **Internet Software & Services 0.8%** | | |
| AOL, Inc.* | 13,900 | 329,569 |
| IAC/InterActiveCorp.* (a) | 16,300 | 467,810 |
| | | **797,379** |
| **IT Services 5.4%** | | |
| Automatic Data Processing, Inc. | 12,100 | 559,988 |
| Cognizant Technology Solutions Corp. "A"* | 3,700 | 271,173 |
| Computer Sciences Corp. | 26,200 | 1,299,520 |
| International Business Machines Corp. | 18,800 | 2,759,088 |
| Western Union Co. (a) | 29,500 | 547,815 |
| | | **5,437,584** |
| **Semiconductors & Semiconductor Equipment 3.4%** | | |
| Altera Corp. (a) | 9,800 | 348,684 |
| Analog Devices, Inc. | 8,100 | 305,127 |
| Fairchild Semiconductor International, Inc.* (a) | 7,900 | 123,319 |
| Intel Corp. | 87,400 | 1,838,022 |
| Lam Research Corp.* | 2,800 | 144,984 |
| Marvell Technology Group Ltd.* | 18,000 | 333,900 |
| Maxim Integrated Products, Inc. | 6,600 | 155,892 |
| Micron Technology, Inc.* (a) | 23,900 | 191,678 |
| | | **3,441,606** |
| **Software 2.9%** | | |
| Activision Blizzard, Inc. | 30,000 | 373,200 |
| Microsoft Corp. | 90,575 | 2,528,854 |
| | | **2,902,054** |

| | Shares | Value ($) |
|---|---|---|
| **Materials 5.3%** | | |
| **Chemicals 2.4%** | | |
| Ashland, Inc. | 6,200 | 315,332 |
| Cytec Industries, Inc. | 1,400 | 74,284 |
| E.I. du Pont de Nemours & Co. | 19,900 | 992,612 |
| Lubrizol Corp. | 8,100 | 865,728 |
| Potash Corp. of Saskatchewan, Inc. (a) | 900 | 139,347 |
| | | **2,387,303** |
| **Metals & Mining 2.6%** | | |
| Barrick Gold Corp. | 6,900 | 366,942 |
| Freeport-McMoRan Copper & Gold, Inc. | 10,400 | 1,248,936 |
| Newmont Mining Corp. | 17,100 | 1,050,453 |
| | | **2,666,331** |
| **Paper & Forest Products 0.3%** | | |
| Domtar Corp. | 2,000 | 151,840 |
| MeadWestvaco Corp. | 4,500 | 117,720 |
| | | **269,560** |
| **Telecommunication Services 2.5%** | | |
| **Diversified Telecommunication Services 2.2%** | | |
| AT&T, Inc. | 15,480 | 454,803 |
| Verizon Communications, Inc. | 47,800 | 1,710,284 |
| | | **2,165,087** |
| **Wireless Telecommunication Services 0.3%** | | |
| Vodafone Group PLC (ADR) | 13,300 | **351,519** |
| **Utilities 1.6%** | | |
| **Electric Utilities 0.8%** | | |
| Duke Energy Corp. | 32,100 | 571,701 |
| Exelon Corp. | 7,000 | 291,480 |
| | | **863,181** |
| **Independent Power Producers & Energy Traders 0.6%** | | |
| NRG Energy, Inc.* (a) | 31,541 | **616,311** |
| **Multi-Utilities 0.2%** | | |
| Ameren Corp. | 6,300 | **177,596** |
| **Total Common Stocks** (Cost $85,529,136) | | **99,325,233** |
| **Securities Lending Collateral 12.1%** | | |
| Daily Assets Fund Institutional, 0.27% (b) (c) (Cost $12,109,203) | 12,109,203 | **12,109,203** |
| **Cash Equivalents 0.9%** | | |
| Central Cash Management Fund, 0.19% (b) (Cost $862,150) | 862,150 | **862,150** |

| | % of Net Assets | Value ($) |
|---|---|---|
| **Total Investment Portfolio** (Cost $98,500,489)† | 112.0 | **112,296,586** |
| **Other Assets and Liabilities, Net** | (12.0) | **(12,016,763)** |
| **Net Assets** | 100.0 | **100,279,823** |

*The accompanying notes are an integral part of the financial statements.*

* Non-income producing security.

† The cost for federal income tax purposes was $99,375,854. At December 31, 2010, net unrealized appreciation for all securities based on tax cost was $12,920,732. This consisted of aggregate gross unrealized appreciation for all securities in which there was an excess of value over tax cost of $14,304,323 and aggregate gross unrealized depreciation for all securities in which there was an excess of tax cost over value of $1,383,591.

(a) All or a portion of these securities were on loan (see Notes to Financial Statements). The value of all securities loaned at December 31, 2010 amounted to $11,776,143, which is 11.7% of net assets.

(b) Affiliated fund managed by Deutsche Investment Management Americas Inc. The rate shown is the annualized seven-day yield at period end.

(c) Represents collateral held in connection with securities lending. Income earned by the Fund is net of borrower rebates.

ADR: American Depositary Receipt

REIT: Real Estate Investment Trust

At December 31, 2010, open futures contracts purchased were as follows:

| Futures | Currency | Expiration Date | Contracts | Notional Value ($) | Unrealized Appreciation ($) |
|---|---|---|---|---|---|
| S&P 500 E-Mini Index | USD | 3/18/2011 | 16 | 1,002,400 | **14,510** |

| **Currency Abbreviation** | |
|---|---|
| USD | United States Dollar |

For information on the Fund's policy and additional disclosures regarding futures contracts, please refer to the Derivatives section of Note A in the accompanying Notes to Financial Statements.

## Fair Value Measurements

Various inputs are used in determining the value of the Fund's investments. These inputs are summarized in three broad levels. Level 1 includes quoted prices in active markets for identical securities. Level 2 includes other significant observable inputs (including quoted prices for similar securities, interest rates, prepayment speeds, and credit risk). Level 3 includes significant unobservable inputs (including the Fund's own assumptions in determining the fair value of investments). The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities.

The following is a summary of the inputs used as of December 31, 2010 in valuing the Fund's investments. For information on the Fund's policy regarding the valuation of investments, please refer to the Security Valuation section of Note A in the accompanying Notes to Financial Statements.

| Assets | Level 1 | Level 2 | Level 3 | Total |
|---|---|---|---|---|
| Common Stocks (d) | $ 99,325,233 | $ — | $ — | $ 99,325,233 |
| Short-Term Investments (d) | 12,971,353 | — | — | 12,971,353 |
| Derivatives (e) | 14,510 | — | — | 14,510 |
| **Total** | **$ 112,311,096** | **$ —** | **$ —** | **$ 112,311,096** |

There have been no significant transfers in and out of Level 1 and Level 2 fair value measurements during the year ended December 31, 2010.

(d) See Investment Portfolio for additional detailed categorizations.

(e) Derivatives include unrealized appreciation (depreciation) on open futures contracts.

The accompanying notes are an integral part of the financial statements.

# Statement of Assets and Liabilities

as of December 31, 2010

| Assets | | |
|---|---|---|
| Investments: | | |
| Investments in securities, at value (cost $85,529,136), including $11,776,143 of securities loaned | $ | 99,325,233 |
| Investment in Daily Assets Fund Institutional (cost $12,109,203)* | | 12,109,203 |
| Investment in Central Cash Management Fund (cost $862,150) | | 862,150 |
| Total investments, at value (cost $98,500,489) | | 112,296,586 |
| Foreign currency, at value (cost $1,777) | | 1,847 |
| Deposits with broker for open futures contracts | | 110,209 |
| Receivable for Fund shares sold | | 72,187 |
| Receivable for variation margin on open futures contracts | | 14,510 |
| Interest receivable | | 2,780 |
| Dividends receivable | | 71,249 |
| Other assets | | 531 |
| Total assets | | 112,569,899 |

| Liabilities | | |
|---|---|---|
| Payable upon return of securities loaned | | 12,109,203 |
| Payable for Fund shares redeemed | | 63,304 |
| Accrued management fee | | 34,058 |
| Accrued distribution service fee (Class B) | | 410 |
| Other accrued expenses and payables | | 83,101 |
| Total liabilities | | 12,290,076 |
| **Net assets, at value** | **$** | **100,279,823** |

| Net Assets Consist of | | |
|---|---|---|
| Undistributed net investment income | | 1,201,576 |
| Net unrealized appreciation (depreciation) on: | | |
| Investments | | 13,796,097 |
| Futures | | 14,510 |
| Foreign currency | | 70 |
| Accumulated net realized gain (loss) | | (47,839,390) |
| Paid-in capital | | 133,106,960 |
| **Net assets, at value** | **$** | **100,279,823** |
| **Class A** | | |
| **Net Asset Value,** offering and redemption price per share ($98,342,904 ÷ 13,004,152 outstanding shares of beneficial interest, $.01 par value, unlimited number of shares authorized) | **$** | **7.56** |
| **Class B** | | |
| **Net Asset Value,** offering and redemption price per share ($1,936,919 ÷ 256,466 outstanding shares of beneficial interest, $.01 par value, unlimited number of shares authorized) | **$** | **7.55** |

* *Represents collateral on securities loaned.*

# Statement of Operations

for the year ended December 31, 2010

| Investment Income | | |
|---|---|---|
| Income: | | |
| Dividends (net of foreign taxes withheld of $1,154) | $ | 1,803,774 |
| Interest | | 594 |
| Income distributions — Central Cash Management Fund | | 1,101 |
| Securities lending income, including income from Daily Assets Fund Institutional, net of borrower rebates | | 68,938 |
| Total income | | 1,874,407 |
| Expenses: | | |
| Management fee | | 381,068 |
| Administration fee | | 97,710 |
| Services to shareholders | | 4,142 |
| Custodian fee | | 23,254 |
| Distribution service fee (Class B) | | 4,837 |
| Legal fees | | 17,720 |
| Audit and tax fees | | 41,911 |
| Trustees' fees and expenses | | 6,663 |
| Reports to shareholders | | 31,298 |
| Other | | 8,782 |
| Total expenses before expense reductions | | 617,385 |
| Expense reductions | | (29,349) |
| Total expenses after expense reductions | | 588,036 |
| **Net investment income (loss)** | | **1,286,371** |

| Realized and Unrealized Gain (Loss) | | |
|---|---|---|
| Net realized gain (loss) from: | | |
| Investments | | 10,640,783 |
| Futures | | 91,175 |
| Foreign currency | | (35) |
| | | 10,731,923 |
| Change in net unrealized appreciation (depreciation) on: | | |
| Investments | | 853,941 |
| Futures | | 6,737 |
| Foreign currency | | 109 |
| | | 860,787 |
| **Net gain (loss)** | | **11,592,710** |
| **Net increase (decrease) in net assets resulting from operations** | **$** | **12,879,081** |

*The accompanying notes are an integral part of the financial statements.*

# Statement of Changes in Net Assets

| Increase (Decrease) in Net Assets | Years Ended December 31, 2010 | 2009 |
|---|---|---|
| Operations: | | |
| Net investment income | $ 1,286,371 | $ 1,607,557 |
| Net realized gain (loss) | 10,731,923 | (17,473,719) |
| Change in net unrealized appreciation (depreciation) | 860,787 | 42,884,018 |
| Net increase (decrease) in net assets resulting from operations | 12,879,081 | 27,017,856 |
| Distributions to shareholders from: | | |
| Net investment income: | | |
| Class A | (1,597,628) | (1,967,417) |
| Class B | (27,222) | (35,839) |
| Total distributions | (1,624,850) | (2,003,256) |
| Fund share transactions: | | |
| **Class A** | | |
| Proceeds from shares sold | 5,336,052 | 5,456,883 |
| Reinvestment of distributions | 1,597,628 | 1,967,417 |
| Cost of shares redeemed | (20,642,306) | (25,400,088) |
| Net increase (decrease) in net assets from Class A share transactions | (13,708,626) | (17,975,788) |
| **Class B** | | |
| Proceeds from shares sold | 68,140 | 93,741 |
| Reinvestment of distributions | 27,222 | 35,839 |
| Cost of shares redeemed | (453,581) | (431,050) |
| Net increase (decrease) in net assets from Class B share transactions | (358,219) | (301,470) |
| **Increase (decrease) in net assets** | (2,812,614) | 6,737,342 |
| Net assets at beginning of period | 103,092,437 | 96,355,095 |
| Net assets at end of period (including undistributed net investment income of $1,201,576 and $1,542,732, respectively) | **$ 100,279,823** | **$ 103,092,437** |

| Other Information | | |
|---|---|---|
| **Class A** | | |
| Shares outstanding at beginning of period | 15,048,001 | 18,437,278 |
| Shares sold | 774,532 | 954,520 |
| Shares issued to shareholders in reinvestment of distributions | 219,153 | 399,070 |
| Shares redeemed | (3,037,534) | (4,742,867) |
| Net increase (decrease) in Class A shares | (2,043,849) | (3,389,277) |
| Shares outstanding at end of period | **13,004,152** | **15,048,001** |
| **Class B** | | |
| Shares outstanding at beginning of period | 309,228 | 364,787 |
| Shares sold | 10,025 | 16,377 |
| Shares issued to shareholders in reinvestment of distributions | 3,734 | 7,270 |
| Shares redeemed | (66,521) | (79,206) |
| Net increase (decrease) in Class B shares | (52,762) | (55,559) |
| Shares outstanding at end of period | **256,466** | **309,228** |

*The accompanying notes are an integral part of the financial statements.*

# Financial Highlights

## Class A

| Years Ended December 31, | 2010 | 2009 | 2008 | 2007 | 2006 |
|---|---|---|---|---|---|
| **Selected Per Share Data** | | | | | |
| **Net asset value, beginning of period** | **$ 6.71** | **$ 5.12** | **$10.81** | **$10.94** | **$ 9.72** |
| *Income (loss) from investment operations:* | | | | | |
| Net investment income (loss)[a] | .09 | .10 | .10 | .13 | .13[c] |
| Net realized and unrealized gain (loss) | .87 | 1.61 | (3.45) | .02 | 1.19 |
| **Total from investment operations** | .96 | 1.71 | (3.35) | .15 | 1.32 |
| *Less distributions from:* | | | | | |
| Net investment income | (.11) | (.12) | (.18) | (.13) | (.10) |
| Net realized gains | — | — | (2.16) | (.15) | — |
| **Total distributions** | (.11) | (.12) | (2.34) | (.28) | (.10) |
| **Net asset value, end of period** | **$ 7.56** | **$ 6.71** | **$ 5.12** | **$10.81** | **$10.94** |
| Total Return (%)[b] | 14.40 | 34.15 | (38.31) | 1.36 | 13.63[c] |
| **Ratios to Average Net Assets and Supplemental Data** | | | | | |
| Net assets, end of period ($ millions) | 98 | 101 | 94 | 196 | 280 |
| Ratio of expenses before expense reductions (%) | .63 | .63 | .60 | .57 | .56 |
| Ratio of expenses after expense reductions (%) | .60 | .54 | .54 | .56 | .54 |
| Ratio of net investment income (loss) (%) | 1.32 | 1.74 | 1.34 | 1.18 | 1.24[c] |
| Portfolio turnover rate (%) | 145 | 82 | 130 | 310 | 105 |

a *Based on average shares outstanding during the period.*

b *Total return would have been lower had certain expenses not been reduced.*

c *Includes non-recurring income from the Advisor recorded as a result of an administrative proceeding regarding disclosure of brokerage allocation practices in connection with sales of DWS Funds. The non-recurring income resulted in an increase in net investment income of $0.007 per share and an increase in the ratio of net investment income of 0.07%. Excluding this non-recurring income, total return would have been 0.06% lower.*

## Class B

| Years Ended December 31, | 2010 | 2009 | 2008 | 2007 | 2006 |
|---|---|---|---|---|---|
| **Selected Per Share Data** | | | | | |
| **Net asset value, beginning of period** | **$ 6.70** | **$ 5.12** | **$10.77** | **$10.90** | **$ 9.68** |
| *Income (loss) from investment operations:* | | | | | |
| Net investment income (loss)[a] | .07 | .08 | .08 | .09 | .09[c] |
| Net realized and unrealized gain (loss) | .87 | 1.60 | (3.42) | .02 | 1.19 |
| **Total from investment operations** | .94 | 1.68 | (3.34) | .11 | 1.28 |
| *Less distributions from:* | | | | | |
| Net investment income | (.09) | (.10) | (.15) | (.09) | (.06) |
| Net realized gains | — | — | (2.16) | (.15) | — |
| **Total distributions** | (.09) | (.10) | (2.31) | (.24) | (.06) |
| **Net asset value, end of period** | **$ 7.55** | **$ 6.70** | **$ 5.12** | **$10.77** | **$10.90** |
| Total Return (%)[b] | 14.12 | 33.64 | (38.29) | 1.00 | 13.28[c] |
| | | | | | |
| Net assets, end of period ($ millions) | 2 | 2 | 2 | 15 | 52 |
| Ratio of expenses before expense reductions (%) | .88 | .89 | .82 | .95 | .94 |
| Ratio of expenses after expense reductions (%) | .85 | .80 | .77 | .92 | .89 |
| Ratio of net investment income (loss) (%) | 1.07 | 1.48 | 1.12 | .82 | .89[c] |
| Portfolio turnover rate (%) | 145 | 82 | 130 | 310 | 105 |

a *Based on average shares outstanding during the period.*

b *Total return would have been lower had certain expenses not been reduced.*

c *Includes non-recurring income from the Advisor recorded as a result of an administrative proceeding regarding disclosure of brokerage allocation practices in connection with sales of DWS Funds. The non-recurring income resulted in an increase in net investment income of $0.007 per share and an increase in the ratio of net investment income of 0.07%. Excluding this non-recurring income, total return would have been 0.06% lower.*

# Notes to Financial Statements

## A. Organization and Significant Accounting Policies

DWS Variable Series I (the "Series") is registered under the Investment Company Act of 1940, as amended (the "1940 Act"), as an open-end, registered management investment company organized as a Massachusetts business trust. The Series consists of six diversified funds: DWS Bond VIP, DWS Growth & Income VIP, DWS Capital Growth VIP, DWS Global Opportunities VIP, DWS International VIP and DWS Health Care VIP (individually or collectively hereinafter referred to as a "Fund" or the "Funds"). These financial statements report on DWS Growth & Income VIP. The Series is intended to be the underlying investment vehicle for variable annuity contracts and variable life insurance policies to be offered by the separate accounts of certain life insurance companies ("Participating Insurance Companies").

**Multiple Classes of Shares of Beneficial Interest.** The Fund offers two classes of shares (Class A shares and Class B shares). Class B shares are subject to Rule 12b-1 distribution fees under the 1940 Act and record keeping fees equal to an annual rate of 0.25% and up to 0.15%, respectively, of the average daily net assets of the Class B shares of the Fund. Class A shares are not subject to such fees.

Investment income, realized and unrealized gains and losses, and certain fund-level expenses and expense reductions, if any, are borne pro rata on the basis of relative net assets by the holders of all classes of shares, except that each class bears certain expenses unique to that class (including the applicable 12b-1 distribution fees and record keeping fees). Differences in class-level expenses may result in payment of different per share dividends by class. All shares have equal rights with respect to voting subject to class-specific arrangements.

The Series' financial statements are prepared in accordance with accounting principles generally accepted in the United States of America, which require the use of management estimates. Actual results could differ from those estimates. The policies described below are followed consistently by the Series in the preparation of the financial statements for its Funds.

**Security Valuation.** Investments are stated at value determined as of the close of regular trading on the New York Stock Exchange on each day the exchange is open for trading.

Various inputs are used in determining the value of the Fund's investments. These inputs are summarized in three broad levels. Level 1 includes quoted prices in active markets for identical securities. Level 2 includes other significant observable inputs (including quoted prices for similar securities, interest rates, prepayment speeds, and credit risk). Level 3 includes significant unobservable inputs (including the Fund's own assumptions in determining the fair value of investments). The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities.

Equity securities are valued at the most recent sale price or official closing price reported on the exchange (US or foreign) or over-the-counter market on which they trade and are categorized as Level 1 securities. Securities for which no sales are reported are valued at the calculated mean between the most recent bid and asked quotations on the relevant market or, if a mean cannot be determined, at the most recent bid quotation.

Futures contracts are generally valued at the settlement prices established each day on the exchange on which they are traded and are categorized as Level 1.

Money market instruments purchased with an original or remaining maturity of sixty days or less, maturing at par, are valued at amortized cost, which approximates value, and are categorized as Level 2. Investments in open-end investment companies are valued at their net asset value each business day and are categorized as Level 1.

Securities and other assets for which market quotations are not readily available or for which the above valuation procedures are deemed not to reflect fair value are valued in a manner that is intended to reflect their fair value as determined in accordance with procedures approved by the Trustees and are generally categorized as Level 3. In accordance with the Fund's valuation procedures, factors used in determining value may include, but are not limited to, the type of the security; the size of the holding; the initial cost of the security; the existence of any contractual restrictions on the security's disposition; the price and extent of public trading in similar securities of the issuer or of comparable companies; quotations or evaluated prices from broker-dealers and/or pricing services; information obtained from the issuer, analysts, and/or the appropriate stock exchange (for exchange-traded securities); an analysis of the company's or issuer's financial statements; an evaluation of the forces that influence the issuer and the market(s) in which the security is purchased and sold and with respect to debt securities; the maturity, coupon, creditworthiness, currency denomination and the movement of the market in which the security is normally traded. The value determined under these procedures may differ from published values for the same securities.

Disclosure about the classification of fair value measurements is included in a table following the Fund's Investment Portfolio.

**Securities Lending.** The Fund lends securities to certain financial institutions. The Fund retains beneficial ownership of the securities it has loaned and continues to receive interest and dividends paid by the issuer of securities and to participate in any changes in their market value. The Fund requires the borrowers of the securities to maintain collateral with the Fund consisting of either cash or liquid, unencumbered assets having a value at least equal to the value of the securities loaned. When the collateral falls below specified amounts, the lending agent will use its best effort to obtain additional collateral on the next business day to meet required amounts under the security lending agreement. The Fund may invest the cash collateral into a joint trading account in an affiliated money market fund pursuant to Exemptive Orders issued by the SEC. The Fund receives compensation for lending its securities either in the form of fees or by earning interest on invested cash collateral net of borrower rebates and fees paid to a lending agent. Either the Fund or the borrower may terminate the loan. There may be risks of delay and costs in recovery of securities or even loss of rights in the collateral should the borrower of the securities fail financially. The Fund is also subject to all investment risks associated with the reinvestment of any cash collateral received, including, but not limited to, interest rate, credit and liquidity risk associated with such investments.

**Foreign Currency Translations.** The books and records of the Fund are maintained in US dollars. Investment securities and other assets and liabilities denominated in a foreign currency are translated into US dollars at the prevailing exchange rates at period end. Purchases and sales of investment securities, income and expenses are translated into US dollars at the prevailing exchange rates on the respective dates of the transactions.

Net realized and unrealized gains and losses on foreign currency transactions represent net gains and losses between trade and settlement dates on securities transactions, the disposition of forward foreign currency exchange contracts and foreign currencies, and the difference between the amount of net investment income accrued and the US dollar amount actually received. That portion of both realized and unrealized gains and losses on investments that results from fluctuations in foreign currency exchange rates is not separately disclosed but is included with net realized and unrealized gain/appreciation and loss/depreciation on investments.

**Taxes.** The Fund is treated as a separate taxpayer as provided for in the Internal Revenue Code, as amended. It is the Fund's policy to comply with the requirements of the Internal Revenue Code, as amended, which are applicable to regulated investment companies, and to distribute all of its taxable income to the separate accounts of the Participating Insurance Companies which hold its shares.

At December 31, 2010, the Fund had an approximate net tax basis capital loss carryforward which may be applied against any realized net taxable capital gains of each succeeding year until fully utilized or until the following expiration dates, whichever occurs first:

| Fund | Capital Loss Carryforwards ($) | Expiration Date | Capital Loss Carryfowards Utilized ($) |
|---|---|---|---|
| DWS Growth & Income VIP | 46,950,000 | 12/31/2016–12/31/2017 | 10,057,000 |

The Fund has reviewed the tax positions for the open tax years as of December 31, 2010 and has determined that no provision for income tax is required in the Fund's financial statements. The Fund's federal tax returns for the prior three fiscal years remain open subject to examination by the Internal Revenue Service.

**Distribution of Income and Gains.** The Fund will declare and distribute dividends from its net investment income, if any, annually, although additional distributions may be made if necessary. Net realized gains from investment transactions, in excess of available capital loss carryforwards, would be taxable to the Fund if not distributed, and, therefore, will be distributed to shareholders at least annually.

The timing and characterization of certain income and capital gains distributions are determined annually in accordance with federal tax regulations which may differ from accounting principles generally accepted in the United States of America. These differences primarily relate to certain securities sold at a loss. As a result, net investment income (loss) and net realized gain (loss) on investment transactions for a reporting period may differ significantly from distributions during such period. Accordingly, the Fund may periodically make reclassifications among certain of its capital accounts without impacting the net asset value of the Fund.

At December 31, 2010, the Fund's components of distributable earnings (accumulated losses) on a tax-basis are as follows:

| Fund | Undistributed Ordinary Income ($)* | Capital Loss Carryforwards ($) | Net Unrealized Gain (Loss) on Investments ($) |
|---|---|---|---|
| DWS Growth & Income VIP | 1,201,576 | (46,950,000) | 12,920,732 |

In addition, the tax character of distributions paid to shareholders by the Fund is summarized as follows:

| | Distributions from Ordinary Income ($)* Years Ended December 31, | |
|---|---|---|
| Fund | 2010 | 2009 |
| DWS Growth & Income VIP | 1,624,850 | 2,003,256 |

* *For tax purposes, short-term capital gains distributions are considered ordinary income distributions.*

**Expenses.** Expenses of the Series arising in connection with a specific Fund are allocated to that Fund. Other Series expenses which cannot be directly attributed to a Fund are apportioned among the Funds in the Series.

**Contingencies.** In the normal course of business, the Fund may enter into contracts with service providers that contain general indemnification clauses. The Fund's maximum exposure under these arrangements is unknown as this would involve future claims that may be made against the Fund that have not yet been made. However, based on experience, the Fund expects the risk of loss to be remote.

**Other.** Investment transactions are accounted for on a trade date plus one basis for daily net asset value calculations. However, for financial reporting purposes, investment transactions are reported on trade date. Interest income is recorded on the accrual basis net of foreign withholding taxes. Dividend income is recorded on the ex-dividend date net of foreign withholding taxes. Certain dividends from foreign securities may be recorded subsequent to the ex-dividend date as soon as the Fund is informed of such dividends. Realized gains and losses from investment transactions are recorded on an identified cost basis. All discounts and premiums are accreted/amortized for both tax and financial reporting purposes.

## B. Derivative Instruments

**Futures Contracts.** A futures contract is an agreement between a buyer or seller and an established futures exchange or its clearinghouse in which the buyer or seller agrees to take or make a delivery of a specific amount of a financial instrument at a specified price on a specific date (settlement date). For the year ended December 31, 2010, the Fund entered into futures contracts in circumstances where portfolio management believed they offered an economic means of gaining exposure to a particular asset class or to keep cash on hand to meet shareholder redemptions or other needs while maintaining exposure to the market.

Futures contracts are valued at the most recent settlement price. Upon entering into a futures contract, the Fund is required to deposit with a financial intermediary cash or securities ("initial margin") in an amount equal to a certain percentage of the face value indicated in the futures contract. Subsequent payments ("variation margin") are made or received by the Fund dependent upon the daily fluctuations in the value and are recorded for financial reporting purposes as unrealized gains or losses by the Fund. Gains or losses are realized when the contract expires or is closed. Since all futures contracts are exchange traded, counterparty risk is minimized as the exchange's clearinghouse acts as the counterparty, and guarantees the futures against default.

Certain risks may arise upon entering into futures contracts, including the risk that an illiquid market will limit the Fund's ability to close out a futures contract prior to the settlement date and that a change in the value of a futures contract may not correlate exactly with the changes in the value of the underlying hedged security, index or currency. Risk of loss may exceed amounts recognized in the Statement of Assets and Liabilities.

A summary of the open futures contracts as of December 31, 2010, is included in a table following the Fund's Investment Portfolio. For the year ended December 31, 2010, the Fund's investment in futures contracts purchased had a total notional value generally indicative of a range from approximately $51,000 to $1,515,000.

The following table summarizes the value of the Fund's derivative instruments held as of December 31, 2010 and the related location in the accompanying Statement of Assets and Liabilities, presented by primary underlying risk exposure:

| Asset Derivative | Futures Contracts |
|---|---|
| Equity Contracts (a) | $ 14,510 |

*The above derivative is located in the following Statement of Assets and Liabilities account:*

(a) *Net unrealized appreciation (depreciation) on futures. Asset of Receivable for daily variation margin on open futures contracts reflects unsettled variation margin.*

Additionally, the amount of unrealized and realized gains and losses on derivative instruments recognized in Fund earnings during the year ended December 31, 2010 and the related location in the accompanying Statement of Operations is summarized in the following tables by primary underlying risk exposure:

| Realized Gain (Loss) | Futures Contracts |
|---|---|
| Equity Contracts (a) | $ 91,175 |

*The above derivative is located in the following Statement of Operations account:*

(a) *Net realized gain (loss) from futures*

| Change in Net Unrealized Appreciation (Depreciation) | Futures Contracts |
|---|---|
| Equity Contracts (a) | $ 6,737 |

*The above derivative is located in the following Statement of Operations account:*

(a) *Change in net unrealized appreciation (depreciation) on futures*

## C. Purchases and Sales of Securities

During the year ended December 31, 2010, purchases and sales of investment securities (excluding short-term investments) were as follows:

| Fund | Purchases ($) | Sales ($) |
|---|---|---|
| DWS Growth & Income VIP | 139,171,485 | 153,000,110 |

## D. Related Parties

Under the Investment Management Agreement with Deutsche Investment Management Americas Inc. ("DIMA" or the "Advisor"), an indirect, wholly owned subsidiary of Deutsche Bank AG, the Advisor directs the investments of the Fund in accordance with its investment objectives, policies and restrictions. The Advisor determines the securities, instruments and other contracts relating to investments to be purchased, sold or entered into by the Fund or delegates such responsibility to the Fund's subadvisor.

Under the Investment Management Agreement with the Advisor, the Fund pays a monthly management fee, based on the average daily net assets of the Fund, computed and accrued daily and payable monthly, at the annual rates shown below:

| Fund | Annual Management Fee Rate |
|---|---|
| DWS Growth & Income VIP | |
| first $250 million of average daily net assets | .390% |
| next $750 million of average daily net assets | .365% |
| over $1 billion of average daily net assets | .340% |

QS Investors, LLC ("QS Investors") acts as investment sub-advisor to the Fund. On August 1, 2010, members of the Advisor's Quantitative Strategies Group, including members of the Fund's portfolio management team, separated from the Advisor and formed QS Investors as a separate investment advisory firm unaffiliated with the Advisor. As an investment sub-advisor to the Fund, QS Investors makes investment decisions and buys and sells securities for the Fund. QS Investors is paid by the Advisor, not the Fund, for the services QS Investors provides to the Fund.

For the period from January 1, 2010 through April 30, 2010, the Advisor, the underwriter and accounting agent contractually agreed to waive a portion of their fee to the extent necessary to maintain the operating expenses of each class (excluding certain expenses such as extraordinary expenses, taxes, brokerage and interest) as follows:

| Fund | Annual Rate |
|---|---|
| DWS Growth & Income VIP Class A | .54% |
| DWS Growth & Income VIP Class B | .87% |

In addition, for the period from January 1, 2010 through April 27, 2010, the Advisor had contractually agreed to waive 0.01% of the management fee for the Fund.

Accordingly, for the year ended December 31, 2010, the total management fee, management fee waived and effective management fee rate are as follows:

| Fund | Total Aggregated ($) | Waived ($) | Annual Effective Rate |
|---|---|---|---|
| DWS Growth & Income VIP | 381,068 | 28,777 | .36% |

**Administration Fee.** Pursuant to an Administrative Services Agreement, DIMA provides most administrative services to the Series. For all services provided under the Administrative Services Agreement, the Fund pays the

Advisor an annual fee ("Administration Fee") of 0.10% of the Fund's average daily net assets, computed and accrued daily and payable monthly. For the year ended December 31, 2010, the Administration Fee was as follows:

| Fund | Total Aggregated ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS Growth & Income VIP | 97,710 | 8,441 |

**Service Provider Fees.** DWS Investments Service Company ("DISC"), an affiliate of the Advisor, is the transfer agent, dividend-paying agent and shareholder service agent for the Series. Pursuant to a sub-transfer agency agreement between DISC and DST Systems, Inc. ("DST"), DISC has delegated certain transfer agent, dividend-paying agent and shareholder service agent functions to DST. DISC compensates DST out of the shareholder servicing fee it receives from the Fund. For the year ended December 31, 2010, the amounts charged to the Fund by DISC were as follows:

| Fund | Total Aggregated ($) | Waived ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|---|
| DWS Growth & Income VIP Class A | 572 | 572 | — |
| DWS Growth & Income VIP Class B | 96 | — | 24 |

DWS Investments Distributors, Inc. ("DIDI"), also an affiliate of the Advisor, is the Series' Distributor. In accordance with the Master Distribution Plan, DIDI receives 12b-1 fees of 0.25% of average daily net assets of Class B shares. Pursuant to the Master Distribution Plan, DIDI remits these fees to the Participating Insurance Companies for various costs incurred or paid by these companies in connection with marketing and distribution of Class B shares. These fees are detailed in the Fund's Statement of Operations.

**Typesetting and Filing Service Fees.** Under an agreement with DIMA, DIMA is compensated for providing typesetting and certain regulatory filing services to the Fund. For the year ended December 31, 2010, the amount charged to the Fund by DIMA included in the Statement of Operations under "reports to shareholders" was as follows:

| Fund | Total Aggregated ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS Growth & Income VIP | 13,057 | 2,726 |

**Trustees' Fees and Expenses.** The Fund paid each Trustee not affiliated with the Advisor retainer fees plus specified amounts for various committee services and for the Board Chairperson.

**Affiliated Cash Management Vehicles.** The Fund may invest uninvested cash balances in Central Cash Management Fund, which is managed by the Advisor. The Fund indirectly bears its proportionate share of the expenses of the underlying money market funds. Central Cash Management Fund does not pay the Advisor an investment management fee. Central Cash Management Fund seeks a high level of current income consistent with liquidity and the preservation of capital.

## E. Ownership of the Fund

Three participating insurance companies were owners of record of 10% or more of the total outstanding Class A shares of the Fund, each owning 35%, 26% and 15%. Two participating insurance companies were owners of record of 10% or more of the total outstanding Class B shares of the Fund, owning 86% and 11%.

## F. Line of Credit

The Series and other affiliated funds (the "Participants") share in a $450 million revolving credit facility provided by a syndication of banks. The Fund may borrow for temporary or emergency purposes, including the meeting of redemption requests that otherwise might require the untimely disposition of securities. The Participants are charged an annual commitment fee which is allocated based on net assets, among each of the Participants. Interest is calculated at a rate per annum equal to the sum of the Federal Funds Rate plus 1.25 percent plus if LIBOR exceeds the Federal Funds Rate the amount of such excess. The Fund may borrow up to a maximum of 33 percent of its net assets under the agreement.

# Report of Independent Registered Public Accounting Firm

**To the Trustees of DWS Variable Series I and the Shareholders of DWS Growth & Income VIP:**

In our opinion, the accompanying statement of assets and liabilities, including the investment portfolio, and the related statements of operations and of changes in net assets and the financial highlights present fairly, in all material respects, the financial position of DWS Growth & Income VIP (the "Fund") at December 31, 2010 and the results of its operations, the changes in its net assets, and the financial highlights for the periods indicated therein, in conformity with accounting principles generally accepted in the United States of America. These financial statements and financial highlights (hereafter referred to as "financial statements") are the responsibility of the Fund's management. Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these financial statements in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits, which included confirmation of securities at December 31, 2010 by correspondence with the custodians and brokers, provide a reasonable basis for our opinion.

Boston, Massachusetts
February 11, 2011

PricewaterhouseCoopers LLP

## Tax Information

**(Unaudited)**

For corporate shareholders of the Fund, 100% of the ordinary dividends (i.e., income dividends plus short-term capital gains) paid during the Fund's fiscal year ended December 31, 2010 qualified for the dividends received deduction.

Please consult a tax advisor if you have questions about federal or state income tax laws, or on how to prepare your tax returns. If you have specific questions about your account, please contact your insurance provider.

## Proxy Voting

The Series' policies and procedures for voting proxies for portfolio securities and information about how the Series voted proxies related to its portfolio securities during the 12-month period ended June 30 are available on our Web site — www.dws-investments.com (click on "proxy voting"at the bottom of the page) — or on the SEC's Web site — www.sec.gov. To obtain a written copy of the Series' policies and procedures without charge, upon request, call us toll free at (800) 728-3337.

# Investment Management Agreement Approval

The Board of Trustees, including the Independent Trustees, approved the renewal of your Fund's investment management agreement (the "Agreement") with Deutsche Investment Management Americas Inc. ("DWS") and sub-advisory agreement (the "Sub-Advisory Agreement" and together with the Agreement, the "Agreements") between DWS and QS Investors, LLC ("QS Investors") in September 2010.

In terms of the process that the Board followed prior to approving the Agreements, shareholders should know that:

- In September 2010, all of the Fund's Trustees were independent of DWS and its affiliates.
- The Trustees meet frequently to discuss fund matters. Each year, the Trustees dedicate substantial time to contract review matters. Over the course of several months, the Board's Contract Committee, in coordination with the Board's Fixed Income and Quant Oversight Committee, reviewed comprehensive materials received from DWS, independent third parties and independent counsel. These materials included an analysis of the Fund's performance, fees and expenses, and profitability compiled by the Fund's independent fee consultant. The Board also received extensive information throughout the year regarding performance of the Fund.
- The Independent Trustees regularly meet privately with their independent counsel to discuss contract review and other matters. In addition, the Independent Trustees were also advised by the Fund's independent fee consultant in the course of their review of the Fund's contractual arrangements and considered a comprehensive report prepared by the independent fee consultant in connection with their deliberations (the "IFC Report").
- In connection with reviewing the Agreements, the Board also reviewed the terms of the Fund's Rule 12b-1 plan, distribution agreement, administrative services agreement, transfer agency agreement and other material service agreements.
- Based on its evaluation of the information provided, the Contract Committee presented its findings and recommendations to the Independent Trustees as a group. The Independent Trustees reviewed the Contract Committee's findings and recommendations and presented their recommendations to the full Board.

In connection with the contract review process, the Contract Committee and the Board considered the factors discussed below, among others. The Board also considered that DWS and its predecessors have managed the Fund since its inception, and the Board believes that a long-term relationship with a capable, conscientious advisor is in the best interests of the Fund. The Board considered, generally, that shareholders chose to invest or remain invested in the Fund knowing that DWS managed the Fund, and that the Agreement was approved by the Fund's shareholders. DWS is part of Deutsche Bank, a major global banking institution that is engaged in a wide range of financial services. The Board believes that there are significant advantages to being part of a global asset management business that offers a wide range of investing expertise and resources, including hundreds of portfolio managers and analysts with research capabilities in many countries throughout the world.

While shareholders may focus primarily on fund performance and fees, the Fund's Board considers these and many other factors, including the quality and integrity of DWS's and QS Investors' personnel and such other issues as back-office operations, fund valuations, and compliance policies and procedures. In addition, in connection with approving the continuation of the Fund's Sub-Advisory Agreement, the Board noted it had engaged in a comprehensive review of the agreement in connection with its initial approval in May 2010.

**Nature, Quality and Extent of Services.** The Board considered the terms of the Agreements, including the scope of advisory services provided under the Agreements. The Board noted that, under the Agreements, DWS and QS Investors provide portfolio management services to the Fund and that, pursuant to a separate administrative services agreement, DWS provides administrative services to the Fund. The Board considered the experience and skills of senior management and investment personnel, the resources made available to such personnel, the ability of DWS and QS Investors to attract and retain high-quality personnel, and the organizational depth and stability of DWS and QS Investors. The Board reviewed the Fund's performance over short-term and long-term periods and compared those returns to various agreed-upon performance measures, including market indices and a peer universe compiled by the independent fee consultant using information supplied by Lipper Inc. ("Lipper"). The Board also noted that it has put into place a process of identifying "Focus Funds" (e.g., funds performing poorly relative to their benchmark or a peer universe compiled by Lipper), and receives more frequent reporting and information from DWS regarding such funds, along with DWS's remedial plans to address underperformance. The Board believes this process is an effective manner of identifying and addressing underperforming funds. Based on the information provided, the Board noted that for the one-, three- and five-year periods ended December 31, 2009, the Fund's performance (Class A shares) was in the 1st quartile, 3rd quartile and 3rd quartile, respectively, of the applicable Lipper universe (the 1st quartile being the best performers and the 4th quartile being the worst performers). The Board also observed that the Fund has outperformed its benchmark in the one-year period and has underperformed its benchmark in the three- and five-year periods ended December 31, 2009.

On the basis of this evaluation and the ongoing review of investment results by the Board, the Board concluded that the nature, quality and extent of services provided by DWS and QS Investors historically have been and continue to be satisfactory.

**Fees and Expenses.** The Board considered the Fund's investment management fee schedule, sub-advisory fee schedule, operating expenses and total expense ratios, and comparative information provided by Lipper and the independent fee consultant regarding investment management fee rates paid to other investment advisors by similar funds (1st quartile being the most favorable and 4th quartile being the least favorable). With respect to management fees paid to other investment advisors by similar funds, the Board noted that the contractual fee rates paid by the Fund, which include a 0.10% fee paid to DWS under the Fund's administrative services agreement, were lower than the median (1st quartile) of the applicable Lipper peer group (based on Lipper data provided as of December 31, 2009). With respect to the sub-advisory fee paid to QS Investors, the Board noted that the fee is paid by DWS out of its fee and not directly by the Fund. The Board noted that the Fund's Class A shares total (net) operating expenses were expected to be lower than the median (1st quartile) of the applicable Lipper expense universe (based on Lipper data provided as of December 31, 2009) ("Lipper Universe Expenses"). The Board also reviewed data comparing each share class's total (net) operating expenses to the applicable Lipper Universe Expenses. The Board considered the Fund's management fee rate as compared to fees charged by DWS and certain of its affiliates for comparable mutual funds and considered differences in fund and fee structures between the DWS Funds. The Board also considered how the Fund's total (net) operating expenses compared to the total (net) operating expenses of a more customized peer group selected by Lipper (based on such factors as asset size).

The information considered by the Board as part of its review of management fees included information regarding fees charged by DWS and its affiliates to similar institutional accounts and to similar funds offered primarily to European investors ("DWS Europe funds"), in each case as applicable. The Board observed that advisory fee rates for institutional accounts generally were lower than the management fees charged by similarly managed DWS US mutual funds ("DWS Funds"), but also took note of the differences in services provided to DWS Funds as compared to institutional accounts. In the case of DWS Europe funds, the Board observed that fee rates for DWS Europe funds generally were higher than for similarly managed DWS Funds, but noted that differences in the types of services provided to DWS Funds relative to DWS Europe funds made it difficult to compare such fees.

On the basis of the information provided, the Board concluded that management fees were reasonable and appropriate in light of the nature, quality and extent of services provided by DWS and QS Investors.

**Profitability.** The Board reviewed detailed information regarding revenues received by DWS under the Agreement. The Board considered the estimated costs and pre-tax profits realized by DWS from advising the DWS Funds, as well as estimates of the pre-tax profits attributable to managing the Fund in particular. The Board also received information regarding the estimated enterprise-wide profitability of DWS and its affiliates with respect to all fund services in totality and by fund. The Board reviewed DWS's methodology in allocating its costs to the management of the Fund. Based on the information provided, the Board concluded that the pre-tax profits realized by DWS in connection with the management of the Fund were not unreasonable. The Board also reviewed information regarding the profitability of certain similar investment management firms. The Board noted that while information regarding the profitability of such firms is limited (and in some cases is not necessarily prepared on a comparable basis), DWS and its affiliates' overall profitability with respect to the DWS fund complex (after taking into account distribution and other services provided to the funds by DWS and its affiliates) was lower than the overall profitability levels of many comparable firms for which such data was available. The Board did not consider the profitability of QS Investors with respect to the Fund. The Board noted that DWS pays QS Investors' fee out of its management fee, and its understanding that the Fund's sub-advisory fee schedule was the product of an arm's length negotiation with DWS.

**Economies of Scale.** The Board considered whether there are economies of scale with respect to the management of the Fund and whether the Fund benefits from any economies of scale. The Board noted that the Fund's management fee schedule includes fee breakpoints. The Board concluded that the Fund's fee schedule represents an appropriate sharing between the Fund and DWS of such economies of scale as may exist in the management of the Fund at current asset levels.

**Other Benefits to DWS and QS Investors and Their Affiliates.** The Board also considered the character and amount of other incidental benefits received by DWS and QS Investors and their affiliates, including any fees received by DWS for administrative services provided to the Fund and any fees received by an affiliate of DWS for distribution services. The Board also considered benefits to DWS and QS Investors related to brokerage and soft-dollar allocations, including allocating brokerage to pay for research generated by parties other than the executing broker dealers, which pertain primarily to funds investing in equity securities, along with the incidental public relations benefits to DWS and QS Investors related to DWS Funds advertising and cross-selling opportunities among DWS products and services. The Board concluded that management fees were reasonable in light of these fallout benefits.

**Compliance.** The Board considered the significant attention and resources dedicated by DWS to documenting and enhancing its compliance processes in recent years. The Board noted in particular (i) the experience and seniority of both DWS's chief compliance officer and the Fund's chief compliance officer; (ii) the large number of DWS compliance personnel; and (iii) the substantial commitment of resources by DWS and its affiliates to compliance matters. The Board also considered the attention and resources dedicated by DWS to the oversight of the investment sub-advisor's compliance program and compliance with the applicable fund policies and procedures.

Based on all of the information considered and the conclusions reached, the Board unanimously determined that the continuation of the Agreements is in the best interests of the Fund. In making this determination, the Board did not give particular weight to any single factor identified above. The Board considered these factors over the course of numerous meetings, certain of which were in executive session with only the Independent Trustees and their counsel present. It is possible that individual Trustees may have weighed these factors differently in reaching their individual decisions to approve the continuation of the Agreements.

# Summary of Management Fee Evaluation by Independent Fee Consultant

October 3, 2010

Pursuant to an Order entered into by Deutsche Investment Management Americas and affiliates (collectively, "DeAM") with the Attorney General of New York, I, Thomas H. Mack, have been appointed the Independent Fee Consultant for the DWS Funds (formerly the DWS Scudder Funds). My duties include preparing an annual written evaluation of the management fees DeAM charges the Funds, considering among other factors the management fees charged by other mutual fund companies for like services, management fees DeAM charges other clients for like services, DeAM's costs of supplying services under the management agreements and related profit margins, possible economies of scale if a Fund grows larger, and the nature and quality of DeAM's services, including fund performance. This report summarizes my evaluation for 2010, including my qualifications, the evaluation process for each of the DWS Funds, consideration of certain complex-level factors, and my conclusions. I served in substantially the same capacity in 2007, 2008, and 2009.

## Qualifications

For more than 35 years I have served in various professional capacities within the investment management business. I have held investment analysis and advisory positions, including securities analyst, portfolio strategist and director of investment policy with a large investment firm. I have also performed business management functions, including business development, financial management and marketing research and analysis.

Since 1991, I have been an independent consultant within the asset management industry. I have provided services to over 125 client organizations, including investment managers, mutual fund boards, product distributors and related organizations. Over the past ten years I have completed a number of assignments for mutual fund boards, specifically including assisting boards with management contract renewal.

I hold a Master of Business Administration degree, with highest honors, from Harvard University and Master of Science and Bachelor of Science (highest honors) degrees from the University of California at Berkeley. I am an independent director and audit committee financial expert for two closed-end mutual funds and have served in various leadership and financial oversight capacities with non-profit organizations.

## Evaluation of Fees for each DWS Fund

My work focused primarily on evaluating, fund-by-fund, the fees charged to each of the 118 publicly offered Fund portfolios in the DWS Fund family. For each Fund, I considered each of the key factors mentioned above, as well as any other relevant information. In doing so I worked closely with the Funds' Independent Directors in their annual contract renewal process, as well as in their approval of contracts for several new funds (documented separately).

In evaluating each Fund's fees, I reviewed comprehensive materials provided by or on behalf of DeAM, including expense information prepared by Lipper Analytical, comparative performance information, profitability data, manager histories, and other materials. I also accessed certain additional information from the Lipper and Morningstar databases and drew on my industry knowledge and experience.

To facilitate evaluating this considerable body of information, I prepared for each Fund a document summarizing the key data elements in each area as well as additional analytics discussed below. This made it possible to consider each key data element in the context of the others.

In the course of contract renewal, DeAM agreed to implement a number of fee and expense adjustments requested by the Independent Directors which will favorably impact future fees and expenses, and my evaluation includes the effects of these changes.

### Fees and Expenses Compared with Other Funds

The competitive fee and expense evaluation for each fund focused on two primary comparisons:

The Fund's contractual management fee (the advisory fee plus the administration fee where applicable) compared with those of a group of typically 12–15 funds in the same Lipper investment category (e.g. Large Capitalization Growth) having similar distribution arrangements and being of similar size.

The Fund's total expenses compared with a broader universe of funds from the same Lipper investment category and having similar distribution arrangements.

These two comparisons provide a view of not only the level of the fee compared with funds of similar scale but also the total expense the Fund bears for all the services it receives, in comparison with the investment choices available in the Fund's investment category and distribution channel. The principal figure-of-merit used in these comparisons was the subject Fund's percentile ranking against peers.

### DeAM's Fees for Similar Services to Others

DeAM provided management fee schedules for all of its US domiciled fund and non-fund investment management accounts in any of the investment categories where there is a DWS Fund. These similar products included the other DWS Funds, non-fund pooled accounts, institutional accounts and sub-advisory accounts. Using this information, I calculated for each Fund the fee that would be charged to each similar product, at the subject Fund's asset level.

Evaluating information regarding non-fund products is difficult because there are varying levels of services required for different types of accounts, with mutual funds generally requiring considerably more regulatory and administrative types of service as well as having more frequent cash flows than other types of accounts. Also, while mutual fund fees for similar fund products can be expected to be similar, there will be some differences due to different pricing conditions in different distribution channels (e.g. retail funds versus those used in variable insurance products), differences in underlying investment processes and other factors.

### Costs and Profit Margins

DeAM provided a detailed profitability analysis for each Fund. After making some adjustments so that the presentation would be more comparable to the available industry figures, I reviewed profit margins from investment management alone, from investment management plus other fund services (excluding distribution) provided to the Funds by DeAM (principally shareholder services), and DeAM profits from all sources, including distribution. A later section comments on overall profitability.

### Economies of Scale

Economies of scale — an expected decline in management cost per dollar of fund assets as fund assets grow — are very rarely quantified and documented because of inherent difficulties in collecting and analyzing relevant data. However, in virtually every investment category that I reviewed, larger funds tend to have lower fees and lower total expenses than smaller funds. To see how each DWS Fund compares with this industry observation, I reviewed:

- The trend in Fund assets over the last five years and the accompanying trend in total expenses. This shows if the Fund has grown and, if so, whether total expense (management fees as well as other expenses) have declined as a percent of assets.
- Whether the Fund has break-points in its management fee schedule, the extent of the fee reduction built into the schedule and the asset levels where the breaks take effect, and in the case of a sub-advised Fund how the Fund's break-points compare with those of the sub-advisory fee schedule.
- How the Fund's contractual fee schedule compares with trends in the industry data. To accomplish this, I constructed a chart showing how actual latest-fiscal-year contractual fees of the Fund and of other similar funds relate to average fund assets, with the subject Fund's contractual fee schedule superimposed.

### Quality of Service — Performance

The quality-of-service evaluation focused on investment performance, which is the principal result of the investment management service. Each Fund's performance was reviewed over the past 1, 3, 5 and 10 years, as applicable, and compared with that of other funds in the same investment category and with a suitable market index.

In addition, I calculated and reviewed risk-adjusted returns relative to an index of similar mutual funds' returns and a suitable market index. The risk-adjusted returns analysis provides a way of determining the extent to which the Fund's return comparisons are mainly the product of investment value-added (or lack thereof) or alternatively taking considerably more or less risk than is typical in its investment category.

I also received and considered the history of portfolio manager changes for each Fund, as this provided an important context for evaluating the performance results.

## Complex-Level Considerations

While this evaluation was conducted mainly at the individual fund level, there are some issues relating to the reasonableness of fees that can alternatively be considered across the whole fund complex:

- I reviewed DeAM's profitability analysis for all DWS Funds, with a view toward determining if the allocation procedures used were reasonable and how profit levels compared with public data for other investment managers.
- I considered whether DeAM and affiliates receive any significant ancillary or "fall-out" benefits that should be considered in interpreting the direct profitability results. These would be situations where serving as the investment manager of the Funds is beneficial to another part of the Deutsche Bank organization.
- I considered how aggregated DWS Fund expenses had varied over the years, by asset class and in the context of trends in asset levels.
- I reviewed the structure of the DeAM organization, trends in staffing levels, and information on compensation of investment management and other professionals compared with industry data.

## Findings

Based on the process and analysis discussed above, which included reviewing a wide range of information from management and external data sources and considering among other factors the fees DeAM charges other clients, the fees charged by other fund managers, DeAM's costs and profits associated with managing the Funds, economies of scale, possible fall-out benefits, and the nature and quality of services provided, in my opinion the management fees charged the DWS Funds are reasonable.

Thomas H. Mack

Thomas H. Mack

# Board Members and Officers

The following table presents certain information regarding the Board Members and Officers of the Trust as of December 31, 2010. Each Board Member's year of birth is set forth in parentheses after his or her name. Unless otherwise noted, (i) each Board Member has engaged in the principal occupation(s) noted in the table for at least the most recent five years, although not necessarily in the same capacity; and (ii) the address of each Independent Board Member is c/o Paul K. Freeman, Independent Chairman, DWS Funds, PO Box 101833, Denver, CO 80250-1833. Except as otherwise noted below, the term of office for each Board Member is until the election and qualification of a successor, or until such Board Member sooner dies, resigns, is removed or as otherwise provided in the governing documents of the fund. Because the fund does not hold an annual meeting of shareholders, each Board Member will hold office for an indeterminate period. The Board Members may also serve in similar capacities with other funds in the fund complex. The Length of Time Served represents the year in which the Board Member joined the board of one or more DWS funds now overseen by the Board.

### Independent Board Members

| Name, Year of Birth, Position with the Fund and Length of Time Served[1] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Paul K. Freeman (1950)<br>Chairperson since 2009<br>Board Member since 1993 | Consultant, World Bank/Inter-American Development Bank; Executive and Governing Council of the Independent Directors Council (education committees); formerly, Project Leader, International Institute for Applied Systems Analysis (1998–2001); Chief Executive Officer, The Eric Group, Inc. (environmental insurance) (1986–1998) | 122 |
| John W. Ballantine (1946)<br>Board Member since 1999 | Retired; formerly, Executive Vice President and Chief Risk Management Officer, First Chicago NBD Corporation/The First National Bank of Chicago (1996–1998); Executive Vice President and Head of International Banking (1995–1996). Directorships: Healthways, Inc. (provider of disease and care management services); Portland General Electric (utility company); Stockwell Capital Investments PLC (private equity). Former Directorships: First Oak Brook Bancshares, Inc. and Oak Brook Bank; Prisma Energy International | 122 |
| Henry P. Becton, Jr. (1943)<br>Board Member since 1990 | Vice Chair and former President, WGBH Educational Foundation. Directorships: Association of Public Television Stations; Lead Director, Becton Dickinson and Company[3] (medical technology company); Lead Director, Belo Corporation[3] (media company); Public Radio International; Public Radio Exchange (PRX); The PBS Foundation. Former Directorships: Boston Museum of Science; American Public Television; Concord Academy; New England Aquarium; Mass. Corporation for Educational Telecommunications; Committee for Economic Development; Public Broadcasting Service | 122 |
| Dawn-Marie Driscoll (1946)<br>Board Member since 1987 | President, Driscoll Associates (consulting firm); Executive Fellow, Center for Business Ethics, Bentley University; formerly, Partner, Palmer & Dodge (1988–1990); Vice President of Corporate Affairs and General Counsel, Filene's (1978–1988). Directorships: Trustee of 22 open-end mutual funds managed by Sun Capital Advisers, Inc. (since 2007); Director of ICI Mutual Insurance Company (since 2007); Advisory Board, Center for Business Ethics, Bentley University; Trustee, Southwest Florida Community Foundation (charitable organization). Former Directorships: Investment Company Institute (audit, executive, nominating committees) and Independent Directors Council (governance, executive committees) | 122 |
| Keith R. Fox (1954)<br>Board Member since 1996 | Managing General Partner, Exeter Capital Partners (a series of private investment funds). Directorships: Progressive International Corporation (kitchen goods importer and distributor); BoxTop Media Inc. (advertising); The Kennel Shop (retailer); former Chairman, National Association of Small Business Investment Companies | 122 |
| Kenneth C. Froewiss (1945)<br>Board Member since 2001 | Adjunct Professor of Finance, NYU Stern School of Business (September 2009–present; Clinical Professor from 1997–September 2009); Member, Finance Committee, Association for Asian Studies (2002–present); Director, Mitsui Sumitomo Insurance Group (US) (2004–present); prior thereto, Managing Director, J.P. Morgan (investment banking firm) (until 1996) | 122 |
| Richard J. Herring (1946)<br>Board Member since 1990 | Jacob Safra Professor of International Banking and Professor, Finance Department, The Wharton School, University of Pennsylvania (since July 1972); Co-Director, Wharton Financial Institutions Center (since July 2000); Co-Chair, U.S. Shadow Financial Regulatory Committee; Executive Director, Financial Economists Roundtable; Director, Japan Equity Fund, Inc. (since September 2007), Thai Capital Fund, Inc. (since September 2007), Singapore Fund, Inc. (since September 2007); Independent Director of Barclays Bank Delaware (since September 2010). Formerly, Vice Dean and Director, Wharton Undergraduate Division (July 1995–June 2000); Director, Lauder Institute of International Management Studies (July 2000–June 2006) | 122 |
| William McClayton (1944)<br>Board Member since 2004+ | Private equity investor (since October 2009); previously, Managing Director, Diamond Management & Technology Consultants, Inc. (global consulting firm) (2001–2009); Directorship: Board of Managers, YMCA of Metropolitan Chicago; formerly: Senior Partner, Arthur Andersen LLP (accounting) (1966–2001); Trustee, Ravinia Festival | 122 |

| Name, Year of Birth, Position with the Fund and Length of Time Served[1] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Rebecca W. Rimel (1951)<br>Board Member since 1995 | President and Chief Executive Officer, The Pew Charitable Trusts (charitable organization) (1994 to present); Trustee, Thomas Jefferson Foundation (charitable organization) (1994 to present); Trustee, Executive Committee, Philadelphia Chamber of Commerce (2001–2007); Director, CardioNet, Inc.[2] (2009–present) (health care). Formerly, Executive Vice President, The Glenmede Trust Company (investment trust and wealth management) (1983–2004); Board Member, Investor Education (charitable organization) (2004–2005); Director, Viasys Health Care[2] (January 2007–June 2007); Trustee, Pro Publica (charitable organization) (2007–2010) | 122 |
| William N. Searcy, Jr. (1946)<br>Board Member since 1993 | Private investor since October 2003; Trustee of 22 open-end mutual funds managed by Sun Capital Advisers, Inc. (since October 1998). Formerly, Pension & Savings Trust Officer, Sprint Corporation[2] (telecommunications) (November 1989–September 2003) | 122 |
| Jean Gleason Stromberg (1943)<br>Board Member since 1997 | Retired. Formerly, Consultant (1997–2001); Director, Financial Markets US Government Accountability Office (1996–1997); Partner, Fulbright & Jaworski, L.L.P. (law firm) (1978–1996). Directorships: The William and Flora Hewlett Foundation. Former Directorships: Service Source, Inc., Mutual Fund Directors Forum (2002–2004), American Bar Retirement Association (funding vehicle for retirement plans) (1987–1990 and 1994–1996) | 122 |
| Robert H. Wadsworth (1940)<br>Board Member since 1999 | President, Robert H. Wadsworth & Associates, Inc. (consulting firm) (1983 to present); Director, The Phoenix Boys Choir Association | 125 |

## Officers[4]

| Name, Year of Birth, Position with the Fund and Length of Time Served[5] | Principal Occupation(s) During Past 5 Years and Other Directorships Held |
|---|---|
| Michael G. Clark[6] (1965)<br>President, 2006–present | Managing Director[3], Deutsche Asset Management (2006–present); President of DWS family of funds; Director, ICI Mutual Insurance Company (since October 2007); formerly, Director of Fund Board Relations (2004–2006) and Director of Product Development (2000–2004), Merrill Lynch Investment Managers; Senior Vice President Operations, Merrill Lynch Asset Management (1999–2000) |
| Ingo Gefeke[7] (1967)<br>Executive Vice President since 2010 | Managing Director[3], Deutsche Asset Management; Global Head of Distribution and Product Management, DWS Global Head of Trading and Securities Lending. Member of the Board of Directors of DWS Investment GmbH Frankfurt (since July 2009) and DWS Holding & Service GmbH Frankfurt (since January 2010); formerly, Global Chief Administrative Officer, Deutsche Asset Management (2004–2009); Global Chief Operating Officer, Global Transaction Banking, Deutsche Bank AG, New York (2001–2004); Chief Operating Officer, Global Banking Division Americas, Deutsche Bank AG, New York (1999–2001); Central Management, Global Banking Services, Deutsche Bank AG, Frankfurt (1998–1999); Relationship Management, Deutsche Bank AG, Tokyo, Japan (1997–1998) |
| John Millette[8] (1962)<br>Vice President and Secretary, 1999–present | Director[3], Deutsche Asset Management |
| Paul H. Schubert[6] (1963)<br>Chief Financial Officer, 2004–present<br>Treasurer, 2005–present | Managing Director[3], Deutsche Asset Management (since July 2004); formerly, Executive Director, Head of Mutual Fund Services and Treasurer for UBS Family of Funds (1998–2004); Vice President and Director of Mutual Fund Finance at UBS Global Asset Management (1994–1998) |
| Caroline Pearson[8] (1962)<br>Chief Legal Officer, April 2010–present | Managing Director[3], Deutsche Asset Management; formerly, Assistant Secretary for DWS family of funds (1997–2010) |
| Rita Rubin[9] (1970)<br>Assistant Secretary, 2009–present | Vice President and Counsel, Deutsche Asset Management (since October 2007); formerly, Vice President, Morgan Stanley Investment Management (2004–2007) |
| Paul Antosca[8] (1957)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management (since 2006); Vice President, The Manufacturers Life Insurance Company (U.S.A.) (1990–2006) |
| Jack Clark[8] (1967)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management (since 2007); formerly, Vice President, State Street Corporation (2002–2007) |
| Diane Kenneally[8] (1966)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management |
| John Caruso[9] (1965)<br>Anti-Money Laundering Compliance Officer, 2010–present | Managing Director[3], Deutsche Asset Management |

| Name, Year of Birth, Position with the Fund and Length of Time Served[5] | Principal Occupation(s) During Past 5 Years and Other Directorships Held |
|---|---|
| Robert Kloby[9] (1962)<br>Chief Compliance Officer, 2006–present | Managing Director[3], Deutsche Asset Management |

1 *The length of time served represents the year in which the Board Member joined the board of one or more DWS funds currently overseen by the Board.*

2 *A publicly held company with securities registered pursuant to Section 12 of the Securities Exchange Act of 1934.*

3 *Executive title, not a board directorship.*

4 *As a result of their respective positions held with the Advisor, these individuals are considered "interested persons" of the Advisor within the meaning of the 1940 Act. Interested persons receive no compensation from the fund.*

5 *The length of time served represents the year in which the officer was first elected in such capacity for one or more DWS funds.*

6 *Address: 100 Plaza One, Jersey City, NJ 07311.*

7 *Effective January 11, 2011, Mr. Gefeke, Executive Vice President, resigned as an officer of the fund.*

*The mailing address of Mr. Gefeke is 345 Park Avenue, New York, New York 10154. Mr. Gefeke was an interested Board Member of certain DWS funds by virtue of his positions with Deutsche Asset Management. As an interested person, Mr. Gefeke received no compensation from the fund.*

8 *Address: One Beacon Street, Boston, MA 02108.*

9 *Address: 60 Wall Street, New York, New York 10005.*

*The fund's Statement of Additional Information ("SAI") includes additional information about the Board Members. The SAI is available, without charge, upon request. If you would like to request a copy of the SAI, you may do so by calling the following toll-free number: (800) 728-3337.*

DWS Investments is part of Deutsche Bank's Asset Management division and, within the US, represents the retail asset management activities of Deutsche Bank AG, Deutsche Bank Trust Company Americas, Deutsche Investment Management Americas Inc. and DWS Trust Company.

The views expressed in this report reflect those of the portfolio managers only through the end of the period of the report as stated on the cover. The managers' views are subject to change at any time based on market and other conditions and should not be construed as a recommendation.

This information must be preceded or accompanied by a current prospectus.

Portfolio changes should not be considered recommendations for action by individual investors.

DWS Investments Distributors, Inc.
222 South Riverside Plaza
Chicago, IL 60606
(800) 621-1148

VS1groinc-2 (2/11)

DWS INVESTMENTS
Deutsche Bank Group

DECEMBER 31, 2010

# ANNUAL REPORT

## DWS VARIABLE SERIES I

## DWS Health Care VIP

**This report must be preceded or accompanied by a prospectus. To obtain an additional prospectus or summary prospectus, if available, call (800) 728-3337 or your financial representative. We advise you to consider the Fund's objectives, risks, charges and expenses carefully before investing. The summary prospectus and prospectus contain this and other important information about the Fund. Please read the prospectus carefully before you invest.**

*Investments in variable insurance portfolios (VIPs) involve risk. Stocks may decline in value. Bond investments are subject to interest-rate and credit risks. When interest rates rise, bond prices generally fall. Credit risk refers to the ability of an issuer to make timely payments of principal and interest. Investing in derivatives entails special risks relating to liquidity, leverage and credit that may reduce returns and/or increased volatility. Investing in foreign securities, particularly those of emerging markets, presents certain risks, such as currency fluctuations, political and economic changes, and market risks. There are additional risks associated with investing in commodities, high-yield bonds, aggressive growth stocks, non-diversified/ concentrated funds and small- and mid-cap stocks which are more fully explained in the prospectuses. Please read the prospectus for more information.*

*DWS Investments is part of Deutsche Bank's Asset Management division and, within the US, represents the retail asset management activities of Deutsche Bank AG, Deutsche Bank Trust Company Americas, Deutsche Investment Management Americas Inc. and DWS Trust Company.*

*NOT FDIC/NCUA INSURED NO BANK GUARANTEE MAY LOSE VALUE NOT A DEPOSIT*
*NOT INSURED BY ANY FEDERAL GOVERNMENT AGENCY*

DWS INVESTMENTS
Deutsche Bank Group

# Performance Summary

**December 31, 2010**

## DWS Health Care VIP

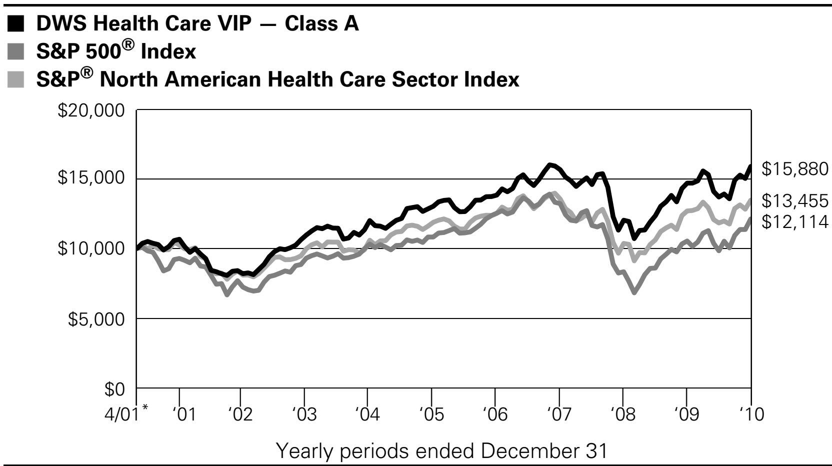
**All performance shown is historical, assumes reinvestment of all dividend and capital gain distributions, and does not guarantee future results. Investment return and principal value fluctuate with changing market conditions so that, when redeemed, shares may be worth more or less then their original cost. Current performance may be lower or higher than the performance data quoted. Please contact your participating insurance company for the Fund's most recent month-end performance. Performance doesn't reflect charges and fees ("contract charges") associated with the separate account that invests in the Fund or any variable life insurance policy or variable annuity contract for which the Fund is an investment option. These charges and fees will reduce returns. While all share classes have the same underlying portfolio, their performance will differ.**

**The gross expense ratios of the Fund, as stated in the fee table of the prospectus dated May 1, 2010 are 0.96% and 1.34% for Class A and Class B shares, respectively, and may differ from the expense ratios disclosed in the Financial Highlights tables in this report.**

### Risk Considerations

Any fund that concentrates in a particular segment of the market will generally be more volatile than a fund that invests more broadly. Stocks may decline in value. See the prospectus for details.

### Growth of an Assumed $10,000 Investment




*The Standard & Poor's® 500 (S&P 500) Index is an unmanaged, capitalization-weighted index of 500 stocks. The index is designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries. The S&P® North American Health Care Sector Index is an unmanaged, market-capitalization weighted index of 123 stocks designed to measure the performance of companies in the health care sector.*

*Index returns assume the reinvestment of dividends and, unlike fund returns, do not reflect any fees or expenses. It is not possible to invest directly into an index.*

### Comparative Results

| DWS Health Care VIP | | 1-Year | 3-Year | 5-Year | Life of Fund* |
|---|---|---|---|---|---|
| **Class A** | Growth of $10,000 | $10,815 | $10,149 | $12,197 | $15,880 |
| | Average annual total return | 8.15% | .49% | 4.05% | 4.89% |
| S&P 500 Index | Growth of $10,000 | $11,506 | $9,168 | $11,199 | $12,114 |
| | Average annual total return | 15.06% | –2.86% | 2.29% | 2.00% |
| S&P North American Health Care Sector Index | Growth of $10,000 | $10,608 | $9,929 | $11,333 | $13,455 |
| | Average annual total return | 6.08% | –.24% | 2.53% | 3.12% |

| DWS Health Care VIP | | 1-Year | 3-Year | 5-Year | Life of Class** |
|---|---|---|---|---|---|
| **Class B** | Growth of $10,000 | $10,768 | $10,034 | $11,980 | $19,059 |
| | Average annual total return | 7.68% | .11% | 3.68% | 7.88% |
| S&P 500 Index | Growth of $10,000 | $11,506 | $9,168 | $11,199 | $15,038 |
| | Average annual total return | 15.06% | –2.86% | 2.29% | 4.92% |
| S&P North American Health Care Sector Index | Growth of $10,000 | $10,608 | $9,929 | $11,333 | $16,109 |
| | Average annual total return | 6.08% | –.24% | 2.53% | 5.76% |

*The growth of $10,000 is cumulative.*

* *The Fund commenced operations on May 1, 2001. Index returns began on April 30, 2001.*

** *The Fund commenced offering Class B shares on July 1, 2002. Index returns began on June 30, 2002.*

# Information About Your Fund's Expenses

## DWS Health Care VIP

As an investor of the Fund, you incur two types of costs: ongoing expenses and transaction costs. Ongoing expenses include management fees, distribution and service (12b-1) fees and other Fund expenses. Examples of transaction costs include contract charges, redemption fees and account maintenance fees, which are not shown in this section. The following tables are intended to help you understand your ongoing expenses (in dollars) of investing in the Fund and to help you compare these expenses with the ongoing expenses of investing in other mutual funds. The example in the table is based on an investment of $1,000 invested at the beginning of the six-month period and held for the entire period (July 1, 2010 to December 31, 2010).

The tables illustrate your Fund's expenses in two ways:

- **Actual Fund Return.** This helps you estimate the actual dollar amount of ongoing expenses (but not transaction costs) paid on a $1,000 investment in the Fund using the Fund's actual return during the period. To estimate the expenses you paid over the period, simply divide your account value by $1,000 (for example, an $8,600 account value divided by $1,000 = 8.6), then multiply the result by the number in the "Expenses Paid per $1,000" line under the share class you hold.
- **Hypothetical 5% Fund Return.** This helps you to compare your Fund's ongoing expenses (but not transaction costs) with those of other mutual funds using the Fund's actual expense ratio and a hypothetical rate of return of 5% per year before expenses. Examples using a 5% hypothetical Fund return may be found in the shareholder reports of other mutual funds. The hypothetical account values and expenses may not be used to estimate the actual ending account balance or expenses you paid for the period.

Please note that the expenses shown in these tables are meant to highlight your ongoing expenses only and do not reflect any transaction costs. The "Expenses Paid per $1,000" line of the tables is useful in comparing ongoing expenses only and will not help you determine the relative total expense of owning different funds. If these transaction costs had been included, your costs would have been higher.

**Expenses and Value of a $1,000 Investment** for the six months ended December 31, 2010

| **Actual Fund Return** | **Class A** | **Class B** |
|---|---|---|
| Beginning Account Value 7/1/10 | $1,000.00 | $1,000.00 |
| Ending Account Value 12/31/10 | $1,160.70 | $1,158.90 |
| Expenses Paid per $1,000* | $ 4.30 | $ 6.20 |
| **Hypothetical 5% Fund Return** | **Class A** | **Class B** |
| Beginning Account Value 7/1/10 | $1,000.00 | $1,000.00 |
| Ending Account Value 12/31/10 | $1,021.22 | $1,019.46 |
| Expenses Paid per $1,000* | $ 4.02 | $ 5.80 |

* *Expenses are equal to the Fund's annualized expense ratio for each share class, multiplied by the average account value over the period, multiplied by the number of days in the most recent six-month period, then divided by 365.*

| **Annualized Expense Ratios** | **Class A** | **Class B** |
|---|---|---|
| DWS Variable Series I — DWS Health Care VIP | .79% | 1.14% |

For more information, please refer to the Fund's prospectus.

These tables do not reflect charges and fees ("contract charges") associated with the separate account that invests in the Fund or any variable life insurance policy or variable annuity contract for which the Fund is an investment option.

## DWS Health Care VIP

For 2010, health care underperformed the broader market as investors continued to prefer companies leveraged to global economic recovery. Additionally, lower health care consumption (e.g., fewer medical procedures and physician visits) and pricing pressures from European Union governments' austerity programs weighed on the sector. For its most recent fiscal year ended December 31, 2010, DWS Health Care VIP returned 8.15% (Class A shares, unadjusted for contract charges). In comparison, the Standard & Poor's 500® (S&P 500) Index returned 15.06% and the S&P® North American Health Care Sector Index returned 6.08%. (Past performance is no guarantee of future results.)

Our overweight to several biotechnology stocks contributed significantly to performance during the year.[1] Alexion Pharmaceuticals, Inc. appreciated meaningfully following continued strong sales of Soliris, its drug for a rare disorder in which the body destroys red blood cells, and early clinical data demonstrating the drug's potential for treatment of other disorders. Incyte Corp. shares benefited from positive clinical data for its drug under development for myelofibrosis, a life-threatening blood cancer, as well as progress regarding its oral drug for rheumatoid arthritis. The largest detractor from relative performance during the 12-month period came from the Fund's position in Roche Holding AG. Shares of Roche declined as the company experienced several setbacks in its drug pipeline. We trimmed our position in Roche during the period.

Longer term, we believe that health care stocks remain attractive based on favorable global demographic trends and the continuing emergence of new technologies.

*The following person is responsible for the day-to-day management of the Fund:*

Leefin Lai, CFA
*Portfolio Manager*

*The following person serves as consultant to the Advisor:*

Thomas E. Bucher, CFA
*Consultant*

*The Standard & Poor's 500 (S&P 500) Index is an unmanaged, capitalization-weighted index of 500 stocks. The index is designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries.*

*The S&P North American Health Care Sector Index is an unmanaged, market-capitalization-weighted index of 123 stocks designed to measure the performance of companies in the health care sector.*

*Index returns assume the reinvestment of dividends and, unlike fund returns, do not reflect any fees or expenses. It is not possible to invest directly into an index.*

1 *"Overweight" means the Fund holds a higher weighting in a given sector or security than the benchmark. "Underweight" means the Fund holds a lower weighting.*

*Portfolio management market commentary is as of December 31, 2010, and may not come to pass. This information is subject to change at any time based on market and other conditions. Past performance does not guarantee future results. Current and future portfolio holdings are subject to risk.*

# Portfolio Summary

## DWS Health Care VIP

| **Asset Allocation** (As a % of Investment Portfolio excluding Securities Lending Collateral) | **12/31/10** | **12/31/09** |
|---|---|---|
| Common Stocks | 98% | 100% |
| Cash Equivalents | 2% | — |
| | 100% | 100% |

| **Industry Diversification** (As a % of Common Stocks) | **12/31/10** | **12/31/09** |
|---|---|---|
| Pharmaceuticals | 32% | 34% |
| Biotechnology | 25% | 23% |
| Health Care Services | 19% | 17% |
| Medical Supply & Specialty | 18% | 20% |
| Life Sciences Equipment | 6% | 6% |
| | 100% | 100% |

*Asset allocation and industry diversification are subject to change.*

*For more complete details about the Fund's investment portfolio, see page 6.*

Following the Fund's fiscal first and third quarter-end, a complete portfolio holdings listing is filed with the SEC on Form N-Q. The form will be available on the SEC's Web site at www.sec.gov, and it also may be reviewed and copied at the SEC's Public Reference Room in Washington, D.C. Information on the operation of the SEC's Public Reference Room may be obtained by calling (800) SEC-0330. The Fund's portfolio holdings are also posted on www.dws-investments.com from time to time. Please see the Fund's current prospectus for more information.

## DWS Health Care VIP

| | Shares | Value ($) |
|---|---|---|
| **Common Stocks 97.5%** | | |
| **Health Care 97.5%** | | |
| **Biotechnology 24.0%** | | |
| Acorda Therapeutics, Inc.* (a) | 5,300 | 144,478 |
| Alexion Pharmaceuticals, Inc.* | 12,261 | 987,624 |
| Allos Therapeutics, Inc.* | 21,526 | 99,235 |
| AMAG Pharmaceuticals, Inc.* | 5,095 | 92,219 |
| Amgen, Inc.* (a) | 26,038 | 1,429,486 |
| Amylin Pharmaceuticals, Inc.* (a) | 11,727 | 172,504 |
| ArQule, Inc.* (a) | 21,500 | 126,205 |
| Biogen Idec, Inc.* (a) | 9,141 | 612,904 |
| BioMarin Pharmaceutical, Inc.* (a) | 22,673 | 610,584 |
| Celera Corp.* | 26,966 | 169,886 |
| Celgene Corp.* (a) | 21,411 | 1,266,247 |
| Dendreon Corp.* | 6,266 | 218,809 |
| Exelixis, Inc.* (a) | 17,859 | 146,622 |
| Gen-Probe, Inc.* (a) | 5,900 | 344,265 |
| Genzyme Corp.* | 11,203 | 797,654 |
| Gilead Sciences, Inc.* | 22,983 | 832,904 |
| Halozyme Therapeutics, Inc.* (a) | 32,400 | 256,608 |
| Human Genome Sciences, Inc.* (a) | 11,969 | 285,939 |
| ImmunoGen, Inc.* (a) | 24,500 | 226,870 |
| Immunomedics, Inc.* (a) | 29,700 | 106,326 |
| Incyte Corp.* (a) | 29,112 | 482,095 |
| Intercell AG* | 5,637 | 87,480 |
| InterMune, Inc.* | 4,000 | 145,600 |
| Myriad Genetics, Inc.* (a) | 3,761 | 85,901 |
| Onyx Pharmaceuticals, Inc.* (a) | 5,261 | 193,973 |
| Regeneron Pharmaceuticals, Inc.* (a) | 10,800 | 354,564 |
| Savient Pharmaceuticals, Inc.* | 7,315 | 81,489 |
| Theravance, Inc.* (a) | 5,042 | 126,403 |
| United Therapeutics Corp.* (a) | 7,959 | 503,168 |
| Vertex Pharmaceuticals, Inc.* (a) | 18,700 | 655,061 |
| | | **11,643,103** |
| **Health Care Services 18.9%** | | |
| Aetna, Inc. | 16,400 | 500,364 |
| Allscripts Healthcare Solutions, Inc.* | 13,589 | 261,860 |
| Cardinal Health, Inc. | 14,100 | 540,171 |
| Cerner Corp.* (a) | 5,258 | 498,143 |
| CIGNA Corp. | 11,300 | 414,258 |
| Coventry Health Care, Inc.* | 8,500 | 224,400 |
| CVS Caremark Corp. | 14,931 | 519,151 |
| Express Scripts, Inc.* | 19,242 | 1,040,030 |
| Fresenius Medical Care AG & Co. KGaA | 13,433 | 776,212 |
| Genoptix, Inc.* | 4,603 | 87,549 |
| Laboratory Corp. of America Holdings* (a) | 3,895 | 342,448 |
| McKesson Corp. | 14,210 | 1,000,100 |
| MedAssets, Inc.* (a) | 6,976 | 140,845 |
| Medco Health Solutions, Inc.* | 13,573 | 831,618 |
| Quest Diagnostics, Inc. | 5,836 | 314,969 |
| Tenet Healthcare Corp.* | 21,540 | 144,103 |
| UnitedHealth Group, Inc. | 34,767 | 1,255,436 |
| WellPoint, Inc.* | 4,600 | 261,556 |
| | | **9,153,213** |
| **Life Sciences Tools & Services 6.1%** | | |
| Illumina, Inc.* (a) | 1,707 | 108,121 |
| Life Technologies Corp.* | 17,606 | 977,133 |
| Mettler-Toledo International, Inc.* | 1,540 | 232,864 |
| PerkinElmer, Inc. (a) | 15,490 | 399,952 |
| Thermo Fisher Scientific, Inc.* | 16,598 | 918,865 |
| Waters Corp.* | 4,148 | 322,341 |
| | | **2,959,276** |
| **Medical Supply & Specialty 17.7%** | | |
| Accuray, Inc.* | 11,500 | 77,625 |
| American Medical Systems Holdings, Inc.* | 12,296 | 231,902 |
| Baxter International, Inc. | 22,514 | 1,139,659 |
| Beckman Coulter, Inc. | 714 | 53,714 |
| Becton, Dickinson & Co. (a) | 8,264 | 698,473 |
| BioMimetic Therapeutics, Inc.* | 5,936 | 75,387 |
| C.R. Bard, Inc. | 4,526 | 415,351 |
| Covidien PLC | 22,976 | 1,049,084 |
| Hologic, Inc.* | 8,799 | 165,597 |
| Kinetic Concepts, Inc.* (a) | 6,914 | 289,558 |
| Masimo Corp. (a) | 5,400 | 156,978 |
| Medtronic, Inc. | 33,449 | 1,240,623 |
| Owens & Minor, Inc. (a) | 4,241 | 124,813 |
| Sirona Dental Systems, Inc.* (a) | 3,711 | 155,046 |
| Spectranetics Corp.* | 16,885 | 87,127 |
| St. Jude Medical, Inc.* | 19,000 | 812,250 |
| Stryker Corp. (a) | 10,298 | 553,003 |
| Thoratec Corp.* (a) | 7,921 | 224,323 |
| Varian Medical Systems, Inc.* | 2,686 | 186,086 |
| Wright Medical Group, Inc.* | 5,945 | 92,326 |
| Zimmer Holdings, Inc.* (a) | 13,603 | 730,209 |
| | | **8,559,134** |
| **Pharmaceuticals 30.8%** | | |
| Abbott Laboratories | 30,292 | 1,451,290 |
| Allergan, Inc. | 8,500 | 583,695 |
| Ardea Biosciences, Inc.* | 7,300 | 189,800 |
| Auxilium Pharmaceuticals, Inc.* (a) | 11,211 | 236,552 |
| Bristol-Myers Squibb Co. | 41,884 | 1,109,088 |
| Cardiome Pharma Corp.* | 14,200 | 91,164 |
| Cephalon, Inc.* (a) | 4,396 | 271,321 |
| Eli Lilly & Co. (a) | 6,678 | 233,997 |
| Forest Laboratories, Inc.* | 15,000 | 479,700 |
| Impax Laboratories, Inc.* | 12,712 | 255,638 |
| Inspire Pharmaceuticals, Inc.* | 22,300 | 187,320 |
| Ironwood Pharmaceuticals, Inc. "A"* | 4,500 | 46,575 |
| Johnson & Johnson | 28,150 | 1,741,077 |
| Merck & Co., Inc. | 54,753 | 1,973,298 |
| Mylan, Inc.* | 36,566 | 772,640 |
| Novartis AG (Registered) | 12,139 | 714,314 |
| Pfizer, Inc. | 134,911 | 2,362,292 |
| Pharmasset, Inc.* (a) | 2,987 | 129,666 |
| Questcor Pharmaceuticals, Inc.* (a) | 14,822 | 218,328 |
| Roche Holding AG (Genusschein) | 3,522 | 516,299 |
| Salix Pharmaceuticals Ltd.* (a) | 7,700 | 361,592 |
| Shire PLC (ADR) (a) | 6,532 | 472,786 |
| Valeant Pharmaceuticals International, Inc. | 17,054 | 482,458 |
| VIVUS, Inc.* (a) | 2,999 | 28,101 |
| | | **14,908,991** |
| **Total Common Stocks** (Cost $33,443,187) | | **47,223,717** |

*The accompanying notes are an integral part of the financial statements.*

| | Shares | Value ($) |
|---|---|---|
| **Securities Lending Collateral 26.8%** | | |
| Daily Assets Fund Institutional, 0.27% (b) (c) (Cost $12,965,325) | 12,965,325 | **12,965,325** |
| **Cash Equivalents 2.4%** | | |
| Central Cash Management Fund, 0.19% (b) (Cost $1,171,099) | 1,171,099 | **1,171,099** |

| | % of Net Assets | Value ($) |
|---|---|---|
| **Total Investment Portfolio** (Cost $47,579,611)† | 126.7 | **61,360,141** |
| **Other Assets and Liabilities, Net** | (26.7) | **(12,949,111)** |
| **Net Assets** | 100.0 | **48,411,030** |

* *Non-income producing security.*

† *The cost for federal income tax purposes was $48,011,212. At December 31, 2010, net unrealized appreciation for all securities based on tax cost was $13,348,929. This consisted of aggregate gross unrealized appreciation for all securities in which there was an excess of value over tax cost of $14,541,563 and aggregate gross unrealized depreciation for all securities in which there was an excess of tax cost over value of $1,192,634.*

(a) *All or a portion of these securities were on loan (see Notes to Financial Statements). The value of all securities loaned at December 31, 2010 amounted to $12,570,150, which is 26.0% of net assets.*

(b) *Affiliated fund managed by Deutsche Investment Management Americas Inc. The rate shown is the annualized seven-day yield at period end.*

(c) *Represents collateral held in connection with securities lending. Income earned by the Fund is net of borrower rebates.*

*ADR: American Depositary Receipt*

### Fair Value Measurements

*Various inputs are used in determining the value of the Fund's investments. These inputs are summarized in three broad levels. Level 1 includes quoted prices in active markets for identical securities. Level 2 includes other significant observable inputs (including quoted prices for similar securities, interest rates, prepayment speeds, and credit risk). Level 3 includes significant unobservable inputs (including the Fund's own assumptions in determining the fair value of investments). The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities.*

*The following is a summary of the inputs used as of December 31, 2010 in valuing the Fund's investments. For information on the Fund's policy regarding the valuation of investments, please refer to the Security Valuation section of Note A in the accompanying Notes to Financial Statements.*

| Assets | Level 1 | Level 2 | Level 3 | Total |
|---|---|---|---|---|
| Common Stocks | | | | |
| Biotechnology | $ 11,555,623 | $ 87,480 | $ — | $ 11,643,103 |
| Health Care Services | 8,377,001 | 776,212 | — | 9,153,213 |
| Life Sciences Tools & Specialty | 2,959,276 | — | — | 2,959,276 |
| Medical Supply & Specialty | 8,559,134 | — | — | 8,559,134 |
| Pharmaceuticals | 13,678,378 | 1,230,613 | — | 14,908,991 |
| Short-Term Investments (d) | 14,136,424 | — | — | 14,136,424 |
| **Total** | **$ 59,265,836** | **$ 2,094,305** | **$ —** | **$ 61,360,141** |

*There have been no significant transfers in and out of Level 1 and Level 2 fair value measurements during the year ended December 31, 2010.*

(d) *See Investment Portfolio for additional detailed categorizations.*

*The accompanying notes are an integral part of the financial statements.*

# Statement of Assets and Liabilities

as of December 31, 2010

| Assets | | |
|---|---|---|
| Investments: | | |
| Investments in securities, at value (cost $33,443,187), including $12,570,150 of securities loaned | $ | 47,223,717 |
| Investment in Daily Assets Fund Institutional (cost $12,965,325)* | | 12,965,325 |
| Investment in Central Cash Management Fund (cost $1,171,099) | | 1,171,099 |
| Total investments, at value (cost $47,579,611) | | 61,360,141 |
| Foreign currency, at value (cost $130) | | 132 |
| Receivable for investments sold | | 28,704 |
| Receivable for Fund shares sold | | 30,920 |
| Interest receivable | | 1,364 |
| Dividends receivable | | 34,946 |
| Foreign taxes recoverable | | 16,873 |
| Other assets | | 270 |
| Total assets | | 61,473,350 |
| **Liabilities** | | |
| Payable upon return of securities loaned | | 12,965,325 |
| Payable for Fund shares redeemed | | 15,277 |
| Accrued management fee | | 26,793 |
| Accrued distribution service fee (Class B) | | 637 |
| Other accrued expenses and payables | | 54,288 |
| Total liabilities | | 13,062,320 |
| **Net assets, at value** | **$** | **48,411,030** |
| **Net Assets Consist of** | | |
| Undistributed net investment income | | 251,765 |
| Net unrealized appreciation (depreciation) on: | | |
| Investments | | 13,780,530 |
| Foreign currency | | 2,439 |
| Accumulated net realized gain (loss) | | 1,145,472 |
| Paid-in capital | | 33,230,824 |
| **Net assets, at value** | **$** | **48,411,030** |
| **Class A** | | |
| **Net Asset Value,** offering and redemption price per share ($45,390,479 ÷ 4,002,304 outstanding shares of beneficial interest, $.01 par value, unlimited number of shares authorized) | **$** | **11.34** |
| **Class B** | | |
| **Net Asset Value,** offering and redemption price per share ($3,020,551 ÷ 274,245 outstanding shares of beneficial interest, $.01 par value, unlimited number of shares authorized) | **$** | **11.01** |

* *Represents collateral on securities loaned.*

# Statement of Operations

for the year ended December 31, 2010

| Investment Income | | |
|---|---|---|
| Income: | | |
| Dividends (net of foreign taxes withheld of $15,568) | $ | 680,141 |
| Income distributions — Central Cash Management Fund | | 1,440 |
| Securities lending income, including income from Daily Assets Fund Institutional, net of borrower rebates | | 18,213 |
| Total income | | 699,794 |
| Expenses: | | |
| Management fee | | 328,345 |
| Administration fee | | 49,375 |
| Services to Shareholders | | 2,211 |
| Record keeping fee (Class B) | | 2,927 |
| Custodian fee | | 10,321 |
| Distribution service fee (Class B) | | 7,384 |
| Audit and tax fees | | 29,355 |
| Legal fees | | 17,332 |
| Trustees' fees and expenses | | 3,736 |
| Other | | 4,824 |
| Total expenses | | 455,810 |
| **Net investment income** | | **243,984** |
| **Realized and Unrealized Gain (Loss)** | | |
| Net realized gain (loss) from: | | |
| Investments | | 1,617,209 |
| Foreign currency | | 7,781 |
| | | 1,624,990 |
| Change in net unrealized appreciation (depreciation) on: | | |
| Investments | | 1,802,611 |
| Foreign currency | | 6,567 |
| | | 1,809,178 |
| **Net gain (loss)** | | **3,434,168** |
| **Net increase (decrease) in net assets resulting from operations** | **$** | **3,678,152** |

*The accompanying notes are an integral part of the financial statements.*

# Statement of Changes in Net Assets

| Increase (Decrease) in Net Assets | Years Ended December 31, 2010 | 2009 |
|---|---|---|
| Operations: | | |
| Net investment income | $ 243,984 | $ (54,312) |
| Net realized gain (loss) | 1,624,990 | 4,360,035 |
| Change in net unrealized appreciation (depreciation) | 1,809,178 | 5,459,026 |
| Net increase (decrease) in net assets resulting from operations | 3,678,152 | 9,764,749 |
| Distributions to shareholders from: | | |
| Net investment income: | | |
| Class A | — | (711,488) |
| Class B | — | (35,875) |
| Net realized gains: | | |
| Class A | (3,243,143) | (673,607) |
| Class B | (203,682) | (45,473) |
| Total distributions | (3,446,825) | (1,466,443) |
| Fund share transactions: | | |
| **Class A** | | |
| Proceeds from shares sold | 4,393,397 | 3,080,971 |
| Reinvestment of distributions | 3,243,143 | 1,385,095 |
| Cost of shares redeemed | (11,708,727) | (23,233,574) |
| Net increase (decrease) in net assets from Class A share transactions | (4,072,187) | (18,767,508) |
| **Class B** | | |
| Proceeds from shares sold | 286,173 | 467,768 |
| Reinvestment of distributions | 203,682 | 81,348 |
| Cost of shares redeemed | (570,175) | (1,479,410) |
| Net increase (decrease) in net assets from Class B share transactions | (80,320) | (930,294) |
| **Increase (decrease) in net assets** | (3,921,180) | (11,399,496) |
| Net assets at beginning of period | 52,332,210 | 63,731,706 |
| Net assets at end of period (including undistributed net investment income of $251,765 and $0, respectively) | **$ 48,411,030** | **$ 52,332,210** |

| Other Information | | |
|---|---|---|
| **Class A** | | |
| Shares outstanding at beginning of period | 4,392,554 | 6,373,629 |
| Shares sold | 401,779 | 320,687 |
| Shares issued to shareholders in reinvestment of distributions | 294,563 | 164,892 |
| Shares redeemed | (1,086,592) | (2,466,654) |
| Net increase (decrease) in Class A shares | (390,250) | (1,981,075) |
| Shares outstanding at end of period | **4,002,304** | **4,392,554** |
| **Class B** | | |
| Shares outstanding at beginning of period | 281,083 | 379,018 |
| Shares sold | 27,448 | 50,217 |
| Shares issued to shareholders in reinvestment of distributions | 19,000 | 9,896 |
| Shares redeemed | (53,286) | (158,048) |
| Net increase (decrease) in Class B shares | (6,838) | (97,935) |
| Shares outstanding at end of period | **274,245** | **281,083** |

*The accompanying notes are an integral part of the financial statements.*

# Financial Highlights

## Class A

| Years Ended December 31, | 2010 | 2009 | 2008 | 2007 | 2006 |
|---|---|---|---|---|---|
| **Selected Per Share Data** | | | | | |
| **Net asset value, beginning of period** | **$11.21** | **$ 9.45** | **$14.68** | **$13.77** | **$13.02** |
| *Income (loss) from investment operations:* | | | | | |
| Net investment income (loss)[a] | .06 | (.01) | .09[c] | .03[c] | (.01)[b] |
| Net realized and unrealized gain (loss) | .83 | 2.02 | (3.08) | 1.75 | .81 |
| **Total from investment operations** | .89 | 2.01 | (2.99) | 1.78 | .80 |
| *Less distributions from:* | | | | | |
| Net investment income | — | (.13) | (.04) | — | — |
| Net realized gains | (.76) | (.12) | (2.20) | (.87) | (.05) |
| **Total distributions** | (.76) | (.25) | (2.24) | (.87) | (.05) |
| **Net asset value, end of period** | **$11.34** | **$11.21** | **$ 9.45** | **$14.68** | **$13.77** |
| Total Return (%) | 8.15 | 22.19 | (23.20) | 13.20 | 6.17[b] |
| **Ratios to Average Net Assets and Supplemental Data** | | | | | |
| Net assets, end of period ($ millions) | 45 | 49 | 60 | 98 | 101 |
| Ratio of expenses (%) | .90 | .96 | .92 | .93 | .89 |
| Ratio of net investment income (loss) (%) | .52 | (.08) | .79[c] | .19[c] | (.03)[b] |
| Portfolio turnover rate (%) | 16 | 31 | 24 | 37 | 47 |

a *Based on average shares outstanding during the period.*

b *Includes non-recurring income from the Advisor recorded as a result of an administrative proceeding regarding disclosure of brokerage allocation practices in connection with sales of DWS Funds. The non-recurring income resulted in an increase in net investment income of $0.003 per share and an increase in the ratio of net investment income of 0.02%. Excluding this non-recurring income, total return would have been 0.02% lower.*

c *Net investment income per share and ratio of net investment income include non-recurring dividend income amounting to $0.03 and $0.02 per share and 0.28% and 0.13% of average daily net assets for the years ended December 31, 2008 and 2007, respectively.*

## Class B

| Years Ended December 31, | 2010 | 2009 | 2008 | 2007 | 2006 |
|---|---|---|---|---|---|
| **Selected Per Share Data** | | | | | |
| **Net asset value, beginning of period** | **$10.95** | **$ 9.23** | **$14.40** | **$13.55** | **$12.87** |
| *Income (loss) from investment operations:* | | | | | |
| Net investment income (loss)[a] | .02 | (.04) | .05[c] | (.03)[c] | (.06)[b] |
| Net realized and unrealized gain (loss) | .80 | 1.98 | (3.02) | 1.75 | .79 |
| **Total from investment operations** | .82 | 1.94 | (2.97) | 1.72 | .73 |
| *Less distributions from:* | | | | | |
| Net investment income | — | (.10) | — | — | — |
| Net realized gains | (.76) | (.12) | (2.20) | (.87) | (.05) |
| **Total distributions** | (.76) | (.22) | (2.20) | (.87) | (.05) |
| **Net asset value, end of period** | **$11.01** | **$10.95** | **$ 9.23** | **$14.40** | **$13.55** |
| Total Return (%) | 7.68 | 21.80 | (23.50) | 12.88 | 5.77[b] |
| **Ratios to Average Net Assets and Supplemental Data** | | | | | |
| Net assets, end of period ($ millions) | 3 | 3 | 3 | 5 | 21 |
| Ratio of expenses (%) | 1.25 | 1.34 | 1.27 | 1.34 | 1.28 |
| Ratio of net investment income (loss) (%) | .16 | (.46) | .43[c] | (.22)[c] | (.42)[b] |
| Portfolio turnover rate (%) | 16 | 31 | 24 | 37 | 47 |

a *Based on average shares outstanding during the period.*

b *Includes non-recurring income from the Advisor recorded as a result of an administrative proceeding regarding disclosure of brokerage allocation practices in connection with sales of DWS Funds. The non-recurring income resulted in an increase in net investment income of $0.003 per share and an increase in the ratio of net investment income of 0.02%. Excluding this non-recurring income, total return would have been 0.02% lower.*

c *Net investment income per share and ratio of net investment income include non-recurring dividend income amounting to $0.03 and $0.02 per share and 0.28% and 0.13% of average daily net assets for the year ended December 31, 2008 and 2007, respectively.*

# Notes to Financial Statements

## A. Organization and Significant Accounting Policies

DWS Variable Series I (the "Series") is registered under the Investment Company Act of 1940, as amended (the "1940 Act"), as an open-end, registered management investment company organized as a Massachusetts business trust. The Series consists of six diversified funds: DWS Bond VIP, DWS Growth & Income VIP, DWS Capital Growth VIP, DWS Global Opportunities VIP, DWS International VIP and DWS Health Care VIP (individually or collectively hereinafter referred to as a "Fund" or the "Funds"). These financial statements report on DWS Health Care VIP. The Series is intended to be the underlying investment vehicle for variable annuity contracts and variable life insurance policies to be offered by the separate accounts of certain life insurance companies ("Participating Insurance Companies").

**Multiple Classes of Shares of Beneficial Interest.** The Fund offers two classes of shares (Class A shares and Class B shares). Class B shares are subject to Rule 12b-1 distribution fees under the 1940 Act and record keeping fees equal to an annual rate of 0.25% and up to 0.15%, respectively, of the average daily net assets of the Class B shares of the Fund. Class A shares are not subject to such fees.

Investment income, realized and unrealized gains and losses, and certain fund-level expenses and expense reductions, if any, are borne pro rata on the basis of relative net assets by the holders of all classes of shares, except that each class bears certain expenses unique to that class (including the applicable 12b-1 distribution fees and record keeping fees). Differences in class-level expenses may result in payment of different per share dividends by class. All shares have equal rights with respect to voting subject to class-specific arrangements.

The Series' financial statements are prepared in accordance with accounting principles generally accepted in the United States of America, which require the use of management estimates. Actual results could differ from those estimates. The policies described below are followed consistently by the Series in the preparation of the financial statements for its Funds.

**Security Valuation.** Investments are stated at value determined as of the close of regular trading on the New York Stock Exchange on each day the exchange is open for trading.

Various inputs are used in determining the value of the Fund's investments. These inputs are summarized in three broad levels. Level 1 includes quoted prices in active markets for identical securities. Level 2 includes other significant observable inputs (including quoted prices for similar securities, interest rates, prepayment speeds, and credit risk). Level 3 includes significant unobservable inputs (including the Fund's own assumptions in determining the fair value of investments). The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities.

Equity securities are valued at the most recent sale price or official closing price reported on the exchange (US or foreign) or over-the-counter market on which they trade and are categorized as Level 1 securities. Securities for which no sales are reported are valued at the calculated mean between the most recent bid and asked quotations on the relevant market or, if a mean cannot be determined, at the most recent bid quotation. For certain international equity securities, in order to adjust for events which may occur between the close of the foreign exchanges and the close of the New York Stock Exchange, a fair valuation model may be used. This fair valuation model takes into account comparisons to the valuation of American Depository Receipts (ADRs), exchange-traded funds, futures contracts and certain indices and these securities are categorized as Level 2.

Money market instruments purchased with an original or remaining maturity of sixty days or less, maturing at par, are valued at amortized cost, which approximates value, and are categorized as Level 2. Investments in open-end investment companies are valued at their net asset value each business day and are categorized as Level 1.

Securities and other assets for which market quotations are not readily available or for which the above valuation procedures are deemed not to reflect fair value are valued in a manner that is intended to reflect their fair value as determined in accordance with procedures approved by the Trustees and are generally categorized as Level 3. In accordance with the Fund's valuation procedures, factors used in determining value may include, but are not limited to, the type of the security; the size of the holding; the initial cost of the security; the existence of any contractual restrictions on the security's disposition; the price and extent of public trading in similar securities of the issuer or of comparable companies; quotations or evaluated prices from broker-dealers and/or pricing services; information obtained from the issuer, analysts, and/or the appropriate stock exchange (for exchange-traded securities); an analysis of the company's or issuer's financial statements; an evaluation of the forces that influence the issuer and the market(s) in which the security is purchased and sold and with respect to debt securities; the maturity, coupon, creditworthiness, currency denomination and the movement of the market in which the security is normally traded. The value determined under these procedures may differ from published values for the same securities.

Disclosure about the classification of fair value measurements is included in a table following the Fund's Investment Portfolio.

**Securities Lending.** The Fund lends securities to certain financial institutions. The Fund retains beneficial ownership of the securities it has loaned and continues to receive interest and dividends paid by the issuer of securities and to participate in any changes in their market value. The Fund requires the borrowers of the securities to maintain collateral with the Fund consisting of either cash or liquid, unencumbered assets having a value at least equal to the value of the securities loaned. When the collateral falls below specified amounts, the lending agent will use its best effort to obtain additional collateral on the next business day to meet required amounts under the security lending agreement. The Fund may invest the cash collateral into a joint trading account in an affiliated money market fund pursuant to Exemptive Orders issued by the SEC. The Fund receives compensation for lending its securities either in the form of fees or by earning interest on invested cash collateral net of borrower rebates and fees paid to a lending agent. Either the Fund or the borrower may terminate the loan. There may be risks of delay and costs in recovery of securities or even loss of rights in the collateral should the borrower of the securities fail financially. The Fund is also subject to all investment risks associated with the reinvestment of any cash collateral received, including, but not limited to, interest rate, credit and liquidity risk associated with such investments.

**Foreign Currency Translations.** The books and records of the Fund are maintained in US dollars. Investment securities and other assets and liabilities denominated in a foreign currency are translated into US dollars at the prevailing exchange rates at period end. Purchases and sales of investment securities, income and expenses are translated into US dollars at the prevailing exchange rates on the respective dates of the transactions.

Net realized and unrealized gains and losses on foreign currency transactions represent net gains and losses between trade and settlement dates on securities transactions, the disposition of forward foreign currency exchange contracts and foreign currencies, and the difference between the amount of net investment income accrued and the US dollar amount actually received. That portion of both realized and unrealized gains and losses on investments that results from fluctuations in foreign currency exchange rates is not separately disclosed but is included with net realized and unrealized gain/appreciation and loss/depreciation on investments.

**Taxes.** The Fund is treated as a separate taxpayer as provided for in the Internal Revenue Code, as amended. It is the Fund's policy to comply with the requirements of the Internal Revenue Code, as amended, which are applicable to regulated investment companies, and to distribute all of its taxable income to the separate accounts of the Participating Insurance Companies which hold its shares.

Additionally, based on the Series' understanding of the tax rules and rates related to income, gains and transactions for the foreign jurisdictions in which the Fund invests, the Fund will provide for foreign taxes, and where appropriate, deferred foreign taxes.

The Fund has reviewed the tax positions for the open tax years as of December 31, 2010 and has determined that no provision for income tax is required in the Fund's financial statements. The Fund's federal tax returns for the prior three fiscal years remain open subject to examination by the Internal Revenue Service.

**Distribution of Income and Gains.** The Fund will declare and distribute dividends from its net investment income, if any, annually, although additional distributions may be made if necessary. Net realized gains from investment transactions, in excess of available capital loss carryforwards, would be taxable to the Fund if not distributed, and, therefore, will be distributed to shareholders at least annually.

The timing and characterization of certain income and capital gains distributions are determined annually in accordance with federal tax regulations which may differ from accounting principles generally accepted in the United States of America. These differences primarily relate to certain securities sold at a loss. As a result, net investment income (loss) and net realized gain (loss) on investment transactions for a reporting period may differ significantly from distributions during such period. Accordingly, the Fund may periodically make reclassifications among certain of its capital accounts without impacting the net asset value of the Fund.

At December 31, 2010, the Fund's components of distributable earnings (accumulated losses) on a tax-basis are as follows:

| Fund | Undistributed Ordinary Income ($)* | Undistributed Net Long-Term Capital Gains ($) | Net Unrealized Gain (Loss) on Investments ($) |
|---|---|---|---|
| DWS Health Care VIP | 628,235 | 1,200,334 | 13,348,929 |

In addition, the tax character of distributions paid to shareholders by the Fund is summarized as follows:

| | Distributions from Ordinary Income ($)* Years Ended December 31, | | Distributions from Long-Term Capital Gains ($) Years Ended December 31, | |
|---|---|---|---|---|
| **Fund** | **2010** | **2009** | **2010** | **2009** |
| DWS Health Care VIP | 77,482 | 724,315 | 3,369,342 | 742,128 |

* *For tax purposes, short-term capital gains distributions are considered ordinary income distributions.*

**Expenses.** Expenses of the Series arising in connection with a specific Fund are allocated to that Fund. Other Series expenses which cannot be directly attributed to a Fund are apportioned among the Fund in the Series.

**Contingencies.** In the normal course of business, the Fund may enter into contracts with service providers that contain general indemnification clauses. The Fund's maximum exposure under these arrangements is unknown as this would involve future claims that may be made against the Fund that have not yet been made. However, based on experience, the Fund expects the risk of loss to be remote.

**Other.** Investment transactions are accounted for on a trade date plus one basis for daily net asset value calculations. However, for financial reporting purposes, investment transactions are reported on trade date. Interest income is recorded on the accrual basis net of foreign withholding taxes. Dividend income is recorded on the ex-dividend date net of foreign withholding taxes. Certain dividends from foreign securities may be recorded subsequent to the ex-dividend date as soon as the Fund is informed of such dividends. Realized gains and losses from investment transactions are recorded on an identified cost basis.

## B. Purchases and Sales of Securities

During the year ended December 31, 2010, purchases and sales of investment securities (excluding short-term investments) were as follows:

| Fund | Purchases ($) | Sales ($) |
|---|---|---|
| DWS Health Care VIP | 7,933,990 | 16,178,401 |

## C. Related Parties

Under the Investment Management Agreement with Deutsche Investment Management Americas Inc. ("DIMA" or the "Advisor"), an indirect, wholly owned subsidiary of Deutsche Bank AG, the Advisor directs the investments of the Fund in accordance with its investment objectives, policies and restrictions. The Advisor determines the securities, instruments and other contracts relating to investments to be purchased, sold or entered into by the Fund.

Under the Investment Management Agreement with the Advisor, the Fund pays a monthly management fee, based on the average daily net assets of the Fund, computed and accrued daily and payable monthly, at the annual rates shown below:

| Fund | Annual Management Fee Rate |
|---|---|
| DWS Health Care VIP | |
| first $250 million of average daily net assets | .665% |
| next $750 million of average daily net assets | .640% |
| next $1.5 billion of average daily net assets | .615% |
| next $2.5 billion of average daily net assets | .595% |
| next $2.5 billion of average daily net assets | .565% |
| next $2.5 billion of average daily net assets | .555% |
| next $2.5 billion of average daily net assets | .545% |
| over $12.5 billion of average daily net assets | .535% |

Accordingly, for the year ended December 31, 2010, the total management fee and effective management fee rate are as follows:

| Fund | Total Aggregated ($) | Annual Effective Rate |
|---|---|---|
| DWS Health Care VIP | 328,345 | .665% |

**Administration Fee.** Pursuant to an Administrative Services Agreement, DIMA provides most administrative services to the Series. For all services provided under the Administrative Services Agreement, the Fund pays the

Advisor an annual fee ("Administration Fee") of 0.10% of the Fund's average daily net assets, computed and accrued daily and payable monthly. For the year ended December 31, 2010, the Administration Fee was as follows:

| Fund | Total Aggregated ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS Health Care VIP | 49,375 | 4,088 |

**Service Provider Fees.** DWS Investments Service Company ("DISC"), an affiliate of the Advisor, is the transfer agent, dividend-paying agent and shareholder service agent for the Series. Pursuant to a sub-transfer agency agreement between DISC and DST Systems, Inc. ("DST"), DISC has delegated certain transfer agent, dividend-paying agent and shareholder service agent functions to DST. DISC compensates DST out of the shareholder servicing fee it receives from the Fund. For the year ended December 31, 2010, the amounts charged to the Fund by DISC were as follows:

| Fund | Total Aggregated ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS Health Care VIP Class A | 243 | 57 |
| DWS Health Care VIP Class B | 67 | 18 |

DWS Investments Distributors, Inc. ("DIDI"), also an affiliate of the Advisor, is the Series' Distributor. In accordance with the Master Distribution Plan, DIDI receives 12b-1 fees of 0.25% of average daily net assets of Class B shares. Pursuant to the Master Distribution Plan, DIDI remits these fees to the Participating Insurance Companies for various costs incurred or paid by these companies in connection with marketing and distribution of Class B shares. These fees are detailed in the Fund's Statement of Operations.

**Typesetting and Filing Service Fees.** Under an agreement with DIMA, DIMA is compensated for providing typesetting and certain regulatory filing services to the Fund. For the year ended December 31, 2010, the amount charged to the Fund by DIMA included in the Statement of Operations under "reports to shareholders" was as follows:

| Fund | Total Aggregated ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS Health Care VIP | 12,122 | 3,201 |

**Trustees' Fees and Expenses.** The Fund paid each Trustee not affiliated with the Advisor retainer fees plus specified amounts for various committee services and for the Board Chairperson.

**Affiliated Cash Management Vehicles.** The Fund may invest uninvested cash balances in Central Cash Management Fund, which is managed by the Advisor. The Fund indirectly bears its proportionate share of the expenses of the underlying money market funds. Central Cash Management Fund does not pay the Advisor an investment management fee. Central Cash Management Fund seeks a high level of current income consistent with liquidity and the preservation of capital.

## D. Ownership of the Fund

Two participating insurance companies were owners of record of 10% or more of the total outstanding Class A shares of the Fund, each owning 68% and 23%. One participating insurance company was an owner of record of 10% or more of the total outstanding Class B shares of the Fund, owning 98%.

## E. Line of Credit

The Series and other affiliated funds (the "Participants") share in a $450 million revolving credit facility provided by a syndication of banks. The Fund may borrow for temporary or emergency purposes, including the meeting of redemption requests that otherwise might require the untimely disposition of securities. The Participants are charged an annual commitment fee which is allocated based on net assets, among each of the Participants. Interest is calculated at a rate per annum equal to the sum of the Federal Funds Rate plus 1.25 percent plus if LIBOR exceeds the Federal Funds Rate the amount of such excess. The Fund may borrow up to a maximum of 33 percent of its net assets under the agreement.

## F. Subsequent Event

On January 12, 2011, the Board of the following Acquired Fund approved, in principle, the merger of the Acquired Fund into the Acquiring Fund. Completion of the merger is subject to a number of conditions, including final approval by Acquired Fund's Board and approval by the shareholders of the Acquired Fund at a shareholder meeting expected to be held during the month of April 2011. If shareholder approval is obtained, the merger is expected to occur on or about May 1, 2011.

| Acquired Fund | Acquiring Fund |
|---|---|
| DWS Variable Series I — DWS Health Care VIP | DWS Variable Series I — DWS Capital Growth VIP |

# Report of Independent Registered Public Accounting Firm

**To the Trustees of DWS Variable Series I and the Shareholders of DWS Health Care VIP:**

In our opinion, the accompanying statement of assets and liabilities, including the investment portfolio, and the related statements of operations and of changes in net assets and the financial highlights present fairly, in all material respects, the financial position of DWS Health Care VIP (the "Fund") at December 31, 2010 and the results of its operations, the changes in its net assets, and the financial highlights for the periods indicated therein, in conformity with accounting principles generally accepted in the United States of America. These financial statements and financial highlights (hereafter referred to as "financial statements") are the responsibility of the Fund's management. Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these financial statements in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits, which included confirmation of securities at December 31, 2010 by correspondence with the custodians and brokers, provide a reasonable basis for our opinion.

Boston, Massachusetts
February 11, 2011

PricewaterhouseCoopers LLP

# Tax Information

**(Unaudited)**

The Fund paid distributions of $0.74 per share from net long-term capital gains during the year ended December 31, 2010, of which 100% represents 15% rate gains.

Pursuant to Section 852 of the Internal Revenue Code, the Fund designates approximately $1,333,000 as capital gain dividends for its year ended December 31, 2010, of which 100% represents 15% rate gains.

For corporate shareholders of the Fund, 100% of the ordinary dividends (i.e., income dividends plus short-term capital gains) paid during the Fund's fiscal year ended December 31, 2010 qualified for the dividends received deduction.

Please consult a tax advisor if you have questions about federal or state income tax laws, or on how to prepare your tax returns. If you have specific questions about your account, please contact your insurance provider.

# Proxy Voting

The Series' policies and procedures for voting proxies for portfolio securities and information about how the Series voted proxies related to its portfolio securities during the 12-month period ended June 30 are available on our Web site — www.dws-investments.com (click on "proxy voting" at the bottom of the page) — or on the SEC's Web site — www.sec.gov. To obtain a written copy of the Series' policies and procedures without charge, upon request, call us toll free at (800) 728-3337.

# Investment Management Agreement Approval

The Board of Trustees, including the Independent Trustees, approved the renewal of your Fund's investment management agreement (the "Agreement") with Deutsche Investment Management Americas Inc. ("DWS") in September 2010.

In terms of the process that the Board followed prior to approving the Agreement, shareholders should know that:

- In September 2010, all of the Fund's Trustees were independent of DWS and its affiliates.
- The Trustees meet frequently to discuss fund matters. Each year, the Trustees dedicate substantial time to contract review matters. Over the course of several months, the Board's Contract Committee, in coordination with the Board's Equity Oversight Committee, reviewed comprehensive materials received from DWS, independent third parties and independent counsel. These materials included an analysis of the Fund's performance, fees and expenses, and profitability compiled by the Fund's independent fee consultant. The Board also received extensive information throughout the year regarding performance of the Fund.
- The Independent Trustees regularly meet privately with their independent counsel to discuss contract review and other matters. In addition, the Independent Trustees were also advised by the Fund's independent fee consultant in the course of their review of the Fund's contractual arrangements and considered a comprehensive report prepared by the independent fee consultant in connection with their deliberations (the "IFC Report").
- In connection with reviewing the Agreement, the Board also reviewed the terms of the Fund's Rule 12b-1 plan, distribution agreement, administrative services agreement, transfer agency agreement and other material service agreements.
- Based on its evaluation of the information provided, the Contract Committee presented its findings and recommendations to the Independent Trustees as a group. The Independent Trustees reviewed the Contract Committee's findings and recommendations and presented their recommendations to the full Board.

In connection with the contract review process, the Contract Committee and the Board considered the factors discussed below, among others. The Board also considered that DWS and its predecessors have managed the Fund since its inception, and the Board believes that a long-term relationship with a capable, conscientious advisor is in the best interests of the Fund. The Board considered, generally, that shareholders chose to invest or remain invested in the Fund knowing that DWS managed the Fund, and that the Agreement was approved by the Fund's shareholders. DWS is part of Deutsche Bank, a major global banking institution that is engaged in a wide range of financial services. The Board believes that there are significant advantages to being part of a global asset management business that offers a wide range of investing expertise and resources, including hundreds of portfolio managers and analysts with research capabilities in many countries throughout the world.

While shareholders may focus primarily on fund performance and fees, the Fund's Board considers these and many other factors, including the quality and integrity of DWS's personnel and such other issues as back-office operations, fund valuations, and compliance policies and procedures.

**Nature, Quality and Extent of Services.** The Board considered the terms of the Agreement, including the scope of advisory services provided under the Agreement. The Board noted that, under the Agreement, DWS provides portfolio management services to the Fund and that, pursuant to a separate administrative services agreement, DWS provides administrative services to the Fund. The Board considered the experience and skills of senior management and investment personnel, the resources made available to such personnel, the ability of DWS to attract and retain high-quality personnel, and the organizational depth and stability of DWS. The Board reviewed the Fund's performance over short-term and long-term periods and compared those returns to various agreed-upon performance measures, including market indices and a peer universe compiled by the independent fee consultant using information supplied by Lipper Inc. ("Lipper"). The Board also noted that it has put into place a process of identifying "Focus Funds" (e.g., funds performing poorly relative to their benchmark or a peer universe compiled by Lipper), and receives more frequent reporting and information from DWS regarding such funds, along with DWS's remedial plans to address underperformance. The Board believes this process is an effective manner of identifying and addressing underperforming funds. Based on the information provided, the Board noted that for the one-, three- and five-year periods ended December 31, 2009, the Fund's performance (Class A shares) was in the 3rd quartile, 2nd quartile and 2nd quartile, respectively, of the applicable Lipper universe (the 1st quartile being the best performers and the 4th quartile being the worst performers). The Board also observed that the Fund has outperformed its benchmark in the three- and five-year periods and has underperformed its benchmark in the one-year period ended December 31, 2009.

On the basis of this evaluation and the ongoing review of investment results by the Board, the Board concluded that the nature, quality and extent of services provided by DWS historically have been and continue to be satisfactory.

**Fees and Expenses.** The Board considered the Fund's investment management fee schedule, operating expenses and total expense ratios, and comparative information provided by Lipper and the independent fee consultant regarding investment management fee rates paid to other investment advisors by similar funds (1st quartile being the most favorable and 4th quartile being the least favorable). With respect to management fees paid to other investment advisors by similar funds, the Board noted that the contractual fee rates paid by the Fund, which include a 0.10% fee paid to DWS under the Fund's administrative services agreement, were lower than the median (2nd quartile) of the applicable Lipper peer group (based on Lipper data provided as of December 31, 2009). The Board noted that the Fund's Class A shares total (net) operating expenses were expected to be higher than the median (3rd quartile) of the applicable Lipper expense universe (based on Lipper data provided as of December 31, 2009) ("Lipper Universe Expenses"). The Board also reviewed data comparing each share class's total (net) operating expenses to the applicable Lipper Universe Expenses. The Board considered the Fund's management fee rate as compared to fees charged by DWS and certain of its affiliates for comparable mutual funds and considered differences in fund and fee structures between the DWS Funds. The Board also considered how the Fund's total (net) operating expenses compared to the total (net) operating expenses of a more customized peer group selected by Lipper (based on such factors as asset size).

The information considered by the Board as part of its review of management fees included information regarding fees charged by DWS and its affiliates to similar institutional accounts and to similar funds offered primarily to European investors ("DWS Europe funds"), in each case as applicable. The Board observed that advisory fee rates for institutional accounts generally were lower than the management fees charged by similarly managed DWS US mutual funds ("DWS Funds"), but also took note of the differences in services provided to DWS Funds as compared to institutional accounts. In the case of DWS Europe funds, the Board observed that fee rates for DWS Europe funds generally were higher than for similarly managed DWS Funds, but noted that differences in the types of services provided to DWS Funds relative to DWS Europe funds made it difficult to compare such fees.

On the basis of the information provided, the Board concluded that management fees were reasonable and appropriate in light of the nature, quality and extent of services provided by DWS.

**Profitability.** The Board reviewed detailed information regarding revenues received by DWS under the Agreement. The Board considered the estimated costs and pre-tax profits realized by DWS from advising the DWS Funds, as well as estimates of the pre-tax profits attributable to managing the Fund in particular. The Board also received information regarding the estimated enterprise-wide profitability of DWS and its affiliates with respect to all fund services in totality and by fund. The Board reviewed DWS's methodology in allocating its costs to the management of the Fund. Based on the information provided, the Board concluded that the pre-tax profits realized by DWS in connection with the management of the Fund were not unreasonable. The Board also reviewed information regarding the profitability of certain similar investment management firms. The Board noted that while information regarding the profitability of such firms is limited (and in some cases is not necessarily prepared on a comparable basis), DWS and its affiliates' overall profitability with respect to the DWS fund complex (after taking into account distribution and other services provided to the funds by DWS and its affiliates) was lower than the overall profitability levels of many comparable firms for which such data was available.

**Economies of Scale.** The Board considered whether there are economies of scale with respect to the management of the Fund and whether the Fund benefits from any economies of scale. The Board noted that the Fund's management fee schedule includes fee breakpoints. The Board concluded that the Fund's fee schedule represents an appropriate sharing between the Fund and DWS of such economies of scale as may exist in the management of the Fund at current asset levels.

**Other Benefits to DWS and Its Affiliates.** The Board also considered the character and amount of other incidental benefits received by DWS and its affiliates, including any fees received by DWS for administrative services provided to the Fund and any fees received by an affiliate of DWS for distribution services. The Board also considered benefits to DWS related to brokerage and soft-dollar allocations, including allocating brokerage to pay for research generated by parties other than the executing broker dealers, which pertain primarily to funds investing in equity securities, along with the incidental public relations benefits to DWS related to DWS Funds advertising and cross-selling opportunities among DWS products and services. The Board concluded that management fees were reasonable in light of these fallout benefits.

**Compliance.** The Board considered the significant attention and resources dedicated by DWS to documenting and enhancing its compliance processes in recent years. The Board noted in particular (i) the experience and seniority of both DWS's chief compliance officer and the Fund's chief compliance officer; (ii) the large number of

DWS compliance personnel; and (iii) the substantial commitment of resources by DWS and its affiliates to compliance matters.

Based on all of the information considered and the conclusions reached, the Board unanimously determined that the continuation of the Agreement is in the best interests of the Fund. In making this determination, the Board did not give particular weight to any single factor identified above. The Board considered these factors over the course of numerous meetings, certain of which were in executive session with only the Independent Trustees and their counsel present. It is possible that individual Trustees may have weighed these factors differently in reaching their individual decisions to approve the continuation of the Agreement.

# Summary of Management Fee Evaluation by Independent Fee Consultant

October 3, 2010

Pursuant to an Order entered into by Deutsche Investment Management Americas and affiliates (collectively, "DeAM") with the Attorney General of New York, I, Thomas H. Mack, have been appointed the Independent Fee Consultant for the DWS Funds (formerly the DWS Scudder Funds). My duties include preparing an annual written evaluation of the management fees DeAM charges the Funds, considering among other factors the management fees charged by other mutual fund companies for like services, management fees DeAM charges other clients for like services, DeAM's costs of supplying services under the management agreements and related profit margins, possible economies of scale if a Fund grows larger, and the nature and quality of DeAM's services, including fund performance. This report summarizes my evaluation for 2010, including my qualifications, the evaluation process for each of the DWS Funds, consideration of certain complex-level factors, and my conclusions. I served in substantially the same capacity in 2007, 2008, and 2009.

## Qualifications

For more than 35 years I have served in various professional capacities within the investment management business. I have held investment analysis and advisory positions, including securities analyst, portfolio strategist and director of investment policy with a large investment firm. I have also performed business management functions, including business development, financial management and marketing research and analysis.

Since 1991, I have been an independent consultant within the asset management industry. I have provided services to over 125 client organizations, including investment managers, mutual fund boards, product distributors and related organizations. Over the past ten years I have completed a number of assignments for mutual fund boards, specifically including assisting boards with management contract renewal.

I hold a Master of Business Administration degree, with highest honors, from Harvard University and Master of Science and Bachelor of Science (highest honors) degrees from the University of California at Berkeley. I am an independent director and audit committee financial expert for two closed-end mutual funds and have served in various leadership and financial oversight capacities with non-profit organizations.

## Evaluation of Fees for each DWS Fund

My work focused primarily on evaluating, fund-by-fund, the fees charged to each of the 118 publicly offered Fund portfolios in the DWS Fund family. For each Fund, I considered each of the key factors mentioned above, as well as any other relevant information. In doing so I worked closely with the Funds' Independent Directors in their annual contract renewal process, as well as in their approval of contracts for several new funds (documented separately).

In evaluating each Fund's fees, I reviewed comprehensive materials provided by or on behalf of DeAM, including expense information prepared by Lipper Analytical, comparative performance information, profitability data, manager histories, and other materials. I also accessed certain additional information from the Lipper and Morningstar databases and drew on my industry knowledge and experience.

To facilitate evaluating this considerable body of information, I prepared for each Fund a document summarizing the key data elements in each area as well as additional analytics discussed below. This made it possible to consider each key data element in the context of the others.

In the course of contract renewal, DeAM agreed to implement a number of fee and expense adjustments requested by the Independent Directors which will favorably impact future fees and expenses, and my evaluation includes the effects of these changes.

### Fees and Expenses Compared with Other Funds

The competitive fee and expense evaluation for each fund focused on two primary comparisons:

The Fund's contractual management fee (the advisory fee plus the administration fee where applicable) compared with those of a group of typically 12–15 funds in the same Lipper investment category (e.g. Large Capitalization Growth) having similar distribution arrangements and being of similar size.

The Fund's total expenses compared with a broader universe of funds from the same Lipper investment category and having similar distribution arrangements.

These two comparisons provide a view of not only the level of the fee compared with funds of similar scale but also the total expense the Fund bears for all the services it receives, in comparison with the investment choices available in the Fund's investment category and distribution channel. The principal figure-of-merit used in these comparisons was the subject Fund's percentile ranking against peers.

### DeAM's Fees for Similar Services to Others

DeAM provided management fee schedules for all of its US domiciled fund and non-fund investment management accounts in any of the investment categories where there is a DWS Fund. These similar products included the other DWS Funds, non-fund pooled accounts, institutional accounts and sub-advisory accounts. Using this information, I calculated for each Fund the fee that would be charged to each similar product, at the subject Fund's asset level.

Evaluating information regarding non-fund products is difficult because there are varying levels of services required for different types of accounts, with mutual funds generally requiring considerably more regulatory and administrative types of service as well as having more frequent cash flows than other types of accounts. Also, while mutual fund fees for similar fund products can be expected to be similar, there will be some differences due to different pricing conditions in different distribution channels (e.g. retail funds versus those used in variable insurance products), differences in underlying investment processes and other factors.

**Costs and Profit Margins**

DeAM provided a detailed profitability analysis for each Fund. After making some adjustments so that the presentation would be more comparable to the available industry figures, I reviewed profit margins from investment management alone, from investment management plus other fund services (excluding distribution) provided to the Funds by DeAM (principally shareholder services), and DeAM profits from all sources, including distribution. A later section comments on overall profitability.

**Economies of Scale**

Economies of scale — an expected decline in management cost per dollar of fund assets as fund assets grow — are very rarely quantified and documented because of inherent difficulties in collecting and analyzing relevant data. However, in virtually every investment category that I reviewed, larger funds tend to have lower fees and lower total expenses than smaller funds. To see how each DWS Fund compares with this industry observation, I reviewed:

- The trend in Fund assets over the last five years and the accompanying trend in total expenses. This shows if the Fund has grown and, if so, whether total expense (management fees as well as other expenses) have declined as a percent of assets.
- Whether the Fund has break-points in its management fee schedule, the extent of the fee reduction built into the schedule and the asset levels where the breaks take effect, and in the case of a sub-advised Fund how the Fund's break-points compare with those of the sub-advisory fee schedule.
- How the Fund's contractual fee schedule compares with trends in the industry data. To accomplish this, I constructed a chart showing how actual latest-fiscal-year contractual fees of the Fund and of other similar funds relate to average fund assets, with the subject Fund's contractual fee schedule superimposed.

**Quality of Service — Performance**

The quality-of-service evaluation focused on investment performance, which is the principal result of the investment management service. Each Fund's performance was reviewed over the past 1, 3, 5 and 10 years, as applicable, and compared with that of other funds in the same investment category and with a suitable market index.

In addition, I calculated and reviewed risk-adjusted returns relative to an index of similar mutual funds' returns and a suitable market index. The risk-adjusted returns analysis provides a way of determining the extent to which the Fund's return comparisons are mainly the product of investment value-added (or lack thereof) or alternatively taking considerably more or less risk than is typical in its investment category.

I also received and considered the history of portfolio manager changes for each Fund, as this provided an important context for evaluating the performance results.

## Complex-Level Considerations

While this evaluation was conducted mainly at the individual fund level, there are some issues relating to the reasonableness of fees that can alternatively be considered across the whole fund complex:

- I reviewed DeAM's profitability analysis for all DWS Funds, with a view toward determining if the allocation procedures used were reasonable and how profit levels compared with public data for other investment managers.
- I considered whether DeAM and affiliates receive any significant ancillary or "fall-out" benefits that should be considered in interpreting the direct profitability results. These would be situations where serving as the investment manager of the Funds is beneficial to another part of the Deutsche Bank organization.
- I considered how aggregated DWS Fund expenses had varied over the years, by asset class and in the context of trends in asset levels.
- I reviewed the structure of the DeAM organization, trends in staffing levels, and information on compensation of investment management and other professionals compared with industry data.

## Findings

Based on the process and analysis discussed above, which included reviewing a wide range of information from management and external data sources and considering among other factors the fees DeAM charges other clients, the fees charged by other fund managers, DeAM's costs and profits associated with managing the Funds, economies of scale, possible fall-out benefits, and the nature and quality of services provided, in my opinion the management fees charged the DWS Funds are reasonable.

Thomas H. Mack

# Board Members and Officers

The following table presents certain information regarding the Board Members and Officers of the Trust as of December 31, 2010. Each Board Member's year of birth is set forth in parentheses after his or her name. Unless otherwise noted, (i) each Board Member has engaged in the principal occupation(s) noted in the table for at least the most recent five years, although not necessarily in the same capacity; and (ii) the address of each Independent Board Member is c/o Paul K. Freeman, Independent Chairman, DWS Funds, PO Box 101833, Denver, CO 80250-1833. Except as otherwise noted below, the term of office for each Board Member is until the election and qualification of a successor, or until such Board Member sooner dies, resigns, is removed or as otherwise provided in the governing documents of the fund. Because the fund does not hold an annual meeting of shareholders, each Board Member will hold office for an indeterminate period. The Board Members may also serve in similar capacities with other funds in the fund complex. The Length of Time Served represents the year in which the Board Member joined the board of one or more DWS funds now overseen by the Board.

### Independent Board Members

| Name, Year of Birth, Position with the Fund and Length of Time Served[1] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Paul K. Freeman (1950)<br>Chairperson since 2009<br>Board Member since 1993 | Consultant, World Bank/Inter-American Development Bank; Executive and Governing Council of the Independent Directors Council (education committees); formerly, Project Leader, International Institute for Applied Systems Analysis (1998–2001); Chief Executive Officer, The Eric Group, Inc. (environmental insurance) (1986–1998) | 122 |
| John W. Ballantine (1946)<br>Board Member since 1999 | Retired; formerly, Executive Vice President and Chief Risk Management Officer, First Chicago NBD Corporation/The First National Bank of Chicago (1996–1998); Executive Vice President and Head of International Banking (1995–1996). Directorships: Healthways, Inc. (provider of disease and care management services); Portland General Electric (utility company); Stockwell Capital Investments PLC (private equity). Former Directorships: First Oak Brook Bancshares, Inc. and Oak Brook Bank; Prisma Energy International | 122 |
| Henry P. Becton, Jr. (1943)<br>Board Member since 1990 | Vice Chair and former President, WGBH Educational Foundation. Directorships: Association of Public Television Stations; Lead Director, Becton Dickinson and Company[3] (medical technology company); Lead Director, Belo Corporation[3] (media company); Public Radio International; Public Radio Exchange (PRX); The PBS Foundation. Former Directorships: Boston Museum of Science; American Public Television; Concord Academy; New England Aquarium; Mass. Corporation for Educational Telecommunications; Committee for Economic Development; Public Broadcasting Service | 122 |
| Dawn-Marie Driscoll (1946)<br>Board Member since 1987 | President, Driscoll Associates (consulting firm); Executive Fellow, Center for Business Ethics, Bentley University; formerly, Partner, Palmer & Dodge (1988–1990); Vice President of Corporate Affairs and General Counsel, Filene's (1978–1988). Directorships: Trustee of 22 open-end mutual funds managed by Sun Capital Advisers, Inc. (since 2007); Director of ICI Mutual Insurance Company (since 2007); Advisory Board, Center for Business Ethics, Bentley University; Trustee, Southwest Florida Community Foundation (charitable organization). Former Directorships: Investment Company Institute (audit, executive, nominating committees) and Independent Directors Council (governance, executive committees) | 122 |
| Keith R. Fox (1954)<br>Board Member since 1996 | Managing General Partner, Exeter Capital Partners (a series of private investment funds). Directorships: Progressive International Corporation (kitchen goods importer and distributor); BoxTop Media Inc. (advertising); The Kennel Shop (retailer); former Chairman, National Association of Small Business Investment Companies | 122 |
| Kenneth C. Froewiss (1945)<br>Board Member since 2001 | Adjunct Professor of Finance, NYU Stern School of Business (September 2009–present; Clinical Professor from 1997–September 2009); Member, Finance Committee, Association for Asian Studies (2002–present); Director, Mitsui Sumitomo Insurance Group (US) (2004–present); prior thereto, Managing Director, J.P. Morgan (investment banking firm) (until 1996) | 122 |
| Richard J. Herring (1946)<br>Board Member since 1990 | Jacob Safra Professor of International Banking and Professor, Finance Department, The Wharton School, University of Pennsylvania (since July 1972); Co-Director, Wharton Financial Institutions Center (since July 2000); Co-Chair, U.S. Shadow Financial Regulatory Committee; Executive Director, Financial Economists Roundtable; Director, Japan Equity Fund, Inc. (since September 2007), Thai Capital Fund, Inc. (since September 2007), Singapore Fund, Inc. (since September 2007); Independent Director of Barclays Bank Delaware (since September 2010). Formerly, Vice Dean and Director, Wharton Undergraduate Division (July 1995–June 2000); Director, Lauder Institute of International Management Studies (July 2000–June 2006) | 122 |
| William McClayton (1944)<br>Board Member since 2004+ | Private equity investor (since October 2009); previously, Managing Director, Diamond Management & Technology Consultants, Inc. (global consulting firm) (2001–2009); Directorship: Board of Managers, YMCA of Metropolitan Chicago; formerly: Senior Partner, Arthur Andersen LLP (accounting) (1966–2001); Trustee, Ravinia Festival | 122 |

| Name, Year of Birth, Position with the Fund and Length of Time Served[1] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Rebecca W. Rimel (1951)<br>Board Member since 1995 | President and Chief Executive Officer, The Pew Charitable Trusts (charitable organization) (1994 to present); Trustee, Thomas Jefferson Foundation (charitable organization) (1994 to present); Trustee, Executive Committee, Philadelphia Chamber of Commerce (2001–2007); Director, CardioNet, Inc.[2] (2009–present) (health care). Formerly, Executive Vice President, The Glenmede Trust Company (investment trust and wealth management) (1983–2004); Board Member, Investor Education (charitable organization) (2004–2005); Director, Viasys Health Care[2] (January 2007–June 2007); Trustee, Pro Publica (charitable organization) (2007–2010) | 122 |
| William N. Searcy, Jr. (1946)<br>Board Member since 1993 | Private investor since October 2003; Trustee of 22 open-end mutual funds managed by Sun Capital Advisers, Inc. (since October 1998). Formerly, Pension & Savings Trust Officer, Sprint Corporation[2] (telecommunications) (November 1989–September 2003) | 122 |
| Jean Gleason Stromberg (1943)<br>Board Member since 1997 | Retired. Formerly, Consultant (1997–2001); Director, Financial Markets US Government Accountability Office (1996–1997); Partner, Fulbright & Jaworski, L.L.P. (law firm) (1978–1996). Directorships: The William and Flora Hewlett Foundation. Former Directorships: Service Source, Inc., Mutual Fund Directors Forum (2002–2004), American Bar Retirement Association (funding vehicle for retirement plans) (1987–1990 and 1994–1996) | 122 |
| Robert H. Wadsworth (1940)<br>Board Member since 1999 | President, Robert H. Wadsworth & Associates, Inc. (consulting firm) (1983 to present); Director, The Phoenix Boys Choir Association | 125 |

## Officers[4]

| Name, Year of Birth, Position with the Fund and Length of Time Served[5] | Principal Occupation(s) During Past 5 Years and Other Directorships Held |
|---|---|
| Michael G. Clark[6] (1965)<br>President, 2006–present | Managing Director[3], Deutsche Asset Management (2006–present); President of DWS family of funds; Director, ICI Mutual Insurance Company (since October 2007); formerly, Director of Fund Board Relations (2004–2006) and Director of Product Development (2000–2004), Merrill Lynch Investment Managers; Senior Vice President Operations, Merrill Lynch Asset Management (1999–2000) |
| Ingo Gefeke[7] (1967)<br>Executive Vice President since 2010 | Managing Director[3], Deutsche Asset Management; Global Head of Distribution and Product Management, DWS Global Head of Trading and Securities Lending. Member of the Board of Directors of DWS Investment GmbH Frankfurt (since July 2009) and DWS Holding & Service GmbH Frankfurt (since January 2010); formerly, Global Chief Administrative Officer, Deutsche Asset Management (2004–2009); Global Chief Operating Officer, Global Transaction Banking, Deutsche Bank AG, New York (2001–2004); Chief Operating Officer, Global Banking Division Americas, Deutsche Bank AG, New York (1999–2001); Central Management, Global Banking Services, Deutsche Bank AG, Frankfurt (1998–1999); Relationship Management, Deutsche Bank AG, Tokyo, Japan (1997–1998) |
| John Millette[8] (1962)<br>Vice President and Secretary, 1999–present | Director[3], Deutsche Asset Management |
| Paul H. Schubert[6] (1963)<br>Chief Financial Officer, 2004–present<br>Treasurer, 2005–present | Managing Director[3], Deutsche Asset Management (since July 2004); formerly, Executive Director, Head of Mutual Fund Services and Treasurer for UBS Family of Funds (1998–2004); Vice President and Director of Mutual Fund Finance at UBS Global Asset Management (1994–1998) |
| Caroline Pearson[8] (1962)<br>Chief Legal Officer, April 2010–present | Managing Director[3], Deutsche Asset Management; formerly, Assistant Secretary for DWS family of funds (1997–2010) |
| Rita Rubin[9] (1970)<br>Assistant Secretary, 2009–present | Vice President and Counsel, Deutsche Asset Management (since October 2007); formerly, Vice President, Morgan Stanley Investment Management (2004–2007) |
| Paul Antosca[8] (1957)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management (since 2006); Vice President, The Manufacturers Life Insurance Company (U.S.A.) (1990–2006) |
| Jack Clark[8] (1967)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management (since 2007); formerly, Vice President, State Street Corporation (2002–2007) |
| Diane Kenneally[8] (1966)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management |
| John Caruso[9] (1965)<br>Anti-Money Laundering Compliance Officer, 2010–present | Managing Director[3], Deutsche Asset Management |

| Name, Year of Birth, Position with the Fund and Length of Time Served[5] | Principal Occupation(s) During Past 5 Years and Other Directorships Held |
|---|---|
| Robert Kloby[9] (1962)<br>Chief Compliance Officer, 2006–present | Managing Director[3], Deutsche Asset Management |

1 *The length of time served represents the year in which the Board Member joined the board of one or more DWS funds currently overseen by the Board.*

2 *A publicly held company with securities registered pursuant to Section 12 of the Securities Exchange Act of 1934.*

3 *Executive title, not a board directorship.*

4 *As a result of their respective positions held with the Advisor, these individuals are considered "interested persons" of the Advisor within the meaning of the 1940 Act. Interested persons receive no compensation from the fund.*

5 *The length of time served represents the year in which the officer was first elected in such capacity for one or more DWS funds.*

6 *Address: 100 Plaza One, Jersey City, NJ 07311.*

7 *Effective January 11, 2011, Mr. Gefeke, Executive Vice President, resigned as an officer of the fund.*

*The mailing address of Mr. Gefeke is 345 Park Avenue, New York, New York 10154. Mr. Gefeke was an interested Board Member of certain DWS funds by virtue of his positions with Deutsche Asset Management. As an interested person, Mr. Gefeke received no compensation from the fund.*

8 *Address: One Beacon Street, Boston, MA 02108.*

9 *Address: 60 Wall Street, New York, New York 10005.*

*The fund's Statement of Additional Information ("SAI") includes additional information about the Board Members. The SAI is available, without charge, upon request. If you would like to request a copy of the SAI, you may do so by calling the following toll-free number: (800) 728-3337.*

DWS Investments is part of Deutsche Bank's Asset Management division and, within the US, represents the retail asset management activities of Deutsche Bank AG, Deutsche Bank Trust Company Americas, Deutsche Investment Management Americas Inc. and DWS Trust Company.

The views expressed in this report reflect those of the portfolio managers only through the end of the period of the report as stated on the cover. The managers' views are subject to change at any time based on market and other conditions and should not be construed as a recommendation.

This information must be preceded or accompanied by a current prospectus.

Portfolio changes should not be considered recommendations for action by individual investors.

DWS Investments Distributors, Inc.
222 South Riverside Plaza
Chicago, IL 60606
(800) 621-1148

VS1health-2 (2/11)

DWS INVESTMENTS
Deutsche Bank Group

DECEMBER 31, 2010

# ANNUAL REPORT

## DWS VARIABLE SERIES I

## DWS International VIP

**This report must be preceded or accompanied by a prospectus. To obtain an additional prospectus or summary prospectus, if available, call (800) 728-3337 or your financial representative. We advise you to consider the Fund's objectives, risks, charges and expenses carefully before investing. The summary prospectus and prospectus contain this and other important information about the Fund. Please read the prospectus carefully before you invest.**

*Investments in variable insurance portfolios (VIPs) involve risk. Stocks may decline in value. Bond investments are subject to interest-rate and credit risks. When interest rates rise, bond prices generally fall. Credit risk refers to the ability of an issuer to make timely payments of principal and interest. Investing in derivatives entails special risks relating to liquidity, leverage and credit that may reduce returns and/or increased volatility. Investing in foreign securities, particularly those of emerging markets, presents certain risks, such as currency fluctuations, political and economic changes, and market risks. There are additional risks associated with investing in commodities, high-yield bonds, aggressive growth stocks, non-diversified/ concentrated funds and small- and mid-cap stocks which are more fully explained in the prospectuses. Please read the prospectus for more information.*

*DWS Investments is part of Deutsche Bank's Asset Management division and, within the US, represents the retail asset management activities of Deutsche Bank AG, Deutsche Bank Trust Company Americas, Deutsche Investment Management Americas Inc. and DWS Trust Company.*

*NOT FDIC/NCUA INSURED NO BANK GUARANTEE MAY LOSE VALUE NOT A DEPOSIT*
*NOT INSURED BY ANY FEDERAL GOVERNMENT AGENCY*

DWS INVESTMENTS
Deutsche Bank Group

# Performance Summary

December 31, 2010

## DWS International VIP

**All performance shown is historical, assumes reinvestment of all dividend and capital gain distributions, and does not guarantee future results. Investment return and principal value fluctuate with changing market conditions so that, when redeemed, shares may be worth more or less than their original cost. Current performance may be lower or higher than the performance data quoted. Please contact your participating insurance company for the Fund's most recent month-end performance. Performance doesn't reflect charges and fees ("contract charges") associated with the separate account that invests in the Fund or any variable life insurance policy or variable annuity contract for which the Fund is an investment option. These charges and fees will reduce returns. While all share classes have the same underlying portfolio, their performance will differ.**

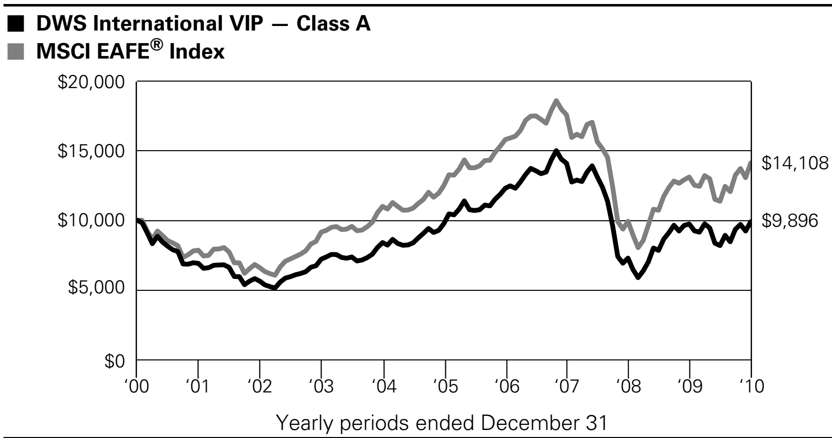
**The gross expense ratios of the Fund, as stated in the fee table of the prospectus dated May 1, 2010 are 0.96% and 1.24% for Class A and Class B shares, respectively, and may differ from the expense ratios disclosed in the Financial Highlights tables in this report.**

Fund returns during all periods shown reflect a fee waiver and/or reimbursement. Without this waiver/reimbursement, returns would have been lower.

### Risk Considerations

Investing in foreign securities, particularly those of emerging markets, presents certain risks, such as currency fluctuations, political and economic changes, and market risks. Stocks may decline in value. See the prospectus for details.

### Growth of an Assumed $10,000 Investment




*The Morgan Stanley Capital International (MSCI) Europe, Australasia and Far East (EAFE®) Index is an unmanaged index that tracks international stock performance in the 21 developed markets in Europe, Australasia and the Far East. The index is calculated using closing local market prices and translates into US dollars using the London close foreign exchange rates.*

*Index returns assume the reinvestment of dividends net of withholding tax and, unlike fund returns, do not reflect any fees or expenses. It is not possible to invest directly into an index.*

### Comparative Results

| **DWS International VIP** | | **1-Year** | **3-Year** | **5-Year** | **10-Year** |
|---|---|---|---|---|---|
| **Class A** | Growth of $10,000 | $10,162 | $7,027 | $10,138 | $9,896 |
| | Average annual total return | 1.62% | –11.10% | .27% | –.10% |
| MSCI EAFE® Index | Growth of $10,000 | $10,775 | $8,040 | $11,292 | $14,108 |
| | Average annual total return | 7.75% | –7.02% | 2.46% | 3.50% |

| **DWS International VIP** | | **1-Year** | **3-Year** | **5-Year** | **10-Year** |
|---|---|---|---|---|---|
| **Class B** | Growth of $10,000 | $10,133 | $6,969 | $9,988 | $9,646 |
| | Average annual total return | 1.33% | –11.34% | –.02% | –.36% |
| MSCI EAFE® Index | Growth of $10,000 | $10,775 | $8,040 | $11,292 | $14,108 |
| | Average annual total return | 7.75% | –7.02% | 2.46% | 3.50% |

*The growth of $10,000 is cumulative.*

# Information About Your Fund's Expenses

## DWS International VIP

As an investor of the Fund, you incur two types of costs: ongoing expenses and transaction costs. Ongoing expenses include management fees, distribution and service (12b-1) fees and other Fund expenses. Examples of transaction costs include contract charges, redemption fees and account maintenance fees, which are not shown in this section. The following tables are intended to help you understand your ongoing expenses (in dollars) of investing in the Fund and to help you compare these expenses with the ongoing expenses of investing in other mutual funds. The example in the table is based on an investment of $1,000 invested at the beginning of the six-month period and held for the entire period (July 1, 2010 to December 31, 2010).

The tables illustrate your Fund's expenses in two ways:

- **Actual Fund Return.** This helps you estimate the actual dollar amount of ongoing expenses (but not transaction costs) paid on a $1,000 investment in the Fund using the Fund's actual return during the period. To estimate the expenses you paid over the period, simply divide your account value by $1,000 (for example, an $8,600 account value divided by $1,000 = 8.6), then multiply the result by the number in the "Expenses Paid per $1,000" line under the share class you hold.
- **Hypothetical 5% Fund Return.** This helps you to compare your Fund's ongoing expenses (but not transaction costs) with those of other mutual funds using the Fund's actual expense ratio and a hypothetical rate of return of 5% per year before expenses. Examples using a 5% hypothetical Fund return may be found in the shareholder reports of other mutual funds. The hypothetical account values and expenses may not be used to estimate the actual ending account balance or expenses you paid for the period.

Please note that the expenses shown in these tables are meant to highlight your ongoing expenses only and do not reflect any transaction costs. The "Expenses Paid per $1,000" line of the tables is useful in comparing ongoing expenses only and will not help you determine the relative total expense of owning different funds. If these transaction costs had been included, your costs would have been higher.

**Expenses and Value of a $1,000 Investment** for the six months ended December 31, 2010

| Actual Fund Return | Class A | Class B |
|---|---|---|
| Beginning Account Value 7/1/10 | $1,000.00 | $1,000.00 |
| Ending Account Value 12/31/10 | $1,208.80 | $1,207.00 |
| Expenses Paid per $1,000* | $ 5.51 | $ 7.06 |
| **Hypothetical 5% Fund Return** | **Class A** | **Class B** |
| Beginning Account Value 7/1/10 | $1,000.00 | $1,000.00 |
| Ending Account Value 12/31/10 | $1,020.21 | $1,018.80 |
| Expenses Paid per $1,000* | $ 5.04 | $ 6.46 |

* *Expenses are equal to the Fund's annualized expense ratio for each share class, multiplied by the average account value over the period, multiplied by the number of days in the most recent six-month period, then divided by 365.*

| Annualized Expense Ratios | Class A | Class B |
|---|---|---|
| DWS Variable Series I — DWS International VIP | .99% | 1.27% |

For more information, please refer to the Fund's prospectus.

These tables do not reflect charges and fees ("contract charges") associated with the separate account that invests in the Fund or any variable life insurance policy or variable annuity contract for which the Fund is an investment option.

## DWS International VIP

International equities produced a modest gain in 2010 based on the 7.75% return of the the Morgan Stanley Capital International (MSCI) Europe, Australasia and Far East (EAFE) Index. While positive, this return lagged the 15.06% gain of the US market — as gauged by the Standard & Poor's 500® (S&P 500) Index — by a substantial margin. The relative performance of the foreign stocks was dampened by the progression of the European sovereign debt crisis and concerns about the impact of the rising yen on Japan's already sluggish economy.

The Class A shares of DWS International VIP returned 1.62% (unadjusted for contract charges) and underperformed the benchmark in 2010, a time in which investors were focused largely on top-down macroeconomic factors rather than company-specific fundamentals. (Past performance is no guarantee of future results.) For example, higher-quality large-cap companies with strong balance sheets and large cash reserves — in other words, the types of companies in which we invest — underperformed during the year. While there will often be times when higher-quality stocks lag the broader indices, we believe that focusing on stocks with the strongest fundamentals is the most effective way to achieve longer-term outperformance.

In terms of specific drivers of the Fund's performance, the most important sources of our shortfall in 2010 were our overweight in energy — which lagged the broader market — and our ineffective stock selection in the materials, industrials and health care sectors.[1] We offset these negatives, to some extent, through our stronger results in information technology and financials.

With regard to portfolio activity, we began to take selective positions in the emerging markets in order to capitalize on the many attractive growth opportunities that the asset class has to offer. We also reduced the deviations in the Fund's country, sector and currency weightings versus the benchmark in an effort to dampen the volatility of our relative performance.

Nikolaus Poehlmann, CFA
*Lead Portfolio Manager*

Udo Rosendahl *(until 2/1/2011)*
Mark Schumann
Andreas Wendelken
*Portfolio Managers*

*The Morgan Stanley Capital International (MSCI) Europe, Australasia and Far East (EAFE) Index is an unmanaged index that tracks international stock performance in the 21 developed markets in Europe, Australasia and the Far East. The index is calculated using closing local market prices and translates into US dollars using the London close foreign exchange rates.*

*The Standard & Poor's 500 (S&P 500) Index is an unmanaged, capitalization-weighted index of 500 stocks. The index is designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries.*

*Index returns assume the reinvestment of dividends net of withholding tax and, unlike fund returns, do not reflect any fees or expenses. It is not possible to invest directly into an index.*

1 *"Overweight" means the Fund holds a higher weighting in a given sector or security than the benchmark. "Underweight" means the Fund holds a lower weighting.*

*Portfolio management market commentary is as of December 31, 2010, and may not come to pass. This information is subject to change at any time based on market and other conditions. Past performance does not guarantee future results. Current and future portfolio holdings are subject to risk.*

# Portfolio Summary

## DWS International VIP

| **Asset Allocation** (As a % of Investment Portfolio excluding Securities Lending Collateral) | **12/31/10** | **12/31/09** |
|---|---|---|
| Common Stocks | 96% | 93% |
| Preferred Stocks | 4% | — |
| Cash Equivalents | — | 4% |
| Exchange-Traded Funds | — | 3% |
| | 100% | 100% |

| **Geographical Diversification**<br>(As a % of Investment Portfolio excluding Cash Equivalents and Securities Lending Collateral) | **12/31/10** | **12/31/09** |
|---|---|---|
| Continental Europe | 41% | 63% |
| Japan | 20% | 18% |
| United Kingdom | 15% | 9% |
| Pacific Basin | 11% | 6% |
| Australia | 8% | 4% |
| Latin America | 4% | — |
| Africa | 1% | — |
| | 100% | 100% |

| **Sector Diversification** (As a % of Investment Portfolio excluding Exchange-Traded Fund, Cash Equivalents and Securities Lending Collateral) | **12/31/10** | **12/31/09** |
|---|---|---|
| Financials | 19% | 24% |
| Industrials | 16% | 13% |
| Consumer Staples | 15% | 5% |
| Materials | 11% | 15% |
| Energy | 10% | 13% |
| Consumer Discretionary | 9% | 9% |
| Telecommunication Services | 6% | 5% |
| Health Care | 6% | 8% |
| Information Technology | 6% | 3% |
| Utilities | 2% | 5% |
| | 100% | 100% |

*Asset allocation, geographical diversification and sector diversification are subject to change.*

*For more complete details about the Fund's investment portfolio, see page 6.*

Following the Fund's fiscal first and third quarter-end, a complete portfolio holdings listing is filed with the SEC on Form N-Q. The form will be available on the SEC's Web site at www.sec.gov, and it also may be reviewed and copied at the SEC's Public Reference Room in Washington, D.C. Information on the operation of the SEC's Public Reference Room may be obtained by calling (800) SEC-0330. The Fund's portfolio holdings are also posted on www.dws-investments.com from time to time. Please see the Fund's current prospectus for more information.

## DWS International VIP

| | Shares | Value ($) |
|---|---|---|
| **Common Stocks 95.8%** | | |
| **Australia 8.2%** | | |
| Australia & New Zealand Banking Group Ltd. | 134,879 | 3,221,232 |
| BHP Billiton Ltd. | 132,607 | 6,137,279 |
| National Australia Bank Ltd. | 125,310 | 3,037,560 |
| Newcrest Mining Ltd. | 27,592 | 1,141,261 |
| Wesfarmers Ltd. | 73,691 | 2,411,878 |
| Woodside Petroleum Ltd. | 66,708 | 2,903,825 |
| Woolworths Ltd. | 168,602 | 4,650,873 |
| (Cost $20,902,062) | | **23,503,908** |
| **Brazil 0.7%** | | |
| Banco Santander Brasil SA (Units) (Cost $2,163,676) | 146,403 | **1,991,785** |
| **China 1.5%** | | |
| China Construction Bank Corp. "H" | 1,490,354 | 1,342,178 |
| China National Building Material Co., Ltd. "H" | 630,603 | 1,444,104 |
| Industrial & Commercial Bank of China Ltd. "H" | 2,018,366 | 1,498,298 |
| (Cost $4,673,081) | | **4,284,580** |
| **Denmark 2.4%** | | |
| A P Moller-Maersk AS "B" | 382 | 3,460,127 |
| Carlsberg AS "B" | 13,939 | 1,394,963 |
| Novo Nordisk AS "B" | 19,428 | 2,186,717 |
| (Cost $5,428,284) | | **7,041,807** |
| **Finland 0.8%** | | |
| Fortum Oyj | 41,036 | 1,244,938 |
| Sampo Oyj "A" | 43,826 | 1,174,867 |
| (Cost $2,272,480) | | **2,419,805** |
| **France 9.1%** | | |
| Air Liquide SA | 9,723 | 1,229,643 |
| BNP Paribas | 33,347 | 2,121,578 |
| Compagnie Generale de Geophysique-Veritas* | 53,340 | 1,623,362 |
| GDF Suez | 65,458 | 2,348,610 |
| LVMH Moet Hennessy Louis Vuitton SA | 10,066 | 1,655,842 |
| PPR | 9,451 | 1,502,895 |
| Sanofi-Aventis | 46,220 | 2,955,397 |
| Schneider Electric SA | 21,374 | 3,198,952 |
| Societe Generale | 36,567 | 1,965,330 |
| Technip SA | 16,316 | 1,506,592 |
| Total SA | 77,220 | 4,091,447 |
| Vivendi | 79,766 | 2,153,144 |
| (Cost $24,846,422) | | **26,352,792** |
| **Germany 7.9%** | | |
| Allianz SE (Registered) | 14,554 | 1,729,449 |
| BASF SE | 50,896 | 4,060,262 |
| Bayerische Motoren Werke (BMW) AG | 15,111 | 1,187,558 |
| Daimler AG (Registered)* | 42,381 | 2,871,983 |
| Deutsche Lufthansa AG (Registered)* | 63,783 | 1,393,977 |
| Linde AG | 9,699 | 1,472,189 |
| MAN SE | 10,828 | 1,287,406 |
| Metro AG | 22,831 | 1,643,779 |
| SAP AG | 30,010 | 1,528,114 |
| Siemens AG (Registered) | 37,691 | 4,666,325 |
| ThyssenKrupp AG | 21,008 | 870,359 |
| (Cost $18,982,348) | | **22,711,401** |
| **Hong Kong 3.3%** | | |
| AIA Group Ltd.* | 496,827 | 1,396,623 |
| BOC Hong Kong (Holdings) Ltd. | 467,321 | 1,599,261 |
| Hong Kong Exchanges & Clearing Ltd. | 174,798 | 3,964,709 |
| Hongkong Electric Holdings Ltd. | 406,705 | 2,563,882 |
| (Cost $9,148,344) | | **9,524,475** |
| **India 1.6%** | | |
| Infosys Technologies Ltd. | 21,645 | 1,662,814 |
| ITC Ltd. | 389,302 | 1,523,602 |
| Larsen & Toubro Ltd. | 32,378 | 1,432,264 |
| (Cost $4,498,515) | | **4,618,680** |
| **Italy 1.9%** | | |
| Saipem SpA | 70,516 | 3,474,261 |
| UniCredit SpA | 1,013,511 | 2,096,056 |
| (Cost $3,738,049) | | **5,570,317** |
| **Japan 19.9%** | | |
| Canon, Inc. | 132,065 | 6,770,269 |
| FANUC Corp. | 34,788 | 5,336,695 |
| Honda Motor Co., Ltd. | 84,499 | 3,339,707 |
| Kao Corp. | 118,076 | 3,179,866 |
| Komatsu Ltd. | 98,212 | 2,968,853 |
| Kubota Corp. | 156,905 | 1,484,630 |
| Mitsubishi Corp. | 130,157 | 3,519,787 |
| Mitsubishi Heavy Industries Ltd. | 769,511 | 2,888,812 |
| Mitsui O.S.K Lines Ltd. | 499,397 | 3,404,211 |
| NTT DoCoMo, Inc. | 2,696 | 4,707,325 |
| Panasonic Corp. | 209,682 | 2,959,905 |
| Seven & I Holdings Co., Ltd. | 156,982 | 4,192,889 |
| Shin-Etsu Chemical Co., Ltd. | 78,197 | 4,233,348 |
| Sumitomo Mitsui Financial Group, Inc. | 104,975 | 3,736,585 |
| Takeda Pharmaceutical Co., Ltd. | 61,442 | 3,021,859 |
| Toshiba Corp. | 313,447 | 1,706,141 |
| (Cost $48,388,296) | | **57,450,882** |
| **Mexico 0.7%** | | |
| America Movil SAB de CV Series L (Cost $2,036,853) | 734,889 | **2,106,483** |
| **Netherlands 5.9%** | | |
| ING Groep NV (CVA)* | 244,598 | 2,379,514 |
| Koninklijke (Royal) KPN NV | 106,256 | 1,550,529 |
| Koninklijke Philips Electronics NV | 60,208 | 1,844,050 |
| Royal Dutch Shell PLC "A" | 270,903 | 9,032,268 |
| Unilever NV (CVA) | 69,385 | 2,160,357 |
| (Cost $15,691,874) | | **16,966,718** |
| **Norway 0.9%** | | |
| DnB NOR ASA (Cost $2,187,993) | 190,147 | **2,668,569** |
| **Russia 1.2%** | | |
| Sberbank of Russia (Cost $1,376,791) | 979,941 | **3,338,686** |

*The accompanying notes are an integral part of the financial statements.*

| | Shares | Value ($) |
|---|---|---|
| **Singapore 2.6%** | | |
| Keppel Corp., Ltd. | 377,584 | 3,330,542 |
| Oversea-Chinese Banking Corp., Ltd. | 366,991 | 2,825,317 |
| Singapore Airlines Ltd. | 117,806 | 1,424,669 |
| (Cost $6,774,240) | | **7,580,528** |
| **South Africa 0.6%** | | |
| Remgro Ltd. (Cost $1,537,047) | 97,815 | **1,677,147** |
| **Spain 1.3%** | | |
| Telefonica SA (Cost $3,881,026) | 164,233 | **3,729,899** |
| **Sweden 2.6%** | | |
| Atlas Copco AB "A" | 62,478 | 1,577,731 |
| Hennes & Mauritz AB "B" | 32,583 | 1,085,641 |
| Swedbank AB "A"* | 114,409 | 1,595,317 |
| TeliaSonera AB | 81,801 | 648,542 |
| Volvo AB "B"* | 150,083 | 2,674,895 |
| (Cost $6,416,955) | | **7,582,126** |
| **Switzerland 6.4%** | | |
| Compagnie Financiere Richemont SA "A" | 53,823 | 3,166,467 |
| Givaudan SA (Registered) | 1,445 | 1,560,225 |
| Nestle SA (Registered) | 148,448 | 8,695,716 |
| Novartis AG (Registered) | 23,786 | 1,399,677 |
| Xstrata PLC | 150,227 | 3,526,164 |
| (Cost $11,917,651) | | **18,348,249** |
| **Taiwan 0.9%** | | |
| Taiwan Semiconductor Manufacturing Co., Ltd. (Cost $2,147,196) | 1,051,788 | **2,561,245** |
| **United Kingdom 15.4%** | | |
| AMEC PLC | 103,492 | 1,855,574 |
| AstraZeneca PLC | 59,327 | 2,702,753 |
| British American Tobacco PLC | 106,006 | 4,071,522 |
| Diageo PLC | 261,723 | 4,835,418 |
| GlaxoSmithKline PLC | 232,345 | 4,491,886 |
| HSBC Holdings PLC | 627,409 | 6,369,014 |
| Johnson Matthey PLC | 23,673 | 752,196 |
| Legal & General Group PLC | 1,460,870 | 2,203,618 |
| Lloyds Banking Group PLC* | 1,046,822 | 1,072,289 |
| Reckitt Benckiser Group PLC | 43,011 | 2,363,809 |
| Rio Tinto PLC | 38,762 | 2,711,363 |
| Tesco PLC | 218,671 | 1,448,952 |
| Vodafone Group PLC | 2,349,805 | 6,074,214 |
| WPP PLC | 282,863 | 3,481,787 |
| (Cost $40,608,564) | | **44,434,395** |
| **Total Common Stocks** (Cost $239,617,747) | | **276,464,477** |

## Preferred Stocks 3.8%

| | Shares | Value ($) |
|---|---|---|
| **Brazil 2.2%** | | |
| Itau Unibanco Holding SA | 60,990 | 1,463,372 |
| Petroleo Brasileiro SA | 94,650 | 1,598,269 |
| Ultrapar Participacoes SA | 24,793 | 1,585,280 |
| Vale SA "A" | 53,943 | 1,576,263 |
| (Cost $6,016,853) | | **6,223,184** |
| **Germany 0.8%** | | |
| Volkswagen AG (Cost $2,418,936) | 14,410 | **2,335,096** |
| **Korea 0.8%** | | |
| Samsung Electronics Co., Ltd. (Cost $2,171,594) | 4,200 | **2,401,055** |
| **Total Preferred Stocks** (Cost $10,607,383) | | **10,959,335** |

## Participatory Note 0.5%

| | Shares | Value ($) |
|---|---|---|
| **Indonesia** | | |
| PT Astra International Tbk (issuer Merrill Lynch International & Co.), Expiration Date 10/13/2015* (Cost $1,487,467) | 228,174 | **1,381,453** |

## Cash Equivalents 0.0%

| | Shares | Value ($) |
|---|---|---|
| Central Cash Management Fund, 0.19% (a) (Cost $13,356) | 13,356 | **13,356** |

| | % of Net Assets | Value ($) |
|---|---|---|
| **Total Investment Portfolio** (Cost $251,725,953)† | 100.1 | **288,818,621** |
| **Other Assets and Liabilities, Net** | (0.1) | **(159,838)** |
| **Net Assets** | 100.0 | **288,658,783** |

* *Non-income producing security.*

† *The cost for federal income tax purposes was $252,899,809. At December 31, 2010, net unrealized appreciation for all securities based on tax cost was $35,918,812. This consisted of aggregate gross unrealized appreciation for all securities in which there was an excess of value over tax cost of $40,745,849 and aggregate gross unrealized depreciation for all securities in which there was an excess of tax cost over value of $4,827,037.*

(a) *Affiliated fund managed by Deutsche Investment Management Americas Inc. The rate shown is the annualized seven-day yield at period end.*

*CVA: Certificaten Van Aandelen*

*The accompanying notes are an integral part of the financial statements.*

## Fair Value Measurements

*Various inputs are used in determining the value of the Fund's investments. These inputs are summarized in three broad levels. Level 1 includes quoted prices in active markets for identical securities. Level 2 includes other significant observable inputs (including quoted prices for similar securities, interest rates, prepayment speeds, and credit risk). Level 3 includes significant unobservable inputs (including the Fund's own assumptions in determining the fair value of investments). The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities.*

*The following is a summary of the inputs used as of December 31, 2010 in valuing the Fund's investments. For information on the Fund's policy regarding the valuation of investments, please refer to the Security Valuation section of Note A in the accompanying Notes to Financial Statements.*

| **Assets** | **Level 1** | **Level 2** | **Level 3** | **Total** |
|---|---|---|---|---|
| Common and Preferred Stocks | | | | |
| Australia | $ — | $ 23,503,908 | $ — | $ 23,503,908 |
| Brazil | 8,214,969 | — | — | 8,214,969 |
| China | — | 4,284,580 | — | 4,284,580 |
| Denmark | — | 7,041,807 | — | 7,041,807 |
| Finland | — | 2,419,805 | — | 2,419,805 |
| France | — | 26,352,792 | — | 26,352,792 |
| Germany | — | 25,046,497 | — | 25,046,497 |
| Hong Kong | — | 9,524,475 | — | 9,524,475 |
| India | — | 4,618,680 | — | 4,618,680 |
| Italy | — | 5,570,317 | — | 5,570,317 |
| Japan | — | 57,450,882 | — | 57,450,882 |
| Korea | — | 2,401,055 | — | 2,401,055 |
| Mexico | 2,106,483 | — | — | 2,106,483 |
| Netherlands | — | 16,966,718 | — | 16,966,718 |
| Norway | — | 2,668,569 | — | 2,668,569 |
| Russia | — | 3,338,686 | — | 3,338,686 |
| Singapore | — | 7,580,528 | — | 7,580,528 |
| South Africa | — | 1,677,147 | — | 1,677,147 |
| Spain | — | 3,729,899 | — | 3,729,899 |
| Sweden | — | 7,582,126 | — | 7,582,126 |
| Switzerland | — | 18,348,249 | — | 18,348,249 |
| Taiwan | — | 2,561,245 | — | 2,561,245 |
| United Kingdom | — | 44,434,395 | — | 44,434,395 |
| Participatory Note (b) | — | 1,381,453 | — | 1,381,453 |
| Short-Term Investments (b) | 13,356 | — | — | 13,356 |
| **Total** | **$ 10,334,808** | **$ 278,483,813** | **$ —** | **$ 288,818,621** |

*There have been no significant transfers in and out of Level 1 and Level 2 fair value measurements during the year ended December 31, 2010.*

(b) *See Investment Portfolio for additional detailed categorizations.*

*The accompanying notes are an integral part of the financial statements.*

# Statement of Assets and Liabilities

as of December 31, 2010

| Assets | |
|---|---|
| Investments: | |
| Investments in securities, at value (cost $251,712,597) | $ 288,805,265 |
| Investment in Central Cash Management Fund (cost $13,356) | 13,356 |
| Total investments, at value (cost $251,725,953) | 288,818,621 |
| Foreign currency, at value (cost $862,831) | 868,757 |
| Receivable for Fund shares sold | 75,593 |
| Interest receivable | 133 |
| Dividends receivable | 391,955 |
| Foreign taxes recoverable | 214,116 |
| Other assets | 1,690 |
| Total assets | 290,370,865 |

| Liabilities | |
|---|---|
| Line of credit loan payable | 650,000 |
| Cash overdraft | 500,000 |
| Payable for Fund shares redeemed | 260,006 |
| Accrued management fee | 177,572 |
| Accrued distribution service fee (Class B) | 78 |
| Other accrued expenses and payables | 124,426 |
| Total liabilities | 1,712,082 |
| **Net assets, at value** | **$ 288,658,783** |

| Net Assets Consist of | |
|---|---|
| Undistributed net investment income | 4,383,767 |
| Net unrealized appreciation (depreciation) on: | |
| Investments | 37,092,668 |
| Foreign currency | 27,534 |
| Accumulated net realized gain (loss) | (151,238,256) |
| Paid-in capital | 398,393,070 |
| **Net assets, at value** | **$ 288,658,783** |
| **Class A** | |
| **Net Asset Value,** offering and redemption price per share ($288,292,676 ÷ 35,091,522 outstanding shares of beneficial interest, $.01 par value, unlimited number of shares authorized) | **$ 8.22** |
| **Class B** | |
| **Net Asset Value,** offering and redemption price per share ($366,107 ÷ 44,527 outstanding shares of beneficial interest, $.01 par value, unlimited number of shares authorized) | **$ 8.22** |

# Statement of Operations

for the year ended December 31, 2010

| Investment Income | |
|---|---|
| Income: | |
| Dividends (net of foreign taxes withheld of $993,419) | $ 7,803,741 |
| Interest | 230 |
| Income distributions — Central Cash Management Fund | 25,298 |
| Securities lending income, including income from Daily Assets Fund Institutional, net of borrower rebates | 320,474 |
| Total income | 8,149,743 |
| Expenses: | |
| Management fee | 2,410,956 |
| Administration fee | 305,184 |
| Services to shareholders | 17,714 |
| Custodian fee | 89,837 |
| Distribution service fee (Class B) | 993 |
| Professional fees | 64,456 |
| Trustees' fees and expenses | 13,197 |
| Reports to shareholders | 77,372 |
| Other | 43,906 |
| Total expenses before expense reductions | 3,023,615 |
| Expense reductions | (12,878) |
| Total expenses after expense reductions | 3,010,737 |
| **Net investment income (loss)** | **5,139,006** |

| Realized and Unrealized Gain (Loss) | |
|---|---|
| Net realized gain (loss) from: | |
| Investments | 33,117,429 |
| Foreign currency | (1,084,039) |
| | 32,033,390 |
| Change in net unrealized appreciation (depreciation) on: | |
| Investments | (35,517,787) |
| Foreign currency | 33,833 |
| | (35,483,954) |
| **Net gain (loss)** | **(3,450,564)** |
| **Net increase (decrease) in net assets resulting from operations** | **$ 1,688,442** |

*The accompanying notes are an integral part of the financial statements.*

# Statement of Changes in Net Assets

| Increase (Decrease) in Net Assets | Years Ended December 31, 2010 | 2009 |
|---|---|---|
| Operations: | | |
| Net investment income (loss) | $ 5,139,006 | $ 5,093,925 |
| Net realized gain (loss) | 32,033,390 | (62,986,953) |
| Change in net unrealized appreciation (depreciation) | (35,483,954) | 145,310,993 |
| Net increase (decrease) in net assets resulting from operations | 1,688,442 | 87,417,965 |
| Distributions to shareholders from: | | |
| Net investment income: | | |
| Class A | (6,697,099) | (13,459,468) |
| Class B | (8,035) | (17,118) |
| Total distributions | (6,705,134) | (13,476,586) |
| Fund share transactions: | | |
| **Class A** | | |
| Proceeds from shares sold | 11,044,552 | 14,392,350 |
| Reinvestment of distributions | 6,697,099 | 13,459,468 |
| Cost of shares redeemed | (68,414,073) | (55,084,882) |
| Net increase (decrease) in net assets from Class A share transactions | (50,672,422) | (27,233,064) |
| **Class B** | | |
| Proceeds from shares sold | 28,325 | 18,639 |
| Reinvestment of distributions | 8,035 | 17,118 |
| Cost of shares redeemed | (124,745) | (67,424) |
| Net increase (decrease) in net assets from Class B share transactions | (88,385) | (31,667) |
| **Increase (decrease) in net assets** | (55,777,499) | 46,676,648 |
| Net assets at beginning of period | 344,436,282 | 297,759,634 |
| Net assets at end of period (including undistributed net investment income of $4,383,767 and $4,263,585, respectively) | **$ 288,658,783** | **$ 344,436,282** |

| Other Information | | |
|---|---|---|
| **Class A** | | |
| Shares outstanding at beginning of period | 41,648,336 | 45,605,566 |
| Shares sold | 1,324,213 | 2,028,682 |
| Shares issued to shareholders in reinvestment of distributions | 845,593 | 2,308,657 |
| Shares redeemed | (8,726,620) | (8,294,569) |
| Net increase (decrease) in Class A shares | (6,556,814) | (3,957,230) |
| Shares outstanding at end of period | **35,091,522** | **41,648,336** |
| **Class B** | | |
| Shares outstanding at beginning of period | 56,405 | 60,497 |
| Shares sold | 3,694 | 2,856 |
| Shares issued to shareholders in reinvestment of distributions | 1,012 | 2,931 |
| Shares redeemed | (16,584) | (9,879) |
| Net increase (decrease) in Class B shares | (11,878) | (4,092) |
| Shares outstanding at end of period | **44,527** | **56,405** |

*The accompanying notes are an integral part of the financial statements.*

# Financial Highlights

## Class A

| Years Ended December 31, | 2010 | 2009 | 2008 | 2007 | 2006 |
|---|---|---|---|---|---|
| **Selected Per Share Data** | | | | | |
| **Net asset value, beginning of period** | **$ 8.26** | **$ 6.52** | **$15.01** | **$13.42** | **$10.85** |
| *Income (loss) from investment operations:* | | | | | |
| Net investment income (loss)[a] | .13 | .12 | .29[c] | .21[c] | .28[c] |
| Net realized and unrealized gain (loss) | (.00)* | 1.93 | (6.46) | 1.73 | 2.51 |
| **Total from investment operations** | .13 | 2.05 | (6.17) | 1.94 | 2.79 |
| *Less distributions from:* | | | | | |
| Net investment income | (.17) | (.31) | (.17) | (.35) | (.22) |
| Net realized gains | — | — | (2.15) | — | — |
| **Total distributions** | (.17) | (.31) | (2.32) | (.35) | (.22) |
| **Net asset value, end of period** | **$ 8.22** | **$ 8.26** | **$ 6.52** | **$15.01** | **$13.42** |
| Total Return (%) | 1.62[b] | 33.52 | (48.21)[b,d] | 14.59 | 25.91 |
| **Ratios to Average Net Assets and Supplemental Data** | | | | | |
| Net assets, end of period ($ millions) | 288 | 344 | 297 | 702 | 702 |
| Ratio of expenses before expense reductions (%) | .99 | .94 | 1.01 | .98 | .98 |
| Ratio of expenses after expense reductions (%) | .99 | .94 | .97 | .98 | .98 |
| Ratio of net investment income (loss) (%) | 1.68 | 1.69 | 2.74[c] | 1.48[c] | 2.32[c] |
| Portfolio turnover rate (%) | 228 | 81 | 123 | 108 | 105 |

a *Based on average shares outstanding during the period.*

b *Total return would have been lower had certain expenses not been reduced.*

c *Net investment income per share and the ratio of net investment income include non-recurring dividend income amounting to $0.09, $0.05 and $0.11 per share and 0.82%, 0.33% and 0.92% of average daily net assets for the years ended December 31, 2008, 2007 and 2006, respectively.*

d *Includes a reimbursement from the Advisor to reimburse the effect of losses incurred as the result of certain operation errors during the period. Excluding this reimbursement, total return would have been 0.06% lower.*

* *Amount is less than $.005.*

## Class B

| Years Ended December 31, | 2010 | 2009 | 2008 | 2007 | 2006 |
|---|---|---|---|---|---|
| **Selected Per Share Data** | | | | | |
| **Net asset value, beginning of period** | **$ 8.26** | **$ 6.52** | **$14.98** | **$13.38** | **$10.82** |
| *Income (loss) from investment operations:* | | | | | |
| Net investment income (loss)[a] | .11 | .10 | .23[c] | .16[c] | .24[c] |
| Net realized and unrealized gain (loss) | (.00)* | 1.94 | (6.43) | 1.73 | 2.50 |
| **Total from investment operations** | .11 | 2.04 | (6.20) | 1.89 | 2.74 |
| *Less distributions from:* | | | | | |
| Net investment income | (.15) | (.30) | (.11) | (.29) | (.18) |
| Net realized gains | — | — | (2.15) | — | — |
| **Total distributions** | (.15) | (.30) | (2.26) | (.29) | (.18) |
| **Net asset value, end of period** | **$ 8.22** | **$ 8.26** | **$ 6.52** | **$14.98** | **$13.38** |
| Total Return (%) | 1.33[b] | 32.89 | (48.25)[b,d] | 14.25[b] | 25.44[b] |
| **Ratios to Average Net Assets and Supplemental Data** | | | | | |
| Net assets, end of period ($ millions) | .36 | .50 | .40 | 12 | 51 |
| Ratio of expenses before expense reductions (%) | 1.26 | 1.22 | 1.33 | 1.41 | 1.37 |
| Ratio of expenses after expense reductions (%) | 1.26 | 1.22 | 1.28 | 1.39 | 1.36 |
| Ratio of net investment income (loss) (%) | 1.41 | 1.42 | 2.42[c] | 1.07[c] | 1.94[c] |
| Portfolio turnover rate (%) | 228 | 81 | 123 | 108 | 105 |

a *Based on average shares outstanding during the period.*

b *Total return would have been lower had certain expenses not been reduced.*

c *Net investment income per share and the ratio of net investment income include non-recurring dividend income amounting to $0.09, $0.05 and $0.11 per share and 0.82%, 0.33% and 0.92% of average daily net assets for the years ended December 31, 2008, 2007 and 2006, respectively.*

d *Includes a reimbursement from the Advisor to reimburse the effect of losses incurred as the result of certain operation errors during the period. Excluding this reimbursement, total return would have been 0.06% lower.*

* *Amount is less than $.005.*

# Notes to Financial Statements

## A. Organization and Significant Accounting Policies

DWS Variable Series I (the "Series") is registered under the Investment Company Act of 1940, as amended (the "1940 Act"), as an open-end, registered management investment company organized as a Massachusetts business trust. The Series consists of six diversified funds: DWS Bond VIP, DWS Growth & Income VIP, DWS Capital Growth VIP, DWS Global Opportunities VIP, DWS International VIP and DWS Health Care VIP (individually or collectively hereinafter referred to as a "Fund" or the "Funds"). These financial statements report on DWS International VIP. The Series is intended to be the underlying investment vehicle for variable annuity contracts and variable life insurance policies to be offered by the separate accounts of certain life insurance companies ("Participating Insurance Companies").

**Multiple Classes of Shares of Beneficial Interest.** The Fund offers two classes of shares (Class A shares and Class B shares). Class B shares are subject to Rule 12b-1 distribution fees under the 1940 Act and record keeping fees equal to an annual rate of 0.25% and up to 0.15%, respectively, of the average daily net assets of the Class B shares of the Fund. Class A shares are not subject to such fees.

Investment income, realized and unrealized gains and losses, and certain fund-level expenses and expense reductions, if any, are borne pro rata on the basis of relative net assets by the holders of all classes of shares, except that each class bears certain expenses unique to that class (including the applicable 12b-1 distribution fees and record keeping fees). Differences in class-level expenses may result in payment of different per share dividends by class. All shares have equal rights with respect to voting subject to class-specific arrangements.

The Series' financial statements are prepared in accordance with accounting principles generally accepted in the United States of America, which require the use of management estimates. Actual results could differ from those estimates. The policies described below are followed consistently by the Series in the preparation of the financial statements for its Funds.

**Security Valuation.** Investments are stated at value determined as of the close of regular trading on the New York Stock Exchange on each day the exchange is open for trading.

Various inputs are used in determining the value of the Fund's investments. These inputs are summarized in three broad levels. Level 1 includes quoted prices in active markets for identical securities. Level 2 includes other significant observable inputs (including quoted prices for similar securities, interest rates, prepayment speeds, and credit risk). Level 3 includes significant unobservable inputs (including the Fund's own assumptions in determining the fair value of investments). The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities.

Equity securities are valued at the most recent sale price or official closing price reported on the exchange (US or foreign) or over-the-counter market on which they trade and are categorized as Level 1 securities. Securities for which no sales are reported are valued at the calculated mean between the most recent bid and asked quotations on the relevant market or, if a mean cannot be determined, at the most recent bid quotation. For certain international equity securities, in order to adjust for events which may occur between the close of the foreign exchanges and the close of the New York Stock Exchange, a fair valuation model may be used. This fair valuation model takes into account comparisons to the valuation of American Depository Receipts (ADRs), exchange-traded funds, futures contracts and certain indices and these securities are categorized as Level 2.

Forward currency contracts are valued at the prevailing forward exchange rate of the underlying currencies and are categorized as Level 2.

Money market instruments purchased with an original or remaining maturity of sixty days or less, maturing at par, are valued at amortized cost, which approximates value, and are categorized as Level 2. Investments in open-end investment companies are valued at their net asset value each business day and are categorized as Level 1.

Securities and other assets for which market quotations are not readily available or for which the above valuation procedures are deemed not to reflect fair value are valued in a manner that is intended to reflect their fair value as determined in accordance with procedures approved by the Trustees and are generally categorized as Level 3. In accordance with the Fund's valuation procedures, factors used in determining value may include, but are not limited to, the type of the security; the size of the holding; the initial cost of the security; the existence of any contractual restrictions on the security's disposition; the price and extent of public trading in similar securities of the issuer or of comparable companies; quotations or evaluated prices from broker-dealers and/or pricing services; information obtained from the issuer, analysts, and/or the appropriate stock exchange (for exchange-traded securities); an analysis of the company's or issuer's financial statements; an evaluation of the forces that influence the issuer and the market(s) in which the security is purchased and sold and with respect to debt securities; the maturity, coupon, creditworthiness, currency denomination and the movement of the market

in which the security is normally traded. The value determined under these procedures may differ from published values for the same securities.

Disclosure about the classification of fair value measurements is included in a table following the Fund's Investment Portfolio.

**Securities Lending.** The Fund lends securities to certain financial institutions. The Fund retains beneficial ownership of the securities it has loaned and continues to receive interest and dividends paid by the issuer of securities and to participate in any changes in their market value. The Fund requires the borrowers of the securities to maintain collateral with the Fund consisting of either cash or liquid, unencumbered assets having a value at least equal to the value of the securities loaned. When the collateral falls below specified amounts, the lending agent will use its best effort to obtain additional collateral on the next business day to meet required amounts under the security lending agreement. The Fund may invest the cash collateral into a joint trading account in an affiliated money market fund pursuant to Exemptive Orders issued by the SEC. The Fund receives compensation for lending its securities either in the form of fees or by earning interest on invested cash collateral net of borrower rebates and fees paid to a lending agent. Either the Fund or the borrower may terminate the loan. There may be risks of delay and costs in recovery of securities or even loss of rights in the collateral should the borrower of the securities fail financially. The Fund is also subject to all investment risks associated with the reinvestment of any cash collateral received, including, but not limited to, interest rate, credit and liquidity risk associated with such investments. The Fund had no securities on loan as of December 31, 2010.

**Foreign Currency Translations.** The books and records of the Fund are maintained in US dollars. Investment securities and other assets and liabilities denominated in a foreign currency are translated into US dollars at the prevailing exchange rates at period end. Purchases and sales of investment securities, income and expenses are translated into US dollars at the prevailing exchange rates on the respective dates of the transactions.

Net realized and unrealized gains and losses on foreign currency transactions represent net gains and losses between trade and settlement dates on securities transactions, the disposition of forward foreign currency exchange contracts and foreign currencies, and the difference between the amount of net investment income accrued and the US dollar amount actually received. That portion of both realized and unrealized gains and losses on investments that results from fluctuations in foreign currency exchange rates is not separately disclosed but is included with net realized and unrealized gain/appreciation and loss/depreciation on investments.

**Taxes.** The Fund is treated as a separate taxpayer as provided for in the Internal Revenue Code, as amended. It is the Fund's policy to comply with the requirements of the Internal Revenue Code, as amended, which are applicable to regulated investment companies, and to distribute all of its taxable income to the separate accounts of the Participating Insurance Companies which hold its shares.

Additionally, based on the Series' understanding of the tax rules and rates related to income, gains and transactions for the foreign jurisdictions in which the Fund invests, the Fund will provide for foreign taxes, and where appropriate, deferred foreign taxes.

At December 31, 2010, the Fund had an approximate net tax basis capital loss carryforward which may be applied against any realized net taxable capital gains of each succeeding year until fully utilized or until the following expiration dates, whichever occurs first:

| Fund | Capital Loss Carryforwards ($) | Expiration Date | Capital Loss Carryfowards Utilized ($) |
|---|---|---|---|
| DWS International VIP | 150,205,000 | 12/31/2016–12/31/2017 | 26,324,000 |

The Fund has reviewed the tax positions for the open tax years as of December 31, 2010 and has determined that no provision for income tax is required in the Fund's financial statements. The Fund's federal tax returns for the prior three fiscal years remain open subject to examination by the Internal Revenue Service.

**Distribution of Income and Gains.** The Fund will declare and distribute dividends from its net investment income, if any, annually, although additional distributions may be made if necessary. Net realized gains from investment transactions, in excess of available capital loss carryforwards, would be taxable to the Fund if not distributed, and, therefore, will be distributed to shareholders at least annually.

The timing and characterization of certain income and capital gains distributions are determined annually in accordance with federal tax regulations which may differ from accounting principles generally accepted in the United States of America. These differences primarily relate to investments in foreign denominated investments, investments in forward foreign currency exchange contracts, passive foreign investment companies and certain securities sold at a loss. As a result, net investment income (loss) and net realized gain (loss) on investment transactions for a reporting period may differ significantly from distributions during such period. Accordingly, the Fund may periodically make reclassifications among certain of its capital accounts without impacting the net asset value of the Fund.

At December 31, 2010, the Fund's components of distributable earnings (accumulated losses) on a tax-basis are as follows:

| Fund | Undistributed Ordinary Income ($)* | Capital Loss Carryforwards ($) | Net Unrealized Gain (Loss) on Investments ($) |
|---|---|---|---|
| DWS International VIP | 4,523,867 | (150,205,000) | 35,918,812 |

In addition, the tax character of distributions paid to shareholders by the Fund is summarized as follows:

| | Distributions from Ordinary Income ($)* Years Ended December 31, | |
|---|---|---|
| Fund | 2010 | 2009 |
| DWS International VIP | 6,705,134 | 13,476,586 |

* *For tax purposes, short-term capital gains distributions are considered ordinary income distributions.*

**Expenses.** Expenses of the Series arising in connection with a specific Fund are allocated to that Fund. Other Series expenses which cannot be directly attributed to a Fund are apportioned among the Funds in the Series.

**Contingencies.** In the normal course of business, the Fund may enter into contracts with service providers that contain general indemnification clauses. The Fund's maximum exposure under these arrangements is unknown as this would involve future claims that may be made against the Fund that have not yet been made. However, based on experience, the Fund expects the risk of loss to be remote.

**Other.** Investment transactions are accounted for on a trade date plus one basis for daily net asset value calculations. However, for financial reporting purposes, investment transactions are reported on trade date. Interest income is recorded on the accrual basis net of foreign withholding taxes. Dividend income is recorded on the ex-dividend date net of foreign withholding taxes. Certain dividends from foreign securities may be recorded subsequent to the ex-dividend date as soon as the Fund is informed of such dividends. Realized gains and losses from investment transactions are recorded on an identified cost basis.

## B. Derivative Instruments

**Forward Foreign Currency Exchange Contracts.** A forward foreign currency exchange contract ("forward currency contract") is a commitment to purchase or sell a foreign currency at the settlement date at a negotiated rate. The Fund is subject to foreign exchange rate risk in its securities denominated in foreign currencies. Changes in exchange rates between foreign currencies and the US dollar may affect the US dollar value of foreign securities or the income or gains received on these securities. To reduce the effect of currency fluctuations, the Fund may enter into forward foreign currency exchange contracts. For the year ended December 31, 2010, the Fund invested in forward foreign currency contracts to hedge its exposure to changes in foreign currency exchange rates on its foreign currency denominated securities.

Forward currency contracts are valued at the prevailing forward exchange rate of the underlying currencies and unrealized gain (loss) is recorded daily. On the settlement date of the forward currency contract, the Fund records a realized gain or loss equal to the difference between the value of the contract at the time it was opened and the value of the contract at the time it was closed. Certain risks may arise upon entering into forward currency contracts from the potential inability of counterparties to meet the terms of their contracts. The maximum counterparty credit risk to the Fund is measured by the unrealized gain on appreciated contracts. Additionally, when utilizing forward currency contracts to hedge, the Fund gives up the opportunity to profit from favorable exchange rate movements during the term of the contract.

There are no open forward currency contracts for the Fund as of December 31, 2010. For the year ended December 31, 2010, the investment in forward currency contracts US dollars purchased had a total contract value generally indicative of a range from $0 to approximately $24,890,000.

The amount of realized gains and losses on derivative instruments recognized in Fund earnings during the year ended December 31, 2010 and the related location in the accompanying Statement of Operations is summarized in the following table by primary underlying risk exposure:

| Realized Gain (Loss) | Forward Contracts |
|---|---|
| Foreign Exchange Contracts (a) | $ (1,370,343) |

*The above derivative is located in the following Statement of Operations account:*

(a) *Net realized gain (loss) from foreign currency (Statement of Operations includes both forward currency contracts and foreign currency transactions)*

## C. Purchases and Sales of Securities

During the year ended December 31, 2010, purchases and sales of investment securities (excluding short-term investments) were as follows:

| Fund | Purchases ($) | Sales ($) |
|---|---|---|
| DWS International VIP | 655,754,792 | 694,152,287 |

## D. Related Parties

Under the Investment Management Agreement with Deutsche Investment Management Americas Inc. ("DIMA" or the "Advisor"), an indirect, wholly owned subsidiary of Deutsche Bank AG, the Advisor directs the investments of the Fund in accordance with its investment objectives, policies and restrictions. The Advisor determines the securities, instruments and other contracts relating to investments to be purchased, sold or entered into by the Fund.

Under the Investment Management Agreement with the Advisor, the Fund pays a monthly management fee, based on the average daily net assets of the Fund, computed and accrued daily and payable monthly, at the annual rates shown below:

| Fund | Annual Management Fee Rate |
|---|---|
| DWS International VIP | |
| first $500 million of average daily net assets | .790% |
| over $500 million of average daily net assets | .640% |

For the period from January 1, 2010 through April 30, 2010, the Advisor, the underwriter and accounting agent contractually agreed to waive a portion of their fee to the extent necessary to maintain the operating expenses of each class (excluding certain expenses such as extraordinary expenses, taxes, brokerage and interest) as follows:

| Fund | Annual Rate |
|---|---|
| DWS International VIP Class A | .96% |
| DWS International VIP Class B | 1.29% |

Accordingly, for the year ended December 31, 2010, the total management fee, management fee waived and effective management fee rate are as follows:

| Fund | Total Aggregated ($) | Waived ($) | Annual Effective Rate |
|---|---|---|---|
| DWS International VIP | 2,410,956 | 12,024 | .79% |

**Administration Fee.** Pursuant to an Administrative Services Agreement, DIMA provides most administrative services to the Series. For all services provided under the Administrative Services Agreement, the Fund pays the Advisor an annual fee ("Administration Fee") of 0.10% of the Fund's average daily net assets, computed and accrued daily and payable monthly. For the year ended December 31, 2010, the Administration Fee was as follows:

| Fund | Total Aggregated ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS International VIP | 305,184 | 24,377 |

**Service Provider Fees.** DWS Investments Service Company ("DISC"), an affiliate of the Advisor, is the transfer agent, dividend-paying agent and shareholder service agent for the Series. Pursuant to a sub-transfer agency agreement between DISC and DST Systems, Inc. ("DST"), DISC has delegated certain transfer agent, dividend-paying agent and shareholder service agent functions to DST. DISC compensates DST out of the shareholder servicing fee it receives from the Fund. For the year ended December 31, 2010, the amounts charged to the Fund by DISC were as follows:

| Fund | Total Aggregated ($) | Waived ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|---|
| DWS International VIP Class A | 854 | 854 | — |
| DWS International VIP Class B | 96 | — | 24 |

DWS Investments Distributors, Inc. ("DIDI"), also an affiliate of the Advisor, is the Series' Distributor. In accordance with the Master Distribution Plan, DIDI receives 12b-1 fees of 0.25% of average daily net assets of

Class B shares. Pursuant to the Master Distribution Plan, DIDI remits these fees to the Participating Insurance Companies for various costs incurred or paid by these companies in connection with marketing and distribution of Class B shares. These fees are detailed in the Fund's Statement of Operations.

**Typesetting and Filing Service Fees.** Under an agreement with DIMA, DIMA is compensated for providing typesetting and certain regulatory filing services to the Fund. For the year ended December 31, 2010, the amount charged to the Fund by DIMA included in the Statement of Operations under "reports to shareholders" was as follows:

| Fund | Total Aggregated ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS International VIP | 13,860 | 3,470 |

**Trustees' Fees and Expenses.** The Fund paid each Trustee not affiliated with the Advisor retainer fees plus specified amounts for various committee services and for the Board Chairperson.

**Affiliated Cash Management Vehicles.** The Fund may invest uninvested cash balances in Central Cash Management Fund, which is managed by the Advisor. The Fund indirectly bears its proportionate share of the expenses of the underlying money market funds. Central Cash Management Fund does not pay the Advisor an investment management fee. Central Cash Management Fund seeks a high level of current income consistent with liquidity and the preservation of capital.

## E. Investing in Emerging Markets

Investing in emerging markets may involve special risks and considerations not typically associated with investing in developed markets. These risks include revaluation of currencies, high rates of inflation or deflation, repatriation restrictions on income and capital, and future adverse political, social and economic developments. Moreover, securities issued in these markets may be less liquid, subject to government ownership controls or delayed settlements and may have prices more volatile or less easily assessed than those of comparable securities of issuers in developed markets.

## F. Ownership of the Fund

Two participating insurance companies were owners of record of 10% or more of the total outstanding Class A shares of the Fund, each owning 41% and 13%. Three participating insurance companies were owners of record of 10% or more of the total outstanding Class B shares of the Fund, each owning 76%, 13% and 11%.

## G. Line of Credit

The Series and other affiliated funds (the "Participants") share in a $450 million revolving credit facility provided by a syndication of banks. The Fund may borrow for temporary or emergency purposes, including the meeting of redemption requests that otherwise might require the untimely disposition of securities. The Participants are charged an annual commitment fee which is allocated based on net assets, among each of the Participants. Interest is calculated at a rate per annum equal to the sum of the Federal Funds Rate plus 1.25 percent plus if LIBOR exceeds the Federal Funds Rate the amount of such excess. The Fund may borrow up to a maximum of 33 percent of its net assets under the agreement.

At December, 31, 2010, the Fund had a $650,000 outstanding loan. Interest expense incurred on the borrowing was $928 for the year ended December, 31, 2010. The average dollar amount of the borrowings was $693,750, the weighted average interest rate on these borrowings was 1.51% and the Fund had a loan outstanding for thirty two days throughout the period. The borrowings were valued at cost, which approximates fair value.

# Report of Independent Registered Public Accounting Firm

**To the Trustees of DWS Variable Series I and the Shareholders of DWS International VIP:**

In our opinion, the accompanying statement of assets and liabilities, including the investment portfolio, and the related statements of operations and of changes in net assets and the financial highlights present fairly, in all material respects, the financial position of DWS International VIP (the "Fund") at December 31, 2010 and the results of its operations, the changes in its net assets, and the financial highlights for the periods indicated therein, in conformity with accounting principles generally accepted in the United States of America. These financial statements and financial highlights (hereafter referred to as "financial statements") are the responsibility of the Fund's management. Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these financial statements in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits, which included confirmation of securities at December 31, 2010 by correspondence with the custodians and brokers, provide a reasonable basis for our opinion.

Boston, Massachusetts
February 11, 2011

PricewaterhouseCoopers LLP

## Tax Information

**(Unaudited)**

For corporate shareholders of the Fund, 3% of the ordinary dividends (i.e., income dividends plus short-term capital gains) paid during the Fund's fiscal year ended December 31, 2010 qualified for the dividends received deduction.

The Fund paid foreign taxes of $646,822 and earned $4,560,951 of foreign source income during the year ended December 31, 2010. Pursuant to Section 853 of the Internal Revenue Code, the Fund designates $0.02 per share as foreign taxes paid and $0.13 per share as income earned from foreign sources for the year ended December 31, 2010.

Please consult a tax advisor if you have questions about federal or state income tax laws, or on how to prepare your tax returns. If you have specific questions about your account, please contact your insurance provider.

## Proxy Voting

The Series' policies and procedures for voting proxies for portfolio securities and information about how the Series voted proxies related to its portfolio securities during the 12-month period ended June 30 are available on our Web site — www.dws-investments.com (click on "proxy voting"at the bottom of the page) — or on the SEC's Web site — www.sec.gov. To obtain a written copy of the Series' policies and procedures without charge, upon request, call us toll free at (800) 728-3337.

# Investment Management Agreement Approval

The Board of Trustees, including the Independent Trustees, approved the renewal of your Fund's investment management agreement (the "Agreement") with Deutsche Investment Management Americas Inc. ("DWS") in September 2010.

In terms of the process that the Board followed prior to approving the Agreement, shareholders should know that:

- In September 2010, all of the Fund's Trustees were independent of DWS and its affiliates.
- The Trustees meet frequently to discuss fund matters. Each year, the Trustees dedicate substantial time to contract review matters. Over the course of several months, the Board's Contract Committee, in coordination with the Board's Equity Oversight Committee, reviewed comprehensive materials received from DWS, independent third parties and independent counsel. These materials included an analysis of the Fund's performance, fees and expenses, and profitability compiled by the Fund's independent fee consultant. The Board also received extensive information throughout the year regarding performance of the Fund.
- The Independent Trustees regularly meet privately with their independent counsel to discuss contract review and other matters. In addition, the Independent Trustees were also advised by the Fund's independent fee consultant in the course of their review of the Fund's contractual arrangements and considered a comprehensive report prepared by the independent fee consultant in connection with their deliberations (the "IFC Report").
- In connection with reviewing the Agreement, the Board also reviewed the terms of the Fund's Rule 12b-1 plan, distribution agreement, administrative services agreement, transfer agency agreement and other material service agreements.
- Based on its evaluation of the information provided, the Contract Committee presented its findings and recommendations to the Independent Trustees as a group. The Independent Trustees reviewed the Contract Committee's findings and recommendations and presented their recommendations to the full Board.

In connection with the contract review process, the Contract Committee and the Board considered the factors discussed below, among others. The Board also considered that DWS and its predecessors have managed the Fund since its inception, and the Board believes that a long-term relationship with a capable, conscientious advisor is in the best interests of the Fund. The Board considered, generally, that shareholders chose to invest or remain invested in the Fund knowing that DWS managed the Fund, and that the Agreement was approved by the Fund's shareholders. DWS is part of Deutsche Bank, a major global banking institution that is engaged in a wide range of financial services. The Board believes that there are significant advantages to being part of a global asset management business that offers a wide range of investing expertise and resources, including hundreds of portfolio managers and analysts with research capabilities in many countries throughout the world.

While shareholders may focus primarily on fund performance and fees, the Fund's Board considers these and many other factors, including the quality and integrity of DWS's personnel and such other issues as back-office operations, fund valuations, and compliance policies and procedures.

**Nature, Quality and Extent of Services.** The Board considered the terms of the Agreement, including the scope of advisory services provided under the Agreement. The Board noted that, under the Agreement, DWS provides portfolio management services to the Fund and that, pursuant to a separate administrative services agreement, DWS provides administrative services to the Fund. The Board considered the experience and skills of senior management and investment personnel, the resources made available to such personnel, the ability of DWS to attract and retain high-quality personnel, and the organizational depth and stability of DWS. The Board reviewed the Fund's performance over short-term and long-term periods and compared those returns to various agreed-upon performance measures, including market indices and a peer universe compiled by the independent fee consultant using information supplied by Lipper Inc. ("Lipper"). The Board also noted that it has put into place a process of identifying "Focus Funds" (e.g., funds performing poorly relative to their benchmark or a peer universe compiled by Lipper), and receives more frequent reporting and information from DWS regarding such funds, along with DWS's remedial plans to address underperformance. The Board believes this process is an effective manner of identifying and addressing underperforming funds. Based on the information provided, the Board noted that for the one-, three- and five-year periods ended December 31, 2009, the Fund's performance (Class A shares) was in the 2nd quartile, 4th quartile and 3rd quartile, respectively, of the applicable Lipper universe (the 1st quartile being the best performers and the 4th quartile being the worst performers). The Board also observed that the Fund has outperformed its benchmark in the one-year period and has underperformed its benchmark in the three- and five-year periods ended December 31, 2009.

On the basis of this evaluation and the ongoing review of investment results by the Board, the Board concluded that the nature, quality and extent of services provided by DWS historically have been and continue to be satisfactory.

**Fees and Expenses.** The Board considered the Fund's investment management fee schedule, operating expenses and total expense ratios, and comparative information provided by Lipper and the independent fee consultant regarding investment management fee rates paid to other investment advisors by similar funds (1st quartile being the most favorable and 4th quartile being the least favorable). With respect to management fees paid to other investment advisors by similar funds, the Board noted that the contractual fee rates paid by the Fund, which include a 0.10% fee paid to DWS under the Fund's administrative services agreement, were lower than the median (2nd quartile) of the applicable Lipper peer group (based on Lipper data provided as of December 31, 2009). The Board noted that the Fund's Class A shares total (net) operating expenses were expected to be higher than the median (3rd quartile) of the applicable Lipper expense universe (based on Lipper data provided as of December 31, 2009) ("Lipper Universe Expenses"). The Board also reviewed data comparing each share class's total (net) operating expenses to the applicable Lipper Universe Expenses. The Board considered the Fund's management fee rate as compared to fees charged by DWS and certain of its affiliates for comparable mutual funds and considered differences in fund and fee structures between the DWS Funds. The Board also considered how the Fund's total (net) operating expenses compared to the total (net) operating expenses of a more customized peer group selected by Lipper (based on such factors as asset size).

The information considered by the Board as part of its review of management fees included information regarding fees charged by DWS and its affiliates to similar institutional accounts and to similar funds offered primarily to European investors ("DWS Europe funds"), in each case as applicable. The Board observed that advisory fee rates for institutional accounts generally were lower than the management fees charged by similarly managed DWS US mutual funds ("DWS Funds"), but also took note of the differences in services provided to DWS Funds as compared to institutional accounts. In the case of DWS Europe funds, the Board observed that fee rates for DWS Europe funds generally were higher than for similarly managed DWS Funds, but noted that differences in the types of services provided to DWS Funds relative to DWS Europe funds made it difficult to compare such fees.

On the basis of the information provided, the Board concluded that management fees were reasonable and appropriate in light of the nature, quality and extent of services provided by DWS.

**Profitability.** The Board reviewed detailed information regarding revenues received by DWS under the Agreement. The Board considered the estimated costs and pre-tax profits realized by DWS from advising the DWS Funds, as well as estimates of the pre-tax profits attributable to managing the Fund in particular. The Board also received information regarding the estimated enterprise-wide profitability of DWS and its affiliates with respect to all fund services in totality and by fund. The Board reviewed DWS's methodology in allocating its costs to the management of the Fund. Based on the information provided, the Board concluded that the pre-tax profits realized by DWS in connection with the management of the Fund were not unreasonable. The Board also reviewed information regarding the profitability of certain similar investment management firms. The Board noted that while information regarding the profitability of such firms is limited (and in some cases is not necessarily prepared on a comparable basis), DWS and its affiliates' overall profitability with respect to the DWS fund complex (after taking into account distribution and other services provided to the funds by DWS and its affiliates) was lower than the overall profitability levels of many comparable firms for which such data was available.

**Economies of Scale.** The Board considered whether there are economies of scale with respect to the management of the Fund and whether the Fund benefits from any economies of scale. The Board noted that the Fund's management fee schedule includes fee breakpoints. The Board concluded that the Fund's fee schedule represents an appropriate sharing between the Fund and DWS of such economies of scale as may exist in the management of the Fund at current asset levels.

**Other Benefits to DWS and Its Affiliates.** The Board also considered the character and amount of other incidental benefits received by DWS and its affiliates, including any fees received by DWS for administrative services provided to the Fund and any fees received by an affiliate of DWS for distribution services. The Board also considered benefits to DWS related to brokerage and soft-dollar allocations, including allocating brokerage to pay for research generated by parties other than the executing broker dealers, which pertain primarily to funds investing in equity securities, along with the incidental public relations benefits to DWS related to DWS Funds advertising and cross-selling opportunities among DWS products and services. The Board concluded that management fees were reasonable in light of these fallout benefits.

**Compliance.** The Board considered the significant attention and resources dedicated by DWS to documenting and enhancing its compliance processes in recent years. The Board noted in particular (i) the experience and seniority of both DWS's chief compliance officer and the Fund's chief compliance officer; (ii) the large number of

DWS compliance personnel; and (iii) the substantial commitment of resources by DWS and its affiliates to compliance matters.

Based on all of the information considered and the conclusions reached, the Board unanimously determined that the continuation of the Agreement is in the best interests of the Fund. In making this determination, the Board did not give particular weight to any single factor identified above. The Board considered these factors over the course of numerous meetings, certain of which were in executive session with only the Independent Trustees and their counsel present. It is possible that individual Trustees may have weighed these factors differently in reaching their individual decisions to approve the continuation of the Agreement.

# Summary of Management Fee Evaluation by Independent Fee Consultant

October 3, 2010

Pursuant to an Order entered into by Deutsche Investment Management Americas and affiliates (collectively, "DeAM") with the Attorney General of New York, I, Thomas H. Mack, have been appointed the Independent Fee Consultant for the DWS Funds (formerly the DWS Scudder Funds). My duties include preparing an annual written evaluation of the management fees DeAM charges the Funds, considering among other factors the management fees charged by other mutual fund companies for like services, management fees DeAM charges other clients for like services, DeAM's costs of supplying services under the management agreements and related profit margins, possible economies of scale if a Fund grows larger, and the nature and quality of DeAM's services, including fund performance. This report summarizes my evaluation for 2010, including my qualifications, the evaluation process for each of the DWS Funds, consideration of certain complex-level factors, and my conclusions. I served in substantially the same capacity in 2007, 2008, and 2009.

## Qualifications

For more than 35 years I have served in various professional capacities within the investment management business. I have held investment analysis and advisory positions, including securities analyst, portfolio strategist and director of investment policy with a large investment firm. I have also performed business management functions, including business development, financial management and marketing research and analysis.

Since 1991, I have been an independent consultant within the asset management industry. I have provided services to over 125 client organizations, including investment managers, mutual fund boards, product distributors and related organizations. Over the past ten years I have completed a number of assignments for mutual fund boards, specifically including assisting boards with management contract renewal.

I hold a Master of Business Administration degree, with highest honors, from Harvard University and Master of Science and Bachelor of Science (highest honors) degrees from the University of California at Berkeley. I am an independent director and audit committee financial expert for two closed-end mutual funds and have served in various leadership and financial oversight capacities with non-profit organizations.

## Evaluation of Fees for each DWS Fund

My work focused primarily on evaluating, fund-by-fund, the fees charged to each of the 118 publicly offered Fund portfolios in the DWS Fund family. For each Fund, I considered each of the key factors mentioned above, as well as any other relevant information. In doing so I worked closely with the Funds' Independent Directors in their annual contract renewal process, as well as in their approval of contracts for several new funds (documented separately).

In evaluating each Fund's fees, I reviewed comprehensive materials provided by or on behalf of DeAM, including expense information prepared by Lipper Analytical, comparative performance information, profitability data, manager histories, and other materials. I also accessed certain additional information from the Lipper and Morningstar databases and drew on my industry knowledge and experience.

To facilitate evaluating this considerable body of information, I prepared for each Fund a document summarizing the key data elements in each area as well as additional analytics discussed below. This made it possible to consider each key data element in the context of the others.

In the course of contract renewal, DeAM agreed to implement a number of fee and expense adjustments requested by the Independent Directors which will favorably impact future fees and expenses, and my evaluation includes the effects of these changes.

### Fees and Expenses Compared with Other Funds

The competitive fee and expense evaluation for each fund focused on two primary comparisons:

- The Fund's contractual management fee (the advisory fee plus the administration fee where applicable) compared with those of a group of typically 12–15 funds in the same Lipper investment category (e.g. Large Capitalization Growth) having similar distribution arrangements and being of similar size.
- The Fund's total expenses compared with a broader universe of funds from the same Lipper investment category and having similar distribution arrangements.

These two comparisons provide a view of not only the level of the fee compared with funds of similar scale but also the total expense the Fund bears for all the services it receives, in comparison with the investment choices available in the Fund's investment category and distribution channel. The principal figure-of-merit used in these comparisons was the subject Fund's percentile ranking against peers.

### DeAM's Fees for Similar Services to Others

DeAM provided management fee schedules for all of its US domiciled fund and non-fund investment management accounts in any of the investment categories where there is a DWS Fund. These similar products included the other DWS Funds, non-fund pooled accounts, institutional accounts and sub-advisory accounts. Using this information, I calculated for each Fund the fee that would be charged to each similar product, at the subject Fund's asset level.

Evaluating information regarding non-fund products is difficult because there are varying levels of services required for different types of accounts, with mutual funds generally requiring considerably more regulatory and administrative types of service as well as having more frequent cash flows than other types of accounts. Also, while mutual fund fees for similar fund products can be expected to be similar, there will be some differences due to different pricing conditions in different distribution channels (e.g. retail funds versus those used in variable insurance products), differences in underlying investment processes and other factors.

**Costs and Profit Margins**

DeAM provided a detailed profitability analysis for each Fund. After making some adjustments so that the presentation would be more comparable to the available industry figures, I reviewed profit margins from investment management alone, from investment management plus other fund services (excluding distribution) provided to the Funds by DeAM (principally shareholder services), and DeAM profits from all sources, including distribution. A later section comments on overall profitability.

**Economies of Scale**

Economies of scale — an expected decline in management cost per dollar of fund assets as fund assets grow — are very rarely quantified and documented because of inherent difficulties in collecting and analyzing relevant data. However, in virtually every investment category that I reviewed, larger funds tend to have lower fees and lower total expenses than smaller funds. To see how each DWS Fund compares with this industry observation, I reviewed:

- The trend in Fund assets over the last five years and the accompanying trend in total expenses. This shows if the Fund has grown and, if so, whether total expense (management fees as well as other expenses) have declined as a percent of assets.
- Whether the Fund has break-points in its management fee schedule, the extent of the fee reduction built into the schedule and the asset levels where the breaks take effect, and in the case of a sub-advised Fund how the Fund's break-points compare with those of the sub-advisory fee schedule.
- How the Fund's contractual fee schedule compares with trends in the industry data. To accomplish this, I constructed a chart showing how actual latest-fiscal-year contractual fees of the Fund and of other similar funds relate to average fund assets, with the subject Fund's contractual fee schedule superimposed.

**Quality of Service — Performance**

The quality-of-service evaluation focused on investment performance, which is the principal result of the investment management service. Each Fund's performance was reviewed over the past 1, 3, 5 and 10 years, as applicable, and compared with that of other funds in the same investment category and with a suitable market index.

In addition, I calculated and reviewed risk-adjusted returns relative to an index of similar mutual funds' returns and a suitable market index. The risk-adjusted returns analysis provides a way of determining the extent to which the Fund's return comparisons are mainly the product of investment value-added (or lack thereof) or alternatively taking considerably more or less risk than is typical in its investment category.

I also received and considered the history of portfolio manager changes for each Fund, as this provided an important context for evaluating the performance results.

## Complex-Level Considerations

While this evaluation was conducted mainly at the individual fund level, there are some issues relating to the reasonableness of fees that can alternatively be considered across the whole fund complex:

- I reviewed DeAM's profitability analysis for all DWS Funds, with a view toward determining if the allocation procedures used were reasonable and how profit levels compared with public data for other investment managers.
- I considered whether DeAM and affiliates receive any significant ancillary or "fall-out" benefits that should be considered in interpreting the direct profitability results. These would be situations where serving as the investment manager of the Funds is beneficial to another part of the Deutsche Bank organization.
- I considered how aggregated DWS Fund expenses had varied over the years, by asset class and in the context of trends in asset levels.
- I reviewed the structure of the DeAM organization, trends in staffing levels, and information on compensation of investment management and other professionals compared with industry data.

## Findings

Based on the process and analysis discussed above, which included reviewing a wide range of information from management and external data sources and considering among other factors the fees DeAM charges other clients, the fees charged by other fund managers, DeAM's costs and profits associated with managing the Funds, economies of scale, possible fall-out benefits, and the nature and quality of services provided, in my opinion the management fees charged the DWS Funds are reasonable.

Thomas H. Mack

# Board Members and Officers

The following table presents certain information regarding the Board Members and Officers of the Trust as of December 31, 2010. Each Board Member's year of birth is set forth in parentheses after his or her name. Unless otherwise noted, (i) each Board Member has engaged in the principal occupation(s) noted in the table for at least the most recent five years, although not necessarily in the same capacity; and (ii) the address of each Independent Board Member is c/o Paul K. Freeman, Independent Chairman, DWS Funds, PO Box 101833, Denver, CO 80250-1833. Except as otherwise noted below, the term of office for each Board Member is until the election and qualification of a successor, or until such Board Member sooner dies, resigns, is removed or as otherwise provided in the governing documents of the fund. Because the fund does not hold an annual meeting of shareholders, each Board Member will hold office for an indeterminate period. The Board Members may also serve in similar capacities with other funds in the fund complex. The Length of Time Served represents the year in which the Board Member joined the board of one or more DWS funds now overseen by the Board.

**Independent Board Members**

| Name, Year of Birth, Position with the Fund and Length of Time Served[1] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Paul K. Freeman (1950)<br>Chairperson since 2009<br>Board Member since 1993 | Consultant, World Bank/Inter-American Development Bank; Executive and Governing Council of the Independent Directors Council (education committees); formerly, Project Leader, International Institute for Applied Systems Analysis (1998–2001); Chief Executive Officer, The Eric Group, Inc. (environmental insurance) (1986–1998) | 122 |
| John W. Ballantine (1946)<br>Board Member since 1999 | Retired; formerly, Executive Vice President and Chief Risk Management Officer, First Chicago NBD Corporation/The First National Bank of Chicago (1996–1998); Executive Vice President and Head of International Banking (1995–1996). Directorships: Healthways, Inc. (provider of disease and care management services); Portland General Electric (utility company); Stockwell Capital Investments PLC (private equity). Former Directorships: First Oak Brook Bancshares, Inc. and Oak Brook Bank; Prisma Energy International | 122 |
| Henry P. Becton, Jr. (1943)<br>Board Member since 1990 | Vice Chair and former President, WGBH Educational Foundation. Directorships: Association of Public Television Stations; Lead Director, Becton Dickinson and Company[3] (medical technology company); Lead Director, Belo Corporation[3] (media company); Public Radio International; Public Radio Exchange (PRX); The PBS Foundation. Former Directorships: Boston Museum of Science; American Public Television; Concord Academy; New England Aquarium; Mass. Corporation for Educational Telecommunications; Committee for Economic Development; Public Broadcasting Service | 122 |
| Dawn-Marie Driscoll (1946)<br>Board Member since 1987 | President, Driscoll Associates (consulting firm); Executive Fellow, Center for Business Ethics, Bentley University; formerly, Partner, Palmer & Dodge (1988–1990); Vice President of Corporate Affairs and General Counsel, Filene's (1978–1988). Directorships: Trustee of 22 open-end mutual funds managed by Sun Capital Advisers, Inc. (since 2007); Director of ICI Mutual Insurance Company (since 2007); Advisory Board, Center for Business Ethics, Bentley University; Trustee, Southwest Florida Community Foundation (charitable organization). Former Directorships: Investment Company Institute (audit, executive, nominating committees) and Independent Directors Council (governance, executive committees) | 122 |
| Keith R. Fox (1954)<br>Board Member since 1996 | Managing General Partner, Exeter Capital Partners (a series of private investment funds). Directorships: Progressive International Corporation (kitchen goods importer and distributor); BoxTop Media Inc. (advertising); The Kennel Shop (retailer); former Chairman, National Association of Small Business Investment Companies | 122 |
| Kenneth C. Froewiss (1945)<br>Board Member since 2001 | Adjunct Professor of Finance, NYU Stern School of Business (September 2009–present; Clinical Professor from 1997–September 2009); Member, Finance Committee, Association for Asian Studies (2002–present); Director, Mitsui Sumitomo Insurance Group (US) (2004–present); prior thereto, Managing Director, J.P. Morgan (investment banking firm) (until 1996) | 122 |
| Richard J. Herring (1946)<br>Board Member since 1990 | Jacob Safra Professor of International Banking and Professor, Finance Department, The Wharton School, University of Pennsylvania (since July 1972); Co-Director, Wharton Financial Institutions Center (since July 2000); Co-Chair, U.S. Shadow Financial Regulatory Committee; Executive Director, Financial Economists Roundtable; Director, Japan Equity Fund, Inc. (since September 2007), Thai Capital Fund, Inc. (since September 2007), Singapore Fund, Inc. (since September 2007); Independent Director of Barclays Bank Delaware (since September 2010). Formerly, Vice Dean and Director, Wharton Undergraduate Division (July 1995–June 2000); Director, Lauder Institute of International Management Studies (July 2000–June 2006) | 122 |
| William McClayton (1944)<br>Board Member since 2004+ | Private equity investor (since October 2009); previously, Managing Director, Diamond Management & Technology Consultants, Inc. (global consulting firm) (2001–2009); Directorship: Board of Managers, YMCA of Metropolitan Chicago; formerly: Senior Partner, Arthur Andersen LLP (accounting) (1966–2001); Trustee, Ravinia Festival | 122 |

| Name, Year of Birth, Position with the Fund and Length of Time Served[1] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Rebecca W. Rimel (1951)<br>Board Member since 1995 | President and Chief Executive Officer, The Pew Charitable Trusts (charitable organization) (1994 to present); Trustee, Thomas Jefferson Foundation (charitable organization) (1994 to present); Trustee, Executive Committee, Philadelphia Chamber of Commerce (2001–2007); Director, CardioNet, Inc.[2] (2009–present) (health care). Formerly, Executive Vice President, The Glenmede Trust Company (investment trust and wealth management) (1983–2004); Board Member, Investor Education (charitable organization) (2004–2005); Director, Viasys Health Care[2] (January 2007–June 2007); Trustee, Pro Publica (charitable organization) (2007–2010) | 122 |
| William N. Searcy, Jr. (1946)<br>Board Member since 1993 | Private investor since October 2003; Trustee of 22 open-end mutual funds managed by Sun Capital Advisers, Inc. (since October 1998). Formerly, Pension & Savings Trust Officer, Sprint Corporation[2] (telecommunications) (November 1989–September 2003) | 122 |
| Jean Gleason Stromberg (1943)<br>Board Member since 1997 | Retired. Formerly, Consultant (1997–2001); Director, Financial Markets US Government Accountability Office (1996–1997); Partner, Fulbright & Jaworski, L.L.P. (law firm) (1978–1996). Directorships: The William and Flora Hewlett Foundation. Former Directorships: Service Source, Inc., Mutual Fund Directors Forum (2002–2004), American Bar Retirement Association (funding vehicle for retirement plans) (1987–1990 and 1994–1996) | 122 |
| Robert H. Wadsworth (1940)<br>Board Member since 1999 | President, Robert H. Wadsworth & Associates, Inc. (consulting firm) (1983 to present); Director, The Phoenix Boys Choir Association | 125 |

## Officers[4]

| Name, Year of Birth, Position with the Fund and Length of Time Served[5] | Principal Occupation(s) During Past 5 Years and Other Directorships Held |
|---|---|
| Michael G. Clark[6] (1965)<br>President, 2006–present | Managing Director[3], Deutsche Asset Management (2006–present); President of DWS family of funds; Director, ICI Mutual Insurance Company (since October 2007); formerly, Director of Fund Board Relations (2004–2006) and Director of Product Development (2000–2004), Merrill Lynch Investment Managers; Senior Vice President Operations, Merrill Lynch Asset Management (1999–2000) |
| Ingo Gefeke[7] (1967)<br>Executive Vice President since 2010 | Managing Director[3], Deutsche Asset Management; Global Head of Distribution and Product Management, DWS Global Head of Trading and Securities Lending. Member of the Board of Directors of DWS Investment GmbH Frankfurt (since July 2009) and DWS Holding & Service GmbH Frankfurt (since January 2010); formerly, Global Chief Administrative Officer, Deutsche Asset Management (2004–2009); Global Chief Operating Officer, Global Transaction Banking, Deutsche Bank AG, New York (2001–2004); Chief Operating Officer, Global Banking Division Americas, Deutsche Bank AG, New York (1999–2001); Central Management, Global Banking Services, Deutsche Bank AG, Frankfurt (1998–1999); Relationship Management, Deutsche Bank AG, Tokyo, Japan (1997–1998) |
| John Millette[8] (1962)<br>Vice President and Secretary, 1999–present | Director[3], Deutsche Asset Management |
| Paul H. Schubert[6] (1963)<br>Chief Financial Officer, 2004–present<br>Treasurer, 2005–present | Managing Director[3], Deutsche Asset Management (since July 2004); formerly, Executive Director, Head of Mutual Fund Services and Treasurer for UBS Family of Funds (1998–2004); Vice President and Director of Mutual Fund Finance at UBS Global Asset Management (1994–1998) |
| Caroline Pearson[8] (1962)<br>Chief Legal Officer, April 2010–present | Managing Director[3], Deutsche Asset Management; formerly, Assistant Secretary for DWS family of funds (1997–2010) |
| Rita Rubin[9] (1970)<br>Assistant Secretary, 2009–present | Vice President and Counsel, Deutsche Asset Management (since October 2007); formerly, Vice President, Morgan Stanley Investment Management (2004–2007) |
| Paul Antosca[8] (1957)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management (since 2006); Vice President, The Manufacturers Life Insurance Company (U.S.A.) (1990–2006) |
| Jack Clark[8] (1967)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management (since 2007); formerly, Vice President, State Street Corporation (2002–2007) |
| Diane Kenneally[8] (1966)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management |
| John Caruso[9] (1965)<br>Anti-Money Laundering Compliance Officer, 2010–present | Managing Director[3], Deutsche Asset Management |

| Name, Year of Birth, Position with the Fund and Length of Time Served[5] | Principal Occupation(s) During Past 5 Years and Other Directorships Held |
|---|---|
| Robert Kloby[9] (1962)<br>Chief Compliance Officer, 2006–present | Managing Director[3], Deutsche Asset Management |

1 *The length of time served represents the year in which the Board Member joined the board of one or more DWS funds currently overseen by the Board.*

2 *A publicly held company with securities registered pursuant to Section 12 of the Securities Exchange Act of 1934.*

3 *Executive title, not a board directorship.*

4 *As a result of their respective positions held with the Advisor, these individuals are considered "interested persons" of the Advisor within the meaning of the 1940 Act. Interested persons receive no compensation from the fund.*

5 *The length of time served represents the year in which the officer was first elected in such capacity for one or more DWS funds.*

6 *Address: 100 Plaza One, Jersey City, NJ 07311.*

7 *Effective January 11, 2011, Mr. Gefeke, Executive Vice President, resigned as an officer of the fund.*

*The mailing address of Mr. Gefeke is 345 Park Avenue, New York, New York 10154. Mr. Gefeke was an interested Board Member of certain DWS funds by virtue of his positions with Deutsche Asset Management. As an interested person, Mr. Gefeke received no compensation from the fund.*

8 *Address: One Beacon Street, Boston, MA 02108.*

9 *Address: 60 Wall Street, New York, New York 10005.*

*The fund's Statement of Additional Information ("SAI") includes additional information about the Board Members. The SAI is available, without charge, upon request. If you would like to request a copy of the SAI, you may do so by calling the following toll-free number: (800) 728-3337.*

# Notes

DWS Investments is part of Deutsche Bank's Asset Management division and, within the US, represents the retail asset management activities of Deutsche Bank AG, Deutsche Bank Trust Company Americas, Deutsche Investment Management Americas Inc. and DWS Trust Company.

The views expressed in this report reflect those of the portfolio managers only through the end of the period of the report as stated on the cover. The managers' views are subject to change at any time based on market and other conditions and should not be construed as a recommendation.

This information must be preceded or accompanied by a current prospectus.

Portfolio changes should not be considered recommendations for action by individual investors.

DWS Investments Distributors, Inc.
222 South Riverside Plaza
Chicago, IL 60606
(800) 621-1148

VS1int-2 (2/11)

DWS INVESTMENTS
Deutsche Bank Group

DECEMBER 31, 2010

# ANNUAL REPORT

## DWS VARIABLE SERIES II

## DWS Balanced VIP

**This report must be preceded or accompanied by a prospectus. To obtain an additional prospectus or summary prospectus, if available, call (800) 728-3337 or your financial representative. We advise you to consider the Fund's objectives, risks, charges and expenses carefully before investing. The summary prospectus and prospectus contain this and other important information about the Fund. Please read the prospectus carefully before you invest.**



DWS INVESTMENTS
Deutsche Bank Group

# Performance Summary

December 31, 2010

## DWS Balanced VIP

**All performance shown is historical, assumes reinvestment of all dividend and capital gain distributions and does not guarantee future results. Investment return and principal value fluctuate with changing market conditions so that, when redeemed, shares may be worth more or less than their original cost. Current performance may be lower or higher than the performance data quoted. Please contact your participating insurance company for the Fund's most recent month-end performance. Performance doesn't reflect charges and fees ("contract charges") associated with the separate account that invests in the Fund or any variable life insurance policy or variable annuity contract for which the Fund is an investment option. These charges and fees will reduce returns.**

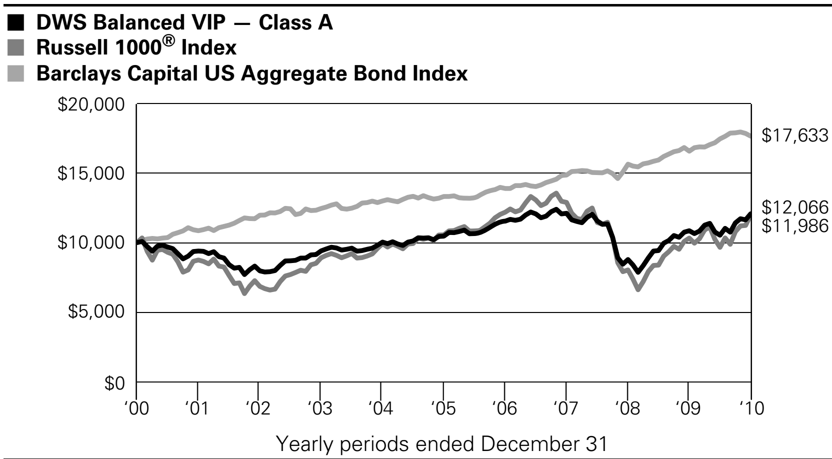
**The gross expense ratio of the Fund, as stated in the fee table of the prospectus dated May 1, 2010 is 0.62% for Class A shares and may differ from the expense ratio disclosed in the Financial Highlights table in this report.**

### Risk Considerations

Although allocation among different asset categories generally limits risk, the investment advisor may favor an asset category that underperforms other assets or markets as a whole. Bond investments are subject to interest-rate and credit risks. When interest rates rise, bond prices generally fall. Credit risk refers to the ability of an issuer to make timely payments of principal and interest. The Fund may use derivatives, including as part of its global alpha strategy. Investing in derivatives entails special risks relating to liquidity, leverage and credit that may reduce returns and/or increase volatility. Stocks may decline in value. See the prospectus for details.

Fund returns for the 3-year, 5-year and 10-year periods shown reflect a fee waiver and/or expense reimbursement. Without this waiver/reimbursement, returns would have been lower.

### Growth of an Assumed $10,000 Investment in DWS Balanced VIP




*The Russell 1000® Index is an unmanaged index that measures the performance of the 1,000 largest companies in the Russell 3000 Index, which represents approximately 92% of the total market capitalization of the Russell 3000 Index.*

*The Barclays Capital US Aggregate Bond Index is an unmanaged, market-value-weighted measure of Treasury issues, agency issues, corporate bond issues and mortgage securities.*

*Index returns assume reinvestment of dividends and, unlike fund returns, do not reflect any fees or expenses. It is not possible to invest directly into an index.*

### Comparative Results

| DWS Balanced VIP | | 1-Year | 3-Year | 5-Year | 10-Year |
|---|---|---|---|---|---|
| **Class A** | Growth of $10,000 | $11,122 | $9,976 | $11,531 | $12,066 |
| | Average annual total return | 11.22% | –0.08% | 2.89% | 1.90% |
| Russell 1000 Index | Growth of $10,000 | $11,610 | $9,305 | $11,364 | $11,986 |
| | Average annual total return | 16.10% | –2.37% | 2.59% | 1.83% |
| Barclays Capital US Aggregate Bond Index | Growth of $10,000 | $10,654 | $11,877 | $13,255 | $17,633 |
| | Average annual total return | 6.54% | 5.90% | 5.80% | 5.84% |

*The growth of $10,000 is cumulative.*

# Information About Your Fund's Expenses

## DWS Balanced VIP

As an investor of the Fund, you incur two types of costs: ongoing expenses and transaction costs. Ongoing expenses include management fees and other Fund expenses. Examples of transaction costs include contract charges, redemption fees and account maintenance fees, which are not shown in this section. The following tables are intended to help you understand your ongoing expenses (in dollars) of investing in the Fund and to help you compare these expenses with the ongoing expenses of investing in other mutual funds. The example in the table is based on an investment of $1,000 invested at the beginning of the six-month period and held for the entire period (July 1, 2010 to December 31, 2010).

The tables illustrate your Fund's expenses in two ways:

- **Actual Fund Return.** This helps you estimate the actual dollar amount of ongoing expenses (but not transaction costs) paid on a $1,000 investment in the Fund using the Fund's actual return during the period. To estimate the expenses you paid over the period, simply divide your account value by $1,000 (for example, an $8,600 account value divided by $1,000 = 8.6), then multiply the result by the number in the "Expenses Paid per $1,000" line under the share class you hold.
- **Hypothetical 5% Fund Return.** This helps you to compare your Fund's ongoing expenses (but not transaction costs) with those of other mutual funds using the Fund's actual expense ratio and a hypothetical rate of return of 5% per year before expenses. Examples using a 5% hypothetical Fund return may be found in the shareholder reports of other mutual funds. The hypothetical account values and expenses may not be used to estimate the actual ending account balance or expenses you paid for the period.

Please note that the expenses shown in these tables are meant to highlight your ongoing expenses only and do not reflect any transaction costs. The "Expenses Paid per $1,000" line of the tables is useful in comparing ongoing expenses only and will not help you determine the relative total expense of owning different funds. If these transaction costs had been included, your costs would have been higher.

**Expenses and Value of a $1,000 Investment** for the six months ended December 31, 2010

| **Actual Fund Return** | **Class A** |
|---|---|
| Beginning Account Value 7/1/10 | $1,000.00 |
| Ending Account Value 12/31/10 | $1,146.00 |
| Expenses Paid per $1,000* | $ 3.68 |
| **Hypothetical 5% Fund Return** | **Class A** |
| Beginning Account Value 7/1/10 | $1,000.00 |
| Ending Account Value 12/31/10 | $1,021.78 |
| Expenses Paid per $1,000* | $ 3.47 |

* *Expenses are equal to the Fund's annualized expense ratio, multiplied by the average account value over the period, multiplied by the number of days in the most recent six-month period, then divided by 365.*

| **Annualized Expense Ratio** | **Class A** |
|---|---|
| DWS Variable Series II — DWS Balanced VIP | .68% |

For more information, please refer to the Fund's prospectus.

These tables do not reflect charges and fees ("contract charges") associated with the separate account that invests in the Fund or any variable life insurance policy or variable annuity contract for which the Fund is an investment option.

## DWS Balanced VIP

The global equity and fixed-income markets both finished 2010 with strong returns, providing a tailwind for DWS Balanced VIP. For the 12 months ended December 31, 2010, the Fund returned 11.22% (Class A shares, unadjusted for contract charges). The Russell 1000® Index, the Fund's equity benchmark, returned 16.10%, and the Barclays Capital US Aggregate Bond Index, the Fund's bond benchmark, returned 6.54%.

The Fund uses several different investment strategies which include investments in five exchange-traded funds, or ETFs.[1] In a reflection of the favorable market environment, all of these investment strategies produced a positive absolute return. We also measure each of the Fund's underlying investments in terms of their relative performance or, in other words, how well they performed in relation to their respective benchmarks. The Fund's shortfall versus the benchmark reflects the collective underperformance of several underlying investment strategies.

We made several shifts to the Fund's positioning during the second half of the year. One of the most significant changes was the liquidation of the quantitative small-cap core sleeve and the addition of the iShares Russell 2000® Value Index Fund. Additionally, we slightly increased the Fund's exposure to large-cap and international equities, and we reduced its exposure to small-cap equities. On the fixed-income side, we augmented the Fund's diversification by reducing exposure to global inflation-linked bonds and cash and increasing our allocation to emerging-market bonds and international developed market bonds. We achieved this via investments in two ETFs — iShares JPMorgan USD Emerging Markets Bond Fund and SPDR Barclays Capital International Treasury Bond.

We believe DWS Balanced VIP, by virtue of its extensive diversification, continues to offer investors a compelling way to gain exposure to a wide range of asset classes within the global financial markets. We will continue to review asset allocation and manager allocation periodically, and we are always looking for opportunities to expand our universe and increase diversification among managers and investment styles.

Robert Wang
Inna Okounkova
Thomas Picciochi
*Portfolio Managers, QS Investors, LLC*
*Subadvisor to the Fund*

*The Russell 1000 Index is an unmanaged index that measures the performance of the 1,000 largest companies in the Russell 3000® Index, which represents approximately 92% of the total market capitalization of the Russell 3000 Index.*

*The Barclays Capital US Aggregate Bond Index is an unmanaged, market-value-weighted measure of Treasury issues, corporate bond issues and mortgage securities.*

*The iShares Russell 2000 Value Index Fund seeks investment results that correspond generally to the price and yield performance, before fees and expenses, of the small capitalization sector of the US equity market as represented by the Russell 2000 Value Index. The index represents approximate 50% of the Russell 2000 Index.*

*The iShares JPMorgan USD Emerging Markets Bond Fund seeks investment results that correspond generally to the price and yield performance, before fees and expenses, of the JPMorgan EMBI Global Core Index.*

*The SPDR Barclays Capital International Treasury Bond ETF tracks the Barclays Global Treasury Ex-US Capped index. The international bond ETF invests at least 80% of securities that are in the underlying index as well as derivatives such as swaps and options. Some of the regions represented in the bond ETF are Japan, Germany, France, Italy and Greece.*

*Index returns assume reinvestment of dividends and, unlike fund returns, do not reflect any fees or expenses. It is not possible to invest directly into an index.*

1 *An exchange-traded fund (ETF) is a security that tracks an index, a commodity or a basket of assets like an index fund, but trades like a stock on an exchange.*

*Portfolio management market commentary is as of December 31, 2010, and may not come to pass. This information is subject to change at any time based on market and other conditions. Past performance does not guarantee future results. Current and future portfolio holdings are subject to risk.*

# Portfolio Summary

## DWS Balanced VIP

| **Asset Allocation** (As a % of Investment Portfolio excluding Securities Lending Collateral) | **12/31/10** | **12/31/09** |
|---|---|---|
| Common Stocks | 55% | 54% |
| Government & Agency Obligations | 9% | 13% |
| Fixed Income — Exchange-Traded Funds | 7% | 3% |
| Mortgage-Backed Securities Pass-Throughs | 7% | 8% |
| Corporate Bonds | 7% | 8% |
| Cash Equivalents | 6% | 10% |
| Equity — Exchange-Traded Funds | 5% | 3% |
| Commercial Mortgage-Backed Securities | 2% | 1% |
| Municipal Bonds and Notes | 1% | 0% |
| Preferred Stocks | 1% | 0% |
| | 100% | 100% |

| **Sector Diversification** (As a % of Equities, Corporate Bonds, Senior Bank Loans and Preferred Securities) | **12/31/10** | **12/31/09** |
|---|---|---|
| Information Technology | 16% | 15% |
| Energy | 14% | 10% |
| Financials | 13% | 16% |
| Consumer Discretionary | 12% | 11% |
| Industrials | 11% | 11% |
| Health Care | 10% | 13% |
| Consumer Staples | 9% | 9% |
| Materials | 6% | 6% |
| Telecommunication Services | 5% | 5% |
| Utilities | 4% | 4% |
| | 100% | 100% |

*Asset allocation and sector diversification exclude derivatives and are subject to change.*

*For more complete details about the Fund's investment portfolio, see page 6.*

Following the Fund's fiscal first and third quarter-end, a complete portfolio holdings listing is filed with the SEC on Form N-Q. The form will be available on the SEC's Web site at www.sec.gov, and it also may be reviewed and copied at the SEC's Public Reference Room in Washington, D.C. Information on the operation of the SEC's Public Reference Room may be obtained by calling (800) SEC-0330. The Fund's portfolio holdings are also posted on www.dws-investments.com from time to time. Please see the Fund's current prospectus for more information.

## DWS Balanced VIP

| | Shares | Value ($) |
|---|---|---|
| **Common Stocks 56.4%** | | |
| **Consumer Discretionary 6.6%** | | |
| **Auto Components 0.8%** | | |
| Autoliv, Inc. (a) | 7,100 | 560,474 |
| BorgWarner, Inc.* (a) | 22,292 | 1,613,049 |
| Minth Group Ltd. | 86,306 | 141,682 |
| Nippon Seiki Co., Ltd. | 8,273 | 99,131 |
| S&T Dynamics Co., Ltd.* | 5,003 | 100,667 |
| | | **2,515,003** |
| **Automobiles 0.3%** | | |
| Bayerische Motoren Werke (BMW) AG | 1,656 | 130,143 |
| Daimler AG (Registered)* | 4,530 | 306,979 |
| Honda Motor Co., Ltd. | 9,032 | 356,978 |
| PT Astra International Tbk | 24,185 | 146,285 |
| | | **940,385** |
| **Distributors 0.5%** | | |
| Genuine Parts Co. | 27,420 | **1,407,743** |
| **Diversified Consumer Services 0.3%** | | |
| H&R Block, Inc. (a) | 67,779 | **807,248** |
| **Hotels Restaurants & Leisure 1.2%** | | |
| Carnival Corp. (Units) | 19,047 | 878,257 |
| Darden Restaurants, Inc. (a) | 17,590 | 816,880 |
| Domino's Pizza UK & IRL PLC | 10,134 | 87,137 |
| Marriott International, Inc. "A" (a) | 24,919 | 1,035,135 |
| McDonald's Corp. | 6,220 | 477,447 |
| Paddy Power PLC | 3,364 | 138,006 |
| PartyGaming PLC* (a) | 16,776 | 53,749 |
| REXLot Holdings Ltd. | 1,209,877 | 127,637 |
| Trump Entertainment Resorts, Inc.* | 2 | 37 |
| | | **3,614,285** |
| **Household Durables 0.1%** | | |
| Advanced Digital Broadcast Holdings SA (Registered) | 414 | 13,547 |
| Hajime Construction Co., Ltd. | 1,994 | 68,443 |
| Jarden Corp. | 1,794 | 55,381 |
| Panasonic Corp. | 22,414 | 316,400 |
| | | **453,771** |
| **Internet & Catalog Retail 0.0%** | | |
| Mecox Lane Ltd. (ADR)* (a) | 4,052 | **30,025** |
| **Leisure Equipment & Products 0.1%** | | |
| Universal Entertainment Corp.* | 6,095 | **178,021** |
| **Media 1.0%** | | |
| Aegis Group PLC | 24,682 | 54,067 |
| Charm Communications, Inc. (ADR)* | 2,894 | 28,535 |
| Dex One Corp.* | 245 | 1,828 |
| JC Decaux SA* | 3,633 | 111,781 |
| News Corp. "A" | 63,987 | 931,651 |
| Scripps Networks Interactive "A" | 23,130 | 1,196,977 |
| SuperMedia, Inc.* | 43 | 375 |
| Vertis Holdings, Inc.* | 1,645 | 0 |
| Vivendi | 8,527 | 230,171 |
| WPP PLC | 30,237 | 372,190 |
| | | **2,927,575** |
| **Multiline Retail 0.6%** | | |
| Dollar General Corp.* (a) | 11,960 | 366,813 |
| Kohl's Corp.* | 14,560 | 791,190 |
| Nordstrom, Inc. (a) | 15,950 | 675,961 |
| PPR | 1,010 | 160,610 |
| | | **1,994,574** |
| **Specialty Retail 0.8%** | | |
| Advance Auto Parts, Inc. (a) | 1,704 | 112,719 |
| Aeropostale, Inc.* | 4,348 | 107,135 |
| Dick's Sporting Goods, Inc.* (a) | 15,840 | 594,000 |
| Guess?, Inc. (a) | 2,421 | 114,562 |
| Hennes & Mauritz AB "B" | 3,513 | 117,050 |
| hhgregg, Inc.* (a) | 3,764 | 78,856 |
| L'Occitane International SA* | 23,750 | 65,694 |
| Limited Brands, Inc. (a) | 37,290 | 1,145,922 |
| Nitori Holdings Co., Ltd. | 1,345 | 117,613 |
| Urban Outfitters, Inc.* | 3,227 | 115,559 |
| | | **2,569,110** |
| **Textiles, Apparel & Luxury Goods 0.9%** | | |
| Burberry Group PLC | 4,298 | 75,319 |
| Compagnie Financiere Richemont SA "A" | 5,753 | 338,456 |
| Deckers Outdoor Corp.* (a) | 2,398 | 191,217 |
| LVMH Moet Hennessy Louis Vuitton SA | 1,076 | 177,000 |
| NIKE, Inc. "B" (a) | 14,970 | 1,278,737 |
| VF Corp. | 8,644 | 744,940 |
| | | **2,805,669** |
| **Consumer Staples 5.2%** | | |
| **Beverages 0.9%** | | |
| C&C Group PLC | 29,374 | 132,791 |
| Carlsberg AS "B" | 1,490 | 149,114 |
| Central European Distribution Corp.* | 2,600 | 59,540 |
| Diageo PLC | 27,977 | 516,884 |
| PepsiCo, Inc. | 28,067 | 1,833,617 |
| | | **2,691,946** |
| **Food & Staples Retailing 1.5%** | | |
| CVS Caremark Corp. | 32,169 | 1,118,516 |
| Kroger Co. | 38,618 | 863,499 |
| Metro AG | 2,441 | 175,746 |
| Seven & I Holdings Co., Ltd. | 16,781 | 448,210 |
| Sysco Corp. | 23,420 | 688,548 |
| Tesco PLC | 23,968 | 158,816 |
| Wal-Mart Stores, Inc. | 8,735 | 471,079 |
| Wesfarmers Ltd. | 7,877 | 257,811 |
| Woolworths Ltd. | 18,023 | 497,163 |
| | | **4,679,388** |
| **Food Products 1.1%** | | |
| Diamond Foods, Inc. (a) | 2,779 | 147,787 |
| General Mills, Inc. | 16,139 | 574,387 |
| Green Mountain Coffee Roasters, Inc.* (a) | 3,078 | 101,143 |
| Kellogg Co. | 13,681 | 698,826 |
| Mead Johnson Nutrition Co. | 9,888 | 615,528 |
| Nestle SA (Registered) | 16,271 | 953,115 |
| SunOpta, Inc.* | 18,642 | 145,780 |

*The accompanying notes are an integral part of the financial statements.*

| | Shares | Value ($) |
|---|---|---|
| Unilever NV (CVA) | 7,417 | 230,934 |
| | | **3,467,500** |
| **Household Products 0.5%** | | |
| Church & Dwight Co., Inc. (a) | 8,968 | 618,971 |
| Colgate-Palmolive Co. (a) | 7,750 | 622,868 |
| Reckitt Benckiser Group PLC | 4,598 | 252,698 |
| | | **1,494,537** |
| **Personal Products 0.1%** | | |
| Kao Corp. | 12,622 | **339,919** |
| **Tobacco 1.1%** | | |
| Altria Group, Inc. | 55,285 | 1,361,117 |
| British American Tobacco PLC | 11,332 | 435,244 |
| ITC Ltd. | 41,615 | 162,867 |
| Philip Morris International, Inc. | 23,311 | 1,364,393 |
| | | **3,323,621** |
| **Energy 7.5%** | | |
| **Energy Equipment & Services 2.3%** | | |
| AMEC PLC | 11,344 | 203,394 |
| Cameron International Corp.* | 1,614 | 81,878 |
| Compagnie Generale de Geophysique-Veritas* | 5,847 | 177,949 |
| Complete Production Services, Inc.* (a) | 3,289 | 97,190 |
| Dresser-Rand Group, Inc.* | 2,152 | 91,654 |
| Ensco PLC (ADR) | 20,744 | 1,107,315 |
| John Wood Group PLC | 10,565 | 92,078 |
| Lamprell PLC | 17,323 | 86,832 |
| National Oilwell Varco, Inc. | 17,589 | 1,182,860 |
| Noble Corp. | 29,144 | 1,042,481 |
| ProSafe SE | 9,053 | 72,039 |
| Saipem SpA | 7,538 | 371,390 |
| SBM Offshore NV | 5,980 | 133,970 |
| Schlumberger Ltd. | 14,350 | 1,198,225 |
| Technip SA | 1,788 | 165,101 |
| Tecnicas Reunidas SA | 1,121 | 71,372 |
| Transocean Ltd.* | 13,310 | 925,178 |
| | | **7,100,906** |
| **Oil, Gas & Consumable Fuels 5.2%** | | |
| Alpha Natural Resources, Inc.* | 22,852 | 1,371,806 |
| Anadarko Petroleum Corp. | 15,650 | 1,191,904 |
| Canadian Natural Resources Ltd. | 21,451 | 952,853 |
| Chevron Corp. | 16,064 | 1,465,840 |
| ConocoPhillips | 16,454 | 1,120,517 |
| EOG Resources, Inc. (a) | 7,880 | 720,311 |
| Exxon Mobil Corp. | 34,248 | 2,504,214 |
| Marathon Oil Corp. | 38,003 | 1,407,251 |
| Nexen, Inc. | 32,026 | 733,395 |
| Northern Oil & Gas, Inc.* | 4,213 | 114,636 |
| Occidental Petroleum Corp. | 11,760 | 1,153,656 |
| Royal Dutch Shell PLC "A" | 29,694 | 990,038 |
| Suncor Energy, Inc. | 39,678 | 1,519,271 |
| Total SA | 8,254 | 437,332 |
| Ultra Petroleum Corp.* (a) | 2,332 | 111,400 |
| Woodside Petroleum Ltd. | 7,131 | 310,415 |
| | | **16,104,839** |
| **Financials 6.2%** | | |
| **Capital Markets 1.2%** | | |
| Affiliated Managers Group, Inc.* (a) | 897 | 89,000 |
| Ashmore Group PLC | 26,439 | 138,132 |
| Charles Schwab Corp. | 31,680 | 542,045 |
| ICAP PLC | 7,881 | 65,737 |
| Jefferies Group, Inc. (a) | 4,571 | 121,726 |
| Lazard Ltd. "A" | 1,564 | 61,762 |
| Morgan Stanley | 29,250 | 795,893 |
| Partners Group Holding AG | 697 | 132,280 |
| T. Rowe Price Group, Inc. (a) | 24,010 | 1,549,605 |
| UOB-Kay Hian Holdings Ltd. | 47,752 | 65,860 |
| Waddell & Reed Financial, Inc. "A" | 2,242 | 79,120 |
| | | **3,641,160** |
| **Commercial Banks 1.5%** | | |
| Australia & New Zealand Banking Group Ltd. | 14,418 | 344,336 |
| Banco Santander Brasil SA (Units) | 15,650 | 212,915 |
| BNP Paribas | 3,655 | 232,536 |
| BOC Hong Kong (Holdings) Ltd. | 49,954 | 170,952 |
| China Construction Bank Corp. "H" | 159,312 | 143,473 |
| Dah Sing Banking Group Ltd. | 44,966 | 76,594 |
| DnB NOR ASA | 20,326 | 285,260 |
| HSBC Holdings PLC | 67,067 | 680,817 |
| Huntington Bancshares, Inc. | 9,478 | 65,114 |
| Industrial & Commercial Bank of China Ltd. "H" | 215,754 | 160,161 |
| Lloyds Banking Group PLC* | 111,900 | 114,622 |
| National Australia Bank Ltd. | 13,395 | 324,700 |
| Oversea-Chinese Banking Corp., Ltd. | 39,230 | 302,016 |
| Prosperity Bancshares, Inc. | 1,972 | 77,460 |
| Sberbank of Russia | 104,751 | 356,889 |
| Societe Generale | 4,008 | 215,414 |
| Sumitomo Mitsui Financial Group, Inc. | 11,221 | 399,412 |
| Swedbank AB "A"* | 12,540 | 174,858 |
| UniCredit SpA | 111,097 | 229,761 |
| Wing Hang Bank Ltd. | 6,818 | 94,295 |
| Zions Bancorp. | 2,784 | 67,456 |
| | | **4,729,041** |
| **Consumer Finance 0.0%** | | |
| Kiatnakin Bank PCL | 81,536 | 105,487 |
| Magma Fincorp Ltd. | 26,821 | 43,037 |
| | | **148,524** |
| **Diversified Financial Services 0.7%** | | |
| Hellenic Exchanges SA | 3,394 | 22,223 |
| Hong Kong Exchanges & Clearing Ltd. | 18,685 | 423,807 |
| ING Groep NV (CVA)* | 26,371 | 256,544 |
| JPMorgan Chase & Co. | 28,724 | 1,218,472 |
| Remgro Ltd. | 10,456 | 179,280 |
| | | **2,100,326** |
| **Insurance 2.7%** | | |
| AIA Group Ltd.* | 53,108 | 149,291 |
| Allianz SE (Registered) | 1,595 | 189,534 |
| Assurant, Inc. | 24,273 | 934,996 |
| Fidelity National Financial, Inc. "A" | 47,478 | 649,499 |
| HCC Insurance Holdings, Inc. | 23,434 | 678,180 |
| Legal & General Group PLC | 160,135 | 241,552 |
| Lincoln National Corp. | 42,889 | 1,192,743 |
| MetLife, Inc. | 40,898 | 1,817,507 |
| PartnerRe Ltd. | 16,288 | 1,308,741 |
| Prudential Financial, Inc. | 18,587 | 1,091,243 |
| Sampo Oyj "A" | 4,685 | 125,593 |
| | | **8,378,879** |
| **Real Estate Management & Development 0.1%** | | |
| K Wah International Holdings Ltd. | 164,519 | 61,593 |
| Kenedix, Inc.* | 296 | 90,010 |

*The accompanying notes are an integral part of the financial statements.*

| | Shares | Value ($) |
|---|---|---|
| Midland Holdings Ltd. | 84,184 | 69,099 |
| | | **220,702** |
| **Health Care 5.9%** | | |
| **Biotechnology 1.0%** | | |
| Amgen, Inc.* (a) | 8,780 | 482,022 |
| Celgene Corp.* (a) | 29,060 | 1,718,608 |
| Gilead Sciences, Inc.* | 21,560 | 781,334 |
| Metabolix, Inc.* | 3,675 | 44,725 |
| Onyx Pharmaceuticals, Inc.* | 1,809 | 66,698 |
| | | **3,093,387** |
| **Health Care Equipment & Supplies 1.2%** | | |
| Accuray, Inc.* | 9,933 | 67,048 |
| Baxter International, Inc. | 23,015 | 1,165,019 |
| Becton, Dickinson & Co. | 10,498 | 887,291 |
| Edwards Lifesciences Corp.* (a) | 8,107 | 655,370 |
| NxStage Medical, Inc.* (a) | 6,901 | 171,697 |
| Thoratec Corp.* (a) | 21,871 | 619,387 |
| | | **3,565,812** |
| **Health Care Providers & Services 1.6%** | | |
| Diagnosticos da America SA | 6,593 | 89,303 |
| ExamWorks Group, Inc.* (a) | 2,193 | 40,527 |
| Express Scripts, Inc.* | 26,630 | 1,439,351 |
| Fleury SA | 6,502 | 104,390 |
| Fresenius Medical Care AG & Co. KGaA | 5,826 | 336,649 |
| McKesson Corp. | 31,628 | 2,225,979 |
| WellPoint, Inc.* | 12,296 | 699,151 |
| | | **4,935,350** |
| **Health Care Technology 0.1%** | | |
| M3, Inc. | 13 | 65,298 |
| SXC Health Solutions Corp.* | 1,972 | 84,520 |
| | | **149,818** |
| **Life Sciences Tools & Services 0.3%** | | |
| ICON PLC (ADR)* (a) | 3,675 | 80,483 |
| Life Technologies Corp.* | 2,421 | 134,365 |
| QIAGEN NV* | 5,288 | 103,430 |
| Thermo Fisher Scientific, Inc.* | 13,189 | 730,143 |
| | | **1,048,421** |
| **Pharmaceuticals 1.7%** | | |
| AstraZeneca PLC | 6,342 | 288,922 |
| Flamel Technologies SA (ADR)* | 12,637 | 86,437 |
| GlaxoSmithKline PLC | 24,837 | 480,169 |
| Johnson & Johnson | 10,584 | 654,620 |
| Merck & Co., Inc. | 34,630 | 1,248,065 |
| Novartis AG (Registered) | 2,607 | 153,408 |
| Novo Nordisk AS "B" | 2,077 | 233,777 |
| Questcor Pharmaceuticals, Inc.* (a) | 9,198 | 135,487 |
| Sanofi-Aventis | 5,066 | 323,930 |
| Takeda Pharmaceutical Co., Ltd. | 6,568 | 323,029 |
| Teva Pharmaceutical Industries Ltd. (ADR) | 24,006 | 1,251,433 |
| VIVUS, Inc.* | 6,883 | 64,494 |
| | | **5,243,771** |
| **Industrials 6.8%** | | |
| **Aerospace & Defense 1.5%** | | |
| BE Aerospace, Inc.* (a) | 3,317 | 122,829 |
| Northrop Grumman Corp. | 13,614 | 881,915 |
| Raytheon Co. | 18,216 | 844,129 |
| TransDigm Group, Inc.* | 9,920 | 714,339 |
| United Technologies Corp. | 25,213 | 1,984,767 |
| | | **4,547,979** |

| | Shares | Value ($) |
|---|---|---|
| **Airlines 0.2%** | | |
| Cebu Air, Inc.* | 20,540 | 53,167 |
| Deutsche Lufthansa AG (Registered)* | 6,877 | 150,297 |
| Ryanair Holdings PLC (ADR) (a) | 3,317 | 102,031 |
| Singapore Airlines Ltd. | 12,701 | 153,597 |
| | | **459,092** |
| **Building Products 0.0%** | | |
| Congoleum Corp.* | 190,000 | **0** |
| **Commercial Services & Supplies 0.4%** | | |
| Babcock International Group PLC | 14,308 | 127,377 |
| EnerNOC, Inc.* (a) | 2,242 | 53,606 |
| Quad Graphics, Inc.* | 38 | 1,568 |
| Serco Group PLC | 9,554 | 82,745 |
| Stericycle, Inc.* (a) | 9,985 | 807,986 |
| | | **1,073,282** |
| **Construction & Engineering 0.1%** | | |
| Aecom Technology Corp.* (a) | 3,764 | 105,279 |
| Chicago Bridge & Iron Co. NV (NY Registered Shares)* | 4,034 | 132,718 |
| Larsen & Toubro Ltd. | 3,461 | 153,100 |
| Shui On Construction & Materials Ltd. | 51,981 | 60,188 |
| | | **451,285** |
| **Electrical Equipment 1.1%** | | |
| AMETEK, Inc. | 41,550 | 1,630,837 |
| Nidec Corp. | 1,189 | 119,892 |
| Prysmian SpA | 3,522 | 59,979 |
| Roper Industries, Inc. | 16,430 | 1,255,745 |
| Schneider Electric SA | 2,285 | 341,986 |
| | | **3,408,439** |
| **Industrial Conglomerates 0.3%** | | |
| Keppel Corp., Ltd. | 40,631 | 358,393 |
| Koninklijke Philips Electronics NV | 6,436 | 197,122 |
| Siemens AG (Registered) | 4,029 | 498,809 |
| | | **1,054,324** |
| **Machinery 2.2%** | | |
| Altra Holdings, Inc.* | 2,203 | 43,752 |
| Amtek Engineering Ltd.* | 153,000 | 128,757 |
| Atlas Copco AB "A" | 6,736 | 170,101 |
| Austal Ltd. | 25,202 | 89,960 |
| Charter International PLC | 5,747 | 75,668 |
| Dover Corp. | 20,402 | 1,192,497 |
| EVA Precision Industrial Holdings Ltd. | 203,716 | 198,925 |
| FANUC Corp. | 3,719 | 570,518 |
| Joy Global, Inc. (a) | 1,704 | 147,822 |
| Komatsu Ltd. | 10,589 | 320,095 |
| Kubota Corp. | 17,198 | 162,727 |
| MAN SE | 1,187 | 141,130 |
| Mitsubishi Heavy Industries Ltd. | 82,257 | 308,800 |
| Navistar International Corp.* | 19,427 | 1,125,018 |
| Parker Hannifin Corp. | 17,890 | 1,543,907 |
| Rational AG | 628 | 138,630 |
| Rotork PLC | 3,646 | 103,912 |
| Volvo AB "B"* | 16,451 | 293,202 |
| | | **6,755,421** |
| **Marine 0.2%** | | |
| A P Moller-Maersk AS "B" | 41 | 371,375 |
| Mitsui O.S.K Lines Ltd. | 53,383 | 363,893 |
| | | **735,268** |

*The accompanying notes are an integral part of the financial statements.*

| | Shares | Value ($) |
|---|---|---|
| **Professional Services 0.1%** | | |
| Brunel International NV | 1,947 | 76,726 |
| FTI Consulting, Inc.* (a) | 2,959 | 110,312 |
| Michael Page International PLC | 15,237 | 131,846 |
| | | **318,884** |
| **Road & Rail 0.5%** | | |
| Norfolk Southern Corp. | 23,040 | **1,447,373** |
| **Trading Companies & Distributors 0.2%** | | |
| MISUMI Group, Inc. | 5,468 | 136,127 |
| Mitsubishi Corp. | 13,913 | 376,244 |
| | | **512,371** |
| **Transportation Infrastructure 0.0%** | | |
| Koninklijke Vopak NV | 2,580 | **121,875** |
| **Information Technology 9.5%** | | |
| **Communications Equipment 1.4%** | | |
| Brocade Communications Systems, Inc.* | 79,295 | 419,470 |
| Cisco Systems, Inc.* | 131,841 | 2,667,143 |
| Harris Corp. | 1,882 | 85,255 |
| QUALCOMM, Inc. | 23,840 | 1,179,842 |
| Sycamore Networks, Inc. | 2,510 | 51,681 |
| | | **4,403,391** |
| **Computers & Peripherals 2.3%** | | |
| Apple, Inc.* | 11,670 | 3,764,275 |
| EMC Corp.* | 58,340 | 1,335,986 |
| Hewlett-Packard Co. | 43,023 | 1,811,268 |
| Toshiba Corp. | 33,506 | 182,379 |
| | | **7,093,908** |
| **Electronic Equipment, Instruments & Components 0.2%** | | |
| E Ink Holdings, Inc.* | 60,785 | 123,210 |
| Itron, Inc.* (a) | 2,242 | 124,319 |
| Kingboard Chemical Holdings Ltd. | 21,062 | 126,137 |
| Venture Corp., Ltd. | 15,763 | 113,738 |
| | | **487,404** |
| **Internet Software & Services 0.8%** | | |
| Akamai Technologies, Inc.* | 15,750 | 741,037 |
| Google, Inc. "A"* | 2,405 | 1,428,498 |
| Internet Initiative Japan, Inc. | 33 | 93,684 |
| Meetic | 1,741 | 37,806 |
| NIC, Inc. (a) | 7,597 | 73,767 |
| United Internet AG (Registered) | 6,095 | 99,058 |
| | | **2,473,850** |
| **IT Services 1.1%** | | |
| Accenture PLC "A" | 10,410 | 504,781 |
| Automatic Data Processing, Inc. | 16,098 | 745,015 |
| Cardtronics, Inc.* | 5,647 | 99,952 |
| Digital Garage, Inc.* | 51 | 126,472 |
| FleetCor Technologies, Inc.* | 715 | 22,108 |
| iGATE Corp. (a) | 4,253 | 83,827 |
| Infosys Technologies Ltd. | 2,314 | 177,766 |
| International Business Machines Corp. | 5,490 | 805,712 |
| Telvent GIT SA* | 2,540 | 67,107 |
| VeriFone Systems, Inc.* (a) | 12,117 | 467,232 |
| Visa, Inc. "A" | 3,410 | 239,996 |
| | | **3,339,968** |
| **Office Electronics 0.2%** | | |
| Canon, Inc. | 14,117 | **723,703** |
| **Semiconductors & Semiconductor Equipment 0.9%** | | |
| ARM Holdings PLC | 22,115 | 145,951 |
| FSI International, Inc.* (a) | 15,326 | 67,741 |
| Intel Corp. | 103,992 | 2,186,952 |
| Lam Research Corp.* | 1,614 | 83,573 |
| Taiwan Semiconductor Manufacturing Co., Ltd. | 113,397 | 276,137 |
| | | **2,760,354** |
| **Software 2.6%** | | |
| Adobe Systems, Inc.* | 11,180 | 344,120 |
| Check Point Software Technologies Ltd.* (a) | 13,600 | 629,136 |
| Concur Technologies, Inc.* (a) | 16,820 | 873,463 |
| Microsoft Corp. | 104,984 | 2,931,153 |
| Norkom Group PLC* | 27,634 | 55,391 |
| Oracle Corp. | 62,100 | 1,943,730 |
| Rovi Corp.* | 1,794 | 111,246 |
| SAP AG | 3,208 | 163,352 |
| Solera Holdings, Inc. | 15,360 | 788,275 |
| TiVo, Inc.* (a) | 6,079 | 52,462 |
| VanceInfo Technologies, Inc. (ADR)* (a) | 2,733 | 94,398 |
| | | **7,986,726** |
| **Materials 3.7%** | | |
| **Chemicals 1.7%** | | |
| Air Liquide SA | 1,039 | 131,400 |
| Air Products & Chemicals, Inc. | 14,167 | 1,288,489 |
| BASF SE | 5,441 | 434,059 |
| Givaudan SA (Registered) | 154 | 166,280 |
| Huntsman Corp. | 40,830 | 637,356 |
| Johnson Matthey PLC | 2,531 | 80,421 |
| Linde AG | 1,046 | 158,770 |
| Praxair, Inc. | 9,802 | 935,797 |
| Shin-Etsu Chemical Co., Ltd. | 8,359 | 452,531 |
| STR Holdings, Inc.* (a) | 3,154 | 63,080 |
| The Mosaic Co. | 10,956 | 836,600 |
| | | **5,184,783** |
| **Construction Materials 0.1%** | | |
| China National Building Material Co., Ltd. "H" | 67,409 | **154,369** |
| **Containers & Packaging 0.7%** | | |
| Owens-Illinois, Inc.* (a) | 33,630 | 1,032,441 |
| Sonoco Products Co. | 32,657 | 1,099,561 |
| | | **2,132,002** |
| **Metals & Mining 1.2%** | | |
| BHP Billiton Ltd. | 14,175 | 656,043 |
| Cliffs Natural Resources, Inc. | 1,498 | 116,859 |
| Freeport-McMoRan Copper & Gold, Inc. | 14,190 | 1,704,077 |
| Lynas Corp., Ltd.* | 94,986 | 200,132 |
| Newcrest Mining Ltd. | 2,950 | 122,018 |
| Northam Platinum Ltd. | 8,616 | 59,249 |
| Randgold Resources Ltd. (ADR) (a) | 987 | 81,260 |
| Rio Tinto PLC | 4,144 | 289,869 |
| Thompson Creek Metals Co., Inc.* | 5,468 | 80,489 |
| ThyssenKrupp AG | 2,303 | 95,413 |
| Xstrata PLC | 16,059 | 376,941 |
| | | **3,782,350** |
| **Paper & Forest Products 0.0%** | | |
| Schweitzer-Mauduit International, Inc. | 1,921 | **120,870** |
| **Telecommunication Services 2.7%** | | |
| **Diversified Telecommunication Services 1.7%** | | |
| AT&T, Inc. | 51,276 | 1,506,489 |
| BCE, Inc. | 9,410 | 333,678 |

*The accompanying notes are an integral part of the financial statements.*

| | Shares | Value ($) |
|---|---|---|
| CenturyLink, Inc. (a) | 40,575 | 1,873,348 |
| Koninklijke (Royal) KPN NV | 11,647 | 169,958 |
| Telefonica SA | 17,556 | 398,715 |
| TeliaSonera AB | 8,744 | 69,325 |
| Verizon Communications, Inc. | 26,558 | 950,245 |
| | | **5,301,758** |
| **Wireless Telecommunication Services 1.0%** | | |
| America Movil SAB de CV "L" | 79,231 | 227,107 |
| American Tower Corp. "A"* | 14,480 | 747,747 |
| NTT DoCoMo, Inc. | 288 | 502,859 |
| Vodafone Group PLC | 251,183 | 649,305 |
| Vodafone Group PLC (ADR) | 37,055 | 979,364 |
| | | **3,106,382** |

## Utilities 2.3%

| | | |
|---|---|---|
| **Electric Utilities 1.8%** | | |
| Allegheny Energy, Inc. | 31,296 | 758,615 |
| American Electric Power Co., Inc. | 23,442 | 843,443 |
| Duke Energy Corp. | 40,980 | 729,854 |
| Entergy Corp. | 11,165 | 790,817 |
| Exelon Corp. | 9,736 | 405,407 |
| FirstEnergy Corp. | 20,855 | 772,052 |
| Fortum Oyj | 4,424 | 134,214 |
| HongKong Electric Holdings Ltd. | 43,475 | 274,068 |
| Southern Co. | 20,943 | 800,651 |
| | | **5,509,121** |
| **Multi-Utilities 0.5%** | | |
| GDF Suez | 7,057 | 253,202 |
| PG&E Corp. | 27,726 | 1,326,412 |
| | | **1,579,614** |
| **Total Common Stocks** (Cost $139,202,524) | | **173,727,402** |

## Preferred Stocks 0.4%

| | | |
|---|---|---|
| **Consumer Discretionary 0.1%** | | |
| Volkswagen AG | 1,540 | **249,552** |
| **Energy 0.1%** | | |
| Petroleo Brasileiro SA | 10,118 | 170,853 |
| Ultrapar Participacoes SA | 2,650 | 169,443 |
| | | **340,296** |
| **Financials 0.0%** | | |
| Itau Unibanco Holding SA | 6,520 | **156,438** |
| **Information Technology 0.1%** | | |
| Samsung Electronics Co., Ltd. | 460 | **262,973** |
| **Materials 0.1%** | | |
| Vale SA "A" | 5,766 | **168,488** |
| **Total Preferred Stocks** (Cost $1,140,028) | | **1,177,747** |

## Warrants 0.0%

| | | |
|---|---|---|
| **Consumer Discretionary 0.0%** | | |
| Reader's Digest Association, Inc., Expiration Date 2/19/2014* | 80 | **2** |
| **Information Technology 0.0%** | | |
| Kingboard Chemical Holdings Ltd., Expiration Date 10/31/2012* | 3,400 | **3,609** |
| **Materials 0.0%** | | |
| Hercules Trust II, Expiration Date 3/31/2029* | 170 | **1,934** |
| **Total Warrants** (Cost $30,284) | | **5,545** |

## Corporate Bonds 6.8%

### Consumer Discretionary 1.2%

| | Principal Amount ($) (b) | Value ($) |
|---|---|---|
| AMC Entertainment, Inc.: | | |
| 8.0%, 3/1/2014 | 35,000 | 35,350 |
| 8.75%, 6/1/2019 | 35,000 | 37,362 |
| Ameristar Casinos, Inc., 9.25%, 6/1/2014 | 25,000 | 26,750 |
| Asbury Automotive Group, Inc., 7.625%, 3/15/2017 | 35,000 | 35,350 |
| Avis Budget Car Rental LLC, 144A, 8.25%, 1/15/2019 | 15,000 | 15,150 |
| CanWest MediaWorks LP, 144A, 9.25%, 8/1/2015** | 25,000 | 4,250 |
| Carrols Corp., 9.0%, 1/15/2013 | 15,000 | 15,038 |
| CBS Corp., 5.9%, 10/15/2040 | 270,000 | 260,085 |
| DineEquity, Inc., 144A, 9.5%, 10/30/2018 | 10,000 | 10,600 |
| DIRECTV Holdings LLC: | | |
| 6.0%, 8/15/2040 | 530,000 | 532,083 |
| 6.35%, 3/15/2040 | 51,000 | 53,650 |
| DISH DBS Corp.: | | |
| 6.625%, 10/1/2014 | 40,000 | 41,500 |
| 7.125%, 2/1/2016 | 35,000 | 36,138 |
| Expedia, Inc., 7.456%, 8/15/2018 | 550,000 | 627,000 |
| Fontainebleau Las Vegas Holdings LLC, 144A, 11.0%, 6/15/2015** | 25,000 | 88 |
| Goodyear Tire & Rubber Co., 10.5%, 5/15/2016 | 10,000 | 11,400 |
| Great Canadian Gaming Corp., 144A, 7.25%, 2/15/2015 | 30,000 | 30,675 |
| Home Depot, Inc.: | | |
| 5.4%, 9/15/2040 | 125,000 | 121,390 |
| 5.875%, 12/16/2036 | 50,000 | 52,007 |
| Lowe's Companies, Inc., 3.75%, 4/15/2021 | 200,000 | 193,362 |
| Mediacom Broadband LLC, 8.5%, 10/15/2015 | 20,000 | 20,100 |
| NBC Universal, Inc., 144A, 5.95%, 4/1/2041 | 247,000 | 246,975 |
| Norcraft Holdings LP, 9.75%, 9/1/2012 | 36,000 | 36,225 |
| Penske Automotive Group, Inc., 7.75%, 12/15/2016 | 50,000 | 51,000 |
| Sabre Holdings Corp., 8.35%, 3/15/2016 | 25,000 | 24,000 |
| Sears Holdings Corp., 144A, 6.625%, 10/15/2018 | 10,000 | 9,325 |
| TCI Communications, Inc., 8.75%, 8/1/2015 | 135,000 | 166,170 |
| Time Warner, Inc.: | | |
| 5.875%, 11/15/2016 | 147,000 | 165,921 |
| 6.2%, 3/15/2040 | 175,000 | 186,034 |
| 7.625%, 4/15/2031 | 175,000 | 212,745 |
| Travelport LLC, 4.921%***, 9/1/2014 | 20,000 | 17,700 |
| Unitymedia Hessen GmbH & Co., KG, 144A, 8.125%, 12/1/2017 | 100,000 | 104,500 |
| Vertis, Inc., 13.5%, 4/1/2014 (PIK)** | 42,609 | 1,278 |
| Young Broadcasting, Inc., 8.75%, 1/15/2014** | 130,000 | 1 |

*The accompanying notes are an integral part of the financial statements.*

| | Principal Amount ($) (b) | Value ($) |
|---|---|---|
| Yum! Brands, Inc.: | | |
| 3.875%, 11/1/2020 (a) | 210,000 | 200,610 |
| 5.3%, 9/15/2019 | 65,000 | 68,846 |
| | | **3,650,658** |
| **Consumer Staples 0.7%** | | |
| Anheuser-Busch InBev Worldwide, Inc., 144A, 7.75%, 1/15/2019 | 500,000 | 622,174 |
| CVS Caremark Corp.: | | |
| 6.125%, 9/15/2039 | 275,000 | 293,826 |
| 6.25%, 6/1/2027 | 300,000 | 329,912 |
| General Nutrition Centers, Inc., 5.75%***, 3/15/2014 (PIK) | 15,000 | 14,850 |
| Kraft Foods, Inc., 5.375%, 2/10/2020 | 600,000 | 645,761 |
| Kroger Co., 5.4%, 7/15/2040 | 110,000 | 104,260 |
| North Atlantic Trading Co., 144A, 10.0%, 3/1/2012 | 108,750 | 102,225 |
| SUPERVALU, Inc., 8.0%, 5/1/2016 | 10,000 | 9,575 |
| | | **2,122,583** |
| **Energy 0.9%** | | |
| Belden & Blake Corp., 8.75%, 7/15/2012 | 130,000 | 124,150 |
| BreitBurn Energy Partners LP, 144A, 8.625%, 10/15/2020 | 10,000 | 10,050 |
| Bristow Group, Inc., 7.5%, 9/15/2017 | 30,000 | 31,650 |
| Chaparral Energy, Inc., 8.5%, 12/1/2015 | 40,000 | 40,700 |
| DCP Midstream LLC, 144A, 9.75%, 3/15/2019 | 200,000 | 258,464 |
| El Paso Corp., 7.25%, 6/1/2018 | 20,000 | 21,410 |
| Enterprise Products Operating LLC, 6.125%, 10/15/2039 | 230,000 | 239,386 |
| Kinder Morgan Energy Partners LP: | | |
| 6.5%, 9/1/2039 | 50,000 | 51,652 |
| 7.3%, 8/15/2033 | 360,000 | 400,717 |
| Linn Energy LLC, 11.75%, 5/15/2017 | 35,000 | 40,075 |
| Newfield Exploration Co., 7.125%, 5/15/2018 | 40,000 | 42,100 |
| ONEOK Partners LP, 6.15%, 10/1/2016 | 201,000 | 225,896 |
| OPTI Canada, Inc., 7.875%, 12/15/2014 | 10,000 | 7,063 |
| Petrohawk Energy Corp., 7.875%, 6/1/2015 | 15,000 | 15,619 |
| Plains All American Pipeline LP, 8.75%, 5/1/2019 | 600,000 | 744,597 |
| Plains Exploration & Production Co., 7.0%, 3/15/2017 | 15,000 | 15,412 |
| Stone Energy Corp., 6.75%, 12/15/2014 | 25,000 | 24,375 |
| Weatherford International Ltd., 5.125%, 9/15/2020 | 300,000 | 298,510 |
| Williams Partners LP, 4.125%, 11/15/2020 | 253,000 | 239,639 |
| | | **2,831,465** |

| | Principal Amount ($) (b) | Value ($) |
|---|---|---|
| **Financials 2.2%** | | |
| Algoma Acquisition Corp., 144A, 9.875%, 6/15/2015 | 20,000 | 18,000 |
| Ally Financial, Inc., 144A, 7.5%, 9/15/2020 | 60,000 | 62,925 |
| American Express Co., 7.0%, 3/19/2018 | 390,000 | 454,261 |
| Ashton Woods USA LLC, 144A, Step-up Coupon, 0% to 6/30/2012, 11.0% to 6/30/2015 | 36,400 | 20,202 |
| Bank of America Corp., Series L, 7.625%, 6/1/2019 | 410,000 | 472,088 |
| Calpine Construction Finance Co., LP, 144A, 8.0%, 6/1/2016 | 30,000 | 31,875 |
| CIT Group, Inc., 7.0%, 5/1/2015 | 65,355 | 65,518 |
| Citigroup, Inc., 5.375%, 8/9/2020 (a) | 500,000 | 519,504 |
| Fifth Third Bancorp., 5.45%, 1/15/2017 | 429,000 | 438,508 |
| Ford Motor Credit Co., LLC, 9.875%, 8/10/2011 | 60,000 | 62,456 |
| General Electric Capital Corp., Series A, 5.25%, 10/19/2012 | 550,000 | 587,831 |
| Hartford Financial Services Group, Inc., 5.95%, 10/15/2036 | 150,000 | 141,515 |
| iPayment, Inc., 9.75%, 5/15/2014 | 25,000 | 23,500 |
| JPMorgan Chase & Co., 2.6%, 1/15/2016 | 700,000 | 679,190 |
| KeyBank NA, 5.7%, 11/1/2017 | 250,000 | 254,588 |
| Lincoln National Corp., 8.75%, 7/1/2019 | 190,000 | 237,661 |
| MetLife, Inc.: | | |
| 6.75%, 6/1/2016 | 113,000 | 131,076 |
| 7.717%, 2/15/2019 | 250,000 | 306,933 |
| Morgan Stanley: | | |
| 3.45%, 11/2/2015 | 45,000 | 43,873 |
| Series F, 6.625%, 4/1/2018 | 225,000 | 244,073 |
| Navios Maritime Acquisition Corp., 144A, 8.625%, 11/1/2017 | 10,000 | 10,225 |
| Nielsen Finance LLC, 144A, 7.75%, 10/15/2018 | 10,000 | 10,350 |
| PNC Bank NA, 6.875%, 4/1/2018 | 300,000 | 342,918 |
| Prudential Financial, Inc.: | | |
| Series B, 5.1%, 9/20/2014 | 100,000 | 107,417 |
| 6.2%, 1/15/2015 | 100,000 | 110,281 |
| 7.375%, 6/15/2019 | 30,000 | 35,371 |
| Rainbow National Services LLC, 144A, 10.375%, 9/1/2014 | 4,000 | 4,150 |
| Reynolds Group Issuer, Inc., 144A, 9.0%, 4/15/2019 | 100,000 | 103,625 |
| Santander US Debt SA Unipersonal, 144A, 2.991%, 10/7/2013 | 500,000 | 485,735 |
| The Goldman Sachs Group, Inc., 6.15%, 4/1/2018 | 400,000 | 440,477 |
| Travelers Companies, Inc., 5.35%, 11/1/2040 | 120,000 | 118,231 |

*The accompanying notes are an integral part of the financial statements.*

| | Principal Amount ($) (b) | Value ($) |
|---|---|---|
| Tropicana Entertainment LLC, 9.625%, 12/15/2014** | 75,000 | 38 |
| UCI Holdco, Inc., 9.25%***, 12/15/2013 (PIK) | 42,024 | 41,919 |
| WMG Acquisition Corp., 9.5%, 6/15/2016 | 20,000 | 21,450 |
| | | **6,627,764** |
| **Health Care 0.5%** | | |
| DaVita, Inc.: | | |
| 6.375%, 11/1/2018 | 10,000 | 9,950 |
| 6.625%, 11/1/2020 | 10,000 | 9,900 |
| Express Scripts, Inc.: | | |
| 6.25%, 6/15/2014 | 250,000 | 279,490 |
| 7.25%, 6/15/2019 | 320,000 | 378,759 |
| HCA, Inc.: | | |
| 8.5%, 4/15/2019 | 10,000 | 10,950 |
| 9.125%, 11/15/2014 | 35,000 | 36,706 |
| 9.625%, 11/15/2016 (PIK) | 42,000 | 44,993 |
| IASIS Healthcare LLC, 8.75%, 6/15/2014 | 30,000 | 30,788 |
| Laboratory Corp. of America Holdings, 4.625%, 11/15/2020 | 180,000 | 178,376 |
| Medco Health Solutions, Inc., 7.125%, 3/15/2018 | 425,000 | 498,736 |
| The Cooper Companies, Inc., 7.125%, 2/15/2015 | 45,000 | 46,350 |
| | | **1,524,998** |
| **Industrials 0.2%** | | |
| Actuant Corp., 6.875%, 6/15/2017 | 20,000 | 20,450 |
| ARAMARK Corp., 8.5%, 2/1/2015 | 10,000 | 10,450 |
| BE Aerospace, Inc., 8.5%, 7/1/2018 | 50,000 | 54,750 |
| Belden, Inc., 7.0%, 3/15/2017 | 25,000 | 25,312 |
| Cenveo Corp., 144A, 10.5%, 8/15/2016 | 10,000 | 9,825 |
| Congoleum Corp., 9.0%, 12/31/2017 (PIK) | 62,700 | 43,225 |
| Corrections Corp. of America, 7.75%, 6/1/2017 | 10,000 | 10,613 |
| CSX Corp.: | | |
| 6.15%, 5/1/2037 | 150,000 | 161,274 |
| 6.25%, 3/15/2018 | 190,000 | 217,961 |
| Great Lakes Dredge & Dock Co., 7.75%, 12/15/2013 | 20,000 | 20,175 |
| K. Hovnanian Enterprises, Inc., 8.875%, 4/1/2012 | 25,000 | 24,500 |
| Kansas City Southern de Mexico SA de CV, 7.375%, 6/1/2014 | 20,000 | 20,900 |
| Navios Maritime Holdings, Inc., 9.5%, 12/15/2014 | 35,000 | 36,400 |
| Owens Corning, Inc., 9.0%, 6/15/2019 | 10,000 | 11,732 |
| United Rentals North America, Inc., 10.875%, 6/15/2016 | 35,000 | 39,987 |
| | | **707,554** |
| **Information Technology 0.2%** | | |
| Alcatel-Lucent USA, Inc., 6.45%, 3/15/2029 | 30,000 | 23,700 |
| eBay, Inc., 1.625%, 10/15/2015 | 500,000 | 479,763 |
| MasTec, Inc., 7.625%, 2/1/2017 | 35,000 | 34,825 |
| SunGard Data Systems, Inc., 10.25%, 8/15/2015 | 70,000 | 73,588 |
| Vangent, Inc., 9.625%, 2/15/2015 | 15,000 | 13,575 |
| | | **625,451** |
| **Materials 0.3%** | | |
| Appleton Papers, Inc., 144A, 11.25%, 12/15/2015 | 15,000 | 12,000 |
| CPG International I, Inc., 10.5%, 7/1/2013 | 50,000 | 51,000 |
| Crown Americas LLC, 7.625%, 5/15/2017 | 10,000 | 10,750 |
| Domtar Corp., 10.75%, 6/1/2017 | 20,000 | 25,200 |
| Dow Chemical Co., 4.25%, 11/15/2020 | 185,000 | 177,211 |
| Exopack Holding Corp., 11.25%, 2/1/2014 | 80,000 | 83,000 |
| GEO Specialty Chemicals, Inc.: | | |
| 144A, 7.5%, 3/31/2015 (PIK) | 209,283 | 179,983 |
| 10.0%, 3/31/2015 | 206,080 | 187,533 |
| Georgia-Pacific LLC, 144A, 7.125%, 1/15/2017 | 15,000 | 15,975 |
| Graphic Packaging International, Inc., 9.5%, 6/15/2017 | 30,000 | 32,738 |
| Millar Western Forest Products Ltd., 7.75%, 11/15/2013 | 15,000 | 14,213 |
| NewMarket Corp., 7.125%, 12/15/2016 | 65,000 | 66,462 |
| Owens-Brockway Glass Container, Inc., 7.375%, 5/15/2016 | 10,000 | 10,625 |
| Radnor Holdings Corp., 11.0%, 3/15/2010** | 40,000 | 4 |
| Silgan Holdings, Inc., 7.25%, 8/15/2016 | 20,000 | 21,300 |
| Wolverine Tube, Inc., 15.0%, 3/31/2012 (PIK)** | 43,120 | 23,285 |
| | | **911,279** |
| **Telecommunication Services 0.4%** | | |
| American Tower Corp.: | | |
| 5.05%, 9/1/2020 | 350,000 | 344,202 |
| 7.25%, 5/15/2019 | 175,000 | 197,756 |
| AT&T Mobility LLC, 6.5%, 12/15/2011 | 275,000 | 290,207 |
| Cincinnati Bell, Inc., 8.375%, 10/15/2020 | 20,000 | 19,200 |
| Cricket Communications, Inc., 10.0%, 7/15/2015 | 50,000 | 53,563 |
| ERC Ireland Preferred Equity Ltd., 144A, 8.05%***, 2/15/2017 (PIK) EUR | 108,497 | 13,007 |
| Intelsat Corp., 9.25%, 6/15/2016 | 110,000 | 118,800 |
| Intelsat Subsidiary Holding Co. SA, 8.875%, 1/15/2015 | 60,000 | 61,650 |
| iPCS, Inc., 2.412%***, 5/1/2013 | 10,000 | 9,625 |
| Telesat Canada, 11.0%, 11/1/2015 | 70,000 | 78,575 |
| West Corp., 144A, 8.625%, 10/1/2018 | 10,000 | 10,600 |

*The accompanying notes are an integral part of the financial statements.*

| | Principal Amount ($) (b) | Value ($) |
|---|---|---|
| Windstream Corp.: | | |
| 7.0%, 3/15/2019 | 25,000 | 24,625 |
| 8.625%, 8/1/2016 | 10,000 | 10,525 |
| | | **1,232,335** |
| **Utilities 0.2%** | | |
| AES Corp.: | | |
| 8.0%, 10/15/2017 | 35,000 | 37,013 |
| 8.0%, 6/1/2020 | 30,000 | 31,800 |
| DTE Energy Co., 7.625%, 5/15/2014 | 81,000 | 93,362 |
| FirstEnergy Solutions Corp., 6.8%, 8/15/2039 | 234,000 | 226,793 |
| Mirant North America LLC, 7.375%, 12/31/2013 | 20,000 | 20,377 |
| NRG Energy, Inc.: | | |
| 7.375%, 2/1/2016 | 50,000 | 51,250 |
| 7.375%, 1/15/2017 | 60,000 | 61,800 |
| Sempra Energy, 6.5%, 6/1/2016 | 135,000 | 156,723 |
| | | **679,118** |
| **Total Corporate Bonds** (Cost $20,453,751) | | **20,913,205** |

## Asset-Backed 0.3%

| | Principal Amount ($) (b) | Value ($) |
|---|---|---|
| **Automobile Receivables 0.1%** | | |
| Ford Credit Auto Owner Trust, "B", Series 2007-B, 5.69%, 11/15/2012 | 379,000 | **395,663** |
| **Credit Card Receivables 0.2%** | | |
| Citibank Omni Master Trust, "A8", Series 2009-A8, 144A, 2.36%***, 5/16/2016 | 500,000 | **506,197** |
| **Total Asset-Backed** (Cost $885,529) | | **901,860** |

## Mortgage-Backed Securities Pass-Throughs 7.4%

| | Principal Amount ($) (b) | Value ($) |
|---|---|---|
| Federal Home Loan Mortgage Corp.: | | |
| 4.0%, 8/1/2039 | 1,732,457 | 1,723,050 |
| 6.0%, 3/1/2038 | 38,000 | 41,082 |
| Federal National Mortgage Association: | | |
| 3.274%***, 8/1/2037 | 166,007 | 173,882 |
| 3.5%, 7/1/2025 (c) | 3,350,000 | 3,374,078 |
| 4.0%, with various maturities from 5/1/2039 until 9/1/2040 (c) | 4,964,684 | 4,943,524 |
| 4.5%, 9/1/2035 | 50,883 | 52,447 |
| 5.5%, with various maturities from 4/1/2035 until 4/1/2038 (c) | 5,785,220 | 6,198,399 |
| 6.0%, with various maturities from 1/1/2024 until 8/1/2037 (c) | 3,091,323 | 3,370,800 |
| 6.5%, with various maturities from 5/1/2017 until 1/1/2038 (c) | 553,536 | 614,569 |
| 8.0%, 9/1/2015 | 68,510 | 74,278 |
| Government National Mortgage Association: | | |
| 4.5%, 7/1/2039 (c) | 750,000 | 778,770 |
| 5.0%, 5/1/2038 (c) | 750,000 | 797,402 |
| 5.5%, 5/1/2036 (c) | 750,000 | 810,527 |
| **Total Mortgage-Backed Securities Pass-Throughs** (Cost $22,807,624) | | **22,952,808** |

## Commercial Mortgage-Backed Securities 1.8%

| | Principal Amount ($) (b) | Value ($) |
|---|---|---|
| Banc of America Commercial Mortgage, Inc., "A4", Series 2007-4, 5.742%***, 2/10/2051 | 750,000 | 798,887 |
| Bear Stearns Commercial Mortgage Securities, Inc., "A4", Series 2007-PW18, 5.7%, 6/13/2050 | 862,000 | 898,150 |
| Greenwich Capital Commercial Funding Corp., "A4", Series 2006-GG7, 5.883%***, 7/10/2038 | 425,000 | 463,674 |
| JPMorgan Chase Commercial Mortgage Securities Corp.: | | |
| "A4", Series 2006-LDP7, 5.872%***, 4/15/2045 | 315,000 | 344,487 |
| "A4", Series 2007-LD12, 5.882%, 2/15/2051 | 625,000 | 661,722 |
| LB-UBS Commercial Mortgage Trust: | | |
| "A2", Series 2005-C2, 4.821%, 4/15/2030 | 17,711 | 17,718 |
| "A4", Series 2006-C1, 5.156%, 2/15/2031 | 1,250,000 | 1,335,222 |
| "A3", Series 2006-C7, 5.347%, 11/15/2038 | 700,000 | 740,082 |
| "A4", Series 2007-C6, 5.858%, 7/15/2040 | 300,000 | 315,201 |
| **Total Commercial Mortgage-Backed Securities** (Cost $5,188,170) | | **5,575,143** |

## Collateralized Mortgage Obligations 0.3%

| | Principal Amount ($) (b) | Value ($) |
|---|---|---|
| FDIC Structured Sale Guaranteed Notes, "1A", Series 2010-S1, 144A, 0.811%***, 2/25/2048 | 582,444 | 583,358 |
| Federal Home Loan Mortgage Corp., "H", Series 2278, 6.5%, 1/15/2031 | 5,440 | 5,956 |
| NCUA Guaranteed Notes, "1A", Series 2010-R1, 0.715%***, 10/7/2020 | 388,217 | 387,732 |
| **Total Collateralized Mortgage Obligations** (Cost $977,260) | | **977,046** |

## Government & Agency Obligations 9.4%

| | | Principal Amount ($) (b) | Value ($) |
|---|---|---|---|
| **Sovereign Bonds 2.6%** | | | |
| Federal Republic of Germany — Inflation Linked Note, 2.25%, 4/15/2013 | EUR | 214,842 | 304,764 |
| Government of Canada — Inflation Linked Bond, 4.0%, 12/1/2031 | CAD | 269,751 | 419,738 |

*The accompanying notes are an integral part of the financial statements.*

| | | Principal Amount ($) (b) | Value ($) |
|---|---|---|---|
| Government of France — Inflation Linked Bonds: | | | |
| 1.0%, 7/25/2017 | EUR | 242,906 | 331,908 |
| 2.25%, 7/25/2020 | EUR | 510,081 | 736,840 |
| 3.15%, 7/25/2032 | EUR | 543,526 | 917,436 |
| Government of Japan — Inflation Linked Bond, Series 9, 1.1%, 9/10/2016 | JPY | 41,664,000 | 515,989 |
| Government of Sweden, Series 3105, 3.5%, 12/1/2015 | SEK | 2,650,000 | 533,164 |
| Republic of Italy — Inflation Linked Bond, 2.1%, 9/15/2017 | EUR | 152,842 | 199,267 |
| Republic of Poland, 6.375%, 7/15/2019 | | 100,000 | 112,021 |
| State of Qatar, 144A, 6.4%, 1/20/2040 | | 100,000 | 108,500 |
| United Kingdom Treasury — Inflation Linked Bonds: | | | |
| 1.125%, 11/22/2037 | GBP | 413,068 | 729,668 |
| 1.875%, 11/22/2022 | GBP | 532,462 | 947,438 |
| 2.0%, 1/26/2035 | GBP | 225,000 | 591,574 |
| 2.5%, 8/16/2013 | GBP | 120,000 | 521,807 |
| 2.5%, 7/26/2016 | GBP | 112,000 | 547,516 |
| 2.5%, 4/16/2020 | GBP | 91,000 | 453,099 |
| | | | **7,970,729** |

## US Treasury Obligations 6.8%

| | Principal Amount ($) (b) | Value ($) |
|---|---|---|
| US Treasury Bill, 0.185%****, 3/17/2011 (d) | 188,000 | 187,958 |
| US Treasury Bonds: | | |
| 4.75%, 2/15/2037 | 1,500,000 | 1,612,032 |
| 5.375%, 2/15/2031 | 1,500,000 | 1,751,016 |
| US Treasury Inflation-Indexed Bonds: | | |
| 2.375%, 1/15/2025 | 794,754 | 884,412 |
| 3.625%, 4/15/2028 | 845,113 | 1,090,921 |
| 3.875%, 4/15/2029 | 159,643 | 214,109 |
| US Treasury Inflation-Indexed Notes: | | |
| 1.875%, 7/15/2015 | 185,523 | 200,973 |
| 2.375%, 1/15/2017 | 732,031 | 815,757 |
| 2.5%, 7/15/2016 | 481,908 | 540,867 |
| 3.375%, 1/15/2012 | 538,244 | 562,676 |
| US Treasury Notes: | | |
| 1.75%, 1/31/2014 | 8,000,000 | 8,167,504 |
| 3.125%, 5/15/2019 | 500,000 | 505,273 |
| 3.625%, 2/15/2020 | 2,750,000 | 2,853,983 |
| 4.5%, 11/15/2015 | 1,500,000 | 1,679,413 |
| | | **21,066,894** |
| **Total Government & Agency Obligations** (Cost $27,802,685) | | **29,037,623** |

## Loan Participations and Assignments 0.0%

### Senior Loans***

| | Principal Amount ($) (b) | Value ($) |
|---|---|---|
| Hawker Beechcraft Acquisition Co., LLC: | | |
| Term Loan, 2.261%, 3/26/2014 | 22,288 | 19,602 |
| Letter of Credit, 2.289%, 3/26/2014 | 1,336 | 1,175 |
| IASIS Healthcare LLC, Term Loan, 5.538%, 6/13/2014 (PIK) | 91,366 | 88,145 |
| **Total Loan Participations and Assignments** (Cost $113,854) | | **108,922** |

## Municipal Bonds and Notes 0.5%

| | Principal Amount ($) (b) | Value ($) |
|---|---|---|
| California, University Revenues, Build America Bonds, 5.946%, 5/15/2045 | 125,000 | 116,633 |
| Chicago, IL, Transit Authority, Sales Tax Receipts Revenue, Build America Bonds, Series B, 6.2%, 12/1/2040 (e) | 185,000 | 170,342 |
| Kentucky, Asset/Liability Commission, General Fund Revenue, 3.165%, 4/1/2018 | 500,000 | 488,680 |
| Louisville & Jefferson County, KY, Metropolitan Sewer District & Drain System, Build America Bonds, 6.25%, 5/15/2043 | 150,000 | 151,029 |
| Pennsylvania, State General Obligation, First Series, 5.25%, 2/1/2014, INS: NATL | 240,000 | 269,162 |
| Virginia, College Building Authority, Educational Facilities Revenue, 21st Century College, Series B, 5.0%, 2/1/2014 | 365,000 | 405,895 |
| **Total Municipal Bonds and Notes** (Cost $1,639,001) | | **1,601,741** |

## Preferred Securities 0.1%

### Financials 0.1%

| | Principal Amount ($) (b) | Value ($) |
|---|---|---|
| Farm Credit Bank of Texas, Series 1, 7.561%, 12/15/2013 (f) | 218,000 | **225,035** |
| **Materials 0.0%** | | |
| Hercules, Inc., 6.5%, 6/30/2029 | 40,000 | **31,000** |
| **Total Preferred Securities** (Cost $244,655) | | **256,035** |

## Other Investments 0.0%

### Consumer Discretionary

| | Units | Value ($) |
|---|---|---|
| AOT Bedding Super Holdings LLC* (Cost $2,000) | 2 | **2,000** |

## Exchange-Traded Funds 12.7%

| | Shares | Value ($) |
|---|---|---|
| iShares JPMorgan USD Emerging Markets Bond Fund | 41,986 | 4,495,861 |
| iShares Russell 2000 Value Index Fund | 90,940 | 6,464,925 |
| SPDR Barclays Capital International Treasury Bond | 79,818 | 4,666,160 |
| Vanguard Emerging Markets Fund | 198,166 | 9,541,693 |
| Vanguard Total Bond Market Fund | 172,600 | 13,854,602 |
| **Total Exchange-Traded Funds** (Cost $33,133,216) | | **39,023,241** |

## Securities Lending Collateral 6.8%

| | | |
|---|---|---|
| Daily Assets Fund Institutional, 0.27% (g) (h) (Cost $20,930,886) | 20,930,886 | **20,930,886** |

## Cash Equivalents 6.4%

| | | |
|---|---|---|
| Central Cash Management Fund, 0.19% (g) (Cost $19,630,591) | 19,630,591 | **19,630,591** |

*The accompanying notes are an integral part of the financial statements.*

| | % of Net Assets | Value ($) |
|---|---|---|
| **Total Investment Portfolio** (Cost $294,182,058)† | 109.3 | **336,821,795** |
| **Other Assets and Liabilities, Net** | (9.3) | **(28,549,600)** |
| **Net Assets** | 100.0 | **308,272,195** |

* *Non-income producing security.*

** *Non-income producing security. Issuer has defaulted on the payment of principal or the interest or has filed for bankruptcy. The following table represents bonds that are in default:*

| Security | Coupon | Maturity Date | Principal Amount ($) | | Acquisition Cost ($) | Value ($) |
|---|---|---|---|---|---|---|
| CanWest MediaWorks LP | 9.25% | 8/1/2015 | 25,000 | USD | 25,000 | 4,250 |
| Fontainebleau Las Vegas Holdings LLC | 11.0% | 6/15/2015 | 25,000 | USD | 25,000 | 88 |
| Radnor Holdings Corp. | 11.0% | 3/15/2010 | 40,000 | USD | 25,775 | 4 |
| Tropicana Entertainment LLC | 9.625% | 12/15/2014 | 75,000 | USD | 55,245 | 38 |
| Vertis, Inc. | 13.5% | 4/1/2014 | 42,609 | USD | 17,309 | 1,278 |
| Wolverine Tube, Inc. | 15.0% | 3/31/2012 | 43,120 | USD | 43,120 | 23,285 |
| Young Broadcasting, Inc. | 8.75% | 1/15/2014 | 130,000 | USD | 111,175 | 1 |
| | | | | | **302,624** | **28,944** |

*** *These securities are shown at their current rate as of December 31, 2010. Floating rate securities' yields vary with a designated market index or market rate, such as the coupon-equivalent of the US Treasury bill rate.*

**** *Annualized yield at time of purchase; not a coupon rate.*

† *The cost for federal income tax purposes was $297,261,185. At December 31, 2010, net unrealized appreciation for all securities based on tax cost was $39,560,610. This consisted of aggregate gross unrealized appreciation for all securities in which there was an excess of value over tax cost of $46,622,458 and aggregate gross unrealized depreciation for all securities in which there was an excess of tax cost over value of $7,061,848.*

(a) *All or a portion of these securities were on loan (see Notes to Financial Statements). The value of all securities loaned at December 31, 2010 amounted to $20,273,579, which is 6.6% of net assets.*

(b) *Principal amount stated in US dollars unless otherwise noted.*

(c) *When-issued or delayed delivery security included.*

(d) *At December 31, 2010, this security has been pledged, in whole or in part, to cover initial margin requirements for open futures contracts.*

(e) *Taxable issue.*

(f) *Date shown is call date; not a maturity date for the perpetual preferred securities.*

(g) *Affiliated fund managed by Deutsche Investment Management Americas Inc. The rate shown is the annualized seven-day yield at period end.*

(h) *Represents collateral held in connection with securities lending. Income earned by the Fund is net of borrower rebates.*

*144A: Security exempt from registration under Rule 144A of the Securities Act of 1933. These securities may be resold in transactions exempt from registration, normally to qualified institutional buyers.*

*ADR: American Depositary Receipt*

*CVA: Certificaten Van Aandelen*

*FDIC: Federal Deposit Insurance Corp.*

*INS: Insured*

*NATL: National Public Finance Guarantee Corp.*

*PIK: Denotes that all or a portion of the income is paid in-kind.*

*SPDR: Standard & Poor's Depositary Receipt*

*Included in the portfolio are investments in mortgage or asset-backed securities which are interests in separate pools of mortgages or assets. Effective maturities of these investments may be shorter than stated maturities due to prepayments. Some separate investments in the Federal National Mortgage Association issues which have similar coupon rates have been aggregated for presentation purposes in this investment portfolio.*

*At December 31, 2010, open futures contracts purchased were as follows:*

| Futures | Currency | Expiration Date | Contracts | Notional Value ($) | Unrealized Appreciation/ (Depreciation) ($) |
|---|---|---|---|---|---|
| 10 Year Australian Treasury Bond | AUD | 3/15/2011 | 135 | 14,263,722 | 106,442 |
| 10 Year US Treasury Note | USD | 3/22/2011 | 190 | 22,883,125 | (619,876) |
| 2 Year US Treasury Note | USD | 3/31/2011 | 296 | 64,796,250 | 46,626 |
| DAX Index | EUR | 3/18/2011 | 5 | 1,157,069 | (21,631) |
| Federal Republic of Germany Euro-Schatz | EUR | 3/8/2011 | 19 | 2,767,604 | (3,082) |
| FTSE 100 Index | GBP | 3/18/2011 | 23 | 2,113,187 | 20,440 |
| Hang Seng Index | HKD | 1/28/2011 | 2 | 296,161 | 3,975 |
| IBEX 35 Index | EUR | 1/21/2011 | 3 | 392,511 | (10,011) |

*The accompanying notes are an integral part of the financial statements.*

| Futures | Currency | Expiration Date | Contracts | Notional Value ($) | Unrealized Appreciation/ (Depreciation) ($) |
|---|---|---|---|---|---|
| S&P 500 E-Mini Index | USD | 3/18/2011 | 22 | 1,378,300 | 18,810 |
| TOPIX Index | JPY | 3/11/2011 | 13 | 1,434,659 | 27,109 |
| United Kingdom Long Gilt Bond | GBP | 3/29/2011 | 39 | 7,265,574 | (20,286) |
| **Total net unrealized depreciation** | | | | | **(451,484)** |

*At December 31, 2010, open futures contracts sold were as follows:*

| Futures | Currency | Expiration Date | Contracts | Notional Value ($) | Unrealized Appreciation/ (Depreciation) ($) |
|---|---|---|---|---|---|
| 10 Year Canadian Government Bond | CAD | 3/22/2011 | 75 | 9,244,695 | (38,137) |
| 10 Year Japanese Government Bond | JPY | 3/10/2011 | 25 | 43,296,588 | (185,124) |
| 10 Year US Treasury Note | USD | 3/22/2011 | 46 | 5,540,125 | 141,906 |
| 30 Year US Treasury Bond | USD | 3/22/2011 | 20 | 2,442,500 | 100,625 |
| AEX Index | EUR | 1/21/2011 | 8 | 758,591 | (6,200) |
| ASX SPI 200 Index | AUD | 3/17/2011 | 10 | 1,209,461 | 11,251 |
| CAC 40 Index | EUR | 1/21/2011 | 11 | 559,970 | 13,450 |
| DJ Euro Stoxx 50 Index | EUR | 3/18/2011 | 43 | 1,605,457 | 40,797 |
| Federal Republic of Germany Euro-Bund | EUR | 3/8/2011 | 170 | 28,466,796 | 184,919 |
| FTSE MIB Index | EUR | 3/18/2011 | 7 | 944,998 | 25,958 |
| Russell 2000 E-Mini Index | USD | 3/18/2011 | 4 | 312,920 | (3,460) |
| S&P TSE 60 Index | CAD | 3/17/2011 | 3 | 462,899 | (7,640) |
| Ultra Long-Term US Treasury Bond | USD | 3/22/2011 | 5 | 635,469 | 17,461 |
| **Total net unrealized appreciation** | | | | | **295,806** |

*As of December 31, 2010, the Fund had the following open forward foreign currency exchange contracts:*

| Contracts to Deliver | | In Exchange For | | Settlement Date | Unrealized Appreciation ($) | Counterparty |
|---|---|---|---|---|---|---|
| USD | 2,039,377 | JPY | 171,066,000 | 1/25/2011 | 68,229 | UBS AG |
| USD | 6,964,033 | CAD | 7,014,000 | 1/25/2011 | 86,748 | UBS AG |
| USD | 5,657,268 | SEK | 38,571,000 | 1/25/2011 | 72,772 | UBS AG |
| USD | 13,515,110 | AUD | 13,690,000 | 1/25/2011 | 439,420 | UBS AG |
| USD | 5,303,999 | NOK | 31,449,000 | 1/25/2011 | 78,876 | UBS AG |
| GBP | 3,926,000 | USD | 6,134,120 | 1/25/2011 | 14,340 | UBS AG |
| **Total unrealized appreciation** | | | | | **760,385** | |

| Contracts to Deliver | | In Exchange For | | Settlement Date | Unrealized Depreciation ($) | Counterparty |
|---|---|---|---|---|---|---|
| EUR | 8,600 | USD | 11,386 | 1/20/2011 | (105) | JPMorgan Chase Securities, Inc. |
| EUR | 681,000 | USD | 908,241 | 1/25/2011 | (1,740) | UBS AG |
| CHF | 9,665,000 | USD | 10,065,140 | 1/25/2011 | (275,076) | UBS AG |
| NZD | 11,904,000 | USD | 8,855,028 | 1/25/2011 | (400,816) | UBS AG |
| **Total unrealized depreciation** | | | | | **(677,737)** | |

**Currency Abbreviations**

| | | | | | |
|---|---|---|---|---|---|
| AUD | Australian Dollar | GBP | British Pound | NZD | New Zealand Dollar |
| CAD | Canadian Dollar | HKD | Hong Kong Dollar | SEK | Swedish Krona |
| CHF | Swiss Franc | JPY | Japanese Yen | USD | United States Dollar |
| EUR | Euro | NOK | Norwegian Krone | | |

*For information on the Fund's policy and additional disclosures regarding futures contracts and forward foreign currency exchange contracts, please refer to Note B in the accompanying Notes to Financial Statements.*

## Fair Value Measurements

*Various inputs are used in determining the value of the Fund's investments. These inputs are summarized in three broad levels. Level 1 includes quoted prices in active markets for identical securities. Level 2 includes other significant observable inputs (including quoted prices for similar securities, interest rates, prepayment speeds, and credit risk). Level 3 includes significant unobservable inputs (including the Fund's own assumptions in determining the fair value of investments). The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities.*

*The following is a summary of the inputs used as of December 31, 2010 in valuing the Fund's investments. For information on the Fund's policy regarding the valuation of investments, please refer to the Security Valuation section of Note A in the accompanying Notes to Financial Statements.*

| **Assets** | **Level 1** | **Level 2** | **Level 3** | **Total** |
|---|---|---|---|---|
| Common Stocks and/or Other Equity Investments (i) | | | | |
| Consumer Discretionary | $ 16,158,616 | $ 4,334,308 | $ 39 | $ 20,492,963 |
| Consumer Staples | 11,285,599 | 4,711,312 | — | 15,996,911 |
| Energy | 20,434,131 | 3,111,910 | — | 23,546,041 |
| Financials | 12,709,915 | 6,665,155 | — | 19,375,070 |
| Health Care | 15,727,947 | 2,308,612 | — | 18,036,559 |
| Industrials | 14,248,430 | 6,637,163 | 0 | 20,885,593 |
| Information Technology | 26,824,520 | 2,711,366 | — | 29,535,886 |
| Materials | 8,165,367 | 3,377,495 | 1,934 | 11,544,796 |
| Telecommunication Services | 6,617,978 | 1,790,162 | — | 8,408,140 |
| Utilities | 6,427,251 | 661,484 | — | 7,088,735 |
| Fixed Income Investments (i) | | | | |
| Corporate Bonds | — | 20,498,209 | 414,996 | 20,913,205 |
| Asset Backed | — | 901,860 | — | 901,860 |
| Mortgage-Backed Securities Pass-Throughs | — | 22,952,808 | — | 22,952,808 |
| Commercial Mortgage-Backed Securities | — | 5,575,143 | — | 5,575,143 |
| Collateralized Mortgage Obligations | — | 977,046 | — | 977,046 |
| Government & Agency Obligations | — | 28,849,665 | — | 28,849,665 |
| Loan Participations and Assignments | — | 108,922 | — | 108,922 |
| Municipal Bonds and Notes | — | 1,601,741 | — | 1,601,741 |
| Preferred Securities | — | 256,035 | — | 256,035 |
| Other Investments | — | — | 2,000 | 2,000 |
| Exchange-Traded Funds | 39,023,241 | — | — | 39,023,241 |
| Short-Term Investments (i) | 40,561,477 | 187,958 | — | 40,749,435 |
| Derivatives (j) | — | 760,385 | — | 760,385 |
| **Total** | **$ 218,184,472** | **$ 118,978,739** | **$ 418,969** | **$ 337,582,180** |
| **Liabilities** | | | | |
| Derivatives (j) | $ (155,678) | $ (677,737) | $ — | $ (833,415) |
| **Total** | **$ (155,678)** | **$ (677,737)** | **$ —** | **$ (833,415)** |

*There have been no significant transfers between Level 1 and Level 2 fair value measurements during the year ended December 31, 2010.*

(i) *See Investment Portfolio for additional detailed categorizations.*

(j) *Derivatives include unrealized appreciation (depreciation) on open futures contracts and forward foreign currency exchange contracts.*

## Level 3 Reconciliation

*The following is a reconciliation of the Fund's Level 3 investments for which significant unobservable inputs were used in determining value:*

| | **Common Stocks and/or Other Equity Investments** | | | | | | |
|---|---|---|---|---|---|---|---|
| | **Consumer Discretionary** | **Industrials** | **Financials** | **Materials** | **Corporate Bonds** | **Other Investments** | **Total** |
| **Balance as of December 31, 2009** | $ 0 | $ — | $ 278,682 | $ 0 | $ 383,110 | $ — | **$ 661,792** |
| Realized gains (loss) | (8,344) | — | 107,337 | — | — | — | **98,993** |
| Change in unrealized appreciation (depreciation) | 8,342 | 0 | (37,791) | 1,934 | 33,279 | — | **5,764** |
| Amortization premium/discount | — | — | — | — | 5,349 | — | **5,349** |
| Net purchases (sales) | 41 | — | (348,228) | — | — | 2,000 | **(346,187)** |
| Transfers into Level 3 | — | — | — | — | 4,178 (k) | — | **4,178** |
| Transfers (out) of Level 3 | — | — | — | — | (10,920) (l) | — | **(10,920)** |
| **Balance as of December 31, 2010** | **$ 39** | **$ 0** | **$ —** | **$ 1,934** | **$ 414,996** | **$ 2,000** | **$ 418,969** |
| **Net change in unrealized appreciation (depreciation) from investments still held as of December 31, 2010** | **$ (2)** | **$ 0** | **$ —** | **$ 1,934** | **$ 33,279** | **$ —** | **$ 35,211** |

*Transfers between price levels are recognized at the beginning of the reporting period.*

(k) *The investment was transferred from Level 2 to Level 3 because of the lack of observable market data due to a decrease in market activity.*

(l) *The investment was transferred from Level 3 to Level 2 as a result of the availability of a pricing source supported by observable inputs.*

*The accompanying notes are an integral part of the financial statements.*

## Statement of Assets and Liabilities

as of December 31, 2010

| **Assets** | |
|---|---|
| Investments: | |
| Investments in unaffiliated securities, at value (cost $253,620,581) — including $20,273,579 of securities loaned | $ 296,260,318 |
| Investment in Daily Assets Fund Institutional (cost $20,930,886)* | 20,930,886 |
| Investment in Central Cash Management Fund (cost $19,630,591) | 19,630,591 |
| Total investments, at value (cost $294,182,058) | 336,821,795 |
| Cash | 131,748 |
| Foreign currency, at value (cost $192,052) | 209,917 |
| Deposits with broker for open futures contracts | 5,279,599 |
| Receivable for investments sold | 3,698 |
| Receivable for Fund shares sold | 2,493 |
| Dividends receivable | 249,181 |
| Interest receivable | 712,583 |
| Unrealized appreciation on open forward foreign currency exchange contracts | 760,385 |
| Foreign taxes recoverable | 53,154 |
| Other assets | 1,722 |
| Total assets | 344,226,275 |
| **Liabilities** | |
| Payable upon return of securities loaned | 20,930,886 |
| Payable for investments purchased | 203,348 |
| Payable for when-issued and delayed delivery securities purchased | 13,171,613 |
| Payable for Fund shares redeemed | 160,169 |
| Payable for variation margin on open futures contracts | 467,763 |
| Unrealized depreciation on open forward foreign currency exchange contracts | 677,737 |
| Accrued management fee | 106,819 |
| Deferred foreign taxes payable | 5,598 |
| Other accrued expenses and payables | 230,147 |
| Total liabilities | 35,954,080 |
| **Net assets, at value** | **$ 308,272,195** |
| **Net Assets Consist of** | |
| Undistributed net investment income | 4,323,414 |
| Net unrealized appreciation (depreciation) on: | |
| Investments (net of deferred foreign taxes of $5,598) | 42,634,139 |
| Futures | (155,678) |
| Foreign currency | 80,115 |
| Accumulated net realized gain (loss) | (54,154,043) |
| Paid-in capital | 315,544,248 |
| **Net assets, at value** | **$ 308,272,195** |
| **Class A** | |
| **Net Asset Value,** offering and redemption price per share ($308,272,195 ÷ 13,930,205 outstanding shares of beneficial interest, no par value, unlimited number of shares authorized) | **$ 22.13** |

* *Represents collateral on securities loaned.*

## Statement of Operations

for the year ended December 31, 2010

| **Investment Income** | |
|---|---|
| Income: | |
| Dividends (net of foreign taxes withheld of $105,864) | $ 4,481,983 |
| Interest | 3,237,650 |
| Income distributions — Central Cash Management Fund | 63,397 |
| Securities lending income, including income from Daily Assets Fund Institutional, net of borrower rebates | 49,944 |
| Total income | 7,832,974 |
| Expenses: | |
| Management fee | 1,124,396 |
| Administration fee | 307,796 |
| Services to shareholders | 5,088 |
| Custodian fee | 287,824 |
| Professional fees | 99,564 |
| Trustees' fees and expenses | 12,524 |
| Reports to shareholders | 62,119 |
| Other | 116,154 |
| Total expenses | 2,015,465 |
| **Net investment income (loss)** | 5,817,509 |
| **Realized and Unrealized Gain (Loss)** | |
| Net realized gain (loss) from: | |
| Investments (net of deferred foreign taxes of $325) | 19,036,432 |
| Futures | (325,572) |
| Foreign currency | (47,856) |
| | 18,663,004 |
| Change in net unrealized appreciation (depreciation) on: | |
| Investments (net of deferred foreign taxes of $5,598) | 7,992,264 |
| Futures | 94,474 |
| Foreign currency | (135,693) |
| | 7,951,045 |
| **Net gain (loss)** | **26,614,049** |
| **Net increase (decrease) in net assets resulting from operations** | **$ 32,431,558** |

*The accompanying notes are an integral part of the financial statements.*

# Statement of Changes in Net Assets

| Increase (Decrease) in Net Assets | Years Ended December 31, 2010 | 2009 |
|---|---|---|
| Operations: | | |
| Net investment income (loss) | $ 5,817,509 | $ 7,279,172 |
| Net realized gain (loss) | 18,663,004 | (21,287,397) |
| Change in net unrealized appreciation (depreciation) | 7,951,045 | 77,797,202 |
| Net increase (decrease) in net assets resulting from operations | 32,431,558 | 63,788,977 |
| Distributions to shareholders from: | | |
| Net investment income: | | |
| Class A | (9,827,154) | (11,680,702) |
| Total distributions | (9,827,154) | (11,680,702) |
| Fund share transactions: | | |
| **Class A** | | |
| Proceeds from shares sold | 4,966,734 | 6,740,726 |
| Shares issued to shareholders in reinvestment of distributions | 9,827,154 | 11,680,702 |
| Payments for shares redeemed | (48,195,061) | (58,626,337) |
| Shares converted* | — | 39,887 |
| Net increase (decrease) in net assets from Class A share transactions | (33,401,173) | (40,165,022) |
| **Class B** | | |
| Payments for shares redeemed | — | (307) |
| Shares converted* | — | (39,887) |
| Net increase (decrease) in net assets from Class B share transactions | — | (40,194) |
| **Increase (decrease) in net assets** | (10,796,769) | 11,903,059 |
| Net assets at beginning of period | 319,068,964 | 307,165,905 |
| Net assets at end of period (including undistributed net investment income of $4,323,414 and $9,339,818, respectively) | **$ 308,272,195** | **$ 319,068,964** |

| Other Information | | |
|---|---|---|
| **Class A** | | |
| Shares outstanding at beginning of period | 15,551,177 | 17,697,143 |
| Shares sold | 238,427 | 369,933 |
| Shares issued to shareholders in reinvestment of distributions | 467,070 | 740,222 |
| Shares redeemed | (2,326,469) | (3,258,791) |
| Shares converted* | — | 2,670 |
| Net increase (decrease) in Class A shares | (1,620,972) | (2,145,966) |
| Shares outstanding at end of period | 13,930,205 | **15,551,177** |
| **Class B** | | |
| Shares outstanding at beginning of period | — | 2,694 |
| Shares redeemed | — | (19) |
| Shares converted* | — | (2,675) |
| Net increase (decrease) in Class B shares | — | (2,694) |
| Shares outstanding at end of period | **—** | **—** |

* *On March 6, 2009, Class B shares converted into Class A shares.*

*The accompanying notes are an integral part of the financial statements.*

# Financial Highlights

## Class A

| Years Ended December 31, | 2010 | 2009 | 2008 | 2007 | 2006 |
|---|---|---|---|---|---|
| **Selected Per Share Data** | | | | | |
| **Net asset value, beginning of period** | **$20.52** | **$17.35** | **$24.81** | **$24.46** | **$22.75** |
| *Income (loss) from investment operations:* | | | | | |
| Net investment income[a] | .39 | .44 | .61 | .74 | .69[c] |
| Net realized and unrealized gain (loss) | 1.88 | 3.43 | (7.20) | .42 | 1.60 |
| **Total from investment operations** | 2.27 | 3.87 | (6.59) | 1.16 | 2.29 |
| *Less distributions from:* | | | | | |
| Net investment income | (.66) | (.70) | (.87) | (.81) | (.58) |
| **Net asset value, end of period** | **$22.13** | **$20.52** | **$17.35** | **$24.81** | **$24.46** |
| Total Return (%) | 11.22 | 23.43 | (27.33)[b] | 4.84[b] | 10.24[b,c] |
| **Ratios to Average Net Assets and Supplemental Data** | | | | | |
| Net assets, end of period ($ millions) | 308 | 319 | 307 | 528 | 600 |
| Ratio of expenses before expense reductions (%) | .65 | .60 | .64 | .52 | .55 |
| Ratio of expenses after expense reductions (%) | .65 | .60 | .62 | .51 | .51 |
| Ratio of net investment income (%) | 1.89 | 2.40 | 2.83 | 3.00 | 2.99[c] |
| Portfolio turnover rate (%) | 203 | 207 | 263 | 199 | 108 |

a *Based on average shares outstanding during the period.*

b *Total return would have been lower had certain expenses not been reduced.*

c *Includes non-recurring income from the Advisor recorded as a result of an administrative proceeding regarding disclosure of brokerage allocation practices in connection with sales of DWS Funds. The non-recurring income resulted in an increase in net investment income of $0.024 per share and an increase in the ratio of net investment income of 0.10%. Excluding this non-recurring income, total return would have been 0.10% lower.*

# Notes to Financial Statements

## A. Organization and Significant Accounting Policies

DWS Variable Series II (the "Trust") is registered under the Investment Company Act of 1940, as amended (the "1940 Act"), as an open-end management investment company organized as a Massachusetts business trust. The Trust offers seventeen funds (hereinafter referred to individually as "Fund" or collectively as "Funds"). The Fund is classified as a diversified open-end management investment company.

The Trust's financial statements are prepared in accordance with accounting principles generally accepted in the United States of America which require the use of management estimates. Actual results could differ from those estimates. The policies described below are followed consistently by the Trust in the preparation of its financial statements.

**Security Valuation.** Investments are stated at value determined as of the close of regular trading on the New York Stock Exchange on each day the exchange is open for trading.

Various inputs are used in determining the value of the Fund's investments. These inputs are summarized in three broad levels. Level 1 includes quoted prices in active markets for identical securities. Level 2 includes other significant observable inputs (including quoted prices for similar securities, interest rates, prepayment speeds, and credit risk). Level 3 includes significant unobservable inputs (including the Fund's own assumptions in determining the fair value of investments). The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities.

Equity securities and exchange-traded funds ("ETFs") are valued at the most recent sale price or official closing price reported on the exchange (US or foreign) or over-the-counter market on which they trade and are categorized as Level 1 securities. Securities or ETFs for which no sales are reported are valued at the calculated mean between the most recent bid and asked quotations on the relevant market or, if a mean cannot be determined, at the most recent bid quotation. For certain international equity securities, in order to adjust for events which may occur between the close of the foreign exchanges and the close of the New York Stock Exchange, a fair valuation model may be used. This fair valuation model takes into account comparisons to the valuation of American Depository Receipts (ADRs), exchange-traded funds, futures contracts and certain indices and these securities are categorized as Level 2.

Debt securities are valued by independent pricing services approved by the Fund's Board. If the pricing services are unable to provide valuations, securities are valued at the most recent bid quotation or evaluated price, as applicable, obtained from one or more broker-dealers. Such services may use various pricing techniques which take into account appropriate factors such as yield, quality, coupon rate, maturity, type of issue, trading characteristics and other data, as well as broker quotes. These securities are generally categorized as Level 2.

Futures contracts are generally valued at the settlement prices established each day on the exchange on which they are traded and are categorized as Level 1.

Forward currency contracts are valued at the prevailing forward exchange rate of the underlying currencies and are categorized as Level 2.

Money market instruments purchased with an original or remaining maturity of sixty days or less, maturing at par, are valued at amortized cost, which approximates value, and are categorized as Level 2. Investments in open-end investment companies are valued at their net asset value each business day and are categorized as Level 1.

Securities and other assets for which market quotations are not readily available or for which the above valuation procedures are deemed not to reflect fair value are valued in a manner that is intended to reflect their fair value as determined in accordance with procedures approved by the Board and are generally categorized as Level 3. In accordance with the Fund's valuation procedures, factors used in determining value may include, but are not limited to, the type of the security; the size of the holding; the initial cost of the security; the existence of any contractual restrictions on the security's disposition; the price and extent of public trading in similar securities of the issuer or of comparable companies; quotations or evaluated prices from broker-dealers and/or pricing services; information obtained from the issuer, analysts, and/or the appropriate stock exchange (for exchange-traded securities); an analysis of the company's or issuer's financial statements; an evaluation of the forces that influence the issuer and the market(s) in which the security is purchased and sold and with respect to debt securities; the maturity, coupon, creditworthiness, currency denomination and the movement of the market in which the security is normally traded. The value determined under these procedures may differ from published values for the same securities.

Disclosure about the classification of fair value measurements is included in a table following the Fund's Investment Portfolio.

**Foreign Currency Translations.** The books and records of the Trust are maintained in US dollars. Investment securities and other assets and liabilities denominated in a foreign currency are translated into US dollars at the prevailing exchange rates at period end. Purchases and sales of investment securities, income and expenses are translated into US dollars at the prevailing exchange rates on the respective dates of the transactions.

Net realized and unrealized gains and losses on foreign currency transactions represent net gains and losses between trade and settlement dates on securities transactions, the disposition of forward foreign currency exchange contracts and foreign currencies, and the difference between the amount of net investment income accrued and the US dollar amount actually received. That portion of both realized and unrealized gains and losses on investments that results from fluctuations in foreign currency exchange rates is not separately disclosed but is included with net realized and unrealized gain/appreciation and loss/depreciation on investments.

**Securities Lending.** The Fund lends securities to certain financial institutions. The Fund retains beneficial ownership of the securities it has loaned and continues to receive interest and dividends paid by the issuer of securities and to participate in any changes in their market value. The Fund requires the borrowers of the securities to maintain collateral with the Fund consisting of either cash or liquid, unencumbered assets having a value at least equal to the value of the securities loaned. When the collateral falls below specified amounts, the lending agent will use its best effort to obtain additional collateral on the next business day to meet required amounts under the security lending agreement. The Fund may invest the cash collateral into a joint trading account in an affiliated money market fund pursuant to Exemptive Orders issued by the SEC. The Fund receives compensation for lending its securities either in the form of fees or by earning interest on invested cash collateral net of borrower rebates and fees paid to a lending agent. Either the Fund or the borrower may terminate the loan. There may be risks of delay and costs in recovery of securities or even loss of rights in the collateral should the borrower of the securities fail financially. The Fund is also subject to all investment risks associated with the reinvestment of any cash collateral received, including, but not limited to, interest rate, credit and liquidity risk associated with such investments.

**Loan Participations and Assignments.** The Fund invests in Loan Participations and Assignments. Loan Participations and Assignments are portions of loans originated by banks and sold in pieces to investors. These US dollar-denominated fixed and floating rate loans ("Loans") in which the Fund invests, are arranged between the borrower and one or more financial institutions ("Lenders"). These Loans may take the form of Senior Loans, which are corporate obligations often issued in connection with recapitalizations, acquisitions, leveraged buy-outs and refinancings, and Sovereign Loans, which are debt instruments between a foreign sovereign entity and one or more financial institutions. The Fund invests in such Loans in the form of participations in Loans ("Participations") or assignments of all or a portion of Loans from third parties ("Assignments"). Participations typically result in the Fund having a contractual relationship only with the Lender, not with the borrower. The Fund has the right to receive payments of principal, interest and any fees to which it is entitled from the Lender selling the Participation and only upon receipt by the Lender of the payments from the borrower. In connection with purchasing Participations, the Fund generally has no right to enforce compliance by the borrower with the terms of the loan agreement relating to the Loan, or any rights of set-off against the borrower, and the Fund will not benefit directly from any collateral supporting the Loan in which it has purchased the Participation. As a result, the Fund assumes the credit risk of both the borrower and the Lender that is selling the Participation. Assignments typically result in the Fund having a direct contractual relationship with the borrower, and the Fund may enforce compliance by the borrower with the terms of the loan agreement. All Loan Participations and Assignments involve interest rate risk, liquidity risk and credit risk, including the potential default or insolvency of the borrower.

**Mortgage Dollar Rolls.** The Fund may enter into mortgage dollar rolls in which the Fund sells to a bank or broker/dealer (the "counterparty") mortgage-backed securities for delivery in the current month and simultaneously contracts to repurchase similar, but not identical, securities on a fixed date. The counterparty receives all principal and interest payments, including prepayments, made on the security while it is the holder. The Fund receives compensation as consideration for entering into the commitment to repurchase. The compensation is paid in the form of a lower price for the security upon its repurchase, or alternatively, a fee. Mortgage dollar rolls may be renewed with a new sale and repurchase price and a cash settlement made at each renewal without physical delivery of the securities subject to the contract.

Certain risks may arise upon entering into mortgage dollar rolls from the potential inability of counterparties to meet the terms of their commitments. Additionally, the value of such securities may change adversely before the Fund is able to repurchase them. There can be no assurance that the Fund's use of the cash that it receives from a mortgage dollar roll will provide a return that exceeds its costs.

**When-Issued/Delayed Delivery Securities.** The Fund may purchase securities with delivery or payment to occur at a later date beyond the normal settlement period. At the time the Fund enters into a commitment to purchase a security, the transaction is recorded and the value of the security is reflected in the net asset value. The price of such security and the date when the security will be delivered and paid for are fixed at the time the transaction is negotiated. The value of the security may vary with market fluctuations. No interest accrues to the Fund until payment takes place. At the time the Fund enters into this type of transaction it is required to segregate cash or other liquid assets at least equal to the amount of the commitment.

Certain risks may arise upon entering into when-issued or delayed delivery securities from the potential inability of counterparties to meet the terms of their contracts or if the issuer does not issue the securities due to political, economic, or other factors. Additionally, losses may arise due to changes in the value of the underlying securities.

**Taxes.** The Fund's policy is to comply with the requirements of the Internal Revenue Code, as amended, which are applicable to regulated investment companies and to distribute all of its taxable income to its shareholders.

Additionally, based on the Fund's understanding of the tax rules and rates related to income, gains and transactions for the foreign jurisdictions in which it invests, the Fund will provide for foreign taxes, and where appropriate, deferred foreign taxes.

At December 31, 2010, the Fund had an approximate net tax basis capital loss carryforward which may be applied against any realized net taxable capital gains of each succeeding year until fully utilized or until the following expiration dates, whichever occurs first:

| Fund | Capital Loss Carryforward ($) | Expiration Date | Capital Loss Carryforward Utilized ($) |
|---|---|---|---|
| DWS Balanced VIP | 6,483,000 | 12/31/2016 | 16,309,000 |
| | 45,045,000 | 12/31/2017 | |

The Fund has reviewed the tax positions for the open tax years as of December 31, 2010 and has determined that no provision for income tax is required in the Fund's financial statements. The Fund's federal tax returns for the prior three fiscal years remain open subject to examination by the Internal Revenue Service.

**Distribution of Income and Gains.** Distributions of net investment income of the Fund, if any, are made annually. Net realized gains from investment transactions, in excess of available capital loss carryforwards, would be taxable to the Fund if not distributed and, therefore, will be distributed to shareholders at least annually. The Fund may also make additional distributions for tax purposes if necessary.

The timing and characterization of certain income and capital gains distributions are determined annually in accordance with federal tax regulations which may differ from accounting principles generally accepted in the United States of America. These differences primarily relate to investments in foreign denominated investments, investments in forward currency contracts, investments in futures contracts and certain securities sold at a loss. As a result, net investment income (loss) and net realized gain (loss) on investment transactions for a reporting period may differ significantly from distributions during such period. Accordingly, the Fund may periodically make reclassifications among certain of its capital accounts without impacting the net asset value of the Fund.

At December 31, 2010, the Fund's components of distributable earnings on a tax basis were as follows:

| Fund | Undistributed Ordinary Income ($)* | Capital Loss Carryforwards ($) | Unrealized Appreciation (Depreciation) on Investments ($) |
|---|---|---|---|
| DWS Balanced VIP | 4,560,940 | (51,528,000) | 39,560,610 |

In addition, the tax character of distributions paid by the Fund is summarized as follows:

| | Distributions from Ordinary Income ($)* | |
|---|---|---|
| | Years Ended December 31, | |
| Fund | 2010 | 2009 |
| DWS Balanced VIP | 9,827,154 | 11,680,702 |

* *For tax purposes, short-term capital gain distributions are considered ordinary income distributions.*

**Expenses.** Expenses of the Trust arising in connection with a specific fund are allocated to that fund. Other Trust expenses which cannot be directly attributed to a fund are apportioned among the funds in the Trust.

**Contingencies.** In the normal course of business, the Fund may enter into contracts with service providers that contain general indemnification clauses. The Fund's maximum exposure under these arrangements is unknown as this would involve future claims that may be made against the Fund that have not yet been made. However, based on experience, the Fund expects the risk of loss to be remote.

**Other.** Investment transactions are accounted for on a trade date plus one basis for daily net asset value calculations. However, for financial reporting purposes, investment transactions are reported on trade date. Interest income is recorded on the accrual basis. Dividend income is recorded on the ex-dividend date net of foreign withholding taxes. Certain dividends from foreign securities may be recorded subsequent to the ex-dividend date as soon as the Fund is informed of such dividends. Realized gains and losses from investment transactions are recorded on an identified cost basis. All discounts and premiums are accreted/amortized for both tax and financial reporting purposes, with the exception of securities in default of principal.

## B. Derivative Instruments

**Futures Contracts.** A futures contract is an agreement between a buyer or seller and an established futures exchange or its clearinghouse in which the buyer or seller agrees to take or make a delivery of a specific amount of a financial instrument at a specified price on a specific date (settlement date). For the year ended December 31, 2010, the Fund entered into interest rate futures to gain exposure to different parts of the yield curve while managing overall duration. In addition, the Fund seeks to enhance returns by employing a global tactical asset allocation overlay strategy. The Fund enters into futures contracts on fixed-income securities and equities, including on financial indices and security indices, as part of its global tactical asset allocation overlay strategy. For the year ended December 31, 2010, as part of this strategy, the Fund used futures contracts to attempt to take advantage of short-term and medium-term inefficiencies within the global equity and bond markets.

Futures contracts are valued at the most recent settlement price. Upon entering into a futures contract, the Fund is required to deposit with a financial intermediary cash or securities ("initial margin") in an amount equal to a certain percentage of the face value indicated in the futures contract. Subsequent payments ("variation margin") are made or received by the Fund dependent upon the daily fluctuations in the value and are recorded for financial reporting purposes as unrealized gains or losses by the Fund. Gains or losses are realized when the contract expires or is closed. Since all futures contracts are exchange-traded, counterparty risk is minimized as the exchange's clearinghouse acts as the counterparty, and guarantees the futures against default.

Certain risks may arise upon entering into futures contracts, including the risk that an illiquid market will limit the Fund's ability to close out a futures contract prior to the settlement date and that a change in the value of a futures contract may not correlate exactly with the changes in the value of the underlying hedged security, index or currency. Risk of loss may exceed amounts recognized in the Statement of Assets and Liabilities.

A summary of the open futures contracts as of December 31, 2010 is included in a table following the Fund's Investment Portfolio. For the year ended December 31, 2010, the Fund's investment in futures contracts purchased had a total notional value generally indicative of a range from approximately $67,752,000 to $118,748,000. The Fund's investment in futures contracts sold had a total notional value generally indicative of a range from approximately $60,075,000 to $95,480,000.

**Forward Foreign Currency Exchange Contracts.** A forward foreign currency exchange contract ("forward currency contract") is a commitment to purchase or sell a foreign currency at the settlement date at a negotiated rate. For the year ended December 31, 2010, the Fund entered into forward currency contracts in order to hedge its exposure to changes in foreign currency exchange rates on its foreign currency denominated portfolio holdings and to facilitate transactions in foreign currency denominated securities. In addition, the Fund seeks to enhance returns by employing a global tactical asset allocation overlay strategy. For the year ended December 31, 2010, as part of this strategy, the Fund used forward currency contracts to gain exposure to changes in the value of foreign currencies, and to attempt to take advantage of short-term and medium-term inefficiencies within the currency markets.

Forward currency contracts are valued at the prevailing forward exchange rate of the underlying currencies and unrealized gain (loss) is recorded daily. On the settlement date of the forward currency contract, the Fund records a realized gain or loss equal to the difference between the value of the contract at the time it was opened and the value of the contract at the time it was closed. Certain risks may arise upon entering into forward currency contracts from the potential inability of counterparties to meet the terms of their contracts. The maximum counterparty credit risk to the Fund is measured by the unrealized gain on appreciated contracts. Additionally, when utilizing forward currency contracts to hedge, the Fund gives up the opportunity to profit from favorable exchange rate movements during the term of the contract.

A summary of the open forward currency contracts as of December 31, 2010 is included in a table following the Fund's Investment Portfolio. For the year ended December 31, 2010, the Fund's investment in forward currency contracts US dollars purchased had a total contract value generally indicative of a range from approximately $15,249,000 to $33,339,000. The Fund's investment in forward currency contracts US dollars sold had a total contract value generally indicative of a range from approximately $13,605,000 to $33,480,000.

The following tables summarize the value of the Fund's derivative instruments held as of December 31, 2010 and the related location in the accompanying Statement of Assets and Liabilities, presented by primary underlying risk exposure:

| **Asset Derivative** | **Forward Contracts** |
|---|---|
| Foreign Exchange Contracts (a) | $ 760,385 |

*The above derivative is located in the following Statement of Assets and Liabilities account:*

(a) *Unrealized appreciation on open forward foreign currency exchange contracts*

| **Liability Derivatives** | **Forward Contracts** | **Futures Contracts** | **Total** |
|---|---|---|---|
| Equity Contracts (a) | $ — | $ 112,848 | $ 112,848 |
| Interest Rate Contracts (a) | — | (268,526) | (268,526) |
| Foreign Exchange Contracts (b) | (677,737) | — | (677,737) |
| | **$ (677,737)** | **$ (155,678)** | **$ (833,415)** |

*Each of the above derivatives is located in the following Statement of Assets and Liabilities accounts:*

(a) *Net unrealized appreciation (depreciation) on futures. Liability of payable for daily variation margin on open futures contracts reflects unsettled variation margin*

(b) *Unrealized depreciation on open forward foreign currency exchange contracts*

Additionally, the amount of unrealized and realized gains and losses on derivative instruments recognized in Fund earnings during the year ended December 31, 2010 and the related location in the accompanying Statement of Operations is summarized in the following tables by primary underlying risk exposure:

| **Realized Gain (Loss)** | **Forward Contracts** | **Futures Contracts** | **Total** |
|---|---|---|---|
| Equity Contracts (a) | $ — | $ (1,379,315) | $ (1,379,315) |
| Interest Rate Contracts (a) | — | 1,053,743 | 1,053,743 |
| Foreign Exchange Contracts (b) | 171,662 | — | 171,662 |
| | **$ 171,662** | **$ (325,572)** | **$ (153,910)** |

*Each of the above derivatives is located in the following Statement of Operations accounts:*

(a) *Net realized gain (loss) from futures*

(b) *Net realized gain (loss) from foreign currency (Statement of Operations includes both forward currency contracts and foreign currency transactions)*

| **Change in Net Unrealized Appreciation (Depreciation)** | **Forward Contracts** | **Futures Contracts** | **Total** |
|---|---|---|---|
| Equity Contracts (a) | $ — | $ 26,819 | $ 26,819 |
| Interest Rate Contracts (a) | — | 67,655 | 67,655 |
| Foreign Exchange Contracts (b) | (60,489) | — | (60,489) |
| | **$ (60,489)** | **$ 94,474** | **$ 33,985** |

*Each of the above derivatives is located in the following Statement of Operations accounts:*

(a) *Change in net unrealized appreciation (depreciation) on futures*

(b) *Change in net unrealized appreciation (depreciation) on foreign currency (Statement of Operations includes both forward currency contracts and foreign currency transactions)*

## C. Purchases and Sales of Securities

During the year ended December 31, 2010, purchases and sales of investment transactions (excluding short-term investments) were as follows:

| **Fund** | **Purchases ($)** | **Sales ($)** |
|---|---|---|
| DWS Balanced VIP excluding US Treasury Obligations | 501,453,180 | 520,652,361 |
| US Treasury Obligations | 71,576,766 | 77,346,084 |

## D. Related Parties

**Management Agreement.** Under the Investment Management Agreement with Deutsche Investment Management Americas Inc. ("DIMA" or the "Advisor"), an indirect, wholly owned subsidiary of Deutsche Bank AG, the Advisor directs the investments of the Fund in accordance with its investment objectives, policies and restrictions. The Advisor determines the securities, instruments and other contracts relating to investments to be purchased, sold or entered into by the Fund or delegates such responsibility to the Fund's subadvisor.

QS Investors, LLC ("QS Investors") acts as an investment sub-advisor to the Fund. On August 1, 2010, members of the Advisor's Quantitative Strategies Group, including some members of the Fund's portfolio management team, separated from the Advisor and formed QS Investors as a separate investment advisory firm unaffiliated with the Advisor (the "Separation"). As an investment sub-advisor to the Fund, QS Investors renders strategic asset allocation services to the Fund and manages the assets attributable to the Fund's Global Tactical Asset Allocation Overlay Strategy. QS Investors is paid by the Advisor, not the Fund, for the services QS Investors provides to the Fund.

Deutsche Asset Management International GmbH ("DeAMi") serves as a portion of the Fund's large cap value allocation of the portfolio. DeAMi is paid by the Advisor for its services.

Under the Investment Management Agreement with the Advisor, the fee is equivalent to the annual rates shown below of the Fund's average daily net assets, computed and accrued daily and payable monthly:

| Fund | Annual Management Fee Rate |
|---|---|
| DWS Balanced VIP | |
| $0–$250 million | .370% |
| next $750 million | .345% |
| over $1 billion | .310% |

Accordingly, for the year ended December 31, 2010, the total management fee and effective management fee rate were as follows:

| Fund | Total Aggregated ($) | Annual Effective Rate |
|---|---|---|
| DWS Balanced VIP | 1,124,396 | .37% |

**Administration Fee.** Pursuant to an Administrative Services Agreement, DIMA provides most administrative services to the Fund. For all services provided under the Administrative Services Agreement, the Fund pays DIMA an annual fee ("Administration Fee") of 0.10% of the Fund's average daily net assets, computed and accrued daily and payable monthly. For the year ended December 31, 2010, the Administration Fee was as follows:

| Fund | Total Aggregated ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS Balanced VIP | 307,796 | 26,033 |

**Service Provider Fees.** DWS Investments Service Company ("DISC"), an affiliate of the Advisor, is the transfer agent, dividend-paying agent and shareholder service agent for the Fund. Pursuant to a sub-transfer agency agreement between DISC and DST Systems, Inc. ("DST"), DISC has delegated certain transfer agent, dividend-paying agent and shareholder service agent functions to DST. DISC compensates DST out of the shareholder servicing fee it receives from the Fund. For the year ended December 31, 2010, the amounts charged to the Fund by DISC were as follows:

| Fund | Total Aggregated ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS Balanced VIP Class A | 517 | 129 |

**Typesetting and Filing Service Fees.** Under an agreement with DIMA, DIMA is compensated for providing typesetting and certain regulatory filing services to the Fund. For the year ended December 31, 2010, the amount charged to the Fund by DIMA included in the Statement of Operations under "reports to shareholders" was as follows:

| Fund | Amount ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS Balanced VIP | 10,742 | 3,844 |

**Trustees' Fees and Expenses.** The Fund paid each Trustee not affiliated with the Advisor retainer fees plus specified amounts for various committee services and for the Board Chairperson.

**Affiliated Cash Management Vehicles.** The Fund may invest uninvested cash balances in Central Cash Management Fund, which is managed by the Advisor. The Fund indirectly bears their proportionate share of the expenses of the underlying money market funds. Central Cash Management Fund does not pay the Advisor an investment management fee. Central Cash Management Fund seeks a high level of current income consistent with liquidity and the preservation of capital.

### E. Investing in High Yield Securities

The Fund's performance could be hurt if a security declines in credit quality or goes into default, or if an issuer does not make timely payments of interest or principal. Because the issuers of high-yield debt securities or junk bonds (debt securities rated below the fourth-highest category) may be in uncertain financial health, the prices of their debt securities can be more vulnerable to bad economic news, or even the expectation of bad news, than investment-grade debt securities. Because the Fund may invest in securities not paying current interest or in securities already in default, these risks may be more pronounced.

### F. Ownership of the Fund

At December 31, 2010, the beneficial ownership in the Fund was as follows:

**DWS Balanced VIP:** Three Participating Insurance Companies were owners of record of 10% or more of the total outstanding Class A shares of the Fund, each owning 45%, 22% and 15%.

### G. Line of Credit

The Trust and other affiliated fund (the "Participants") share in a $450 million revolving credit facility provided by a syndication of banks. The Fund may borrow for temporary or emergency purposes, including the meeting of redemption requests that otherwise might require the untimely disposition of securities. The Participants are charged an annual commitment fee which is allocated based on net assets, among each of the Participants. Interest is calculated at a rate per annum equal to the sum of the Federal Funds Rate plus 1.25 percent plus if LIBOR exceeds the Federal Funds Rate the amount of such excess. The Fund may borrow up to a maximum of 33 percent of its net assets under the agreement.

# Report of Independent Registered Public Accounting Firm

**To the Board of Trustees and Shareholders of DWS Variable Series II:**

We have audited the accompanying statement of assets and liabilities of DWS Balanced VIP, one of the funds constituting the DWS Variable Series II (the "Trust"), including the investment portfolio, as of December 31, 2010, and the related statement of operations, the statement of changes in net assets and the financial highlights for each of the periods indicated therein. These financial statements and financial highlights are the responsibility of the Trust's management. Our responsibility is to express an opinion on these financial statements and financial highlights based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements and financial highlights are free of material misstatement. We were not engaged to perform an audit of the Trust's internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Trust's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements and financial highlights, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our procedures included confirmation of securities owned as of December 31, 2010, by correspondence with the custodian and brokers or by other appropriate auditing procedures where replies from brokers were not received. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements and financial highlights referred to above present fairly, in all material respects, the financial position of the aforementioned fund of the DWS Variable Series II at December 31, 2010, the results of its operations, the changes in its net assets and the financial highlights for each of the periods indicated therein, in conformity with U.S. generally accepted accounting principles.

Ernst & Young LLP

Boston, Massachusetts
February 14, 2011

## Tax Information

**(Unaudited)**

For corporate shareholders, the following percentage of income dividends paid during the Fund's fiscal year ended December 31, 2010 qualified for the dividends received deduction:

| Fund | Dividends Received % |
|---|---|
| DWS Balanced VIP | 22 |

Please consult a tax advisor if you have questions about federal or state income tax laws, or on how to prepare your tax returns. If you have specific questions about your account, please contact your insurance provider.

## Proxy Voting

The Trust's policies and procedures for voting proxies for portfolio securities and information about how the Trust voted proxies related to its portfolio securities during the 12-month period ended June 30 are available on our Web site — www.dws-investments.com (click on "proxy voting" at the bottom of the page) — or on the SEC's Web site — www.sec.gov. To obtain a written copy of the Trust's policies and procedures without charge, upon request, call us toll free at (800) 728-3337.

# Investment Management Agreement Approval

## DWS Balanced VIP

The Board of Trustees, including the Independent Trustees, approved the renewal of your Fund's investment management agreement (the "Agreement") with Deutsche Investment Management Americas Inc. ("DWS") and sub-advisory agreements (the "Sub-Advisory Agreements" and together with the Agreement, the "Agreements") between DWS and Deutsche Asset Management International GmbH ("DeAMi"), an affiliate of DWS, and DWS and QS Investors, LLC ("QS Investors") in September 2010.

In terms of the process that the Board followed prior to approving the Agreements, shareholders should know that:

- In September 2010, all but one of the Fund's Trustees were independent of DWS and its affiliates.
- The Trustees meet frequently to discuss fund matters. Each year, the Trustees dedicate substantial time to contract review matters. Over the course of several months, the Board's Contract Committee, in coordination with the Board's Fixed Income and Quant Oversight Committee, reviewed comprehensive materials received from DWS, independent third parties and independent counsel. These materials included an analysis of the Fund's performance, fees and expenses, and profitability compiled by the Fund's independent fee consultant. The Board also received extensive information throughout the year regarding performance of the Fund.
- The Independent Trustees regularly meet privately with their independent counsel to discuss contract review and other matters. In addition, the Independent Trustees were also advised by the Fund's independent fee consultant in the course of their review of the Fund's contractual arrangements and considered a comprehensive report prepared by the independent fee consultant in connection with their deliberations (the "IFC Report").
- In connection with reviewing the Agreements, the Board also reviewed the terms of the Fund's distribution agreement, administrative services agreement, transfer agency agreement and other material service agreements.
- Based on its evaluation of the information provided, the Contract Committee presented its findings and recommendations to the Independent Trustees as a group. The Independent Trustees reviewed the Contract Committee's findings and recommendations and presented their recommendations to the full Board.

In connection with the contract review process, the Contract Committee and the Board considered the factors discussed below, among others. The Board also considered that DWS and its predecessors have managed the Fund since its inception, and the Board believes that a long-term relationship with a capable, conscientious advisor is in the best interests of the Fund. The Board considered, generally, that shareholders chose to invest or remain invested in the Fund knowing that DWS managed the Fund, and that the Agreement was approved by the Fund's shareholders. DWS and DeAMi are part of Deutsche Bank, a major global banking institution that is engaged in a wide range of financial services. The Board believes that there are significant advantages to being part of a global asset management business that offers a wide range of investing expertise and resources, including hundreds of portfolio managers and analysts with research capabilities in many countries throughout the world.

While shareholders may focus primarily on fund performance and fees, the Fund's Board considers these and many other factors, including the quality and integrity of DWS's, DeAMi's and QS Investors' personnel and such other issues as back-office operations, fund valuations, and compliance policies and procedures. In addition, in connection with approving the continuation of the Fund's Sub-Advisory Agreement with QS Investors, the Board noted it had engaged in a comprehensive review of the agreement in connection with its initial approval in May 2010.

**Nature, Quality and Extent of Services.** The Board considered the terms of the Agreements, including the scope of advisory services provided under the Agreements. The Board noted that, under the Agreements, DWS, DeAMi and QS Investors provide portfolio management services to the Fund and that, pursuant to a separate administrative services agreement, DWS provides administrative services to the Fund. The Board considered the experience and skills of senior management and investment personnel, the resources made available to such personnel, the ability of DWS to attract and retain high-quality personnel, and the organizational depth and stability of DWS. The Board reviewed the Fund's performance over short-term and long-term periods and compared those returns to various agreed-upon performance measures, including market indices and a peer universe compiled by the independent fee consultant using information supplied by Lipper Inc. ("Lipper"). The Board also noted that it has put into place a process of identifying "Focus Funds" (e.g., funds performing poorly relative to their benchmark or a peer universe compiled by Lipper), and receives more frequent reporting and information from DWS regarding such funds, along with DWS's remedial plans to address underperformance. The

Board believes this process is an effective manner of identifying and addressing underperforming funds. Based on the information provided, the Board noted that for the one-, three- and five-year periods ended December 31, 2009, the Fund's performance (Class A shares) was in the 2nd quartile, 4th quartile and 4th quartile, respectively, of the applicable Lipper universe (the 1st quartile being the best performers and the 4th quartile being the worst performers). The Board also observed that the Fund has outperformed its benchmark in the one-year period and has underperformed its benchmark in the three- and five-year periods ended December 31, 2009.

On the basis of this evaluation and the ongoing review of investment results by the Board, the Board concluded that the nature, quality and extent of services provided by DWS, DeAMi and QS Investors historically have been and continue to be satisfactory.

**Fees and Expenses.** The Board considered the Fund's investment management fee schedule, sub-advisory fee schedules, operating expenses, and total expense ratios, and comparative information provided by Lipper and the independent fee consultant regarding investment management fee rates paid to other investment advisors by similar funds (1st quartile being the most favorable and 4th quartile being the least favorable). With respect to management fees paid to other investment advisors by similar funds, the Board noted that the contractual fee rates paid by the Fund, which include the 0.10% fee paid to DWS under the Fund's administrative services agreement, were lower than the median (1st quartile) of the applicable Lipper peer group (based on Lipper data provided as of December 31, 2009). With respect to the sub-advisory fees paid to DeAMi and QS Investors, the Board noted that the fees are paid by DWS out of its fee and not directly by the Fund. The Board noted that the Fund's Class A shares total (net) operating expenses were expected to be lower than the median (2nd quartile) of the applicable Lipper expense universe (based on Lipper data provided as of December 31, 2009, and analyzing Lipper expense universe Class A expenses less any applicable 12b-1 fees) ("Lipper Universe Expenses"). The Board considered the Fund's management fee rate as compared to fees charged by DWS and certain of its affiliates for comparable mutual funds and considered differences in fund and fee structures between the DWS Funds. The Board also considered how the Fund's total (net) operating expenses compared to the total (net) operating expenses of a more customized peer group selected by Lipper (based on such factors as asset size).

The information considered by the Board as part of its review of management fees included information regarding fees charged by DWS and its affiliates to similar institutional accounts and to similar funds offered primarily to European investors ("DWS Europe funds"), in each case as applicable. The Board observed that advisory fee rates for institutional accounts generally were lower than the management fees charged by similarly managed DWS US mutual funds ("DWS Funds"), but also took note of the differences in services provided to DWS Funds as compared to institutional accounts. In the case of DWS Europe funds, the Board observed that fee rates for DWS Europe funds generally were higher than for similarly managed DWS Funds, but noted that differences in the types of services provided to DWS Funds relative to DWS Europe funds made it difficult to compare such fees.

On the basis of the information provided, the Board concluded that management fees were reasonable and appropriate in light of the nature, quality and extent of services provided by DWS, DeAMi and QS Investors.

**Profitability.** The Board reviewed detailed information regarding revenues received by DWS under the Agreement. The Board considered the estimated costs and pre-tax profits realized by DWS from advising the DWS Funds, as well as estimates of the pre-tax profits attributable to managing the Fund in particular. The Board also received information regarding the estimated enterprise-wide profitability of DWS and its affiliates with respect to all fund services in totality and by fund. The Board reviewed DWS's methodology in allocating its costs to the management of the Fund. Based on the information provided, the Board concluded that the pre-tax profits realized by DWS in connection with the management of the Fund were not unreasonable. The Board also reviewed information regarding the profitability of certain similar investment management firms. The Board noted that while information regarding the profitability of such firms is limited (and in some cases is not necessarily prepared on a comparable basis), DWS and its affiliates' overall profitability with respect to the DWS fund complex (after taking into account distribution and other services provided to the funds by DWS and its affiliates) was lower than the overall profitability levels of many comparable firms for which such data was available. The Board did not consider the profitability of QS Investors with respect to the Fund. The Board noted that DWS pays QS Investors' fee out of its management fee, and its understanding that the Fund's sub-advisory fee schedule was the product of an arm's length negotiation with DWS.

**Economies of Scale.** The Board considered whether there are economies of scale with respect to the management of the Fund and whether the Fund benefits from any economies of scale. The Board noted that the Fund's management fee schedule includes fee breakpoints. The Board concluded that the Fund's fee schedule represents an appropriate sharing between the Fund and DWS of such economies of scale as may exist in the management of the Fund at current asset levels.

**Other Benefits to DWS and QS Investors and Their Affiliates.** The Board also considered the character and amount of other incidental benefits received by DWS and QS Investors and their affiliates, including any fees received by DWS for administrative services provided to the Fund and any fees received by an affiliate of DWS for distribution services. The Board also considered benefits to DWS and QS Investors related to brokerage and soft-dollar allocations, including allocating brokerage to pay for research generated by parties other than the executing broker dealers, which pertain primarily to funds investing in equity securities, along with the incidental public relations benefits to DWS and QS Investors related to DWS Funds advertising and cross-selling opportunities among DWS products and services. The Board concluded that management fees were reasonable in light of these fallout benefits.

**Compliance.** The Board considered the significant attention and resources dedicated by DWS to documenting and enhancing its compliance processes in recent years. The Board noted in particular (i) the experience and seniority of both DWS's chief compliance officer and the Fund's chief compliance officer; (ii) the large number of DWS compliance personnel; and (iii) the substantial commitment of resources by DWS and its affiliates to compliance matters. The Board also considered the attention and resources dedicated by DWS to the oversight of QS Investors' compliance program and compliance with the applicable fund policies and procedures.

Based on all of the information considered and the conclusions reached, the Board unanimously (including the Independent Trustees) determined that the continuation of the Agreements is in the best interests of the Fund. In making this determination, the Board did not give particular weight to any single factor identified above. The Board considered these factors over the course of numerous meetings, certain of which were in executive session with only the Independent Trustees and their counsel present. It is possible that individual Trustees may have weighed these factors differently in reaching their individual decisions to approve the continuation of the Agreements.

# Summary of Management Fee Evaluation by Independent Fee Consultant

October 3, 2010

Pursuant to an Order entered into by Deutsche Investment Management Americas and affiliates (collectively, "DeAM") with the Attorney General of New York, I, Thomas H. Mack, have been appointed the Independent Fee Consultant for the DWS Funds (formerly the DWS Scudder Funds). My duties include preparing an annual written evaluation of the management fees DeAM charges the Funds, considering among other factors the management fees charged by other mutual fund companies for like services, management fees DeAM charges other clients for like services, DeAM's costs of supplying services under the management agreements and related profit margins, possible economies of scale if a Fund grows larger, and the nature and quality of DeAM's services, including fund performance. This report summarizes my evaluation for 2010, including my qualifications, the evaluation process for each of the DWS Funds, consideration of certain complex-level factors, and my conclusions. I served in substantially the same capacity in 2007, 2008, and 2009.

## Qualifications

For more than 35 years I have served in various professional capacities within the investment management business. I have held investment analysis and advisory positions, including securities analyst, portfolio strategist and director of investment policy with a large investment firm. I have also performed business management functions, including business development, financial management and marketing research and analysis.

Since 1991, I have been an independent consultant within the asset management industry. I have provided services to over 125 client organizations, including investment managers, mutual fund boards, product distributors and related organizations. Over the past ten years I have completed a number of assignments for mutual fund boards, specifically including assisting boards with management contract renewal.

I hold a Master of Business Administration degree, with highest honors, from Harvard University and Master of Science and Bachelor of Science (highest honors) degrees from the University of California at Berkeley. I am an independent director and audit committee financial expert for two closed-end mutual funds and have served in various leadership and financial oversight capacities with non-profit organizations.

## Evaluation of Fees for each DWS Fund

My work focused primarily on evaluating, fund-by-fund, the fees charged to each of the 118 publicly offered Fund portfolios in the DWS Fund family. For each Fund, I considered each of the key factors mentioned above, as well as any other relevant information. In doing so I worked closely with the Funds' Independent Directors in their annual contract renewal process, as well as in their approval of contracts for several new funds (documented separately).

In evaluating each Fund's fees, I reviewed comprehensive materials provided by or on behalf of DeAM, including expense information prepared by Lipper Analytical, comparative performance information, profitability data, manager histories, and other materials. I also accessed certain additional information from the Lipper and Morningstar databases and drew on my industry knowledge and experience.

To facilitate evaluating this considerable body of information, I prepared for each Fund a document summarizing the key data elements in each area as well as additional analytics discussed below. This made it possible to consider each key data element in the context of the others.

In the course of contract renewal, DeAM agreed to implement a number of fee and expense adjustments requested by the Independent Directors which will favorably impact future fees and expenses, and my evaluation includes the effects of these changes.

### Fees and Expenses Compared with Other Funds

The competitive fee and expense evaluation for each fund focused on two primary comparisons:

The Fund's contractual management fee (the advisory fee plus the administration fee where applicable) compared with those of a group of typically 12–15 funds in the same Lipper investment category (e.g. Large Capitalization Growth) having similar distribution arrangements and being of similar size.

The Fund's total expenses compared with a broader universe of funds from the same Lipper investment category and having similar distribution arrangements.

These two comparisons provide a view of not only the level of the fee compared with funds of similar scale but also the total expense the Fund bears for all the services it receives, in comparison with the investment choices available in the Fund's investment category and distribution channel. The principal figure-of-merit used in these comparisons was the subject Fund's percentile ranking against peers.

### DeAM's Fees for Similar Services to Others

DeAM provided management fee schedules for all of its US domiciled fund and non-fund investment management accounts in any of the investment categories where there is a DWS Fund. These similar products included the other DWS Funds, non-fund pooled accounts, institutional accounts and sub-advisory accounts. Using this information, I calculated for each Fund the fee that would be charged to each similar product, at the subject Fund's asset level.

Evaluating information regarding non-fund products is difficult because there are varying levels of services required for different types of accounts, with mutual funds generally requiring considerably more regulatory and administrative types of service as well as having more frequent cash flows than other types of accounts. Also, while mutual fund fees for similar fund products can be expected to be similar, there will be some differences due to different pricing conditions in different distribution channels (e.g. retail funds versus those used in variable insurance products), differences in underlying investment processes and other factors.

**Costs and Profit Margins**

DeAM provided a detailed profitability analysis for each Fund. After making some adjustments so that the presentation would be more comparable to the available industry figures, I reviewed profit margins from investment management alone, from investment management plus other fund services (excluding distribution) provided to the Funds by DeAM (principally shareholder services), and DeAM profits from all sources, including distribution. A later section comments on overall profitability.

**Economies of Scale**

Economies of scale — an expected decline in management cost per dollar of fund assets as fund assets grow — are very rarely quantified and documented because of inherent difficulties in collecting and analyzing relevant data. However, in virtually every investment category that I reviewed, larger funds tend to have lower fees and lower total expenses than smaller funds. To see how each DWS Fund compares with this industry observation, I reviewed:

- The trend in Fund assets over the last five years and the accompanying trend in total expenses. This shows if the Fund has grown and, if so, whether total expense (management fees as well as other expenses) have declined as a percent of assets.
- Whether the Fund has break-points in its management fee schedule, the extent of the fee reduction built into the schedule and the asset levels where the breaks take effect, and in the case of a sub-advised Fund how the Fund's break-points compare with those of the sub-advisory fee schedule.
- How the Fund's contractual fee schedule compares with trends in the industry data. To accomplish this, I constructed a chart showing how actual latest-fiscal-year contractual fees of the Fund and of other similar funds relate to average fund assets, with the subject Fund's contractual fee schedule superimposed.

**Quality of Service — Performance**

The quality-of-service evaluation focused on investment performance, which is the principal result of the investment management service. Each Fund's performance was reviewed over the past 1, 3, 5 and 10 years, as applicable, and compared with that of other funds in the same investment category and with a suitable market index.

In addition, I calculated and reviewed risk-adjusted returns relative to an index of similar mutual funds' returns and a suitable market index. The risk-adjusted returns analysis provides a way of determining the extent to which the Fund's return comparisons are mainly the product of investment value-added (or lack thereof) or alternatively taking considerably more or less risk than is typical in its investment category.

I also received and considered the history of portfolio manager changes for each Fund, as this provided an important context for evaluating the performance results.

## Complex-Level Considerations

While this evaluation was conducted mainly at the individual fund level, there are some issues relating to the reasonableness of fees that can alternatively be considered across the whole fund complex:

- I reviewed DeAM's profitability analysis for all DWS Funds, with a view toward determining if the allocation procedures used were reasonable and how profit levels compared with public data for other investment managers.
- I considered whether DeAM and affiliates receive any significant ancillary or "fall-out" benefits that should be considered in interpreting the direct profitability results. These would be situations where serving as the investment manager of the Funds is beneficial to another part of the Deutsche Bank organization.
- I considered how aggregated DWS Fund expenses had varied over the years, by asset class and in the context of trends in asset levels.
- I reviewed the structure of the DeAM organization, trends in staffing levels, and information on compensation of investment management and other professionals compared with industry data.

## Findings

Based on the process and analysis discussed above, which included reviewing a wide range of information from management and external data sources and considering among other factors the fees DeAM charges other clients, the fees charged by other fund managers, DeAM's costs and profits associated with managing the Funds, economies of scale, possible fall-out benefits, and the nature and quality of services provided, in my opinion the management fees charged the DWS Funds are reasonable.

Thomas H. Mack

Thomas H. Mack

# Board Members and Officers

The following table presents certain information regarding the Board Members and Officers of the Trust as of December 31, 2010. Each Board Member's year of birth is set forth in parentheses after his or her name. Unless otherwise noted, (i) each Board Member has engaged in the principal occupation(s) noted in the table for at least the most recent five years, although not necessarily in the same capacity; and (ii) the address of each Independent Board Member is c/o Paul K. Freeman, Independent Chairman, DWS Funds, PO Box 101833, Denver, CO 80250-1833. Except as otherwise noted below, the term of office for each Board Member is until the election and qualification of a successor, or until such Board Member sooner dies, resigns, is removed or as otherwise provided in the governing documents of the fund. Because the fund does not hold an annual meeting of shareholders, each Board Member will hold office for an indeterminate period. The Board Members may also serve in similar capacities with other funds in the fund complex. The Length of Time Served represents the year in which the Board Member joined the board of one or more DWS funds now overseen by the Board.

**Independent Board Members**

| Name, Year of Birth, Position with the Fund and Length of Time Served[1] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Paul K. Freeman (1950)<br>Chairperson since 2009<br>Board Member since 1993 | Consultant, World Bank/Inter-American Development Bank; Executive and Governing Council of the Independent Directors Council (education committees); formerly, Project Leader, International Institute for Applied Systems Analysis (1998–2001); Chief Executive Officer, The Eric Group, Inc. (environmental insurance) (1986–1998) | 122 |
| John W. Ballantine (1946)<br>Board Member since 1999 | Retired; formerly, Executive Vice President and Chief Risk Management Officer, First Chicago NBD Corporation/The First National Bank of Chicago (1996–1998); Executive Vice President and Head of International Banking (1995–1996). Directorships: Healthways, Inc. (provider of disease and care management services); Portland General Electric (utility company); Stockwell Capital Investments PLC (private equity). Former Directorships: First Oak Brook Bancshares, Inc. and Oak Brook Bank; Prisma Energy International | 122 |
| Henry P. Becton, Jr. (1943)<br>Board Member since 1990 | Vice Chair and former President, WGBH Educational Foundation. Directorships: Association of Public Television Stations; Lead Director, Becton Dickinson and Company[3] (medical technology company); Lead Director, Belo Corporation[3] (media company); Public Radio International; Public Radio Exchange (PRX); The PBS Foundation. Former Directorships: Boston Museum of Science; American Public Television; Concord Academy; New England Aquarium; Mass. Corporation for Educational Telecommunications; Committee for Economic Development; Public Broadcasting Service | 122 |
| Dawn-Marie Driscoll (1946)<br>Board Member since 1987 | President, Driscoll Associates (consulting firm); Executive Fellow, Center for Business Ethics, Bentley University; formerly, Partner, Palmer & Dodge (1988–1990); Vice President of Corporate Affairs and General Counsel, Filene's (1978–1988). Directorships: Trustee of 22 open-end mutual funds managed by Sun Capital Advisers, Inc. (since 2007); Director of ICI Mutual Insurance Company (since 2007); Advisory Board, Center for Business Ethics, Bentley University; Trustee, Southwest Florida Community Foundation (charitable organization). Former Directorships: Investment Company Institute (audit, executive, nominating committees) and Independent Directors Council (governance, executive committees) | 122 |
| Keith R. Fox (1954)<br>Board Member since 1996 | Managing General Partner, Exeter Capital Partners (a series of private investment funds). Directorships: Progressive International Corporation (kitchen goods importer and distributor); BoxTop Media Inc. (advertising); The Kennel Shop (retailer); former Chairman, National Association of Small Business Investment Companies | 122 |
| Kenneth C. Froewiss (1945)<br>Board Member since 2001 | Adjunct Professor of Finance, NYU Stern School of Business (September 2009–present; Clinical Professor from 1997–September 2009); Member, Finance Committee, Association for Asian Studies (2002–present); Director, Mitsui Sumitomo Insurance Group (US) (2004–present); prior thereto, Managing Director, J.P. Morgan (investment banking firm) (until 1996) | 122 |
| Richard J. Herring (1946)<br>Board Member since 1990 | Jacob Safra Professor of International Banking and Professor, Finance Department, The Wharton School, University of Pennsylvania (since July 1972); Co-Director, Wharton Financial Institutions Center (since July 2000); Co-Chair, U.S. Shadow Financial Regulatory Committee; Executive Director, Financial Economists Roundtable; Director, Japan Equity Fund, Inc. (since September 2007), Thai Capital Fund, Inc. (since September 2007), Singapore Fund, Inc. (since September 2007); Independent Director of Barclays Bank Delaware (since September 2010). Formerly, Vice Dean and Director, Wharton Undergraduate Division (July 1995–June 2000); Director, Lauder Institute of International Management Studies (July 2000–June 2006) | 122 |
| William McClayton (1944)<br>Board Member since 2004+ | Private equity investor (since October 2009); previously, Managing Director, Diamond Management & Technology Consultants, Inc. (global consulting firm) (2001–2009); Directorship: Board of Managers, YMCA of Metropolitan Chicago; formerly: Senior Partner, Arthur Andersen LLP (accounting) (1966–2001); Trustee, Ravinia Festival | 122 |

| Name, Year of Birth, Position with the Fund and Length of Time Served[1] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Rebecca W. Rimel (1951)<br>Board Member since 1995 | President and Chief Executive Officer, The Pew Charitable Trusts (charitable organization) (1994 to present); Trustee, Thomas Jefferson Foundation (charitable organization) (1994 to present); Trustee, Executive Committee, Philadelphia Chamber of Commerce (2001–2007); Director, CardioNet, Inc.[2] (2009–present) (health care). Formerly, Executive Vice President, The Glenmede Trust Company (investment trust and wealth management) (1983–2004); Board Member, Investor Education (charitable organization) (2004–2005); Director, Viasys Health Care[2] (January 2007–June 2007); Trustee, Pro Publica (charitable organization) (2007–2010) | 122 |
| William N. Searcy, Jr. (1946)<br>Board Member since 1993 | Private investor since October 2003; Trustee of 22 open-end mutual funds managed by Sun Capital Advisers, Inc. (since October 1998). Formerly, Pension & Savings Trust Officer, Sprint Corporation[2] (telecommunications) (November 1989–September 2003) | 122 |
| Jean Gleason Stromberg (1943)<br>Board Member since 1997 | Retired. Formerly, Consultant (1997–2001); Director, Financial Markets US Government Accountability Office (1996–1997); Partner, Fulbright & Jaworski, L.L.P. (law firm) (1978–1996). Directorships: The William and Flora Hewlett Foundation. Former Directorships: Service Source, Inc., Mutual Fund Directors Forum (2002–2004), American Bar Retirement Association (funding vehicle for retirement plans) (1987–1990 and 1994–1996) | 122 |
| Robert H. Wadsworth (1940)<br>Board Member since 1999 | President, Robert H. Wadsworth & Associates, Inc. (consulting firm) (1983 to present); Director, The Phoenix Boys Choir Association | 125 |

## Interested Board Member and Officer[4]

| Name, Year of Birth, Position with the Trust/ Corporation and Length of Time Served[1,5] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Ingo Gefeke[7] (1967)<br>Board Member since 2010<br>Executive Vice President since 2010 | Managing Director[3], Deutsche Asset Management; Global Head of Distribution and Product Management, DWS Global Head of Trading and Securities Lending. Member of the Board of Directors of DWS Investment GmbH Frankfurt (since July 2009) and DWS Holding & Service GmbH Frankfurt (since January 2010); formerly, Global Chief Administrative Officer, Deutsche Asset Management (2004–2009); Global Chief Operating Officer, Global Transaction Banking, Deutsche Bank AG, New York (2001–2004); Chief Operating Officer, Global Banking Division Americas, Deutsche Bank AG, New York (1999–2001); Central Management, Global Banking Services, Deutsche Bank AG, Frankfurt (1998–1999); Relationship Management, Deutsche Bank AG, Tokyo, Japan (1997–1998) | 55 |

## Officers[4]

| Name, Year of Birth, Position with the Fund and Length of Time Served[5] | Principal Occupation(s) During Past 5 Years and Other Directorships Held |
|---|---|
| Michael G. Clark[6] (1965)<br>President, 2006–present | Managing Director[3], Deutsche Asset Management (2006–present); President of DWS family of funds; Director, ICI Mutual Insurance Company (since October 2007); formerly, Director of Fund Board Relations (2004–2006) and Director of Product Development (2000–2004), Merrill Lynch Investment Managers; Senior Vice President Operations, Merrill Lynch Asset Management (1999–2000) |
| John Millette[8] (1962)<br>Vice President and Secretary, 1999–present | Director[3], Deutsche Asset Management |
| Paul H. Schubert[6] (1963)<br>Chief Financial Officer, 2004–present<br>Treasurer, 2005–present | Managing Director[3], Deutsche Asset Management (since July 2004); formerly, Executive Director, Head of Mutual Fund Services and Treasurer for UBS Family of Funds (1998–2004); Vice President and Director of Mutual Fund Finance at UBS Global Asset Management (1994–1998) |
| Caroline Pearson[8] (1962)<br>Chief Legal Officer, April 2010–present | Managing Director[3], Deutsche Asset Management; formerly, Assistant Secretary for DWS family of funds (1997–2010) |
| Rita Rubin[9] (1970)<br>Assistant Secretary, 2009–present | Vice President and Counsel, Deutsche Asset Management (since October 2007); formerly, Vice President, Morgan Stanley Investment Management (2004–2007) |
| Paul Antosca[8] (1957)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management (since 2006); Vice President, The Manufacturers Life Insurance Company (U.S.A.) (1990–2006) |
| Jack Clark[8] (1967)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management (since 2007); formerly, Vice President, State Street Corporation (2002–2007) |

| Name, Year of Birth, Position with the Fund and Length of Time Served[5] | Principal Occupation(s) During Past 5 Years and Other Directorships Held |
|---|---|
| Diane Kenneally[8] (1966)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management |
| John Caruso[9] (1965)<br>Anti-Money Laundering Compliance Officer, 2010–present | Managing Director[3], Deutsche Asset Management |
| Robert Kloby[9] (1962)<br>Chief Compliance Officer, 2006–present | Managing Director[3], Deutsche Asset Management |

1 *The length of time served represents the year in which the Board Member joined the board of one or more DWS funds currently overseen by the Board.*

2 *A publicly held company with securities registered pursuant to Section 12 of the Securities Exchange Act of 1934.*

3 *Executive title, not a board directorship.*

4 *As a result of their respective positions held with the Advisor, these individuals are considered "interested persons" of the Advisor within the meaning of the 1940 Act. Interested persons receive no compensation from the fund.*

5 *The length of time served represents the year in which the officer was first elected in such capacity for one or more DWS funds.*

6 *Address: 100 Plaza One, Jersey City, NJ 07311.*

7 *Effective January 11, 2011, Mr. Gefeke, an interested Board Member and Executive Vice President, resigned from the fund's Board and as an officer.*

*The mailing address of Mr. Gefeke is 345 Park Avenue, New York, New York 10154. Mr. Gefeke was an interested Board Member of certain DWS funds by virtue of his positions with Deutsche Asset Management. As an interested person, Mr. Gefeke received no compensation from the fund.*

8 *Address: One Beacon Street, Boston, MA 02108.*

9 *Address: 60 Wall Street, New York, New York 10005.*

*The fund's Statement of Additional Information ("SAI") includes additional information about the Board Members. The SAI is available, without charge, upon request. If you would like to request a copy of the SAI, you may do so by calling the following toll-free number: (800) 728-3337.*

DWS Investments is part of Deutsche Bank's Asset Management division and, within the US, represents the retail asset management activities of Deutsche Bank AG, Deutsche Bank Trust Company Americas, Deutsche Investment Management Americas Inc. and DWS Trust Company.

The views expressed in this report reflect those of the portfolio managers only through the end of the period of the report as stated on the cover. The managers' views are subject to change at any time based on market and other conditions and should not be construed as a recommendation.

This information must be preceded or accompanied by a current prospectus.

Portfolio changes should not be considered recommendations for action by individual investors.

DWS Investments Distributors, Inc.
222 South Riverside Plaza
Chicago, IL 60606
(800) 621-1148

VS2BAL-2 (2/11)

DWS INVESTMENTS
Deutsche Bank Group

DECEMBER 31, 2010

# ANNUAL REPORT

## DWS VARIABLE SERIES II

## DWS Blue Chip VIP

**This report must be preceded or accompanied by a prospectus. To obtain an additional prospectus or summary prospectus, if available, call (800) 728-3337 or your financial representative. We advise you to consider the Fund's objectives, risks, charges and expenses carefully before investing. The summary prospectus and prospectus contain this and other important information about the Fund. Please read the prospectus carefully before you invest.**

*Investments in variable insurance portfolios (VIPs) involve risk. Stocks may decline in value. Bond investments are subject to interest-rate and credit risks. When interest rates rise, bond prices generally fall. Credit risk refers to the ability of an issuer to make timely payments of principal and interest. Investing in derivatives entails special risks relating to liquidity, leverage and credit that may reduce returns and/or increased volatility. Investing in foreign securities, particularly those of emerging markets, presents certain risks, such as currency fluctuations, political and economic changes, and market risks. There are additional risks associated with investing in commodities, high-yield bonds, aggressive growth stocks, non-diversified/ concentrated funds and small- and mid-cap stocks which are more fully explained in the prospectuses. Please read the prospectus for more information.*

*DWS Investments is part of Deutsche Bank's Asset Management division and, within the US, represents the retail asset management activities of Deutsche Bank AG, Deutsche Bank Trust Company Americas, Deutsche Investment Management Americas Inc. and DWS Trust Company.*



DWS INVESTMENTS
Deutsche Bank Group

# Performance Summary

**December 31, 2010**

## DWS Blue Chip VIP

**All performance shown is historical, assumes reinvestment of all dividend and capital gain distributions and does not guarantee future results. Investment return and principal value fluctuate with changing market conditions so that, when redeemed, shares may be worth more or less than their original cost. Current performance may be lower or higher than the performance data quoted. Please contact your participating insurance company for the Fund's most recent month-end performance. Performance doesn't reflect charges and fees ("contract charges") associated with the separate account that invests in the Fund or any variable life insurance policy or variable annuity contract for which the Fund is an investment option. These charges and fees will reduce returns. While all share classes have the same underlying portfolio, their performance will differ.**

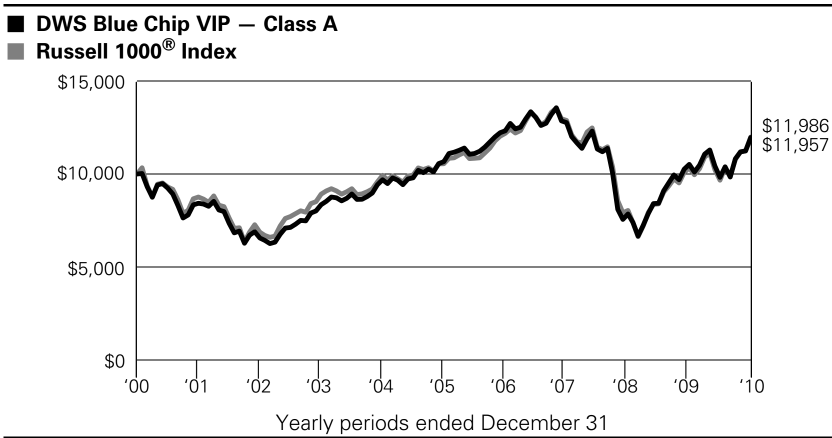
**The gross expense ratios of the Fund, as stated in the fee table of the prospectus dated May 1, 2010 are 0.75% and 1.02% for Class A and Class B shares, respectively, and may differ from the expense ratios disclosed in the Financial Highlights tables in this report.**

### Risk Considerations

Any fund that focuses in a particular segment of the market will generally be more volatile than a fund that invests more broadly. Stocks may decline in value. See the prospectus for details.

Fund returns shown during the 3-year, 5-year and 10-year/Life of Class periods reflect a fee waiver and/or expense reimbursement. Without this waiver/reimbursement, returns would have been lower.

### Growth of an Assumed $10,000 Investment in DWS Blue Chip VIP




*The Russell 1000® Index is an unmanaged index that measures the performance of the 1,000 largest companies in the Russell 3000® Index, which measures the performance of the 3,000 largest US companies based on total market capitalization. The Russell 1000 Index represents approximately 92% of the total market capitalization of the Russell 3000 Index.*

*Index returns assume reinvestment of dividends and, unlike fund returns, do not reflect any fees or expenses. It is not possible to invest directly into an index.*

### Comparative Results

| DWS Blue Chip VIP | | 1-Year | 3-Year | 5-Year | 10-Year |
|---|---|---|---|---|---|
| **Class A** | Growth of $10,000 | $11,377 | $9,375 | $11,221 | $11,957 |
| | Average annual total return | 13.77% | –2.13% | 2.33% | 1.80% |
| Russell 1000 Index | Growth of $10,000 | $11,610 | $9,305 | $11,364 | $11,986 |
| | Average annual total return | 16.10% | –2.37% | 2.59% | 1.83% |

| DWS Blue Chip VIP | | 1-Year | 3-Year | 5-Year | Life of Class* |
|---|---|---|---|---|---|
| **Class B** | Growth of $10,000 | $11,355 | $9,323 | $11,077 | $16,186 |
| | Average annual total return | 13.55% | –2.31% | 2.07% | 5.83% |
| Russell 1000 Index | Growth of $10,000 | $11,610 | $9,305 | $11,364 | $15,703 |
| | Average annual total return | 16.10% | –2.37% | 2.59% | 5.45% |

*The growth of $10,000 is cumulative.*

* *The Fund commenced offering Class B shares on July 1, 2002. Index returns began on June 30, 2002.*

# Information About Your Fund's Expenses

## DWS Blue Chip VIP

As an investor of the Fund, you incur two types of costs: ongoing expenses and transaction costs. Ongoing expenses include management fees, distribution and service (12b-1) fees and other Fund expenses. Examples of transaction costs include contract charges, redemption fees and account maintenance fees, which are not shown in this section. The following tables are intended to help you understand your ongoing expenses (in dollars) of investing in the Fund and to help you compare these expenses with the ongoing expenses of investing in other mutual funds. The example in the table is based on an investment of $1,000 invested at the beginning of the six-month period and held for the entire period (July 1, 2010 to December 31, 2010).

The tables illustrate your Fund's expenses in two ways:

- **Actual Fund Return.** This helps you estimate the actual dollar amount of ongoing expenses (but not transaction costs) paid on a $1,000 investment in the Fund using the Fund's actual return during the period. To estimate the expenses you paid over the period, simply divide your account value by $1,000 (for example, an $8,600 account value divided by $1,000 = 8.6), then multiply the result by the number in the "Expenses Paid per $1,000" line under the share class you hold.
- **Hypothetical 5% Fund Return.** This helps you to compare your Fund's ongoing expenses (but not transaction costs) with those of other mutual funds using the Fund's actual expense ratio and a hypothetical rate of return of 5% per year before expenses. Examples using a 5% hypothetical Fund return may be found in the shareholder reports of other mutual funds. The hypothetical account values and expenses may not be used to estimate the actual ending account balance or expenses you paid for the period.

Please note that the expenses shown in these tables are meant to highlight your ongoing expenses only and do not reflect any transaction costs. The "Expenses Paid per $1,000" line of the tables is useful in comparing ongoing expenses only and will not help you determine the relative total expense of owning different funds. If these transaction costs had been included, your costs would have been higher.

**Expenses and Value of a $1,000 Investment** for the six months ended December 31, 2010

| Actual Fund Return | Class A | Class B |
|---|---|---|
| Beginning Account Value 7/1/10 | $1,000.00 | $1,000.00 |
| Ending Account Value 12/31/10 | $1,218.50 | $1,216.40 |
| Expenses Paid per $1,000* | $ 4.14 | $ 5.59 |
| **Hypothetical 5% Fund Return** | **Class A** | **Class B** |
| Beginning Account Value 7/1/10 | $1,000.00 | $1,000.00 |
| Ending Account Value 12/31/10 | $1,021.48 | $1,020.16 |
| Expenses Paid per $1,000* | $ 3.77 | $ 5.09 |

* *Expenses are equal to the Fund's annualized expense ratio for each share class, multiplied by the average account value over the period, multiplied by the number of days in the most recent six-month period, then divided by 365.*

| Annualized Expense Ratios | Class A | Class B |
|---|---|---|
| DWS Variable Series II — DWS Blue Chip VIP | .74% | 1.00% |

For more information, please refer to the Fund's prospectus.

These tables do not reflect charges and fees ("contract charges") associated with the separate account that invests in the Fund or any variable life insurance policy or variable annuity contract for which the Fund is an investment option.

# Management Summary

**December 31, 2010**

## DWS Blue Chip VIP

US equities performed very well during 2010, as investors were cheered by gradually improving economic data and surprisingly strong corporate profits. The Russell 1000® Index — the Fund's benchmark — gained 16.10% on the year, building on its 28.43% rally of 2009. The Class A shares of the Fund, while also producing a positive return of 13.77%, fell short of the benchmark.

Our approach to managing the Fund is disciplined and dynamic — disciplined in the sense that we use a quantitative approach that measures numerous factors related to growth, value, quality and market sentiment, and dynamic in that we can choose to give different weightings to these factors based on a rigorous analysis of the past that seeks to determine which periods are most like now. The past year was a highly rotational year for style performance, with leadership changing several times — from growth to market sentiment, then to quality and then back to market sentiment. The Fund's growth and market sentiment factors performed relatively well over the full year, whereas the value and quality factors were mostly weak. We started the year with healthy weightings to market sentiment and growth, which added value early in the year. However, our relatively large weighting toward value throughout the year more than offset this and proved to be the biggest drag on relative performance.

From a sector perspective, our stock selection process was least effective in the technology segment, where our overweight positions in Microsoft Corp., Computer Sciences Corp. and the disk-drive maker Western Digital Corp.* weighed on performance.[1] The industrials sector was an additional area of underperformance, due in part to our overweights in Raytheon Co. and the truck manufacturer Oshkosh Corp. Our stock picks also fell short in the utilities and consumer staples sectors. On the plus side, we outperformed the benchmark by a wide margin in the energy sector. We generated strong performance by moving to overweight positions in stocks that plummeted sharply in the wake of the Gulf oil spill and then staged rebounds from undervalued levels, such as Transocean Ltd., Anadarko Petroleum Corp.* and National Oilwell Varco, Inc. We also performed very well within financials, thanks in part to our overweight positions in Berkshire Hathaway, Inc. and ACE Ltd.

Robert Wang
Russell Shtern, CFA
*Portfolio Managers, QS Investors, LLC*
*Subadvisor to the Fund*

*The Russell 1000 Index is an unmanaged index that measures the performance of the 1,000 largest companies in the Russell 3000® Index which measures the performance of the 3,000 largest US companies based on total market capitalization. The Russell 1000 Index represents approximately 92% of the total market capitalization of the Russell 3000 Index.*

*Index returns assume reinvestment of dividends and, unlike fund returns, do not reflect any fees or expenses. It is not possible to invest directly into an index.*

1 *"Overweight" means the Fund holds a higher weighting in a given sector or security than the benchmark. "Underweight" means the Fund holds a lower weighting.*

* *Not held in the Fund as of December 31, 2010.*

*Portfolio management market commentary is as of December 31, 2010, and may not come to pass. This information is subject to change at any time based on market and other conditions. Past performance does not guarantee future results. Current and future portfolio holdings are subject to risk.*

# Portfolio Summary

## DWS Blue Chip VIP

| **Asset Allocation** (As a % of Investment Portfolio excluding Securities Lending Collateral) | **12/31/10** | **12/31/09** |
|---|---|---|
| Common Stocks | 99% | 99% |
| Cash Equivalents* | 1% | 1% |
| | 100% | 100% |

| **Sector Diversification** (As a % of Common Stocks) | **12/31/10** | **12/31/09** |
|---|---|---|
| Information Technology | 19% | 19% |
| Financials | 17% | 11% |
| Health Care | 14% | 14% |
| Industrials | 12% | 13% |
| Energy | 11% | 9% |
| Consumer Discretionary | 11% | 12% |
| Consumer Staples | 7% | 11% |
| Materials | 5% | 5% |
| Telecommunication Services | 2% | 4% |
| Utilities | 2% | 2% |
| | 100% | 100% |

* *In order to keep cash on hand to meet shareholder redemptions or other needs while maintaining exposure to the market, the Fund invests in futures contracts.*

*Asset allocation and sector diversification are subject to change.*

*For more complete details about the Fund's investment portfolio, see page 6.*

Following the Fund's fiscal first and third quarter-end, a complete portfolio holdings listing is filed with the SEC on Form N-Q. The form will be available on the SEC's Web site at www.sec.gov, and it also may be reviewed and copied at the SEC's Public Reference Room in Washington, D.C. Information on the operation of the SEC's Public Reference Room may be obtained by calling (800) SEC-0330. The Fund's portfolio holdings are also posted on www.dws-investments.com from time to time. Please see the Fund's current prospectus for more information.

# Investment Portfolio

December 31, 2010

## DWS Blue Chip VIP

| | Shares | Value ($) |
|---|---|---|
| **Common Stocks 98.8%** | | |
| **Consumer Discretionary 10.4%** | | |
| **Auto Components 0.1%** | | |
| Goodyear Tire & Rubber Co.* | 6,700 | **79,395** |
| **Diversified Consumer Services 0.5%** | | |
| Apollo Group, Inc. "A"* | 3,400 | 134,266 |
| Career Education Corp.* (a) | 9,800 | 203,154 |
| Coinstar, Inc.* | 1,700 | 95,948 |
| DeVry, Inc. | 1,600 | 76,768 |
| Sotheby's | 1,700 | 76,500 |
| | | **586,636** |
| **Hotels Restaurants & Leisure 1.0%** | | |
| Chipotle Mexican Grill, Inc.* (a) | 600 | 127,596 |
| McDonald's Corp. | 3,600 | 276,336 |
| Panera Bread Co. "A"* | 1,500 | 151,815 |
| Starbucks Corp. | 16,200 | 520,506 |
| | | **1,076,253** |
| **Household Durables 0.2%** | | |
| Garmin Ltd. (a) | 6,700 | **207,633** |
| **Internet & Catalog Retail 1.0%** | | |
| Liberty Media Corp. — Interactive "A"* | 35,100 | 553,527 |
| Priceline.com, Inc.* | 1,400 | 559,370 |
| | | **1,112,897** |
| **Media 2.8%** | | |
| CBS Corp. "B" | 9,100 | 173,355 |
| Comcast Corp. "A" (a) | 54,500 | 1,197,365 |
| Liberty Media-Starz "A"* | 1,900 | 126,312 |
| McGraw-Hill Companies, Inc. | 4,700 | 171,127 |
| News Corp. "A" | 9,800 | 142,688 |
| Time Warner, Inc. | 21,233 | 683,066 |
| Walt Disney Co. (a) | 13,900 | 521,389 |
| | | **3,015,302** |
| **Multiline Retail 0.8%** | | |
| Dillard's, Inc. "A" (a) | 17,500 | 663,950 |
| Kohl's Corp.* | 4,600 | 249,964 |
| | | **913,914** |
| **Specialty Retail 2.6%** | | |
| Advance Auto Parts, Inc. | 7,600 | 502,740 |
| American Eagle Outfitters, Inc. | 10,200 | 149,226 |
| AnnTaylor Stores Corp.* | 2,900 | 79,431 |
| Barnes & Noble, Inc. (a) | 8,400 | 118,860 |
| Chico's FAS, Inc. | 6,200 | 74,586 |
| Guess?, Inc. | 2,400 | 113,568 |
| Rent-A-Center, Inc. | 3,900 | 125,892 |
| Ross Stores, Inc. | 2,700 | 170,775 |
| The Gap, Inc. | 39,300 | 870,102 |
| TJX Companies, Inc. | 14,100 | 625,899 |
| | | **2,831,079** |
| **Textiles, Apparel & Luxury Goods 1.4%** | | |
| Coach, Inc. | 7,200 | 398,232 |
| Deckers Outdoor Corp.* | 2,200 | 175,428 |
| NIKE, Inc. "B" (a) | 4,600 | 392,932 |
| VF Corp. | 6,000 | 517,080 |
| | | **1,483,672** |

| | Shares | Value ($) |
|---|---|---|
| **Consumer Staples 6.9%** | | |
| **Beverages 0.2%** | | |
| Molson Coors Brewing Co. "B" | 4,300 | **215,817** |
| **Food & Staples Retailing 1.4%** | | |
| Wal-Mart Stores, Inc. | 26,700 | 1,439,931 |
| Whole Foods Market, Inc.* (a) | 900 | 45,531 |
| | | **1,485,462** |
| **Food Products 2.7%** | | |
| Archer-Daniels-Midland Co. | 15,600 | 469,248 |
| Corn Products International, Inc. | 4,800 | 220,800 |
| Fresh Del Monte Produce, Inc. | 6,200 | 154,690 |
| H.J. Heinz Co. | 6,000 | 296,760 |
| Hormel Foods Corp. | 2,300 | 117,898 |
| The Hershey Co. | 15,700 | 740,255 |
| Tyson Foods, Inc. "A" (a) | 51,600 | 888,552 |
| Unilever PLC (ADR) | 2,900 | 89,552 |
| | | **2,977,755** |
| **Household Products 0.6%** | | |
| Kimberly-Clark Corp. | 2,400 | 151,296 |
| Procter & Gamble Co. | 7,900 | 508,207 |
| | | **659,503** |
| **Personal Products 0.4%** | | |
| Estee Lauder Companies, Inc. "A" | 1,200 | 96,840 |
| Herbalife Ltd. | 5,600 | 382,872 |
| | | **479,712** |
| **Tobacco 1.6%** | | |
| Lorillard, Inc. | 8,900 | 730,334 |
| Philip Morris International, Inc. | 16,400 | 959,892 |
| | | **1,690,226** |
| **Energy 11.2%** | | |
| **Energy Equipment & Services 3.4%** | | |
| Complete Production Services, Inc.* | 11,100 | 328,005 |
| Diamond Offshore Drilling, Inc. | 3,200 | 213,984 |
| FMC Technologies, Inc.* | 1,300 | 115,583 |
| Helmerich & Payne, Inc. | 2,000 | 96,960 |
| Nabors Industries Ltd.* | 12,200 | 286,212 |
| National Oilwell Varco, Inc. | 16,400 | 1,102,900 |
| Noble Corp. (a) | 4,900 | 175,273 |
| Oceaneering International, Inc.* (a) | 2,100 | 154,623 |
| Oil States International, Inc.* | 10,800 | 692,172 |
| Transocean Ltd.* (a) | 7,500 | 521,325 |
| | | **3,687,037** |
| **Oil, Gas & Consumable Fuels 7.8%** | | |
| Chevron Corp. | 13,000 | 1,186,250 |
| Cimarex Energy Co. | 1,500 | 132,795 |
| CNOOC Ltd. (ADR) | 400 | 95,348 |
| Devon Energy Corp. | 13,100 | 1,028,481 |
| Exxon Mobil Corp. | 30,000 | 2,193,600 |
| Hess Corp. | 9,000 | 688,860 |
| Murphy Oil Corp. | 10,300 | 767,865 |
| Newfield Exploration Co.* | 2,800 | 201,908 |
| Noble Energy, Inc. | 4,100 | 352,928 |
| Occidental Petroleum Corp. | 6,700 | 657,270 |
| Valero Energy Corp. | 48,700 | 1,125,944 |
| | | **8,431,249** |

*The accompanying notes are an integral part of the financial statements.*

| | Shares | Value ($) |
|---|---|---|
| **Financials 17.2%** | | |
| **Capital Markets 1.8%** | | |
| Ameriprise Financial, Inc. | 2,900 | 166,895 |
| BlackRock, Inc. | 1,900 | 362,102 |
| Janus Capital Group, Inc. | 5,800 | 75,226 |
| Legg Mason, Inc. | 4,800 | 174,096 |
| State Street Corp. | 5,400 | 250,236 |
| T. Rowe Price Group, Inc. (a) | 4,800 | 309,792 |
| The Goldman Sachs Group, Inc. | 3,600 | 605,376 |
| | | **1,943,723** |
| **Commercial Banks 4.0%** | | |
| CIT Group, Inc.* | 8,800 | 414,480 |
| Fifth Third Bancorp. (a) | 50,600 | 742,808 |
| Huntington Bancshares, Inc. | 36,200 | 248,694 |
| KeyCorp (a) | 45,600 | 403,560 |
| M&T Bank Corp. (a) | 1,800 | 156,690 |
| PNC Financial Services Group, Inc. | 9,900 | 601,128 |
| SunTrust Banks, Inc. | 38,500 | 1,136,135 |
| Wells Fargo & Co. | 22,100 | 684,879 |
| | | **4,388,374** |
| **Consumer Finance 2.4%** | | |
| Capital One Financial Corp. (a) | 40,900 | 1,740,704 |
| Discover Financial Services | 46,200 | 856,086 |
| | | **2,596,790** |
| **Diversified Financial Services 2.7%** | | |
| Bank of America Corp. | 30,900 | 412,206 |
| Citigroup, Inc.* | 75,300 | 356,169 |
| CME Group, Inc. | 800 | 257,400 |
| JPMorgan Chase & Co. | 38,700 | 1,641,654 |
| PHH Corp.* | 7,500 | 173,625 |
| The NASDAQ OMX Group, Inc.* (a) | 5,300 | 125,663 |
| | | **2,966,717** |
| **Insurance 5.8%** | | |
| ACE Ltd. | 21,900 | 1,363,275 |
| Aflac, Inc. | 5,400 | 304,722 |
| Allied World Assurance Co. Holdings Ltd. | 5,400 | 320,976 |
| Arch Capital Group Ltd.* | 2,000 | 176,100 |
| Aspen Insurance Holdings Ltd. | 4,200 | 120,204 |
| Assurant, Inc. | 3,400 | 130,968 |
| Axis Capital Holdings Ltd. | 3,200 | 114,816 |
| Berkshire Hathaway, Inc. "A"* | 2 | 240,900 |
| Berkshire Hathaway, Inc. "B"* | 2,240 | 179,446 |
| Chubb Corp. | 16,300 | 972,132 |
| Everest Re Group Ltd. | 2,000 | 169,640 |
| Hartford Financial Services Group, Inc. | 10,100 | 267,549 |
| Platinum Underwriters Holdings Ltd. | 2,400 | 107,928 |
| The Travelers Companies, Inc. | 33,100 | 1,844,001 |
| | | **6,312,657** |
| **Real Estate Investment Trusts 0.5%** | | |
| HCP, Inc. (REIT) | 5,500 | 202,345 |
| Public Storage (REIT) | 1,700 | 172,414 |
| SL Green Realty Corp. (REIT) | 1,600 | 108,016 |
| | | **482,775** |
| **Health Care 13.5%** | | |
| **Biotechnology 1.7%** | | |
| Biogen Idec, Inc.* | 8,100 | 543,105 |
| Celgene Corp.* | 5,700 | 337,098 |
| Cephalon, Inc.* (a) | 16,700 | 1,030,724 |
| | | **1,910,927** |

| | Shares | Value ($) |
|---|---|---|
| **Health Care Providers & Services 8.1%** | | |
| Aetna, Inc. | 20,800 | 634,608 |
| AmerisourceBergen Corp. | 43,800 | 1,494,456 |
| Cardinal Health, Inc. | 45,700 | 1,750,767 |
| Coventry Health Care, Inc.* | 28,400 | 749,760 |
| Health Net, Inc.* | 5,100 | 139,179 |
| Humana, Inc.* | 16,600 | 908,684 |
| UnitedHealth Group, Inc. | 51,400 | 1,856,054 |
| WellPoint, Inc.* | 21,600 | 1,228,176 |
| | | **8,761,684** |
| **Pharmaceuticals 3.7%** | | |
| Eli Lilly & Co. | 38,000 | 1,331,520 |
| Endo Pharmaceuticals Holdings, Inc.* | 13,700 | 489,227 |
| Forest Laboratories, Inc.* | 57,700 | 1,845,246 |
| Medicis Pharmaceutical Corp. "A" | 4,200 | 112,518 |
| Par Pharmaceutical Companies, Inc.* | 6,300 | 242,613 |
| | | **4,021,124** |
| **Industrials 11.5%** | | |
| **Aerospace & Defense 3.1%** | | |
| General Dynamics Corp. | 9,500 | 674,120 |
| Honeywell International, Inc. | 7,500 | 398,700 |
| Northrop Grumman Corp. (a) | 25,600 | 1,658,368 |
| Raytheon Co. | 13,300 | 616,322 |
| | | **3,347,510** |
| **Air Freight & Logistics 1.6%** | | |
| FedEx Corp. | 4,700 | 437,147 |
| United Parcel Service, Inc. "B" | 18,100 | 1,313,698 |
| | | **1,750,845** |
| **Airlines 0.2%** | | |
| Alaska Air Group, Inc.* | 2,900 | **164,401** |
| **Commercial Services & Supplies 0.4%** | | |
| Cintas Corp. | 4,800 | 134,208 |
| R.R. Donnelley & Sons Co. | 16,600 | 290,002 |
| | | **424,210** |
| **Construction & Engineering 0.4%** | | |
| EMCOR Group, Inc.* | 10,200 | 295,596 |
| KBR, Inc. | 5,200 | 158,444 |
| | | **454,040** |
| **Electrical Equipment 0.2%** | | |
| Rockwell Automation, Inc. | 2,300 | **164,933** |
| **Industrial Conglomerates 1.1%** | | |
| 3M Co. | 14,200 | **1,225,460** |
| **Machinery 2.0%** | | |
| Danaher Corp. | 8,200 | 386,794 |
| Dover Corp. | 3,100 | 181,195 |
| Eaton Corp. | 5,200 | 527,852 |
| Ingersoll-Rand PLC | 7,200 | 339,048 |
| Oshkosh Corp.* | 12,200 | 429,928 |
| Parker Hannifin Corp. | 1,900 | 163,970 |
| Trinity Industries, Inc. (a) | 6,500 | 172,965 |
| | | **2,201,752** |
| **Professional Services 0.3%** | | |
| Manpower, Inc. | 4,600 | **288,696** |
| **Road & Rail 1.6%** | | |
| Norfolk Southern Corp. | 13,200 | 829,224 |
| Ryder System, Inc. | 18,100 | 952,784 |
| | | **1,782,008** |

*The accompanying notes are an integral part of the financial statements.*

| | Shares | Value ($) |
|---|---|---|
| **Trading Companies & Distributors 0.6%** | | |
| W.W. Grainger, Inc. (a) | 4,900 | **676,739** |
| **Information Technology 18.7%** | | |
| **Communications Equipment 1.6%** | | |
| F5 Networks, Inc.* | 4,500 | 585,720 |
| Nokia Corp. (ADR) (a) | 34,100 | 351,912 |
| Research In Motion Ltd.* | 10,900 | 633,617 |
| Tellabs, Inc. | 20,600 | 139,668 |
| | | **1,710,917** |
| **Computers & Peripherals 0.7%** | | |
| Dell, Inc.* | 8,800 | 119,240 |
| Lexmark International, Inc. "A"* | 16,800 | 584,976 |
| | | **704,216** |
| **Electronic Equipment, Instruments & Components 3.9%** | | |
| Anixter International, Inc. | 1,800 | 107,514 |
| Arrow Electronics, Inc.* | 21,600 | 739,800 |
| Avnet, Inc.* | 18,400 | 607,752 |
| FLIR Systems, Inc.* | 2,600 | 77,350 |
| Ingram Micro, Inc. "A"* | 24,900 | 475,341 |
| Jabil Circuit, Inc. | 12,800 | 257,152 |
| Power-One, Inc.* (a) | 11,500 | 117,300 |
| Tech Data Corp.* | 11,600 | 510,632 |
| Tyco Electronics Ltd. | 27,700 | 980,580 |
| Vishay Intertechnology, Inc.* (a) | 28,000 | 411,040 |
| | | **4,284,461** |
| **Internet Software & Services 0.8%** | | |
| AOL, Inc.* | 15,000 | 355,650 |
| IAC/InterActiveCorp.* (a) | 17,700 | 507,990 |
| | | **863,640** |
| **IT Services 5.4%** | | |
| Automatic Data Processing, Inc. | 13,000 | 601,640 |
| Cognizant Technology Solutions Corp. "A"* | 3,900 | 285,831 |
| Computer Sciences Corp. | 28,300 | 1,403,680 |
| International Business Machines Corp. | 20,400 | 2,993,904 |
| Western Union Co. (a) | 31,900 | 592,383 |
| | | **5,877,438** |
| **Semiconductors & Semiconductor Equipment 3.4%** | | |
| Altera Corp. (a) | 10,500 | 373,590 |
| Analog Devices, Inc. | 8,800 | 331,496 |
| Fairchild Semiconductor International, Inc.* (a) | 8,500 | 132,685 |
| Intel Corp. | 94,500 | 1,987,335 |
| Lam Research Corp.* | 3,000 | 155,340 |
| Marvell Technology Group Ltd.* | 19,500 | 361,725 |
| Maxim Integrated Products, Inc. | 7,100 | 167,702 |
| Micron Technology, Inc.* (a) | 25,900 | 207,718 |
| | | **3,717,591** |
| **Software 2.9%** | | |
| Activision Blizzard, Inc. | 32,400 | 403,056 |
| Microsoft Corp. | 97,900 | 2,733,368 |
| | | **3,136,424** |

| | Shares | Value ($) |
|---|---|---|
| **Materials 5.3%** | | |
| **Chemicals 2.4%** | | |
| Ashland, Inc. | 6,700 | 340,762 |
| Cytec Industries, Inc. | 1,600 | 84,896 |
| E.I. du Pont de Nemours & Co. | 21,500 | 1,072,420 |
| Lubrizol Corp. | 8,800 | 940,544 |
| Potash Corp. of Saskatchewan, Inc. (a) | 1,000 | 154,830 |
| | | **2,593,452** |
| **Metals & Mining 2.6%** | | |
| Barrick Gold Corp. | 7,400 | 393,532 |
| Freeport-McMoRan Copper & Gold, Inc. | 11,200 | 1,345,008 |
| Newmont Mining Corp. | 18,500 | 1,136,455 |
| | | **2,874,995** |
| **Paper & Forest Products 0.3%** | | |
| Domtar Corp. | 2,200 | 167,024 |
| MeadWestvaco Corp. | 4,900 | 128,184 |
| | | **295,208** |
| **Telecommunication Services 2.5%** | | |
| **Diversified Telecommunication Services 2.2%** | | |
| AT&T, Inc. | 16,700 | 490,646 |
| Verizon Communications, Inc. | 51,700 | 1,849,826 |
| | | **2,340,472** |
| **Wireless Telecommunication Services 0.3%** | | |
| Vodafone Group PLC (ADR) | 14,300 | **377,949** |
| **Utilities 1.6%** | | |
| **Electric Utilities 0.8%** | | |
| Duke Energy Corp. | 34,700 | 618,007 |
| Exelon Corp. | 7,600 | 316,464 |
| | | **934,471** |
| **Independent Power Producers & Energy Traders 0.6%** | | |
| NRG Energy, Inc.* (a) | 34,108 | **666,470** |
| **Multi-Utilities 0.2%** | | |
| Ameren Corp. | 6,800 | **191,692** |
| **Total Common Stocks** (Cost $91,736,793) | | **107,368,303** |
| **Securities Lending Collateral 12.0%** | | |
| Daily Assets Fund Institutional, 0.27% (b) (c) (Cost $13,084,837) | 13,084,837 | **13,084,837** |
| **Cash Equivalents 1.0%** | | |
| Central Cash Management Fund, 0.19% (b) (Cost $1,081,171) | 1,081,171 | **1,081,171** |

| | % of Net Assets | Value ($) |
|---|---|---|
| **Total Investment Portfolio** (Cost $105,902,801)† | 111.8 | **121,534,311** |
| **Other Assets and Liabilities, Net** | (11.8) | **(12,874,612)** |
| **Net Assets** | 100.0 | **108,659,699** |

* *Non-income producing security.*

† *The cost for federal income tax purposes was $106,855,572. At December 31, 2010, net unrealized appreciation for all securities based on tax cost was $14,678,739. This consisted of aggregate gross unrealized appreciation for all securities in which there was an excess of value over tax cost of $16,161,936 and aggregate gross unrealized depreciation for all securities in which there was an excess of tax cost over value of $1,483,197.*

*The accompanying notes are an integral part of the financial statements.*

(a) *All or a portion of these securities were on loan (see Notes to Financial Statements). The value of all securities loaned at December 31, 2010 amounted to $12,717,748, which is 11.7% of net assets.*

(b) *Affiliated fund managed by Deutsche Investment Management Americas Inc. The rate shown is the annualized seven-day yield at period end.*

(c) *Represents collateral held in connection with securities lending. Income earned by the Fund is net of borrower rebates.*

*ADR: American Depositary Receipt*

*REIT: Real Estate Investment Trust*

*At December 31, 2010, open futures contracts purchased were as follows:*

| Futures | Currency | Expiration Date | Contracts | Notional Value ($) | Unrealized Appreciation ($) |
|---|---|---|---|---|---|
| S&P 500 E-Mini Index | USD | 3/18/2011 | 17 | 1,065,050 | **15,218** |

| Currency Abbreviation | |
|---|---|
| USD | United States Dollar |

## Fair Value Measurements

*Various inputs are used in determining the value of the Fund's investments. These inputs are summarized in three broad levels. Level 1 includes quoted prices in active markets for identical securities. Level 2 includes other significant observable inputs (including quoted prices for similar securities, interest rates, prepayment speeds, and credit risk). Level 3 includes significant unobservable inputs (including the Fund's own assumptions in determining the fair value of investments). The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities.*

*The following is a summary of the inputs used as of December 31, 2010 in valuing the Fund's investments. For information on the Fund's policy regarding the valuation of investments, please refer to the Security Valuation section of Note A in the accompanying Notes to Financial Statements.*

| Assets | Level 1 | Level 2 | Level 3 | Total |
|---|---|---|---|---|
| Common Stocks (d) | $ 107,368,303 | $ — | $ — | $ 107,368,303 |
| Short-Term Investments (d) | 14,166,008 | — | — | 14,166,008 |
| Derivatives (e) | 15,218 | — | — | 15,218 |
| **Total** | **$ 121,549,529** | **$ —** | **$ —** | **$ 121,549,529** |

*There have been no significant transfers between Level 1 and Level 2 fair value measurements during the year ended December 31, 2010.*

(d) *See Investment Portfolio for additional detailed categorizations.*

(e) *Derivatives include unrealized appreciation (depreciation) on open futures contracts.*

# Statement of Assets and Liabilities

as of December 31, 2010

| Assets | | |
|---|---|---|
| Investments: | | |
| Investments in unaffiliated securities, at value (cost $91,736,793) — including $12,717,748 of securities loaned | $ | 107,368,303 |
| Investment in Daily Assets Fund Institutional (cost $13,084,837)* | | 13,084,837 |
| Investment in Central Cash Management Fund (cost $1,081,171) | | 1,081,171 |
| Total investments, at value (cost $105,902,801) | | 121,534,311 |
| Deposit with brokers for open futures contracts | | 128,868 |
| Foreign currency, at value (cost $2,134) | | 2,233 |
| Receivable for Fund shares sold | | 145,708 |
| Receivable for variation margin on open futures contracts | | 15,218 |
| Dividends receivable | | 76,948 |
| Interest receivable | | 2,889 |
| Other assets | | 587 |
| Total assets | | 121,906,762 |

| Liabilities | | |
|---|---|---|
| Payable upon return of securities loaned | | 13,084,837 |
| Payable for Fund shares redeemed | | 35,395 |
| Accrued management fee | | 46,929 |
| Other accrued expenses and payables | | 79,902 |
| Total liabilities | | 13,247,063 |
| **Net assets, at value** | **$** | **108,659,699** |

| Net Assets Consist of | | |
|---|---|---|
| Undistributed net investment income | | 1,146,935 |
| Net unrealized appreciation (depreciation) on: | | |
| Investments | | 15,631,510 |
| Futures | | 15,218 |
| Foreign currency | | 99 |
| Accumulated net realized gain (loss) | | (49,691,433) |
| Paid-in capital | | 141,557,370 |
| **Net assets, at value** | **$** | **108,659,699** |
| **Class A**<br>**Net Asset Value,** offering and redemption price per share ($108,493,126 ÷ 10,190,728 outstanding shares of beneficial interest, no par value, unlimited number of shares authorized) | **$** | **10.65** |
| **Class B**<br>**Net Asset Value,** offering and redemption price per share ($166,573 ÷ 15,598 outstanding shares of beneficial interest, no par value, unlimited number of shares authorized) | **$** | **10.68** |

* *Represents collateral on securities loaned.*

# Statement of Operations

for the year ended December 31, 2010

| Investment Income | | |
|---|---|---|
| Income: | | |
| Dividends (net of foreign taxes withheld of $521) | $ | 1,948,786 |
| Interest | | 205 |
| Income distributions — Central Cash Management Fund | | 1,546 |
| Securities lending income, including income from Daily Assets Fund Institutional, net of borrower rebates | | 74,190 |
| Total income | | 2,024,727 |
| Expenses: | | |
| Management fee | | 580,643 |
| Administration fee | | 105,571 |
| Services to shareholders | | 2,584 |
| Distribution service fee (Class B) | | 399 |
| Custodian fee | | 19,378 |
| Legal fees | | 10,001 |
| Audit and tax fees | | 53,129 |
| Trustees' fees and expenses | | 6,320 |
| Reports to shareholders | | 12,605 |
| Other | | 8,322 |
| Total expenses | | 798,952 |
| **Net investment income (loss)** | | **1,225,775** |

| Realized and Unrealized Gain (Loss) | | |
|---|---|---|
| Net realized gain (loss) from: | | |
| Investments | | 11,523,479 |
| Futures | | 130,929 |
| Foreign currency | | (60) |
| | | 11,654,348 |
| Change in net unrealized appreciation (depreciation) on: | | |
| Investments | | 520,926 |
| Futures | | 7,705 |
| Foreign currency | | 142 |
| | | 528,773 |
| **Net gain (loss)** | | **12,183,121** |
| **Net increase (decrease) in net assets resulting from operations** | **$** | **13,408,896** |

*The accompanying notes are an integral part of the financial statements.*

# Statement of Changes in Net Assets

| Increase (Decrease) in Net Assets | Years Ended December 31, 2010 | 2009 |
|---|---|---|
| Operations: | | |
| Net investment income (loss) | $ 1,225,775 | $ 1,559,434 |
| Net realized gain (loss) | 11,654,348 | (19,218,958) |
| Change in net unrealized appreciation (depreciation) | 528,773 | 46,824,414 |
| Net increase (decrease) in net assets resulting from operations | 13,408,896 | 29,164,890 |
| Distributions to shareholders from: | | |
| Net investment income: | | |
| Class A | (1,575,913) | (2,044,479) |
| Class B | (1,920) | (2,260) |
| Total distributions | (1,577,833) | (2,046,739) |
| Fund share transactions: | | |
| **Class A** | | |
| Proceeds from shares sold | 4,447,701 | 5,027,733 |
| Reinvestment of distributions | 1,575,913 | 2,044,479 |
| Payments for shares redeemed | (20,221,768) | (29,505,512) |
| Net increase (decrease) in net assets from Class A share transactions | (14,198,154) | (22,433,300) |
| **Class B** | | |
| Proceeds from shares sold | 1,931 | 267 |
| Reinvestment of distributions | 1,920 | 2,260 |
| Payments for shares redeemed | (19,529) | (12,442) |
| Net increase (decrease) in net assets from Class B share transactions | (15,678) | (9,915) |
| **Increase (decrease) in net assets** | (2,382,769) | 4,674,936 |
| Net assets at beginning of period | 111,042,468 | 106,367,532 |
| Net assets at end of period (including undistributed net investment income of $1,146,935 and $1,493,480, respectively) | **$ 108,659,699** | **$ 111,042,468** |

| Other Information | | |
|---|---|---|
| **Class A** | | |
| Shares outstanding at beginning of period | 11,688,302 | 14,644,836 |
| Shares sold | 457,619 | 630,574 |
| Shares issued to shareholders in reinvestment of distributions | 153,448 | 313,090 |
| Shares redeemed | (2,108,641) | (3,900,198) |
| Net increase (decrease) in Class A shares | (1,497,574) | (2,956,534) |
| Shares outstanding at end of period | **10,190,728** | **11,688,302** |
| **Class B** | | |
| Shares outstanding at beginning of period | 17,241 | 18,379 |
| Shares sold | 199 | 34 |
| Shares issued to shareholders in reinvestment of distributions | 186 | 344 |
| Shares redeemed | (2,028) | (1,516) |
| Net increase (decrease) in Class B shares | (1,643) | (1,138) |
| Shares outstanding at end of period | **15,598** | **17,241** |

*The accompanying notes are an integral part of the financial statements.*

# Financial Highlights

## Class A

| Years Ended December 31, | 2010 | 2009 | 2008 | 2007 | 2006 |
|---|---|---|---|---|---|
| **Selected Per Share Data** | | | | | |
| **Net asset value, beginning of period** | **$ 9.49** | **$ 7.25** | **$14.65** | **$16.17** | **$14.88** |
| *Income (loss) from investment operations:* | | | | | |
| Net investment income[a] | .11 | .12 | .12 | .17 | .17[c] |
| Net realized and unrealized gain (loss) | 1.19 | 2.27 | (4.97) | .36 | 2.07 |
| **Total from investment operations** | 1.30 | 2.39 | (4.85) | .53 | 2.24 |
| *Less distributions from:* | | | | | |
| Net investment income | (.14) | (.15) | (.21) | (.18) | (.14) |
| Net realized gains | — | — | (2.34) | (1.87) | (.81) |
| **Total distributions** | (.14) | (.15) | (2.55) | (2.05) | (.95) |
| **Net asset value, end of period** | **$10.65** | **$ 9.49** | **$ 7.25** | **$14.65** | **$16.17** |
| Total Return (%) | 13.77 | 33.97 | (38.49)[b] | 3.50 | 15.65[c] |
| **Ratios to Average Net Assets and Supplemental Data** | | | | | |
| Net assets, end of period ($ millions) | 108 | 111 | 106 | 242 | 314 |
| Ratio of expenses before expense reductions (%) | .76 | .75 | .76 | .71 | .71 |
| Ratio of expenses after expense reductions (%) | .76 | .75 | .76 | .71 | .71 |
| Ratio of net investment income (%) | 1.16 | 1.54 | 1.12 | 1.13 | 1.12[c] |
| Portfolio turnover rate (%) | 146 | 82 | 127 | 275 | 226 |

a *Based on average shares outstanding during the period.*

b *Total return would have been lower had certain expenses not been reduced.*

c *Includes non-recurring income from the Advisor recorded as a result of an administrative proceeding regarding disclosure of brokerage allocation practices in connection with sales of DWS Funds. The non-recurring income resulted in an increase in net investment income of $0.003 per share and an increase in the ratio of net investment income of 0.02%. Excluding this non-recurring income, total return would have been 0.02% lower.*

## Class B

| Years Ended December 31, | 2010 | 2009 | 2008 | 2007 | 2006 |
|---|---|---|---|---|---|
| **Selected Per Share Data** | | | | | |
| **Net asset value, beginning of period** | **$ 9.51** | **$ 7.26** | **$14.61** | **$16.12** | **$14.83** |
| *Income (loss) from investment operations:* | | | | | |
| Net investment income[a] | .09 | .10 | .04 | .11 | .11[c] |
| Net realized and unrealized gain (loss) | 1.19 | 2.27 | (4.89) | .36 | 2.07 |
| **Total from investment operations** | 1.28 | 2.37 | (4.85) | .47 | 2.18 |
| *Less distributions from:* | | | | | |
| Net investment income | (.11) | (.12) | (.16) | (.11) | (.08) |
| Net realized gains | — | — | (2.34) | (1.87) | (.81) |
| **Total distributions** | (.11) | (.12) | (2.50) | (1.98) | (.89) |
| **Net asset value, end of period** | **$10.68** | **$ 9.51** | **$ 7.26** | **$14.61** | **$16.12** |
| Total Return (%) | 13.55 | 33.46 | (38.48)[b] | 3.15 | 15.19[c] |
| **Ratios to Average Net Assets and Supplemental Data** | | | | | |
| Net assets, end of period ($ millions) | .17 | .16 | .13 | 11 | 46 |
| Ratio of expenses before expense reductions (%) | 1.02 | 1.02 | 1.22 | 1.09 | 1.09 |
| Ratio of expenses after expense reductions (%) | 1.02 | 1.02 | 1.21 | 1.09 | 1.09 |
| Ratio of net investment income (%) | .90 | 1.27 | .67 | .75 | .74[c] |
| Portfolio turnover rate (%) | 146 | 82 | 127 | 275 | 226 |

a *Based on average shares outstanding during the period.*

b *Total return would have been lower had certain expenses not been reduced.*

c *Includes non-recurring income from the Advisor recorded as a result of an administrative proceeding regarding disclosure of brokerage allocation practices in connection with sales of DWS Funds. The non-recurring income resulted in an increase in net investment income of $0.003 per share and an increase in the ratio of net investment income of 0.02%. Excluding this non-recurring income, total return would have been 0.02% lower.*

# Notes to Financial Statements

## A. Organization and Significant Accounting Policies

DWS Variable Series II (the "Trust") is registered under the Investment Company Act of 1940, as amended (the "1940 Act"), as an open-end management investment company organized as a Massachusetts business trust. The Trust offers seventeen funds (hereinafter referred to individually as "Fund" or collectively as "Funds"). The Fund is classified as a diversified open-end management investment company.

**Multiple Classes of Shares of Beneficial Interest.** Certain Funds of the Trust offer two classes of shares (Class A shares and Class B shares). Sales of Class B shares are subject to record keeping fees up to 0.15% and Rule 12b-1 fees under the 1940 Act equal to an annual rate of 0.25%, of the average daily net assets of the Class B shares of the applicable Fund. Class A shares are not subject to such fees.

Investment income, realized and unrealized gains and losses, and certain fund-level expenses and expense reductions, if any, are borne pro rata on the basis of relative net assets by the holders of all classes of shares except that each class bears certain expenses unique to that class (including the applicable Rule 12b-1 fee and record keeping fees). Differences in class-level expenses may result in payment of different per share dividends by class. All shares have equal rights with respect to voting subject to class-specific arrangements.

The Trust's financial statements are prepared in accordance with accounting principles generally accepted in the United States of America which require the use of management estimates. Actual results could differ from those estimates. The policies described below are followed consistently by the Trust in the preparation of its financial statements.

**Security Valuation.** Investments are stated at value determined as of the close of regular trading on the New York Stock Exchange on each day the exchange is open for trading.

Various inputs are used in determining the value of the Fund's investments. These inputs are summarized in three broad levels. Level 1 includes quoted prices in active markets for identical securities. Level 2 includes other significant observable inputs (including quoted prices for similar securities, interest rates, prepayment speeds, and credit risk). Level 3 includes significant unobservable inputs (including the Fund's own assumptions in determining the fair value of investments). The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities.

Equity securities are valued at the most recent sale price or official closing price reported on the exchange (US or foreign) or over-the-counter market on which they trade and are categorized as Level 1 securities. Securities for which no sales are reported are valued at the calculated mean between the most recent bid and asked quotations on the relevant market or, if a mean cannot be determined, at the most recent bid quotation.

Futures contracts are generally valued at the settlement prices established each day on the exchange on which they are traded and are categorized as Level 1.

Money market instruments purchased with an original or remaining maturity of sixty days or less, maturing at par, are valued at amortized cost, which approximates value, and are categorized as Level 2. Investments in open-end investment companies are valued at their net asset value each business day and are categorized as Level 1.

Securities and other assets for which market quotations are not readily available or for which the above valuation procedures are deemed not to reflect fair value are valued in a manner that is intended to reflect their fair value as determined in accordance with procedures approved by the Board and are generally categorized as Level 3. In accordance with the Fund's valuation procedures, factors used in determining value may include, but are not limited to, the type of the security; the size of the holding; the initial cost of the security; the existence of any contractual restrictions on the security's disposition; the price and extent of public trading in similar securities of the issuer or of comparable companies; quotations or evaluated prices from broker-dealers and/or pricing services; information obtained from the issuer, analysts, and/or the appropriate stock exchange (for exchange-traded securities); an analysis of the company's or issuer's financial statements; an evaluation of the forces that influence the issuer and the market(s) in which the security is purchased and sold and with respect to debt securities; the maturity, coupon, creditworthiness, currency denomination and the movement of the market in which the security is normally traded. The value determined under these procedures may differ from published values for the same securities.

Disclosure about the classification of fair value measurements is included in a table following the Fund's Investment Portfolio.

**Foreign Currency Translations.** The books and records of the Trust are maintained in US dollars. Investment securities and other assets and liabilities denominated in a foreign currency are translated into US dollars at the prevailing exchange rates at period end. Purchases and sales of investment securities, income and expenses are translated into US dollars at the prevailing exchange rates on the respective dates of the transactions.

Net realized and unrealized gains and losses on foreign currency transactions represent net gains and losses between trade and settlement dates on securities transactions, the disposition of forward foreign currency exchange contracts and foreign currencies, and the difference between the amount of net investment income accrued and the US dollar amount actually received. That portion of both realized and unrealized gains and losses on investments that results from fluctuations in foreign currency exchange rates is not separately disclosed but is included with net realized and unrealized gain/appreciation and loss/depreciation on investments.

**Securities Lending.** The Fund lends securities to certain financial institutions. The Fund retains beneficial ownership of the securities it has loaned and continues to receive interest and dividends paid by the issuer of securities and to participate in any changes in their market value. The Fund requires the borrowers of the securities to maintain collateral with the Fund consisting of either cash or liquid, unencumbered assets having a value at least equal to the value of the securities loaned. When the collateral falls below specified amounts, the lending agent will use its best effort to obtain additional collateral on the next business day to meet required amounts under the security lending agreement. The Fund may invest the cash collateral into a joint trading account in an affiliated money market fund pursuant to Exemptive Orders issued by the SEC. The Fund receives compensation for lending its securities either in the form of fees or by earning interest on invested cash collateral net of borrower rebates and fees paid to a lending agent. Either the Fund or the borrower may terminate the loan. There may be risks of delay and costs in recovery of securities or even loss of rights in the collateral should the borrower of the securities fail financially. The Fund is also subject to all investment risks associated with the reinvestment of any cash collateral received, including, but not limited to, interest rate, credit and liquidity risk associated with such investments.

**Taxes.** The Fund's policy is to comply with the requirements of the Internal Revenue Code, as amended, which are applicable to regulated investment companies and to distribute all of its taxable income to its shareholders.

At December 31, 2010, the Fund had an approximate net tax basis capital loss carryforward which may be applied against any realized net taxable capital gains of each succeeding year until fully utilized or until the following expiration dates, whichever occurs first:

| Fund | Capital Loss Carryforward ($) | Expiration Date | Capital Loss Carryforward Utilized ($) |
|---|---|---|---|
| DWS Blue Chip VIP | 15,813,000 | 12/31/2016 | 10,865,000 |
| | 32,910,000 | 12/31/2017 | |

The Fund has reviewed the tax positions for the open tax years as of December 31, 2010 and has determined that no provision for income tax is required in the Fund's financial statements. The Fund's federal tax returns for the prior three fiscal years remain open subject to examination by the Internal Revenue Service.

**Distribution of Income and Gains.** Distributions of net investment income of the Fund, if any, are made annually. Net realized gains from investment transactions, in excess of available capital loss carryforwards, would be taxable to the Fund if not distributed and, therefore, will be distributed to shareholders at least annually. The Fund may also make additional distributions for tax purposes if necessary.

The timing and characterization of certain income and capital gains distributions are determined annually in accordance with federal tax regulations which may differ from accounting principles generally accepted in the United States of America. These differences primarily relate to investments in futures contracts and certain securities sold at a loss. As a result, net investment income (loss) and net realized gain (loss) on investment transactions for a reporting period may differ significantly from distributions during such period. Accordingly, the Fund may periodically make reclassifications among certain of its capital accounts without impacting the net asset value of the Fund.

At December 31, 2010, the Fund's components of distributable earnings on a tax basis were as follows:

| Fund | Undistributed Ordinary Income ($)* | Capital Loss Carryforwards ($) | Unrealized Appreciation (Depreciation) on Investments ($) |
|---|---|---|---|
| DWS Blue Chip VIP | 1,146,935 | (48,723,000) | 14,678,739 |

In addition, the tax character of distributions paid by the Fund is summarized as follows:

| | Distributions from Ordinary Income ($)* | |
|---|---|---|
| | Years Ended December 31, | |
| Fund | 2010 | 2009 |
| DWS Blue Chip VIP | 1,577,833 | 2,046,739 |

* *For tax purposes, short-term capital gain distributions are considered ordinary income distributions.*

**Expenses.** Expenses of the Trust arising in connection with a specific fund are allocated to that fund. Other Trust expenses which cannot be directly attributed to a fund are apportioned among the funds in the Trust.

**Contingencies.** In the normal course of business, the Fund may enter into contracts with service providers that contain general indemnification clauses. The Fund's maximum exposure under these arrangements is unknown as this would involve future claims that may be made against the Fund that have not yet been made. However, based on experience, the Fund expects the risk of loss to be remote.

**Other.** Investment transactions are accounted for on a trade date plus one basis for daily net asset value calculations. However, for financial reporting purposes, investment transactions are reported on trade date. Interest income is recorded on the accrual basis. Dividend income is recorded on the ex-dividend date net of foreign withholding taxes. Realized gains and losses from investment transactions are recorded on an identified cost basis.

## B. Derivative Instruments

**Futures Contracts.** A futures contract is an agreement between a buyer or seller and an established futures exchange or its clearinghouse in which the buyer or seller agrees to take or make a delivery of a specific amount of a financial instrument at a specified price on a specific date (settlement date). For the year ended December 31, 2010, the Fund entered into futures contracts to keep cash on hand to meet shareholder redemptions or other needs while maintaining exposure to the market.

Futures contracts are valued at the most recent settlement price. Upon entering into a futures contract, the Fund is required to deposit with a financial intermediary cash or securities ("initial margin") in an amount equal to a certain percentage of the face value indicated in the futures contract. Subsequent payments ("variation margin") are made or received by the Fund dependent upon the daily fluctuations in the value and are recorded for financial reporting purposes as unrealized gains or losses by the Fund. Gains or losses are realized when the contract expires or is closed. Since all futures contracts are exchange-traded, counterparty risk is minimized as the exchange's clearinghouse acts as the counterparty, and guarantees the futures against default.

Certain risks may arise upon entering into futures contracts, including the risk that an illiquid market will limit the Fund's ability to close out a futures contract prior to the settlement date and that a change in the value of a futures contract may not correlate exactly with the changes in the value of the underlying hedged security, index or currency. Risk of loss may exceed amounts recognized in the Statement of Assets and Liabilities.

A summary of the open futures contracts as of December 31, 2010 is included in a table following the Fund's Investment Portfolio. For the year ended December 31, 2010, the Fund's investment in futures contracts purchased had a total notional value generally indicative of a range from approximately $359,000 to $1,806,000.

The following table summarizes the value of the Fund's derivative instruments held as of December 31, 2010 and the related location in the accompanying Statement of Assets and Liabilities, presented by primary underlying risk exposure:

| Asset Derivative | Futures Contracts |
|---|---|
| Equity Contracts (a) | $ 15,218 |

*The above derivative is located in the following Statement of Assets and Liabilities account:*

(a) *Net unrealized appreciation (depreciation) on futures. Asset of receivable for daily variation margin on open futures contracts reflects unsettled variation margin.*

Additionally, the amount of unrealized and realized gains and losses on derivative instruments recognized in Fund earnings during the year ended December 31, 2010 and the related location in the accompanying Statement of Operations is summarized in the following tables by primary underlying risk exposure:

| Realized Gain (Loss) | Futures Contracts |
|---|---|
| Equity Contracts (a) | $ 130,929 |

*The above derivative is located in the following Statement of Operations account:*

(a) *Net realized gain (loss) from futures*

| Change in Net Unrealized Appreciation (Depreciation) | Futures Contracts |
|---|---|
| Equity Contracts (a) | $ 7,705 |

*The above derivative is located in the following Statement of Operations account:*

(a) *Change in net unrealized appreciation (depreciation) on futures*

## C. Purchases and Sales of Securities

During the year ended December 31, 2010, purchases and sales of investment transactions (excluding short-term investments) were as follows:

| Fund | Purchases ($) | Sales ($) |
|---|---|---|
| DWS Blue Chip VIP | 151,115,169 | 165,670,571 |

## D. Related Parties

**Management Agreement.** Under the Investment Management Agreement with Deutsche Investment Management Americas Inc. ("DIMA" or the "Advisor"), an indirect, wholly owned subsidiary of Deutsche Bank AG, the Advisor directs the investments of the Fund in accordance with its investment objectives, policies and restrictions. The Advisor determines the securities, instruments and other contracts relating to investments to be purchased, sold or entered into by the Fund or delegates such responsibility to the Fund's subadvisor.

QS Investors, LLC ("QS Investors") acts as an investment sub-advisor to the Fund. On August 1, 2010, members of the Advisor's Quantitative Strategies Group, including some members of the Fund's portfolio management team, separated from the Advisor and formed QS Investors as a separate investment advisory firm unaffiliated with the Advisor (the "Separation"). As an investment sub-advisor to the Fund, QS Investors makes investment decisions and buys and sells securities for the Fund. QS Investors is paid by the Advisor, not the Fund, for the services QS Investors provides to the Fund.

Under the Investment Management Agreement with the Advisor, the fee is equivalent to the annual rates shown below of the Fund's average daily net assets, computed and accrued daily and payable monthly:

| Fund | Annual Management Fee Rate |
|---|---|
| DWS Blue Chip VIP | |
| $0–$250 million | .550% |
| next $750 million | .520% |
| next $1.5 billion | .500% |
| next $2.5 billion | .480% |
| next $2.5 billion | .450% |
| next $2.5 billion | .430% |
| next $2.5 billion | .410% |
| over $12.5 billion | .390% |

Accordingly, for the year ended December 31, 2010, the total management fee and effective management fee rate were as follows:

| Fund | Total Aggregated ($) | Annual Effective Rate |
|---|---|---|
| DWS Blue Chip VIP | 580,643 | .55% |

**Administration Fee.** Pursuant to an Administrative Services Agreement, DIMA provides most administrative services to the Fund. For all services provided under the Administrative Services Agreement, the Fund pays DIMA an annual fee ("Administration Fee") of 0.10% of the Fund's average daily net assets, computed and accrued daily and payable monthly. For the year ended December 31, 2010, the Administration Fee was as follows:

| Fund | Total Aggregated ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS Blue Chip VIP | 105,571 | 9,119 |

**Service Provider Fees.** DWS Investments Service Company ("DISC"), an affiliate of the Advisor, is the transfer agent, dividend-paying agent and shareholder service agent for the Fund. Pursuant to a sub-transfer agency agreement between DISC and DST Systems, Inc. ("DST"), DISC has delegated certain transfer agent, dividend-paying agent and shareholder service agent functions to DST. DISC compensates DST out of the shareholder servicing fee it receives from the Fund. For the year ended December 31, 2010, the amounts charged to the Fund by DISC were as follows:

| Fund | Total Aggregated ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS Blue Chip VIP Class A | 223 | 59 |
| DWS Blue Chip VIP Class B | 24 | 6 |

**Distribution Service Agreement**. Under the Fund's Class B 12b-1 plans, DWS Investments Distributors, Inc. ("DIDI") received a fee ("Distribution Service Fee") of 0.25% of average daily net assets of Class B shares. For the year ended December 31, 2010, the Distribution Service Fee was as follows:

| Fund | Total Aggregated ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS Blue Chip VIP | 399 | 277 |

**Typesetting and Filing Service Fees.** Under an agreement with DIMA, DIMA is compensated for providing typesetting and certain regulatory filing services to the Fund. For the year ended December 31, 2010, the amount charged to the Fund by DIMA included in the Statement of Operations under "reports to shareholders" was as follows:

| Fund | Amount ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS Blue Chip VIP | 12,605 | 3,200 |

**Trustees' Fees and Expenses.** The Fund paid each Trustee not affiliated with the Advisor retainer fees plus specified amounts for various committee services and for the Board Chairperson.

**Affiliated Cash Management Vehicles.** The Fund may invest uninvested cash balances in Central Cash Management Fund, which is managed by the Advisor. The Fund indirectly bears their proportionate share of the expenses of the underlying money market funds. Central Cash Management Fund does not pay the Advisor an investment management fee. Central Cash Management Fund seeks a high level of current income consistent with liquidity and the preservation of capital.

## E. Ownership of the Fund

At December 31, 2010, the beneficial ownership in the Fund was as follows:

**DWS Blue Chip VIP:** Two Participating Insurance Companies were owners of record of 10% or more of the total outstanding Class A shares of the Fund, each owning 53% and 39%. One Participating Insurance Company was the owner of record of 10% or more of the total outstanding Class B shares of the Fund, owning 100%.

## F. Line of Credit

The Trust and other affiliated fund (the "Participants") share in a $450 million revolving credit facility provided by a syndication of banks. The Fund may borrow for temporary or emergency purposes, including the meeting of redemption requests that otherwise might require the untimely disposition of securities. The Participants are charged an annual commitment fee which is allocated based on net assets, among each of the Participants. Interest is calculated at a rate per annum equal to the sum of the Federal Funds Rate plus 1.25 percent plus if LIBOR exceeds the Federal Funds Rate the amount of such excess. The Fund may borrow up to a maximum of 33 percent of its net assets under the agreement.

# Report of Independent Registered Public Accounting Firm

**To the Board of Trustees and Shareholders of DWS Variable Series II:**

We have audited the accompanying statement of assets and liabilities of DWS Blue Chip VIP, one of the funds constituting the DWS Variable Series II (the "Trust"), including the investment portfolio, as of December 31, 2010, and the related statement of operations, the statement of changes in net assets and the financial highlights for each of the periods indicated therein. These financial statements and financial highlights are the responsibility of the Trust's management. Our responsibility is to express an opinion on these financial statements and financial highlights based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements and financial highlights are free of material misstatement. We were not engaged to perform an audit of the Trust's internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Trust's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements and financial highlights, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our procedures included confirmation of securities owned as of December 31, 2010, by correspondence with the custodian and brokers or by other appropriate auditing procedures where replies from brokers were not received. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements and financial highlights referred to above present fairly, in all material respects, the financial position of the aforementioned fund of the DWS Variable Series II at December 31, 2010, the results of its operations, the changes in its net assets and the financial highlights for each of the periods indicated therein, in conformity with U.S. generally accepted accounting principles.

Ernst & Young LLP

Boston, Massachusetts
February 14, 2011

## Tax Information

**(Unaudited)**

For corporate shareholders, the following percentage of income dividends paid during the Fund's fiscal year ended December 31, 2010 qualified for the dividends received deduction:

| Fund | Dividends Received % |
|---|---|
| DWS Blue Chip VIP | 100 |

Please consult a tax advisor if you have questions about federal or state income tax laws, or on how to prepare your tax returns. If you have specific questions about your account, please contact your insurance provider.

## Proxy Voting

The Trust's policies and procedures for voting proxies for portfolio securities and information about how the Trust voted proxies related to its portfolio securities during the 12-month period ended June 30 are available on our Web site — www.dws-investments.com (click on "proxy voting" at the bottom of the page) — or on the SEC's Web site — www.sec.gov. To obtain a written copy of the Trust's policies and procedures without charge, upon request, call us toll free at (800) 728-3337.

# Investment Management Agreement Approval

## DWS Blue Chip VIP

The Board of Trustees, including the Independent Trustees, approved the renewal of your Fund's investment management agreement (the "Agreement") with Deutsche Investment Management Americas Inc. ("DWS") and sub-advisory agreement (the "Sub-Advisory Agreement" and together with the Agreement the "Agreements") between DWS and QS Investors, LLC ("QS Investors") in September 2010.

In terms of the process that the Board followed prior to approving the Agreements, shareholders should know that:

- In September 2010, all but one of the Fund's Trustees were independent of DWS and its affiliates.
- The Trustees meet frequently to discuss fund matters. Each year, the Trustees dedicate substantial time to contract review matters. Over the course of several months, the Board's Contract Committee, in coordination with the Board's Fixed Income and Quant Oversight Committee, reviewed comprehensive materials received from DWS, independent third parties and independent counsel. These materials included an analysis of the Fund's performance, fees and expenses, and profitability compiled by the Fund's independent fee consultant. The Board also received extensive information throughout the year regarding performance of the Fund.
- The Independent Trustees regularly meet privately with their independent counsel to discuss contract review and other matters. In addition, the Independent Trustees were also advised by the Fund's independent fee consultant in the course of their review of the Fund's contractual arrangements and considered a comprehensive report prepared by the independent fee consultant in connection with their deliberations (the "IFC Report").
- In connection with reviewing the Agreements, the Board also reviewed the terms of the Fund's Rule 12b-1 plan, distribution agreement, administrative services agreement, transfer agency agreement and other material service agreements.
- Based on its evaluation of the information provided, the Contract Committee presented its findings and recommendations to the Independent Trustees as a group. The Independent Trustees reviewed the Contract Committee's findings and recommendations and presented their recommendations to the full Board.

In connection with the contract review process, the Contract Committee and the Board considered the factors discussed below, among others. The Board also considered that DWS and its predecessors have managed the Fund since its inception, and the Board believes that a long-term relationship with a capable, conscientious advisor is in the best interests of the Fund. The Board considered, generally, that shareholders chose to invest or remain invested in the Fund knowing that DWS managed the Fund, and that the Agreement was approved by the Fund's shareholders. DWS is part of Deutsche Bank, a major global banking institution that is engaged in a wide range of financial services. The Board believes that there are significant advantages to being part of a global asset management business that offers a wide range of investing expertise and resources, including hundreds of portfolio managers and analysts with research capabilities in many countries throughout the world.

While shareholders may focus primarily on fund performance and fees, the Fund's Board considers these and many other factors, including the quality and integrity of DWS's and QS Investors' personnel and such other issues as back-office operations, fund valuations, and compliance policies and procedures. In addition, in connection with approving the continuation of the Fund's Sub-Advisory Agreement, the Board noted it had engaged in a comprehensive review of the agreement in connection with its initial approval in May 2010.

**Nature, Quality and Extent of Services.** The Board considered the terms of the Agreements, including the scope of advisory services provided under the Agreements. The Board noted that, under the Agreements, DWS and QS Investors provide portfolio management services to the Fund and that, pursuant to a separate administrative services agreement, DWS provides administrative services to the Fund. The Board considered the experience and skills of senior management and investment personnel, the resources made available to such personnel, the ability of DWS to attract and retain high-quality personnel, and the organizational depth and stability of DWS. The Board reviewed the Fund's performance over short-term and long-term periods and compared those returns to various agreed-upon performance measures, including market indices and a peer universe compiled by the independent fee consultant using information supplied by Lipper Inc. ("Lipper"). The Board also noted that it has put into place a process of identifying "Focus Funds" (e.g., funds performing poorly relative to their benchmark or a peer universe compiled by Lipper), and receives more frequent reporting and information from DWS regarding such funds, along with DWS's remedial plans to address underperformance. The Board believes this process is an effective manner of identifying and addressing underperforming funds. Based on the information provided, the Board noted that for the one-, three- and five-year periods ended December 31, 2009, the Fund's performance (Class A shares) was in the 2nd quartile of the applicable Lipper universe (the 1st quartile being the best performers and the 4th quartile being the worst performers). The Board also observed that the Fund has outperformed its benchmark in the one-, three- and five-year periods ended December 31, 2009.

On the basis of this evaluation and the ongoing review of investment results by the Board, the Board concluded that the nature, quality and extent of services provided by DWS and QS Investors historically have been and continue to be satisfactory.

**Fees and Expenses.** The Board considered the Fund's investment management fee schedule, sub-advisory fee schedule, operating expenses, and total expense ratios, and comparative information provided by Lipper and the independent fee consultant regarding investment management fee rates paid to other investment advisors by similar funds (1st quartile being the most favorable and 4th quartile being the least favorable). With respect to management fees paid to other investment advisors by similar funds, the Board noted that the contractual fee rates paid by the Fund, which include the 0.10% fee paid to DWS under the Fund's administrative services agreement, were lower than the median (2nd quartile) of the applicable Lipper peer group (based on Lipper data provided as of December 31, 2009). With respect to the sub-advisory fee paid to QS Investors, the Board noted that the fee is paid by DWS out of its fee and not directly by the Fund. The Board noted that the Fund's Class A shares total (net) operating expenses were expected to be lower than the median (2nd quartile) of the applicable Lipper expense universe (based on Lipper data provided as of December 31, 2009, and analyzing Lipper expense universe Class A expenses less any applicable 12b-1 fees) ("Lipper Universe Expenses"). The Board also reviewed data comparing each share class's total (net) operating expenses to the applicable Lipper Universe Expenses. The Board considered the Fund's management fee rate as compared to fees charged by DWS and certain of its affiliates for comparable mutual funds and considered differences in fund and fee structures between the DWS Funds. The Board also considered how the Fund's total (net) operating expenses compared to the total (net) operating expenses of a more customized peer group selected by Lipper (based on such factors as asset size).

The information considered by the Board as part of its review of management fees included information regarding fees charged by DWS and its affiliates to similar institutional accounts and to similar funds offered primarily to European investors ("DWS Europe funds"), in each case as applicable. The Board observed that advisory fee rates for institutional accounts generally were lower than the management fees charged by similarly managed DWS US mutual funds ("DWS Funds"), but also took note of the differences in services provided to DWS Funds as compared to institutional accounts. In the case of DWS Europe funds, the Board observed that fee rates for DWS Europe funds generally were higher than for similarly managed DWS Funds, but noted that differences in the types of services provided to DWS Funds relative to DWS Europe funds made it difficult to compare such fees.

On the basis of the information provided, the Board concluded that management fees were reasonable and appropriate in light of the nature, quality and extent of services provided by DWS and QS Investors.

**Profitability.** The Board reviewed detailed information regarding revenues received by DWS under the Agreement. The Board considered the estimated costs and pre-tax profits realized by DWS from advising the DWS Funds, as well as estimates of the pre-tax profits attributable to managing the Fund in particular. The Board also received information regarding the estimated enterprise-wide profitability of DWS and its affiliates with respect to all fund services in totality and by fund. The Board reviewed DWS's methodology in allocating its costs to the management of the Fund. Based on the information provided, the Board concluded that the pre-tax profits realized by DWS in connection with the management of the Fund were not unreasonable. The Board also reviewed information regarding the profitability of certain similar investment management firms. The Board noted that while information regarding the profitability of such firms is limited (and in some cases is not necessarily prepared on a comparable basis), DWS and its affiliates' overall profitability with respect to the DWS fund complex (after taking into account distribution and other services provided to the funds by DWS and its affiliates) was lower than the overall profitability levels of many comparable firms for which such data was available. The Board did not consider the profitability of QS Investors with respect to the Fund. The Board noted that DWS pays QS Investors' fee out of its management fee, and its understanding that the Fund's sub-advisory fee schedule was the product of an arm's length negotiation with DWS.

**Economies of Scale.** The Board considered whether there are economies of scale with respect to the management of the Fund and whether the Fund benefits from any economies of scale. The Board noted that the Fund's management fee schedule includes fee breakpoints. The Board concluded that the Fund's fee schedule represents an appropriate sharing between the Fund and DWS of such economies of scale as may exist in the management of the Fund at current asset levels.

**Other Benefits to DWS and QS Investors and Their Affiliates.** The Board also considered the character and amount of other incidental benefits received by DWS and QS Investors and their affiliates, including any fees received by DWS for administrative services provided to the Fund and any fees received by an affiliate of DWS for distribution services. The Board also considered benefits to DWS and QS Investors related to brokerage and soft-dollar allocations, including allocating brokerage to pay for research generated by parties other than the executing broker dealers, which pertain primarily to funds investing in equity securities, along with the incidental public relations benefits to DWS and QS Investors related to DWS Funds advertising and cross-selling opportunities among DWS products and services. The Board concluded that management fees were reasonable in light of these fallout benefits.

**Compliance.** The Board considered the significant attention and resources dedicated by DWS to documenting and enhancing its compliance processes in recent years. The Board noted in particular (i) the experience and seniority of both DWS's chief compliance officer and the Fund's chief compliance officer; (ii) the large number of DWS compliance personnel; and (iii) the substantial commitment of resources by DWS and its affiliates to compliance matters. The Board also considered the attention and resources dedicated by DWS to the oversight of the investment sub-advisor's compliance program and compliance with the applicable fund policies and procedures.

Based on all of the information considered and the conclusions reached, the Board unanimously (including the Independent Trustees) determined that the continuation of the Agreements is in the best interests of the Fund. In making this determination, the Board did not give particular weight to any single factor identified above. The Board considered these factors over the course of numerous meetings, certain of which were in executive session with only the Independent Trustees and their counsel present. It is possible that individual Trustees may have weighed these factors differently in reaching their individual decisions to approve the continuation of the Agreements.

# Summary of Management Fee Evaluation by Independent Fee Consultant

October 3, 2010

Pursuant to an Order entered into by Deutsche Investment Management Americas and affiliates (collectively, "DeAM") with the Attorney General of New York, I, Thomas H. Mack, have been appointed the Independent Fee Consultant for the DWS Funds (formerly the DWS Scudder Funds). My duties include preparing an annual written evaluation of the management fees DeAM charges the Funds, considering among other factors the management fees charged by other mutual fund companies for like services, management fees DeAM charges other clients for like services, DeAM's costs of supplying services under the management agreements and related profit margins, possible economies of scale if a Fund grows larger, and the nature and quality of DeAM's services, including fund performance. This report summarizes my evaluation for 2010, including my qualifications, the evaluation process for each of the DWS Funds, consideration of certain complex-level factors, and my conclusions. I served in substantially the same capacity in 2007, 2008, and 2009.

## Qualifications

For more than 35 years I have served in various professional capacities within the investment management business. I have held investment analysis and advisory positions, including securities analyst, portfolio strategist and director of investment policy with a large investment firm. I have also performed business management functions, including business development, financial management and marketing research and analysis.

Since 1991, I have been an independent consultant within the asset management industry. I have provided services to over 125 client organizations, including investment managers, mutual fund boards, product distributors and related organizations. Over the past ten years I have completed a number of assignments for mutual fund boards, specifically including assisting boards with management contract renewal.

I hold a Master of Business Administration degree, with highest honors, from Harvard University and Master of Science and Bachelor of Science (highest honors) degrees from the University of California at Berkeley. I am an independent director and audit committee financial expert for two closed-end mutual funds and have served in various leadership and financial oversight capacities with non-profit organizations.

## Evaluation of Fees for each DWS Fund

My work focused primarily on evaluating, fund-by-fund, the fees charged to each of the 118 publicly offered Fund portfolios in the DWS Fund family. For each Fund, I considered each of the key factors mentioned above, as well as any other relevant information. In doing so I worked closely with the Funds' Independent Directors in their annual contract renewal process, as well as in their approval of contracts for several new funds (documented separately).

In evaluating each Fund's fees, I reviewed comprehensive materials provided by or on behalf of DeAM, including expense information prepared by Lipper Analytical, comparative performance information, profitability data, manager histories, and other materials. I also accessed certain additional information from the Lipper and Morningstar databases and drew on my industry knowledge and experience.

To facilitate evaluating this considerable body of information, I prepared for each Fund a document summarizing the key data elements in each area as well as additional analytics discussed below. This made it possible to consider each key data element in the context of the others.

In the course of contract renewal, DeAM agreed to implement a number of fee and expense adjustments requested by the Independent Directors which will favorably impact future fees and expenses, and my evaluation includes the effects of these changes.

### Fees and Expenses Compared with Other Funds

The competitive fee and expense evaluation for each fund focused on two primary comparisons:

- The Fund's contractual management fee (the advisory fee plus the administration fee where applicable) compared with those of a group of typically 12–15 funds in the same Lipper investment category (e.g. Large Capitalization Growth) having similar distribution arrangements and being of similar size.
- The Fund's total expenses compared with a broader universe of funds from the same Lipper investment category and having similar distribution arrangements.

These two comparisons provide a view of not only the level of the fee compared with funds of similar scale but also the total expense the Fund bears for all the services it receives, in comparison with the investment choices available in the Fund's investment category and distribution channel. The principal figure-of-merit used in these comparisons was the subject Fund's percentile ranking against peers.

### DeAM's Fees for Similar Services to Others

DeAM provided management fee schedules for all of its US domiciled fund and non-fund investment management accounts in any of the investment categories where there is a DWS Fund. These similar products included the other DWS Funds, non-fund pooled accounts, institutional accounts and sub-advisory accounts. Using this information, I calculated for each Fund the fee that would be charged to each similar product, at the subject Fund's asset level.

Evaluating information regarding non-fund products is difficult because there are varying levels of services required for different types of accounts, with mutual funds generally requiring considerably more regulatory and administrative types of service as well as having more frequent cash flows than other types of accounts. Also, while mutual fund fees for similar fund products can be expected to be similar, there will be some differences due to different pricing conditions in different distribution channels (e.g. retail funds versus those used in variable insurance products), differences in underlying investment processes and other factors.

### Costs and Profit Margins

DeAM provided a detailed profitability analysis for each Fund. After making some adjustments so that the presentation would be more comparable to the available industry figures, I reviewed profit margins from investment management alone, from investment management plus other fund services (excluding distribution) provided to the Funds by DeAM (principally shareholder services), and DeAM profits from all sources, including distribution. A later section comments on overall profitability.

### Economies of Scale

Economies of scale — an expected decline in management cost per dollar of fund assets as fund assets grow — are very rarely quantified and documented because of inherent difficulties in collecting and analyzing relevant data. However, in virtually every investment category that I reviewed, larger funds tend to have lower fees and lower total expenses than smaller funds. To see how each DWS Fund compares with this industry observation, I reviewed:

- The trend in Fund assets over the last five years and the accompanying trend in total expenses. This shows if the Fund has grown and, if so, whether total expense (management fees as well as other expenses) have declined as a percent of assets.
- Whether the Fund has break-points in its management fee schedule, the extent of the fee reduction built into the schedule and the asset levels where the breaks take effect, and in the case of a sub-advised Fund how the Fund's break-points compare with those of the sub-advisory fee schedule.
- How the Fund's contractual fee schedule compares with trends in the industry data. To accomplish this, I constructed a chart showing how actual latest-fiscal-year contractual fees of the Fund and of other similar funds relate to average fund assets, with the subject Fund's contractual fee schedule superimposed.

### Quality of Service — Performance

The quality-of-service evaluation focused on investment performance, which is the principal result of the investment management service. Each Fund's performance was reviewed over the past 1, 3, 5 and 10 years, as applicable, and compared with that of other funds in the same investment category and with a suitable market index.

In addition, I calculated and reviewed risk-adjusted returns relative to an index of similar mutual funds' returns and a suitable market index. The risk-adjusted returns analysis provides a way of determining the extent to which the Fund's return comparisons are mainly the product of investment value-added (or lack thereof) or alternatively taking considerably more or less risk than is typical in its investment category.

I also received and considered the history of portfolio manager changes for each Fund, as this provided an important context for evaluating the performance results.

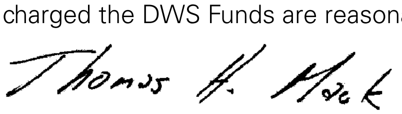
## Complex-Level Considerations

While this evaluation was conducted mainly at the individual fund level, there are some issues relating to the reasonableness of fees that can alternatively be considered across the whole fund complex:

- I reviewed DeAM's profitability analysis for all DWS Funds, with a view toward determining if the allocation procedures used were reasonable and how profit levels compared with public data for other investment managers.
- I considered whether DeAM and affiliates receive any significant ancillary or "fall-out" benefits that should be considered in interpreting the direct profitability results. These would be situations where serving as the investment manager of the Funds is beneficial to another part of the Deutsche Bank organization.
- I considered how aggregated DWS Fund expenses had varied over the years, by asset class and in the context of trends in asset levels.
- I reviewed the structure of the DeAM organization, trends in staffing levels, and information on compensation of investment management and other professionals compared with industry data.

## Findings

Based on the process and analysis discussed above, which included reviewing a wide range of information from management and external data sources and considering among other factors the fees DeAM charges other clients, the fees charged by other fund managers, DeAM's costs and profits associated with managing the Funds, economies of scale, possible fall-out benefits, and the nature and quality of services provided, in my opinion the management fees charged the DWS Funds are reasonable.



Thomas H. Mack

# Board Members and Officers

The following table presents certain information regarding the Board Members and Officers of the Trust as of December 31, 2010. Each Board Member's year of birth is set forth in parentheses after his or her name. Unless otherwise noted, (i) each Board Member has engaged in the principal occupation(s) noted in the table for at least the most recent five years, although not necessarily in the same capacity; and (ii) the address of each Independent Board Member is c/o Paul K. Freeman, Independent Chairman, DWS Funds, PO Box 101833, Denver, CO 80250-1833. Except as otherwise noted below, the term of office for each Board Member is until the election and qualification of a successor, or until such Board Member sooner dies, resigns, is removed or as otherwise provided in the governing documents of the fund. Because the fund does not hold an annual meeting of shareholders, each Board Member will hold office for an indeterminate period. The Board Members may also serve in similar capacities with other funds in the fund complex. The Length of Time Served represents the year in which the Board Member joined the board of one or more DWS funds now overseen by the Board.

### Independent Board Members

| Name, Year of Birth, Position with the Fund and Length of Time Served[1] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Paul K. Freeman (1950)<br>Chairperson since 2009<br>Board Member since 1993 | Consultant, World Bank/Inter-American Development Bank; Executive and Governing Council of the Independent Directors Council (education committees); formerly, Project Leader, International Institute for Applied Systems Analysis (1998–2001); Chief Executive Officer, The Eric Group, Inc. (environmental insurance) (1986–1998) | 122 |
| John W. Ballantine (1946)<br>Board Member since 1999 | Retired; formerly, Executive Vice President and Chief Risk Management Officer, First Chicago NBD Corporation/The First National Bank of Chicago (1996–1998); Executive Vice President and Head of International Banking (1995–1996). Directorships: Healthways, Inc. (provider of disease and care management services); Portland General Electric (utility company); Stockwell Capital Investments PLC (private equity). Former Directorships: First Oak Brook Bancshares, Inc. and Oak Brook Bank; Prisma Energy International | 122 |
| Henry P. Becton, Jr. (1943)<br>Board Member since 1990 | Vice Chair and former President, WGBH Educational Foundation. Directorships: Association of Public Television Stations; Lead Director, Becton Dickinson and Company[3] (medical technology company); Lead Director, Belo Corporation[3] (media company); Public Radio International; Public Radio Exchange (PRX); The PBS Foundation. Former Directorships: Boston Museum of Science; American Public Television; Concord Academy; New England Aquarium; Mass. Corporation for Educational Telecommunications; Committee for Economic Development; Public Broadcasting Service | 122 |
| Dawn-Marie Driscoll (1946)<br>Board Member since 1987 | President, Driscoll Associates (consulting firm); Executive Fellow, Center for Business Ethics, Bentley University; formerly, Partner, Palmer & Dodge (1988–1990); Vice President of Corporate Affairs and General Counsel, Filene's (1978–1988). Directorships: Trustee of 22 open-end mutual funds managed by Sun Capital Advisers, Inc. (since 2007); Director of ICI Mutual Insurance Company (since 2007); Advisory Board, Center for Business Ethics, Bentley University; Trustee, Southwest Florida Community Foundation (charitable organization). Former Directorships: Investment Company Institute (audit, executive, nominating committees) and Independent Directors Council (governance, executive committees) | 122 |
| Keith R. Fox (1954)<br>Board Member since 1996 | Managing General Partner, Exeter Capital Partners (a series of private investment funds). Directorships: Progressive International Corporation (kitchen goods importer and distributor); BoxTop Media Inc. (advertising); The Kennel Shop (retailer); former Chairman, National Association of Small Business Investment Companies | 122 |
| Kenneth C. Froewiss (1945)<br>Board Member since 2001 | Adjunct Professor of Finance, NYU Stern School of Business (September 2009–present; Clinical Professor from 1997–September 2009); Member, Finance Committee, Association for Asian Studies (2002–present); Director, Mitsui Sumitomo Insurance Group (US) (2004–present); prior thereto, Managing Director, J.P. Morgan (investment banking firm) (until 1996) | 122 |
| Richard J. Herring (1946)<br>Board Member since 1990 | Jacob Safra Professor of International Banking and Professor, Finance Department, The Wharton School, University of Pennsylvania (since July 1972); Co-Director, Wharton Financial Institutions Center (since July 2000); Co-Chair, U.S. Shadow Financial Regulatory Committee; Executive Director, Financial Economists Roundtable; Director, Japan Equity Fund, Inc. (since September 2007), Thai Capital Fund, Inc. (since September 2007), Singapore Fund, Inc. (since September 2007); Independent Director of Barclays Bank Delaware (since September 2010). Formerly, Vice Dean and Director, Wharton Undergraduate Division (July 1995–June 2000); Director, Lauder Institute of International Management Studies (July 2000–June 2006) | 122 |
| William McClayton (1944)<br>Board Member since 2004+ | Private equity investor (since October 2009); previously, Managing Director, Diamond Management & Technology Consultants, Inc. (global consulting firm) (2001–2009); Directorship: Board of Managers, YMCA of Metropolitan Chicago; formerly: Senior Partner, Arthur Andersen LLP (accounting) (1966–2001); Trustee, Ravinia Festival | 122 |

| Name, Year of Birth, Position with the Fund and Length of Time Served[1] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Rebecca W. Rimel (1951)<br>Board Member since 1995 | President and Chief Executive Officer, The Pew Charitable Trusts (charitable organization) (1994 to present); Trustee, Thomas Jefferson Foundation (charitable organization) (1994 to present); Trustee, Executive Committee, Philadelphia Chamber of Commerce (2001–2007); Director, CardioNet, Inc.[2] (2009–present) (health care). Formerly, Executive Vice President, The Glenmede Trust Company (investment trust and wealth management) (1983–2004); Board Member, Investor Education (charitable organization) (2004–2005); Director, Viasys Health Care[2] (January 2007–June 2007); Trustee, Pro Publica (charitable organization) (2007–2010) | 122 |
| William N. Searcy, Jr. (1946)<br>Board Member since 1993 | Private investor since October 2003; Trustee of 22 open-end mutual funds managed by Sun Capital Advisers, Inc. (since October 1998). Formerly, Pension & Savings Trust Officer, Sprint Corporation[2] (telecommunications) (November 1989–September 2003) | 122 |
| Jean Gleason Stromberg (1943)<br>Board Member since 1997 | Retired. Formerly, Consultant (1997–2001); Director, Financial Markets US Government Accountability Office (1996–1997); Partner, Fulbright & Jaworski, L.L.P. (law firm) (1978–1996). Directorships: The William and Flora Hewlett Foundation. Former Directorships: Service Source, Inc., Mutual Fund Directors Forum (2002–2004), American Bar Retirement Association (funding vehicle for retirement plans) (1987–1990 and 1994–1996) | 122 |
| Robert H. Wadsworth (1940)<br>Board Member since 1999 | President, Robert H. Wadsworth & Associates, Inc. (consulting firm) (1983 to present); Director, The Phoenix Boys Choir Association | 125 |

## Interested Board Member and Officer[4]

| Name, Year of Birth, Position with the Trust/ Corporation and Length of Time Served[1,5] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Ingo Gefeke[7] (1967)<br>Board Member since 2010<br>Executive Vice President since 2010 | Managing Director[3], Deutsche Asset Management; Global Head of Distribution and Product Management, DWS Global Head of Trading and Securities Lending. Member of the Board of Directors of DWS Investment GmbH Frankfurt (since July 2009) and DWS Holding & Service GmbH Frankfurt (since January 2010); formerly, Global Chief Administrative Officer, Deutsche Asset Management (2004–2009); Global Chief Operating Officer, Global Transaction Banking, Deutsche Bank AG, New York (2001–2004); Chief Operating Officer, Global Banking Division Americas, Deutsche Bank AG, New York (1999–2001); Central Management, Global Banking Services, Deutsche Bank AG, Frankfurt (1998–1999); Relationship Management, Deutsche Bank AG, Tokyo, Japan (1997–1998) | 55 |

## Officers[4]

| Name, Year of Birth, Position with the Fund and Length of Time Served[5] | Principal Occupation(s) During Past 5 Years and Other Directorships Held |
|---|---|
| Michael G. Clark[6] (1965)<br>President, 2006–present | Managing Director[3], Deutsche Asset Management (2006–present); President of DWS family of funds; Director, ICI Mutual Insurance Company (since October 2007); formerly, Director of Fund Board Relations (2004–2006) and Director of Product Development (2000–2004), Merrill Lynch Investment Managers; Senior Vice President Operations, Merrill Lynch Asset Management (1999–2000) |
| John Millette[8] (1962)<br>Vice President and Secretary, 1999–present | Director[3], Deutsche Asset Management |
| Paul H. Schubert[6] (1963)<br>Chief Financial Officer, 2004–present<br>Treasurer, 2005–present | Managing Director[3], Deutsche Asset Management (since July 2004); formerly, Executive Director, Head of Mutual Fund Services and Treasurer for UBS Family of Funds (1998–2004); Vice President and Director of Mutual Fund Finance at UBS Global Asset Management (1994–1998) |
| Caroline Pearson[8] (1962)<br>Chief Legal Officer, April 2010–present | Managing Director[3], Deutsche Asset Management; formerly, Assistant Secretary for DWS family of funds (1997–2010) |
| Rita Rubin[9] (1970)<br>Assistant Secretary, 2009–present | Vice President and Counsel, Deutsche Asset Management (since October 2007); formerly, Vice President, Morgan Stanley Investment Management (2004–2007) |
| Paul Antosca[8] (1957)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management (since 2006); Vice President, The Manufacturers Life Insurance Company (U.S.A.) (1990–2006) |
| Jack Clark[8] (1967)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management (since 2007); formerly, Vice President, State Street Corporation (2002–2007) |

| Name, Year of Birth, Position with the Fund and Length of Time Served[5] | Principal Occupation(s) During Past 5 Years and Other Directorships Held |
|---|---|
| Diane Kenneally[8] (1966)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management |
| John Caruso[9] (1965)<br>Anti-Money Laundering Compliance Officer, 2010–present | Managing Director[3], Deutsche Asset Management |
| Robert Kloby[9] (1962)<br>Chief Compliance Officer, 2006–present | Managing Director[3], Deutsche Asset Management |

1 *The length of time served represents the year in which the Board Member joined the board of one or more DWS funds currently overseen by the Board.*

2 *A publicly held company with securities registered pursuant to Section 12 of the Securities Exchange Act of 1934.*

3 *Executive title, not a board directorship.*

4 *As a result of their respective positions held with the Advisor, these individuals are considered "interested persons" of the Advisor within the meaning of the 1940 Act. Interested persons receive no compensation from the fund.*

5 *The length of time served represents the year in which the officer was first elected in such capacity for one or more DWS funds.*

6 *Address: 100 Plaza One, Jersey City, NJ 07311.*

7 *Effective January 11, 2011, Mr. Gefeke, an interested Board Member and Executive Vice President, resigned from the fund's Board and as an officer.*

*The mailing address of Mr. Gefeke is 345 Park Avenue, New York, New York 10154. Mr. Gefeke was an interested Board Member of certain DWS funds by virtue of his positions with Deutsche Asset Management. As an interested person, Mr. Gefeke received no compensation from the fund.*

8 *Address: One Beacon Street, Boston, MA 02108.*

9 *Address: 60 Wall Street, New York, New York 10005.*

*The fund's Statement of Additional Information ("SAI") includes additional information about the Board Members. The SAI is available, without charge, upon request. If you would like to request a copy of the SAI, you may do so by calling the following toll-free number: (800) 728-3337.*

DWS Investments is part of Deutsche Bank's Asset Management division and, within the US, represents the retail asset management activities of Deutsche Bank AG, Deutsche Bank Trust Company Americas, Deutsche Investment Management Americas Inc. and DWS Trust Company.

The views expressed in this report reflect those of the portfolio managers only through the end of the period of the report as stated on the cover. The managers' views are subject to change at any time based on market and other conditions and should not be construed as a recommendation.

This information must be preceded or accompanied by a current prospectus.

Portfolio changes should not be considered recommendations for action by individual investors.

DWS Investments Distributors, Inc.
222 South Riverside Plaza
Chicago, IL 60606
(800) 621-1148

VS2BC-2 (2/11)

DWS INVESTMENTS
Deutsche Bank Group

DECEMBER 31, 2010

# ANNUAL REPORT

## DWS VARIABLE SERIES II

## DWS Core Fixed Income VIP

**This report must be preceded or accompanied by a prospectus. To obtain an additional prospectus or summary prospectus, if available, call (800) 728-3337 or your financial representative. We advise you to consider the Fund's objectives, risks, charges and expenses carefully before investing. The summary prospectus and prospectus contain this and other important information about the Fund. Please read the prospectus carefully before you invest.**

*Investments in variable insurance portfolios (VIPs) involve risk. Stocks may decline in value. Bond investments are subject to interest-rate and credit risks. When interest rates rise, bond prices generally fall. Credit risk refers to the ability of an issuer to make timely payments of principal and interest. Investing in derivatives entails special risks relating to liquidity, leverage and credit that may reduce returns and/or increased volatility. Investing in foreign securities, particularly those of emerging markets, presents certain risks, such as currency fluctuations, political and economic changes, and market risks. There are additional risks associated with investing in commodities, high-yield bonds, aggressive growth stocks, non-diversified/ concentrated funds and small- and mid-cap stocks which are more fully explained in the prospectuses. Please read the prospectus for more information.*

*DWS Investments is part of Deutsche Bank's Asset Management division and, within the US, represents the retail asset management activities of Deutsche Bank AG, Deutsche Bank Trust Company Americas, Deutsche Investment Management Americas Inc. and DWS Trust Company.*



DWS INVESTMENTS
Deutsche Bank Group

# Performance Summary

December 31, 2010

## DWS Core Fixed Income VIP

**All performance shown is historical, assumes reinvestment of all dividend and capital gain distributions and does not guarantee future results. Investment return and principal value fluctuate with changing market conditions so that, when redeemed, shares may be worth more or less than their original cost. Current performance may be lower or higher than the performance data quoted. Please contact your participating insurance company for the Fund's most recent month-end performance. Performance doesn't reflect charges and fees ("contract charges") associated with the separate account that invests in the Fund or any variable life insurance policy or variable annuity contract for which the Fund is an investment option. These charges and fees will reduce returns.**

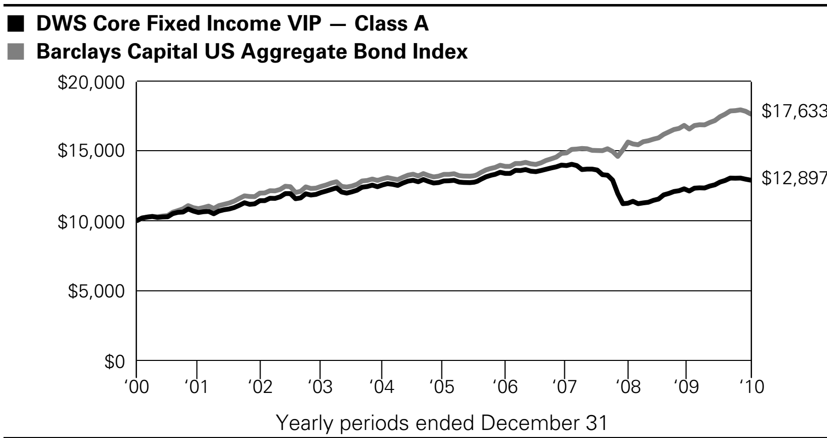
**The gross expense ratios of the Fund, as stated in the fee table of the prospectus dated May 1, 2010 is 0.59% for Class A shares, and may differ from the expense ratios disclosed in the Financial Highlights tables in this report.**

### Risk Considerations

Bond investments are subject to interest-rate and credit risks. When interest rates rise, bond prices generally fall. Credit risk refers to the ability of an issuer to make timely payments of principal and interest. In the current market environment, mortgage backed securities are experiencing increased volatility. See the prospectus for details.

Fund returns shown for the 3-year, 5-year and 10-year periods reflect a fee waiver and/or expense reimbursement. Without this waiver/reimbursement, returns would have been lower.

### Growth of an Assumed $10,000 Investment in DWS Core Fixed Income VIP




*Barclays Capital US Aggregate Bond Index is an unmanaged index representing domestic taxable investment-grade bonds, with index components for government and corporate securities, mortgage pass-through securities, and asset-backed securities with average maturities of one year or more.*

*Index returns, unlike fund returns, do not reflect any fees or expenses. It is not possible to invest directly into an index.*

### Comparative Results

| DWS Core Fixed Income VIP | | 1-Year | 3-Year | 5-Year | 10-Year |
|---|---|---|---|---|---|
| **Class A** | Growth of $10,000 | $10,651 | $9,256 | $10,053 | $12,897 |
| | Average annual total return | 6.51% | –2.54% | 0.10% | 2.58% |
| Barclays Capital US Aggregate Bond Index | Growth of $10,000 | $10,654 | $11,877 | $13,255 | $17,633 |
| | Average annual total return | 6.54% | 5.90% | 5.80% | 5.84% |

*The growth of $10,000 is cumulative.*

# Information About Your Fund's Expenses

## DWS Core Fixed Income VIP

As an investor of the Fund, you incur two types of costs: ongoing expenses and transaction costs. Ongoing expenses include management fees, and other Fund expenses. Examples of transaction costs include contract charges, redemption fees and account maintenance fees, which are not shown in this section. The following tables are intended to help you understand your ongoing expenses (in dollars) of investing in the Fund and to help you compare these expenses with the ongoing expenses of investing in other mutual funds. The example in the table is based on an investment of $1,000 invested at the beginning of the six-month period and held for the entire period (July 1, 2010 to December 31, 2010).

- **Actual Fund Return.** This helps you estimate the actual dollar amount of ongoing expenses (but not transaction costs) paid on a $1,000 investment in the Fund using the Fund's actual return during the period. To estimate the expenses you paid over the period, simply divide your account value by $1,000 (for example, an $8,600 account value divided by $1,000 = 8.6), then multiply the result by the number in the "Expenses Paid per $1,000" line under the share class you hold.
- **Hypothetical 5% Fund Return.** This helps you to compare your Fund's ongoing expenses (but not transaction costs) with those of other mutual funds using the Fund's actual expense ratio and a hypothetical rate of return of 5% per year before expenses. Examples using a 5% hypothetical Fund return may be found in the shareholder reports of other mutual funds. The hypothetical account values and expenses may not be used to estimate the actual ending account balance or expenses you paid for the period.

Please note that the expenses shown in these tables are meant to highlight your ongoing expenses only and do not reflect any transaction costs. The "Expenses Paid per $1,000" line of the tables is useful in comparing ongoing expenses only and will not help you determine the relative total expense of owning different funds. If these transaction costs had been included, your costs would have been higher.

**Expenses and Value of a $1,000 Investment** for the six months ended December 31, 2010

| **Actual Fund Return** | **Class A** |
|---|---|
| Beginning Account Value 7/1/10 | $1,000.00 |
| Ending Account Value 12/31/10 | $1,011.60 |
| Expenses Paid per $1,000* | $ 3.50 |
| **Hypothetical 5% Fund Return** | **Class A** |
| Beginning Account Value 7/1/10 | $1,000.00 |
| Ending Account Value 12/31/10 | $1,021.73 |
| Expenses Paid per $1,000* | $ 3.52 |

* *Expenses are equal to the Fund's annualized expense ratio, multiplied by the average account value over the period, multiplied by the number of days in the most recent six-month period, then divided by 365.*

| **Annualized Expense Ratio** | **Class A** |
|---|---|
| DWS Variable Series II — DWS Core Fixed Income VIP | .69% |

For more information, please refer to the Fund's prospectus.

These tables do not reflect charges and fees ("contract charges") associated with the separate account that invests in the Fund or any variable life insurance policy or variable annuity contract for which the Fund is an investment option.

# Management Summary

**December 31, 2010**

## DWS Core Fixed Income VIP

During the 12-month period ended December 31, 2010, the US Federal Reserve Board (the Fed) maintained the benchmark federal funds rate at near-zero levels and engaged in bond purchases designed to lower longer-term interest rates as it sought to stimulate economic growth.[1] Treasury yields fell for most of the year, before rising in the fourth quarter as market participants reacted to better economic data and the extension of Bush-era tax cuts. For the year, credit-sensitive sectors outperformed as investors sought yield in an environment of low interest rates. Corporate bonds benefited as corporate profits and balance sheets displayed strength throughout the period, with below-investment-grade issues leading returns. Among other credit sectors, commercial mortgage-backed securities were standout performers, despite an ongoing soft leasing environment in many markets.[2]

During the 12-month period, the Fund provided a total return of 6.51% (Class A shares, unadjusted for contract charges), compared with the 6.54% return of its benchmark, the Barclays Capital US Aggregate Bond Index.

The Fund's performance versus the benchmark continued to be driven principally by exposure to more credit-sensitive fixed-income sectors. Our overweighting of investment-grade corporate bonds was the leading contributor to returns, while a modest position in high-yield corporates added to performance as well.[3] On the downside, our underweighting early in the period of commercial mortgage-backed securities constrained returns. The Fund's positioning with respect to overall duration and interest rate exposure was essentially a neutral factor for performance. We are maintaining a somewhat conservative stance with respect to overall interest rate exposure as we monitor the impact of Fed bond purchases on inflation expectations and rates. In addition, we are closely watching economic data, which increasingly appear to indicate that the recovery is taking hold, a trend that would bode well for continued outperformance by credit-oriented sectors. Corporate balance sheets on the whole are in excellent condition and we are maintaining our overweighting of investment-grade corporate bonds. Our small high-yield position is being maintained as well, although we will not hesitate to move out of this sector if tighter spreads versus investment-grade issues change our risk/reward analysis.[4]

Kenneth R. Bowling, CFA
John Brennan
Jamie Guenther, CFA
Bruce Harley, CFA, CEBS
J. Kevin Horsley, CFA, CPA
J. Richard Robben, CFA
David Vignolo, CFA
Stephen Willer, CFA
*Portfolio Managers*

*Barclays Capital US Aggregate Bond Index is an unmanaged index representing domestic taxable investment-grade bonds, with index components for government and corporate securities, mortgage pass-through securities, and asset-backed securities with average maturities of one year or more.*

*Index returns assume reinvestment of dividends and, unlike fund returns, do not reflect any fees or expenses. It is not possible to invest directly into an index.*

1 *The federal funds rate is the interest rate, set by the US Federal Reserve Board, at which banks lend money to each other, usually on an overnight basis.*

2 *Commercial mortgage-backed securities (CMBS) are secured by loans on a commercial property.*

3 *"Overweight" means the Fund holds a higher weighting in a given sector or security than the benchmark. "Underweight" means the Fund holds a lower weighting.*

4 *"Spread" refers to the excess yield various bond sectors offer over Treasuries with similar maturities. When spreads widen, yield differences are increasing between bonds in the two sectors being compared. When spreads narrow, the opposite is true.*

*Portfolio management market commentary is as of December 31, 2010, and may not come to pass. This information is subject to change at any time based on market and other conditions. Past performance does not guarantee future results. Current and future portfolio holdings are subject to risk.*

# Portfolio Summary

## DWS Core Fixed Income VIP

| **Asset Allocation** (As a % of Net Assets) | **12/31/10** | **12/31/09** |
|---|---|---|
| Mortgage-Backed Securities Pass-Throughs | 30% | 39% |
| Government & Agency Obligations | 27% | 19% |
| Corporate Bonds | 23% | 22% |
| Commercial Mortgage-Backed Securities | 7% | 4% |
| Municipal Bonds and Notes | 7% | 6% |
| Cash Equivalents and Other Assets and Liabilities, net | 3% | 5% |
| Collateralized Mortgage Obligations | 2% | 4% |
| Asset-Backed | 1% | 1% |
| | 100% | 100% |

| **Quality** (Excludes Cash Equivalents and Securities Lending Collateral) | **12/31/10** | **12/31/09** |
|---|---|---|
| US Government and Agencies | 59% | 50% |
| AAA | 3% | 23% |
| AA | 7% | 5% |
| A | 13% | 10% |
| BBB | 15% | 11% |
| BB | 2% | — |
| Not Rated | 1% | 1% |
| | 100% | 100% |

| **Interest Rate Sensitivity** | **12/31/10** | **12/31/09** |
|---|---|---|
| Effective Maturity | 7.0 years | 6.8 years |
| Effective Duration | 5.0 years | 4.5 years |

*Asset allocation and Interest Rate Sensitivity are subject to change.*

*Effective maturity is the weighted average of the bonds held by the Fund taking into consideration any maturity shortening features.*

*Effective duration is an approximate measure of the Fund's sensitivity to interest rate changes taking into consideration any maturity shortening features.*

*The quality ratings represent the lower of Moody's Investors Service, Inc. ("Moody's") or Standard & Poor's Corporation ("S&P") credit ratings. The ratings of Moody's and S&P represent their opinions as to the quality of the securities they rate. Ratings are relative and subjective and are not absolute standards of quality. The Fund's credit quality does not remove market risk and is subject to change.*

*For more complete details about the Fund's investment portfolio, see page 6.*

Following the Fund's fiscal first and third quarter-end, a complete portfolio holdings listing is filed with the SEC on Form N-Q. The form will be available on the SEC's Web site at www.sec.gov, and it also may be reviewed and copied at the SEC's Public Reference Room in Washington, D.C. Information on the operation of the SEC's Public Reference Room may be obtained by calling (800) SEC-0330. The Fund's portfolio holdings are also posted on www.dws-investments.com from time to time. Please see the Fund's current prospectus for more information.

## DWS Core Fixed Income VIP

| | Principal Amount ($) | Value ($) |
|---|---|---|
| **Corporate Bonds 29.4%** | | |
| **Consumer Discretionary 4.0%** | | |
| AMC Entertainment, Inc., 8.75%, 6/1/2019 | 143,000 | 152,652 |
| CBS Corp., 5.9%, 10/15/2040 | 380,000 | 366,045 |
| Comcast Cable Holdings LLC, 10.125%, 4/15/2022 | 180,000 | 244,106 |
| DIRECTV Holdings LLC: | | |
| 3.125%, 2/15/2016 | 200,000 | 197,333 |
| 6.35%, 3/15/2040 | 312,000 | 328,215 |
| Home Depot, Inc.: | | |
| 5.4%, 9/15/2040 | 175,000 | 169,946 |
| 5.875%, 12/16/2036 | 75,000 | 78,011 |
| Lowe's Companies, Inc., 3.75%, 4/15/2021 | 300,000 | 290,043 |
| MGM Resorts International, 144A, 9.0%, 3/15/2020 | 500,000 | 550,000 |
| NBC Universal, Inc., 144A, 5.95%, 4/1/2041 | 172,000 | 171,982 |
| Time Warner, Inc.: | | |
| 6.2%, 3/15/2040 | 250,000 | 265,763 |
| 7.625%, 4/15/2031 | 250,000 | 303,921 |
| Yum! Brands, Inc.: | | |
| 3.875%, 11/1/2020 | 300,000 | 286,586 |
| 5.3%, 9/15/2019 | 100,000 | 105,917 |
| | | **3,510,520** |
| **Consumer Staples 3.0%** | | |
| Anheuser-Busch InBev Worldwide, Inc., 144A, 7.75%, 1/15/2019 | 400,000 | 497,739 |
| CVS Caremark Corp., 6.125%, 9/15/2039 | 825,000 | 881,478 |
| Kellogg Co., 4.0%, 12/15/2020 | 200,000 | 197,251 |
| Kraft Foods, Inc., 5.375%, 2/10/2020 | 825,000 | 887,922 |
| Kroger Co., 5.4%, 7/15/2040 | 150,000 | 142,172 |
| | | **2,606,562** |
| **Energy 4.2%** | | |
| DCP Midstream LLC, 144A, 9.75%, 3/15/2019 | 530,000 | 684,930 |
| Enterprise Products Operating LLC, 4.6%, 8/1/2012 | 500,000 | 524,768 |
| Kinder Morgan Energy Partners LP, 6.5%, 9/1/2039 | 300,000 | 309,910 |
| ONEOK Partners LP, 6.15%, 10/1/2016 | 321,000 | 360,760 |
| Plains All American Pipeline LP, 8.75%, 5/1/2019 | 750,000 | 930,746 |
| Weatherford International Ltd., 5.125%, 9/15/2020 | 550,000 | 547,268 |
| Williams Partners LP, 4.125%, 11/15/2020 | 360,000 | 340,988 |
| | | **3,699,370** |
| **Financials 11.5%** | | |
| American Express Co., 7.0%, 3/19/2018 | 700,000 | 815,341 |
| Bank of America Corp.: | | |
| 5.625%, 7/1/2020 | 410,000 | 417,992 |
| 5.65%, 5/1/2018 | 865,000 | 883,833 |
| 6.5%, 8/1/2016 | 80,000 | 86,807 |
| Citigroup, Inc., 5.375%, 8/9/2020 | 800,000 | 831,206 |
| Fifth Third Bancorp., 5.45%, 1/15/2017 | 390,000 | 398,644 |
| Ford Motor Credit Co., LLC, 8.0%, 6/1/2014 | 1,000,000 | 1,101,707 |
| General Electric Capital Corp., Series A, 5.625%, 5/1/2018 | 600,000 | 654,308 |
| Hartford Financial Services Group, Inc., 5.95%, 10/15/2036 | 270,000 | 254,727 |
| JPMorgan Chase & Co., 5.125%, 9/15/2014 | 1,000,000 | 1,064,071 |
| KeyBank NA, 5.7%, 11/1/2017 | 300,000 | 305,505 |
| Lincoln National Corp., 8.75%, 7/1/2019 | 350,000 | 437,797 |
| MetLife, Inc., 7.717%, 2/15/2019 | 395,000 | 484,954 |
| Morgan Stanley, Series F, 6.0%, 4/28/2015 | 490,000 | 530,671 |
| National Rural Utilities Cooperative Finance Corp., 10.375%, 11/1/2018 | 200,000 | 275,885 |
| PNC Funding Corp., 5.25%, 11/15/2015 | 450,000 | 481,587 |
| Prudential Financial, Inc.: | | |
| Series B, 5.1%, 9/20/2014 | 130,000 | 139,642 |
| 6.2%, 1/15/2015 | 90,000 | 99,253 |
| 7.375%, 6/15/2019 | 50,000 | 58,952 |
| The Goldman Sachs Group, Inc., 6.0%, 6/15/2020 | 550,000 | 594,365 |
| Travelers Companies, Inc., 5.35%, 11/1/2040 | 185,000 | 182,273 |
| | | **10,099,520** |
| **Health Care 1.9%** | | |
| Express Scripts, Inc.: | | |
| 6.25%, 6/15/2014 | 205,000 | 229,182 |
| 7.25%, 6/15/2019 | 405,000 | 479,367 |
| Laboratory Corp. of America Holdings, 4.625%, 11/15/2020 | 275,000 | 272,520 |
| Medco Health Solutions, Inc.: | | |
| 4.125%, 9/15/2020 | 125,000 | 120,866 |
| 7.125%, 3/15/2018 | 500,000 | 586,748 |
| | | **1,688,683** |
| **Industrials 0.8%** | | |
| CSX Corp.: | | |
| 6.15%, 5/1/2037 | 250,000 | 268,791 |
| 6.25%, 3/15/2018 | 380,000 | 435,921 |
| | | **704,712** |
| **Materials 1.5%** | | |
| ArcelorMittal, 6.125%, 6/1/2018 | 500,000 | 532,744 |
| Corporacion Nacional del Cobre de Chile, 144A, 3.75%, 11/4/2020 | 550,000 | 521,144 |
| Dow Chemical Co., 4.25%, 11/15/2020 | 285,000 | 273,001 |
| | | **1,326,889** |
| **Telecommunication Services 1.6%** | | |
| American Tower Corp.: | | |
| 5.05%, 9/1/2020 | 550,000 | 540,889 |
| 7.25%, 5/15/2019 | 250,000 | 282,508 |
| Frontier Communications Corp., 7.875%, 4/15/2015 | 500,000 | 546,250 |
| | | **1,369,647** |

*The accompanying notes are an integral part of the financial statements.*

| | Principal Amount ($) | Value ($) |
|---|---|---|
| **Utilities 0.9%** | | |
| DTE Energy Co., 7.625%, 5/15/2014 | 148,000 | 170,588 |
| FirstEnergy Solutions Corp., 6.8%, 8/15/2039 | 292,000 | 283,007 |
| Sempra Energy, 6.5%, 6/1/2016 | 290,000 | 336,664 |
| | | **790,259** |
| **Total Corporate Bonds** (Cost $24,622,597) | | **25,796,162** |

## Mortgage-Backed Securities Pass-Throughs 38.0%

| | Principal Amount ($) | Value ($) |
|---|---|---|
| Federal Home Loan Mortgage Corp.: | | |
| 4.0%, 8/1/2039 | 1,276,547 | 1,269,616 |
| 6.0%, with various maturities from 12/1/2034 until 3/1/2038 | 788,217 | 857,877 |
| Federal National Mortgage Association: | | |
| 3.274%*, 8/1/2037 | 201,551 | 211,112 |
| 3.5%, 7/1/2025 (a) | 4,675,000 | 4,708,602 |
| 4.0%, with various maturities from 9/1/2039 until 9/1/2040 (a) | 5,361,893 | 5,336,903 |
| 4.5%, 10/1/2033 | 412,900 | 426,755 |
| 5.0%, 8/1/2040 | 295,592 | 310,648 |
| 5.152%*, 9/1/2038 | 161,891 | 171,859 |
| 5.5%, with various maturities from 12/1/2032 until 9/1/2036 (a) | 10,439,727 | 11,183,444 |
| 6.0%, with various maturities from 4/1/2024 until 8/1/2035 (a) | 4,208,503 | 4,586,910 |
| 6.5%, with various maturities from 3/1/2017 until 4/1/2037 | 1,050,961 | 1,169,493 |
| 8.0%, 9/1/2015 | 12,340 | 13,379 |
| Government National Mortgage Association: | | |
| 4.5%, 6/1/2039 (a) | 1,000,000 | 1,038,359 |
| 5.0%, 4/1/2038 (a) | 1,000,000 | 1,063,203 |
| 5.5%, 3/1/2036 (a) | 1,000,000 | 1,080,703 |
| **Total Mortgage-Backed Securities Pass-Throughs** (Cost $33,044,315) | | **33,428,863** |

## Asset-Backed 1.4%

### Credit Card Receivables

| | Principal Amount ($) | Value ($) |
|---|---|---|
| Citibank Omni Master Trust, "A8", Series 2009-A8, 144A, 2.36%*, 5/16/2016 (Cost $1,215,844) | 1,200,000 | **1,214,872** |

## Commercial Mortgage-Backed Securities 9.2%

| | Principal Amount ($) | Value ($) |
|---|---|---|
| Banc of America Commercial Mortgage, Inc.: | | |
| "A2", Series 2007-2, 5.634%, 4/10/2049 | 325,000 | 336,967 |
| "A4", Series 2007-4, 5.742%*, 2/10/2051 | 750,000 | 798,887 |
| Bear Stearns Commercial Mortgage Securities, Inc., "A4", Series 2007-PW18, 5.7%, 6/13/2050 | 1,923,000 | 2,003,645 |
| Citigroup/Deutsche Bank Commercial Mortgage Trust, "A4", Series 2006-CD2, 5.347%*, 1/15/2046 | 250,000 | 268,300 |
| Greenwich Capital Commercial Funding Corp., "A4", Series 2006-GG7, 5.883%*, 7/10/2038 | 525,000 | 572,774 |
| JPMorgan Chase Commercial Mortgage Securities Corp.: | | |
| "A4", Series 2006-LDP7, 5.872%*, 4/15/2045 | 600,000 | 656,165 |
| "A4", Series 2007-LD12, 5.882%, 2/15/2051 | 925,000 | 979,348 |
| LB-UBS Commercial Mortgage Trust: | | |
| "A3", Series 2006-C7, 5.347%, 11/15/2038 | 400,000 | 422,904 |
| "A4", Series 2007-C6, 5.858%, 7/15/2040 | 1,000,000 | 1,050,670 |
| Merrill Lynch Mortgage Trust, "ASB", Series 2007-C1, 5.826%*, 6/12/2050 | 900,000 | 967,442 |
| **Total Commercial Mortgage-Backed Securities** (Cost $7,455,238) | | **8,057,102** |

## Collateralized Mortgage Obligations 2.4%

| | Principal Amount ($) | Value ($) |
|---|---|---|
| FDIC Structured Sale Guaranteed Notes, "1A", Series 2010-S1, 144A, 0.811%*, 2/25/2048 | 702,680 | 703,783 |
| Federal National Mortgage Association, "QD", Series 2005-29, 5.0%, 8/25/2033 | 435,000 | 465,656 |
| MASTR Alternative Loans Trust, "5A1", Series 2005-1, 5.5%, 1/25/2020 | 319,006 | 327,165 |
| NCUA Guaranteed Notes, "1A", Series 2010-R1, 0.716%*, 10/7/2020 | 582,325 | 581,598 |
| **Total Collateralized Mortgage Obligations** (Cost $2,041,517) | | **2,078,202** |

## Government & Agency Obligations 33.8%

### Sovereign Bonds 0.6%

| | Principal Amount ($) | Value ($) |
|---|---|---|
| Republic of Poland, 6.375%, 7/15/2019 | 500,000 | **560,105** |

### US Treasury Obligations 33.2%

| | Principal Amount ($) | Value ($) |
|---|---|---|
| US Treasury Bill, 0.185%**, 3/17/2011 (b) | 320,000 | 319,929 |
| US Treasury Bonds: | | |
| 4.75%, 2/15/2037 | 2,000,000 | 2,149,376 |
| 5.375%, 2/15/2031 (c) | 2,500,000 | 2,918,360 |
| US Treasury Notes: | | |
| 1.75%, 1/31/2014 (c) | 18,700,000 | 19,091,540 |
| 3.625%, 2/15/2020 | 4,500,000 | 4,670,154 |
| | | **29,149,359** |
| **Total Government & Agency Obligations** (Cost $29,710,921) | | **29,709,464** |

## Municipal Bonds and Notes 8.1%

| | Principal Amount ($) | Value ($) |
|---|---|---|
| California, University Revenues, Build America Bonds, 5.946%, 5/15/2045 | 180,000 | 167,951 |
| Chicago, IL, Transit Authority, Sales Tax Receipts Revenue, Build America Bonds, Series B, 6.2%, 12/1/2040 (d) | 265,000 | 244,004 |
| Glendale, AZ, Municipal Property Corp., Excise Tax Revenue, Series B, 6.157%, 7/1/2033, INS: AGMC | 420,000 | 401,898 |

*The accompanying notes are an integral part of the financial statements.*

| | Principal Amount ($) | Value ($) |
|---|---|---|
| Jicarilla, NM, Sales & Special Tax Revenue, Apache Nation Revenue, 144A, 5.2%, 12/1/2013 | 575,000 | 569,330 |
| Kentucky, Asset/Liability Commission, General Fund Revenue, 3.165%, 4/1/2018 | 775,000 | 757,454 |
| Louisville & Jefferson County, KY, Metropolitan Sewer District & Drain Systems, Build America Bonds, 6.25%, 5/15/2043 | 200,000 | 201,372 |
| Miami-Dade County, FL, Educational Facilities Authority Revenue, University of Miami, Series B, 6.1%, 4/1/2015 | 825,000 | 876,628 |
| Michigan, Western Michigan University Revenue, 4.41%, 11/15/2014, INS: AMBAC (d) | 620,000 | 630,187 |
| Nashville & Davidson County, TN, Metropolitan Government, Convention Center Authority Revenue, Build America Bonds, Series A2, 7.431%, 7/1/2043 | 250,000 | 266,540 |
| New Jersey, Economic Development Authority Revenue, Series B, 6.5%, 11/1/2014, INS: AGC | 585,000 | 667,403 |
| New Jersey, State Educational Facilities Authority Revenue, NJ City University, Series F, 6.85%, 7/1/2036, INS: AGC | 395,000 | 428,220 |
| Newark, NJ, Pension Obligation, 5.853%, 4/1/2022, INS: AGMC | 865,000 | 857,751 |
| Pennsylvania, State General Obligation, First Series, 5.25%, 2/1/2014, INS: NATL | 385,000 | 431,781 |
| Virginia, College Building Authority, Educational Facilities Revenue, 21st Century College, Series B, 5.0%, 2/1/2014 | 570,000 | 633,864 |
| **Total Municipal Bonds and Notes** (Cost $7,054,531) | | **7,134,383** |

| | Shares | Value ($) |
|---|---|---|

## Securities Lending Collateral 21.0%

| | | |
|---|---|---|
| Daily Assets Fund Institutional, 0.27% (e) (f) (Cost $18,449,851) | 18,449,851 | **18,449,851** |

## Cash Equivalents 3.2%

| | | |
|---|---|---|
| Central Cash Management Fund, 0.19% (e) (Cost $2,798,238) | 2,798,238 | **2,798,238** |

| | % of Net Assets | Value ($) |
|---|---|---|
| **Total Investment Portfolio** (Cost $126,393,052)† | 146.5 | **128,667,137** |
| **Other Assets and Liabilities, Net** | (46.5) | **(40,818,885)** |
| **Net Assets** | 100.0 | **87,848,252** |

* *These securities are shown at their current rate as of December 31, 2010. Floating rate securities' yields vary with a designated market index or market rate, such as the coupon-equivalent of the US Treasury bill rate.*

** *Annualized yield at time of purchase; not a coupon rate.*

† *The cost for federal income tax purposes was $126,399,437. At December 31, 2010, net unrealized appreciation for all securities based on tax cost was $2,267,700. This consisted of aggregate gross unrealized appreciation for all securities in which there was an excess of value over tax cost of $3,032,557 and aggregate gross unrealized depreciation for all securities in which there was an excess of tax cost over value of $764,857.*

(a) *Delayed delivery security included.*

(b) *At December 31, 2010, this security has been pledged, in whole or in part, to cover initial margin requirements for futures closed December 31, 2010.*

(c) *All or a portion of these securities were on loan (see Notes to Financial Statements). The value of all securities loaned at December 31, 2010 amounted to $17,977,097, which is 20.5% of net assets.*

(d) *Taxable issue.*

(e) *Affiliated fund managed by Deutsche Investment Management Americas Inc. The rate shown is the annualized seven-day yield at period end.*

(f) *Represents collateral held in connection with securities lending. Income earned by the Fund is net of borrower rebates.*

*144A: Security exempt from registration under Rule 144A of the Securities Act of 1933. These securities may be resold in transactions exempt from registration, normally to qualified institutional buyers.*

*AGC: Assured Guaranty Corp.*

*AGMC: Assured Guaranty Municipal Corp.*

*AMBAC: Ambac Financial Group, Inc.*

*FDIC: Federal Deposit Insurance Corp.*

*INS: Insured*

*NATL: National Public Finance Guarantee Corp.*

*Included in the portfolio are investments in mortgage or asset-backed securities which are interests in separate pools of mortgages or assets. Effective maturities of these investments may be shorter than stated maturities due to prepayments. Some separate investments in the Federal Home Loan Mortgage Corp. and Federal National Mortgage Association issues which have similar coupon rates have been aggregated for presentation purposes in the investment portfolio.*

*The accompanying notes are an integral part of the financial statements.*

*At December 31, 2010, open futures contracts sold were as follows:*

| Securities | Currency | Expiration Date | Contracts | Notional Value ($) | Unrealized Appreciation ($) |
|---|---|---|---|---|---|
| 10 Year US Treasury Note | USD | 3/22/2011 | 114 | 13,729,875 | 434,891 |
| 30 Year US Treasury Bond | USD | 3/22/2011 | 40 | 4,885,000 | 182,500 |
| **Total unrealized appreciation** | | | | | **$ 617,391** |

| Currency Abbreviation | |
|---|---|
| USD | United States Dollar |

*For information on the Fund's policy and additional disclosures regarding futures contracts, please refer to Note B in the accompanying Notes to Financial Statements.*

## Fair Value Measurements

*Various inputs are used in determining the value of the Fund's investments. These inputs are summarized in three broad levels. Level 1 includes quoted prices in active markets for identical securities. Level 2 includes other significant observable inputs (including quoted prices for similar securities, interest rates, prepayment speeds, and credit risk). Level 3 includes significant unobservable inputs (including the Fund's own assumptions in determining the fair value of investments). The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities.*

*The following is a summary of the inputs used as of December 31, 2010 in valuing the Fund's investments. For information on the Fund's policy regarding the valuation of investments, please refer to the Security Valuation section of Note A in the accompanying Notes to Financial Statements.*

| Assets | Level 1 | Level 2 | Level 3 | Total |
|---|---|---|---|---|
| Fixed Income (g) | | | | |
| Corporate Bonds | $ — | $ 25,796,162 | $ — | $ 25,796,162 |
| Mortgage-Backed Securities Pass-Throughs | — | 33,428,863 | — | 33,428,863 |
| Asset-Backed | — | 1,214,872 | — | 1,214,872 |
| Commercial Mortgage-Backed Securities | — | 8,057,102 | — | 8,057,102 |
| Collateralized Mortgage Obligations | — | 2,078,202 | — | 2,078,202 |
| Government & Agency Obligations | — | 29,389,535 | — | 29,389,535 |
| Municipal Bonds and Notes | — | 7,134,383 | — | 7,134,383 |
| Short-Term Investments (g) | 21,248,089 | 319,929 | — | 21,568,018 |
| Derivatives (h) | 617,391 | — | — | 617,391 |
| **Total** | **$ 21,865,480** | **$ 107,419,048** | **$ —** | **$ 129,284,528** |

*There have been no significant transfers between Level 1 and Level 2 fair value measurements during the year ended December 31, 2010.*

(g) *See Investment Portfolio for additional detailed categorizations.*

(h) *Derivatives include unrealized appreciation (depreciation) on open futures contracts.*

*The accompanying notes are an integral part of the financial statements.*

# Statement of Assets and Liabilities

as of December 31, 2010

| Assets | | |
|---|---|---|
| Investments: | | |
| Investments in unaffiliated securities, at value (cost $105,144,963) — including $17,977,097 of securities loaned | $ | 107,419,048 |
| Investment in Daily Assets Fund Institutional (cost $18,449,851)* | | 18,449,851 |
| Investment in Central Cash Management Fund (cost $2,798,238) | | 2,798,238 |
| Total investments, at value (cost $126,393,052) | | 128,667,137 |
| Cash | | 25,746 |
| Receivable for Fund shares sold | | 16,068 |
| Interest receivable | | 890,390 |
| Other assets | | 608 |
| Total assets | | 129,599,949 |

| Liabilities | | |
|---|---|---|
| Payable upon return of securities loaned | | 18,449,851 |
| Payable for investments purchased — delayed delivery securities | | 23,054,042 |
| Payable for daily variation margin on open futures contracts | | 96,654 |
| Payable for Fund shares redeemed | | 37,396 |
| Accrued management fee | | 41,520 |
| Other accrued expenses and payables | | 72,234 |
| Total liabilities | | 41,751,697 |
| **Net assets, at value** | **$** | **87,848,252** |

| Net Assets Consist of | | |
|---|---|---|
| Undistributed net investment income | | 2,279,173 |
| Net unrealized appreciation (depreciation) on: | | |
| Investments | | 2,274,085 |
| Futures | | 617,391 |
| Accumulated net realized gain (loss) | | (54,331,570) |
| Paid-in capital | | 137,009,173 |
| **Net assets, at value** | **$** | **87,848,252** |
| **Class A** | | |
| **Net Asset Value,** offering and redemption price per share ($87,848,252 ÷ 10,037,687 outstanding shares of beneficial interest, no par value, 24,742,586 shares authorized) | **$** | **8.75** |

* *Represents collateral on securities loaned.*

# Statement of Operations

for the year ended December 31, 2010

| Investment Income | | |
|---|---|---|
| Income: | | |
| Interest | $ | 3,181,169 |
| Income distributions — Central Cash Management Fund | | 36,587 |
| Securities lending income, including income from Daily Assets Fund Institutional, net of borrower rebates | | 6,363 |
| Total income | | 3,224,119 |
| Expenses: | | |
| Management fee | | 482,684 |
| Administration fee | | 96,537 |
| Services to shareholders | | 2,357 |
| Distribution service fee (Class B) | | 14 |
| Record keeping fees (Class B) | | 799 |
| Custodian fee | | 11,701 |
| Legal fees | | 9,744 |
| Audit and tax fees | | 48,504 |
| Trustees' fees and expenses | | 5,860 |
| Reports to shareholders | | 23,774 |
| Other | | 14,233 |
| Total expenses before expense reductions | | 696,207 |
| Expense reductions | | (809) |
| Total expenses after expense reductions | | 695,398 |
| **Net investment income (loss)** | | **2,528,721** |

| Realized and Unrealized Gain (Loss) | | |
|---|---|---|
| Net realized gain (loss) from: | | |
| Investments | | 4,576,974 |
| Futures | | (504,977) |
| | | 4,071,997 |
| Change in net unrealized appreciation (depreciation) on: | | |
| Investments | | (992,270) |
| Futures | | 534,420 |
| | | (457,850) |
| **Net gain (loss)** | | **3,614,147** |
| **Net increase (decrease) in net assets resulting from operations** | **$** | **6,142,868** |

*The accompanying notes are an integral part of the financial statements.*

# Statement of Changes in Net Assets

| Increase (Decrease) in Net Assets | Years Ended December 31, 2010 | 2009 |
|---|---|---|
| Operations: | | |
| Net investment income (loss) | $ 2,528,721 | $ 5,563,396 |
| Net realized gain (loss) | 4,071,997 | (34,052,154) |
| Change in net unrealized appreciation (depreciation) | (457,850) | 38,146,016 |
| Net increase (decrease) in net assets resulting from operations | 6,142,868 | 9,657,258 |
| Distributions to shareholders from: | | |
| Net investment income: | | |
| Class A | (5,749,285) | (8,879,629) |
| Class B | — | (2,500,347) |
| Total distributions | (5,749,285) | (11,379,976) |
| Fund share transactions: | | |
| **Class A** | | |
| Proceeds from shares sold | 26,314,018 | 10,272,493 |
| Shares converted* | 53,582 | — |
| Reinvestment of distributions | 5,749,285 | 8,879,629 |
| Payments for shares redeemed | (38,312,024) | (33,814,458) |
| Net increase (decrease) in net assets from Class A share transactions | (6,195,139) | (14,662,336) |
| **Class B** | | |
| Proceeds from shares sold | 785 | 2,365,047 |
| Shares converted* | (53,582) | — |
| Reinvestment of distributions | — | 2,500,347 |
| Payments for shares redeemed | (78) | (36,868,329) |
| Net increase (decrease) in net assets from Class B share transactions | (52,875) | (32,002,935) |
| **Increase (decrease) in net assets** | (5,854,431) | (48,387,989) |
| Net assets at beginning of period | 93,702,683 | 142,090,672 |
| Net assets at end of period (including undistributed net investment income of $2,279,173 and $5,499,737, respectively) | **$ 87,848,252** | **$ 93,702,683** |

| **Other Information** | | |
|---|---|---|
| **Class A** | | |
| Shares outstanding at beginning of period | 10,676,602 | 12,351,718 |
| Shares sold | 3,026,894 | 1,188,797 |
| Shares converted* | 5,994 | — |
| Shares issued to shareholders in reinvestment of distributions | 681,204 | 1,088,190 |
| Shares redeemed | (4,353,007) | (3,952,103) |
| Net increase (decrease) in Class A shares | (638,915) | (1,675,116) |
| Shares outstanding at end of period | **10,037,687** | **10,676,602** |
| **Class B** | | |
| Shares outstanding at beginning of period | 5,948 | 3,628,194 |
| Shares sold | 89 | 275,459 |
| Shares converted* | (6,028) | — |
| Shares issued to shareholders in reinvestment of distributions | (9) | 305,666 |
| Shares redeemed | — | (4,203,371) |
| Net increase (decrease) in Class B shares | (5,948) | (3,622,246) |
| Shares outstanding at end of period | **—** | **5,948** |

* *On February 5, 2010, Class B shares converted into Class A shares.*

*The accompanying notes are an integral part of the financial statements.*

# Financial Highlights

## Class A

| Years Ended December 31, | 2010 | 2009 | 2008 | 2007 | 2006 |
|---|---|---|---|---|---|
| **Selected Per Share Date** | | | | | |
| **Net asset value, beginning of period** | **$ 8.77** | **$ 8.90** | **$11.82** | **$11.86** | **$11.81** |
| *Income (loss) from investment operations:* | | | | | |
| Net investment income[a] | .23 | .39 | .57 | .56 | .53 |
| Net realized and unrealized gain (loss) | .32 | .24 | (2.72) | (.08) | (.05) |
| **Total from investment operations** | .55 | .63 | (2.15) | .48 | .48 |
| *Less distributions from:* | | | | | |
| Net investment income | (.57) | (.76) | (.77) | (.52) | (.43) |
| Net realized gains | — | — | — | — | (.00)* |
| **Total distributions** | (.57) | (.76) | (.77) | (.52) | (.43) |
| **Net asset value, end of period** | **$ 8.75** | **$ 8.77** | **$ 8.90** | **$11.82** | **$11.86** |
| Total Return (%) | 6.51 | 7.72[c] | (19.33)[b] | 4.17 | 4.26 |
| **Ratios to Average Net Assets and Supplemental Data** | | | | | |
| Net assets, end of period ($ millions) | 88 | 94 | 110 | 186 | 277 |
| Ratio of expenses before expense reductions (%) | .72 | .59 | .70 | .66 | .68 |
| Ratio of expenses after expense reductions (%) | .72 | .59 | .70 | .66 | .68 |
| Ratio of net investment income (%) | 2.62 | 4.50 | 5.36 | 4.78 | 4.56 |
| Portfolio turnover rate (%) | 356 | 222 | 215 | 209 | 198 |

a *Based on average shares outstanding during the period.*

b *Total returns would have been lower had certain expenses not been reduced.*

c *Includes a reimbursement from the Advisor to reimburse the effect of losses incurred as the result of certain operation errors during the period. Excluding this reimbursement, total return would have been 0.02% lower.*

* *Amount is less than $.005.*

# Notes to Financial Statements

## A. Organization and Significant Accounting Policies

DWS Variable Series II (the "Trust") is registered under the Investment Company Act of 1940, as amended (the "1940 Act"), as an open-end management investment company organized as a Massachusetts business trust. The Trust offers seventeen funds (hereinafter referred to individually as "Fund" or collectively as "Funds"). The Fund is classified as a diversified open-end management investment company.

**Multiple Classes of Shares of Beneficial Interest.** Certain Funds of the Trust offer two classes of shares (Class A shares and Class B shares). Effective February 5, 2010, Class B shares of the Fund were converted into the Class A shares of the same Fund. Sales of Class B shares are subject to record keeping fees up to 0.15% and Rule 12b-1 fees under the 1940 Act equal to an annual rate of 0.25%, of the average daily net assets of the Class B shares of the applicable Fund. Class A shares are not subject to such fees.

Investment income, realized and unrealized gains and losses, and certain fund-level expenses and expense reductions, if any, are borne pro rata on the basis of relative net assets by the holders of all classes of shares except that each class bears certain expenses unique to that class (including the applicable Rule 12b-1 fee and record keeping fees). Differences in class-level expenses may result in payment of different per share dividends by class. All shares have equal rights with respect to voting subject to class-specific arrangements.

The Trust's financial statements are prepared in accordance with accounting principles generally accepted in the United States of America which require the use of management estimates. Actual results could differ from those estimates. The policies described below are followed consistently by the Trust in the preparation of its financial statements.

**Security Valuation.** Investments are stated at value determined as of the close of regular trading on the New York Stock Exchange on each day the exchange is open for trading.

Various inputs are used in determining the value of the Fund's investments. These inputs are summarized in three broad levels. Level 1 includes quoted prices in active markets for identical securities. Level 2 includes other significant observable inputs (including quoted prices for similar securities, interest rates, prepayment speeds, and credit risk). Level 3 includes significant unobservable inputs (including the Fund's own assumptions in determining the fair value of investments). The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities.

Debt securities are valued by independent pricing services approved by the Fund's Board. If the pricing services are unable to provide valuations, securities are valued at the most recent bid quotation or evaluated price, as applicable, obtained from one or more broker-dealers. Such services may use various pricing techniques which take into account appropriate factors such as yield, quality, coupon rate, maturity, type of issue, trading characteristics and other data, as well as broker quotes. These securities are generally categorized as Level 2.

Futures contracts are generally valued at the settlement prices established each day on the exchange on which they are traded and are categorized as Level 1.

Money market instruments purchased with an original or remaining maturity of sixty days or less, maturing at par, are valued at amortized cost, which approximates value, and are categorized as Level 2. Investments in open-end investment companies are valued at their net asset value each business day and are categorized as Level 1.

Securities and other assets for which market quotations are not readily available or for which the above valuation procedures are deemed not to reflect fair value are valued in a manner that is intended to reflect their fair value as determined in accordance with procedures approved by the Board and are generally categorized as Level 3. In accordance with the Fund's valuation procedures, factors used in determining value may include, but are not limited to, the type of the security; the size of the holding; the initial cost of the security; the existence of any contractual restrictions on the security's disposition; the price and extent of public trading in similar securities of the issuer or of comparable companies; quotations or evaluated prices from broker-dealers and/or pricing services; information obtained from the issuer, analysts, and/or the appropriate stock exchange (for exchange-traded securities); an analysis of the company's or issuer's financial statements; an evaluation of the forces that influence the issuer and the market(s) in which the security is purchased and sold and with respect to debt securities; the maturity, coupon, creditworthiness, currency denomination and the movement of the market in which the security is normally traded. The value determined under these procedures may differ from published values for the same securities.

Disclosure about the classification of fair value measurements is included in a table following the Fund's Investment Portfolio.

**Securities Lending.** The Fund lends securities to certain financial institutions. The Fund retains beneficial ownership of the securities it has loaned and continues to receive interest and dividends paid by the issuer of securities and to participate in any changes in their market value. The Fund requires the borrowers of the securities to maintain collateral with the Fund consisting of either cash or liquid, unencumbered assets having a value at least equal to the value of the securities loaned. When the collateral falls below specified amounts, the lending agent will use its best effort to obtain additional collateral on the next business day to meet required amounts under the security lending agreement. The Fund may invest the cash collateral into a joint trading account in an affiliated money market fund pursuant to Exemptive Orders issued by the SEC. The Fund receives compensation for lending its securities either in the form of fees or by earning interest on invested cash collateral net of borrower rebates and fees paid to a lending agent. Either the Fund or the borrower may terminate the loan. There may be risks of delay and costs in recovery of securities or even loss of rights in the collateral should the borrower of the securities fail financially. The Fund is also subject to all investment risks associated with the reinvestment of any cash collateral received, including, but not limited to, interest rate, credit and liquidity risk associated with such investments.

**Mortgage Dollar Rolls.** The Fund may enter into mortgage dollar rolls in which the Fund sells to a bank or broker/dealer (the "counterparty") mortgage-backed securities for delivery in the current month and simultaneously contracts to repurchase similar, but not identical, securities on a fixed date. The counterparty receives all principal and interest payments, including prepayments, made on the security while it is the holder. The Fund receives compensation as consideration for entering into the commitment to repurchase. The compensation is paid in the form of a lower price for the security upon its repurchase, or alternatively, a fee. Mortgage dollar rolls may be renewed with a new sale and repurchase price and a cash settlement made at each renewal without physical delivery of the securities subject to the contract.

Certain risks may arise upon entering into mortgage dollar rolls from the potential inability of counterparties to meet the terms of their commitments. Additionally, the value of such securities may change adversely before the Fund is able to repurchase them. There can be no assurance that the Fund's use of the cash that it receives from a mortgage dollar roll will provide a return that exceeds its costs.

**When-Issued/Delayed Delivery Securities.** The Fund may purchase securities with delivery or payment to occur at a later date beyond the normal settlement period. At the time the Fund enters into a commitment to purchase a security, the transaction is recorded and the value of the security is reflected in the net asset value. The price of such security and the date when the security will be delivered and paid for are fixed at the time the transaction is negotiated. The value of the security may vary with market fluctuations. No interest accrues to the Fund until payment takes place. At the time the Fund enters into this type of transaction it is required to segregate cash or other liquid assets at least equal to the amount of the commitment.

Certain risks may arise upon entering into when-issued or delayed delivery securities from the potential inability of counterparties to meet the terms of their contracts or if the issuer does not issue the securities due to political, economic, or other factors. Additionally, losses may arise due to changes in the value of the underlying securities.

**Taxes.** The Fund's policy is to comply with the requirements of the Internal Revenue Code, as amended, which are applicable to regulated investment companies and to distribute all of its taxable income to its shareholders.

At December 31, 2010, the Fund had an approximate net tax basis capital loss carryforward which may be applied against any realized net taxable capital gains of each succeeding year until fully utilized or until the following expiration dates, whichever occurs first:

| Fund | Capital Loss Carryforward ($) | Expiration Date | Capital Loss Carryforward Utilized ($) |
|---|---|---|---|
| DWS Core Fixed Income VIP | 5,512,000 | 12/31/2016 | 4,494,000 |
| | 48,195,000 | 12/31/2017 | |

The Fund has reviewed the tax positions for the open tax years as of December 31, 2010 and has determined that no provision for income tax is required in the Fund's financial statements. The Fund's federal tax returns for the prior three fiscal years remain open subject to examination by the Internal Revenue Service.

**Distribution of Income and Gains.** Distributions of net investment income of the Fund, if any, are made annually. Net realized gains from investment transactions, in excess of available capital loss carryforwards, would be taxable to the Fund if not distributed and, therefore, will be distributed to shareholders at least annually. The Fund may also make additional distributions for tax purposes if necessary.

The timing and characterization of certain income and capital gains distributions are determined annually in accordance with federal tax regulations which may differ from accounting principles generally accepted in the United States of America. These differences primarily relate to investments in futures contracts and certain securities sold at a loss. As a result, net investment income (loss) and net realized gain (loss) on investment transactions for a reporting period may differ significantly from distributions during such period. Accordingly, the

Fund may periodically make reclassifications among certain of its capital accounts without impacting the net asset value of the Fund.

At December 31, 2010, the Fund's components of distributable earnings on a tax basis were as follows:

| Fund | Undistributed Ordinary Income ($)* | Capital Loss Carryforwards ($) | Unrealized Appreciation (Depreciation) on Investments ($) |
|---|---|---|---|
| DWS Core Fixed Income VIP | 2,279,173 | (53,707,000) | 2,267,700 |

In addition, the tax character of distributions paid by the Fund is summarized as follows:

| | Distributions from Ordinary Income ($)* | |
|---|---|---|
| | Years Ended December 31, | |
| Fund | 2010 | 2009 |
| DWS Core Fixed Income VIP | 5,749,285 | 11,379,976 |

* *For tax purposes, short-term capital gain distributions are considered ordinary income distributions.*

**Expenses.** Expenses of the Trust arising in connection with a specific fund are allocated to that fund. Other Trust expenses which cannot be directly attributed to a fund are apportioned among the funds in the Trust.

**Contingencies.** In the normal course of business, the Fund may enter into contracts with service providers that contain general indemnification clauses. The Fund's maximum exposure under these arrangements is unknown as this would involve future claims that may be made against the Fund that have not yet been made. However, based on experience, the Fund expects the risk of loss to be remote.

**Other.** Investment transactions are accounted for on a trade date plus one basis for daily net asset value calculations. However, for financial reporting purposes, investment transactions are reported on trade date. Interest income is recorded on the accrual basis. Realized gains and losses from investment transactions are recorded on an identified cost basis. All discounts and premiums are accreted/amortized for both tax and financial reporting purposes for the Fund.

## B. Derivative Instruments

**Futures Contracts.** A futures contract is an agreement between a buyer or seller and an established futures exchange or its clearinghouse in which the buyer or seller agrees to take or make a delivery of a specific amount of a financial instrument at a specified price on a specific date (settlement date). For the year ended December 31, 2010, the Fund entered into interest rate futures to gain exposure to different parts of the yield curve while managing overall duration.

Futures contracts are valued at the most recent settlement price. Upon entering into a futures contract, the Fund is required to deposit with a financial intermediary cash or securities ("initial margin") in an amount equal to a certain percentage of the face value indicated in the futures contract. Subsequent payments ("variation margin") are made or received by the Fund dependent upon the daily fluctuations in the value and are recorded for financial reporting purposes as unrealized gains or losses by the Fund. Gains or losses are realized when the contract expires or is closed. Since all futures contracts are exchange-traded, counterparty risk is minimized as the exchange's clearinghouse acts as the counterparty, and guarantees the futures against default.

Certain risks may arise upon entering into futures contracts, including the risk that an illiquid market will limit the Fund's ability to close out a futures contract prior to the settlement date and that a change in the value of a futures contract may not correlate exactly with the changes in the value of the underlying hedged security, index or currency. Risk of loss may exceed amounts recognized in the Statement of Assets and Liabilities.

A summary of the open futures contracts as of December 31, 2010 is included in a table following the Fund's Investment Portfolio. For the year ended December 31, 2010, the Fund's investment in futures contracts sold had a total notional value generally indicative of a range from $0 to approximately $25,611,000.

The following table summarizes the value of the Fund's derivative instruments held as of December 31, 2010 and the related location in the accompanying Statement of Assets and Liabilities, presented by primary underlying risk exposure:

| **Asset Derivative** | **Futures Contracts** |
|---|---|
| Interest Rate Contracts (a) | $ 617,391 |

*The above derivative is located in the following Statement of Assets and Liabilities account:*

(a) *Net unrealized appreciation (depreciation) on futures. Liability of payable for daily variation margin on open futures contracts reflects unsettled variation margin.*

Additionally, the amount of unrealized and realized gains and losses on derivative instruments recognized in Fund earnings during the year ended December 31, 2010 and the related location in the accompanying Statement of Operations is summarized in the following tables by primary underlying risk exposure:

| **Realized Gain (Loss)** | **Futures Contracts** |
|---|---|
| Interest Rate Contracts (a) | $ (504,977) |

*The above derivative is located in the following Statement of Operations account:*

(a) *Net realized gain (loss) from futures*

| **Change in Net Unrealized Appreciation (Depreciation)** | **Futures Contracts** |
|---|---|
| Interest Rate Contracts (a) | $ 534,420 |

*The above derivative is located in the following Statement of Operations account:*

(a) *Change in net unrealized appreciation (depreciation) on futures*

## C. Purchases and Sales of Securities

During the year ended December 31, 2010, purchases and sales of investment transactions (excluding short-term investments) were as follows:

| **Fund** | **Purchases ($)** | **Sales ($)** |
|---|---|---|
| DWS Core Fixed Income VIP | | |
| excluding US Treasury Obligations | 255,494,334 | 250,517,214 |
| US Treasury Obligations | 97,533,517 | 86,987,776 |

## D. Related Parties

**Management Agreement.** Under the Investment Management Agreement with Deutsche Investment Management Americas Inc. ("DIMA" or the "Advisor"), an indirect, wholly owned subsidiary of Deutsche Bank AG, the Advisor directs the investments of the Fund in accordance with its investment objectives, policies and restrictions. The Advisor determines the securities, instruments and other contracts relating to investments to be purchased, sold or entered into by the Fund.

Under the Investment Management Agreement with the Advisor, the fee is equivalent to the annual rates shown below of the Fund's average daily net assets, computed and accrued daily and payable monthly:

| **Fund** | **Annual Management Fee Rate** |
|---|---|
| DWS Core Fixed Income VIP | |
| $0–$250 million | .500% |
| next $750 million | .470% |
| next $1.5 billion | .450% |
| next $2.5 billion | .430% |
| next $2.5 billion | .400% |
| next $2.5 billion | .380% |
| next $2.5 billion | .360% |
| over $12.5 billion | .340% |

For the period from October 1, 2010 through September 30, 2011, the Advisor has contractually agreed to waive its fee and/or reimburse certain operating expenses to the extent necessary to maintain the operating expenses (excluding certain expenses such as extraordinary expenses, taxes, brokerage and interest expense) of the class as follows:

| Fund | Annual Rate |
|---|---|
| DWS Core Fixed Income VIP | |
| Class A | .71% |

For the period from January 1, 2010 through February 5, 2010, the Advisor had voluntarily agreed to waive its fee and/or reimburse certain operating expenses to the extent necessary to maintain the operating expenses (excluding certain expenses such as extraordinary expenses, taxes, brokerage and interest expense) of the class as follows:

| Fund | Annual Rate |
|---|---|
| DWS Core Fixed Income VIP | |
| Class B | 1.07% |

Accordingly, for the year ended December 31, 2010, the total management fee and effective management fee rate were as follows:

| Fund | Total Aggregated ($) | Annual Effective Rate |
|---|---|---|
| DWS Core Fixed Income VIP | 482,684 | .50% |

In addition, for the year ended December 31, 2010, the Advisor waived $809 of other expenses.

**Administration Fee.** Pursuant to an Administrative Services Agreement, DIMA provides most administrative services to the Fund. For all services provided under the Administrative Services Agreement, the Fund pays DIMA an annual fee ("Administration Fee") of 0.10% of the Fund's average daily net assets, computed and accrued daily and payable monthly. For the year ended December 31, 2010, the Administration Fee was as follows:

| Fund | Total Aggregated ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS Core Fixed Income VIP | 96,537 | 7,487 |

**Service Provider Fees.** DWS Investments Service Company ("DISC"), an affiliate of the Advisor, is the transfer agent, dividend-paying agent and shareholder service agent for the Fund. Pursuant to a sub-transfer agency agreement between DISC and DST Systems, Inc. ("DST"), DISC has delegated certain transfer agent, dividend-paying agent and shareholder service agent functions to DST. DISC compensates DST out of the shareholder servicing fee it receives from the Fund. For the year ended December 31, 2010 and for the period ended February 5, 2010 for Class B shares, the amounts charged to the Fund by DISC were as follows:

| Fund | Total Aggregated ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS Core Fixed Income VIP Class A | 74 | 33 |
| DWS Core Fixed Income VIP Class B | 60 | 10 |

**Distribution Service Agreement**. Under the Fund's Class B 12b-1 plans, DWS Investments Distributors, Inc. ("DIDI") received a fee ("Distribution Service Fee") of 0.25% of average daily net assets of Class B shares. For the period ended February 5, 2010, the Distribution Service Fee was as follows:

| Fund | Total Aggregated ($) |
|---|---|
| DWS Core Fixed Income VIP | 14 |

**Typesetting and Filing Service Fees.** Under an agreement with DIMA, DIMA is compensated for providing typesetting and certain regulatory filing services to the Fund. For the year ended December 31, 2010, the amount charged to the Fund by DIMA included in the Statement of Operations under "reports to shareholders" was as follows:

| Fund | Amount ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS Core Fixed Income VIP | 11,979 | 3,064 |

**Trustees' Fees and Expenses.** The Fund paid each Trustee not affiliated with the Advisor retainer fees plus specified amounts for various committee services and for the Board Chairperson.

**Affiliated Cash Management Vehicles.** The Fund may invest uninvested cash balances in Central Cash Management Fund, which is managed by the Advisor. The Fund indirectly bears their proportionate share of the expenses of the underlying money market funds. Central Cash Management Fund does not pay the Advisor an investment management fee. Central Cash Management Fund seeks a high level of current income consistent with liquidity and the preservation of capital.

## E. Ownership of the Fund

At December 31, 2010, the beneficial ownership in the Fund was as follows:

**DWS Core Fixed Income VIP:** Three Participating Insurance Companies were owners of record of 10% or more of the total outstanding Class A shares of the Fund, each owning 44%, 41% and 13%.

## F. Line of Credit

The Trust and other affiliated fund (the "Participants") share in a $450 million revolving credit facility provided by a syndication of banks. The Fund may borrow for temporary or emergency purposes, including the meeting of redemption requests that otherwise might require the untimely disposition of securities. The Participants are charged an annual commitment fee which is allocated based on net assets, among each of the Participants. Interest is calculated at a rate per annum equal to the sum of the Federal Funds Rate plus 1.25 percent plus if LIBOR exceeds the Federal Funds Rate the amount of such excess. The Fund may borrow up to a maximum of 33 percent of its net assets under the agreement.

# Report of Independent Registered Public Accounting Firm

**To the Board of Trustees and Shareholders of DWS Variable Series II:**

We have audited the accompanying statement of assets and liabilities of DWS Core Fixed Income VIP, one of the funds constituting the DWS Variable Series II (the "Trust"), including the investment portfolio, as of December 31, 2010, and the related statement of operations, the statement of changes in net assets and the financial highlights for each of the periods indicated therein. These financial statements and financial highlights are the responsibility of the Trust's management. Our responsibility is to express an opinion on these financial statements and financial highlights based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements and financial highlights are free of material misstatement. We were not engaged to perform an audit of the Trust's internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Trust's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements and financial highlights, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our procedures included confirmation of securities owned as of December 31, 2010, by correspondence with the custodian and brokers or by other appropriate auditing procedures where replies from brokers were not received. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements and financial highlights referred to above present fairly, in all material respects, the financial position of the aforementioned fund of the DWS Variable Series II at December 31, 2010, the results of its operations, the changes in its net assets and the financial highlights for each of the periods indicated therein, in conformity with U.S. generally accepted accounting principles.

Ernst + Young LLP

Boston, Massachusetts
February 14, 2011

## Tax Information

**(Unaudited)**

Please consult a tax advisor if you have questions about federal or state income tax laws, or on how to prepare your tax returns. If you have specific questions about your account, please contact your insurance provider.

## Proxy Voting

The Trust's policies and procedures for voting proxies for portfolio securities and information about how the Trust voted proxies related to its portfolio securities during the 12-month period ended June 30 are available on our Web site — www.dws-investments.com (click on "proxy voting" at the bottom of the page) — or on the SEC's Web site — www.sec.gov. To obtain a written copy of the Trust's policies and procedures without charge, upon request, call us toll free at (800) 728-3337.

# Investment Management Agreement Approval

## DWS Core Fixed Income VIP

The Board of Trustees, including the Independent Trustees, approved the renewal of your Fund's investment management agreement (the "Agreement") with Deutsche Investment Management Americas Inc. ("DWS") in September 2010.

In terms of the process that the Board followed prior to approving the Agreement, shareholders should know that:

- In September 2010, all but one of the Fund's Trustees were independent of DWS and its affiliates.
- The Trustees meet frequently to discuss fund matters. Each year, the Trustees dedicate substantial time to contract review matters. Over the course of several months, the Board's Contract Committee, in coordination with the Board's Fixed Income and Quant Oversight Committee, reviewed comprehensive materials received from DWS, independent third parties and independent counsel. These materials included an analysis of the Fund's performance, fees and expenses, and profitability compiled by the Fund's independent fee consultant. The Board also received extensive information throughout the year regarding performance of the Fund.
- The Independent Trustees regularly meet privately with their independent counsel to discuss contract review and other matters. In addition, the Independent Trustees were also advised by the Fund's independent fee consultant in the course of their review of the Fund's contractual arrangements and considered a comprehensive report prepared by the independent fee consultant in connection with their deliberations (the "IFC Report").
- In connection with reviewing the Agreement, the Board also reviewed the terms of the Fund's distribution agreement, administrative services agreement, transfer agency agreement and other material service agreements.
- Based on its evaluation of the information provided, the Contract Committee presented its findings and recommendations to the Independent Trustees as a group. The Independent Trustees reviewed the Contract Committee's findings and recommendations and presented their recommendations to the full Board.

In connection with the contract review process, the Contract Committee and the Board considered the factors discussed below, among others. The Board also considered that DWS and its predecessors have managed the Fund since its inception, and the Board believes that a long-term relationship with a capable, conscientious advisor is in the best interests of the Fund. The Board considered, generally, that shareholders chose to invest or remain invested in the Fund knowing that DWS managed the Fund, and that the Agreement was approved by the Fund's shareholders. DWS is part of Deutsche Bank, a major global banking institution that is engaged in a wide range of financial services. The Board believes that there are significant advantages to being part of a global asset management business that offers a wide range of investing expertise and resources, including hundreds of portfolio managers and analysts with research capabilities in many countries throughout the world.

While shareholders may focus primarily on fund performance and fees, the Fund's Board considers these and many other factors, including the quality and integrity of DWS's personnel and such other issues as back-office operations, fund valuations, and compliance policies and procedures.

**Nature, Quality and Extent of Services.** The Board considered the terms of the Agreement, including the scope of advisory services provided under the Agreement. The Board noted that, under the Agreement, DWS provides portfolio management services to the Fund and that, pursuant to a separate administrative services agreement, DWS provides administrative services to the Fund. The Board considered the experience and skills of senior management and investment personnel, the resources made available to such personnel, the ability of DWS to attract and retain high-quality personnel, and the organizational depth and stability of DWS. The Board reviewed the Fund's performance over short-term and long-term periods and compared those returns to various agreed-upon performance measures, including market indices and a peer universe compiled by the independent fee consultant using information supplied by Lipper Inc. ("Lipper"). The Board also noted that it has put into place a process of identifying "Focus Funds" (e.g., funds performing poorly relative to their benchmark or a peer universe compiled by Lipper), and receives more frequent reporting and information from DWS regarding such funds, along with DWS's remedial plans to address underperformance. The Board believes this process is an effective manner of identifying and addressing underperforming funds. Based on the information provided, the Board noted that for the one-, three- and five-year periods ended December 31, 2009, the Fund's performance (Class A shares) was in the 4th quartile of the applicable Lipper universe (the 1st quartile being the best performers and the 4th quartile being the worst performers). The Board also observed that the Fund has outperformed its benchmark in the one-year period and has underperformed its benchmark in the three- and five-year periods ended December 31, 2009. The Board noted the disappointing investment performance of the

Fund in recent periods and continued to discuss with senior management of DWS the factors contributing to such underperformance and actions being taken to improve performance. The Board recognized that DWS has made significant changes in its investment personnel and processes in recent years in an effort to improve long-term performance.

On the basis of this evaluation and the ongoing review of investment results by the Board, the Board concluded that the nature, quality and extent of services provided by DWS historically have been and continue to be satisfactory.

**Fees and Expenses.** The Board considered the Fund's investment management fee schedule, operating expenses, and total expense ratios, and comparative information provided by Lipper and the independent fee consultant regarding investment management fee rates paid to other investment advisors by similar funds (1st quartile being the most favorable and 4th quartile being the least favorable). With respect to management fees paid to other investment advisors by similar funds, the Board noted that the contractual fee rates paid by the Fund, which include the 0.10% fee paid to DWS under the Fund's administrative services agreement, were higher than the median (3rd quartile) of the applicable Lipper peer group (based on Lipper data provided as of December 31, 2009). The Board noted that the Fund's Class A shares total (net) operating expenses were expected to be higher than the median (3rd quartile) of the applicable Lipper expense universe (based on Lipper data provided as of December 31, 2009, and analyzing Lipper expense universe Class A expenses less any applicable 12b-1 fees) ("Lipper Universe Expenses"). The Board considered the Fund's management fee rate as compared to fees charged by DWS and certain of its affiliates for comparable mutual funds and considered differences in fund and fee structures between the DWS Funds. The Board also considered how the Fund's total (net) operating expenses compared to the total (net) operating expenses of a more customized peer group selected by Lipper (based on such factors as asset size). The Board also noted that the expense limitation agreed to by DWS helped to ensure that the Fund's total (net) operating expenses would remain competitive.

The information considered by the Board as part of its review of management fees included information regarding fees charged by DWS and its affiliates to similar institutional accounts and to similar funds offered primarily to European investors ("DWS Europe funds"), in each case as applicable. The Board observed that advisory fee rates for institutional accounts generally were lower than the management fees charged by similarly managed DWS US mutual funds ("DWS Funds"), but also took note of the differences in services provided to DWS Funds as compared to institutional accounts. In the case of DWS Europe funds, the Board observed that fee rates for DWS Europe funds generally were higher than for similarly managed DWS Funds, but noted that differences in the types of services provided to DWS Funds relative to DWS Europe funds made it difficult to compare such fees.

On the basis of the information provided, the Board concluded that management fees were reasonable and appropriate in light of the nature, quality and extent of services provided by DWS.

**Profitability.** The Board reviewed detailed information regarding revenues received by DWS under the Agreement. The Board considered the estimated costs and pre-tax profits realized by DWS from advising the DWS Funds, as well as estimates of the pre-tax profits attributable to managing the Fund in particular. The Board also received information regarding the estimated enterprise-wide profitability of DWS and its affiliates with respect to all fund services in totality and by fund. The Board reviewed DWS's methodology in allocating its costs to the management of the Fund. Based on the information provided, the Board concluded that the pre-tax profits realized by DWS in connection with the management of the Fund were not unreasonable. The Board also reviewed information regarding the profitability of certain similar investment management firms. The Board noted that while information regarding the profitability of such firms is limited (and in some cases is not necessarily prepared on a comparable basis), DWS and its affiliates' overall profitability with respect to the DWS fund complex (after taking into account distribution and other services provided to the funds by DWS and its affiliates) was lower than the overall profitability levels of many comparable firms for which such data was available.

**Economies of Scale.** The Board considered whether there are economies of scale with respect to the management of the Fund and whether the Fund benefits from any economies of scale. The Board noted that the Fund's management fee schedule includes fee breakpoints. The Board concluded that the Fund's fee schedule represents an appropriate sharing between the Fund and DWS of such economies of scale as may exist in the management of the Fund at current asset levels.

**Other Benefits to DWS and Its Affiliates.** The Board also considered the character and amount of other incidental benefits received by DWS and its affiliates, including any fees received by DWS for administrative services provided to the Fund and any fees received by an affiliate of DWS for distribution services. The Board also considered benefits to DWS related to brokerage and soft-dollar allocations, including allocating brokerage to pay for research generated by parties other than the executing broker dealers, which pertain primarily to funds investing in equity securities, along with the incidental public relations benefits to DWS related to DWS Funds

advertising and cross-selling opportunities among DWS products and services. The Board concluded that management fees were reasonable in light of these fallout benefits.

**Compliance.** The Board considered the significant attention and resources dedicated by DWS to documenting and enhancing its compliance processes in recent years. The Board noted in particular (i) the experience and seniority of both DWS's chief compliance officer and the Fund's chief compliance officer; (ii) the large number of DWS compliance personnel; and (iii) the substantial commitment of resources by DWS and its affiliates to compliance matters.

Based on all of the information considered and the conclusions reached, the Board unanimously (including the Independent Trustees) determined that the continuation of the Agreement is in the best interests of the Fund. In making this determination, the Board did not give particular weight to any single factor identified above. The Board considered these factors over the course of numerous meetings, certain of which were in executive session with only the Independent Trustees and their counsel present. It is possible that individual Trustees may have weighed these factors differently in reaching their individual decisions to approve the continuation of the Agreement.

# Summary of Management Fee Evaluation by Independent Fee Consultant

October 3, 2010

Pursuant to an Order entered into by Deutsche Investment Management Americas and affiliates (collectively, "DeAM") with the Attorney General of New York, I, Thomas H. Mack, have been appointed the Independent Fee Consultant for the DWS Funds (formerly the DWS Scudder Funds). My duties include preparing an annual written evaluation of the management fees DeAM charges the Funds, considering among other factors the management fees charged by other mutual fund companies for like services, management fees DeAM charges other clients for like services, DeAM's costs of supplying services under the management agreements and related profit margins, possible economies of scale if a Fund grows larger, and the nature and quality of DeAM's services, including fund performance. This report summarizes my evaluation for 2010, including my qualifications, the evaluation process for each of the DWS Funds, consideration of certain complex-level factors, and my conclusions. I served in substantially the same capacity in 2007, 2008, and 2009.

## Qualifications

For more than 35 years I have served in various professional capacities within the investment management business. I have held investment analysis and advisory positions, including securities analyst, portfolio strategist and director of investment policy with a large investment firm. I have also performed business management functions, including business development, financial management and marketing research and analysis.

Since 1991, I have been an independent consultant within the asset management industry. I have provided services to over 125 client organizations, including investment managers, mutual fund boards, product distributors and related organizations. Over the past ten years I have completed a number of assignments for mutual fund boards, specifically including assisting boards with management contract renewal.

I hold a Master of Business Administration degree, with highest honors, from Harvard University and Master of Science and Bachelor of Science (highest honors) degrees from the University of California at Berkeley. I am an independent director and audit committee financial expert for two closed-end mutual funds and have served in various leadership and financial oversight capacities with non-profit organizations.

## Evaluation of Fees for each DWS Fund

My work focused primarily on evaluating, fund-by-fund, the fees charged to each of the 118 publicly offered Fund portfolios in the DWS Fund family. For each Fund, I considered each of the key factors mentioned above, as well as any other relevant information. In doing so I worked closely with the Funds' Independent Directors in their annual contract renewal process, as well as in their approval of contracts for several new funds (documented separately).

In evaluating each Fund's fees, I reviewed comprehensive materials provided by or on behalf of DeAM, including expense information prepared by Lipper Analytical, comparative performance information, profitability data, manager histories, and other materials. I also accessed certain additional information from the Lipper and Morningstar databases and drew on my industry knowledge and experience.

To facilitate evaluating this considerable body of information, I prepared for each Fund a document summarizing the key data elements in each area as well as additional analytics discussed below. This made it possible to consider each key data element in the context of the others.

In the course of contract renewal, DeAM agreed to implement a number of fee and expense adjustments requested by the Independent Directors which will favorably impact future fees and expenses, and my evaluation includes the effects of these changes.

### Fees and Expenses Compared with Other Funds

The competitive fee and expense evaluation for each fund focused on two primary comparisons:

- The Fund's contractual management fee (the advisory fee plus the administration fee where applicable) compared with those of a group of typically 12–15 funds in the same Lipper investment category (e.g. Large Capitalization Growth) having similar distribution arrangements and being of similar size.
- The Fund's total expenses compared with a broader universe of funds from the same Lipper investment category and having similar distribution arrangements.

These two comparisons provide a view of not only the level of the fee compared with funds of similar scale but also the total expense the Fund bears for all the services it receives, in comparison with the investment choices available in the Fund's investment category and distribution channel. The principal figure-of-merit used in these comparisons was the subject Fund's percentile ranking against peers.

### DeAM's Fees for Similar Services to Others

DeAM provided management fee schedules for all of its US domiciled fund and non-fund investment management accounts in any of the investment categories where there is a DWS Fund. These similar products included the other DWS Funds, non-fund pooled accounts, institutional accounts and sub-advisory accounts. Using this information, I calculated for each Fund the fee that would be charged to each similar product, at the subject Fund's asset level.

Evaluating information regarding non-fund products is difficult because there are varying levels of services required for different types of accounts, with mutual funds generally requiring considerably more regulatory and administrative types of service as well as having more frequent cash flows than other types of accounts. Also, while mutual fund fees for similar fund products can be expected to be similar, there will be some differences due to different pricing conditions in different distribution channels (e.g. retail funds versus those used in variable insurance products), differences in underlying investment processes and other factors.

**Costs and Profit Margins**

DeAM provided a detailed profitability analysis for each Fund. After making some adjustments so that the presentation would be more comparable to the available industry figures, I reviewed profit margins from investment management alone, from investment management plus other fund services (excluding distribution) provided to the Funds by DeAM (principally shareholder services), and DeAM profits from all sources, including distribution. A later section comments on overall profitability.

**Economies of Scale**

Economies of scale — an expected decline in management cost per dollar of fund assets as fund assets grow — are very rarely quantified and documented because of inherent difficulties in collecting and analyzing relevant data. However, in virtually every investment category that I reviewed, larger funds tend to have lower fees and lower total expenses than smaller funds. To see how each DWS Fund compares with this industry observation, I reviewed:

- The trend in Fund assets over the last five years and the accompanying trend in total expenses. This shows if the Fund has grown and, if so, whether total expense (management fees as well as other expenses) have declined as a percent of assets.
- Whether the Fund has break-points in its management fee schedule, the extent of the fee reduction built into the schedule and the asset levels where the breaks take effect, and in the case of a sub-advised Fund how the Fund's break-points compare with those of the sub-advisory fee schedule.
- How the Fund's contractual fee schedule compares with trends in the industry data. To accomplish this, I constructed a chart showing how actual latest-fiscal-year contractual fees of the Fund and of other similar funds relate to average fund assets, with the subject Fund's contractual fee schedule superimposed.

**Quality of Service — Performance**

The quality-of-service evaluation focused on investment performance, which is the principal result of the investment management service. Each Fund's performance was reviewed over the past 1, 3, 5 and 10 years, as applicable, and compared with that of other funds in the same investment category and with a suitable market index.

In addition, I calculated and reviewed risk-adjusted returns relative to an index of similar mutual funds' returns and a suitable market index. The risk-adjusted returns analysis provides a way of determining the extent to which the Fund's return comparisons are mainly the product of investment value-added (or lack thereof) or alternatively taking considerably more or less risk than is typical in its investment category.

I also received and considered the history of portfolio manager changes for each Fund, as this provided an important context for evaluating the performance results.

## Complex-Level Considerations

While this evaluation was conducted mainly at the individual fund level, there are some issues relating to the reasonableness of fees that can alternatively be considered across the whole fund complex:

- I reviewed DeAM's profitability analysis for all DWS Funds, with a view toward determining if the allocation procedures used were reasonable and how profit levels compared with public data for other investment managers.
- I considered whether DeAM and affiliates receive any significant ancillary or "fall-out" benefits that should be considered in interpreting the direct profitability results. These would be situations where serving as the investment manager of the Funds is beneficial to another part of the Deutsche Bank organization.
- I considered how aggregated DWS Fund expenses had varied over the years, by asset class and in the context of trends in asset levels.
- I reviewed the structure of the DeAM organization, trends in staffing levels, and information on compensation of investment management and other professionals compared with industry data.

## Findings

Based on the process and analysis discussed above, which included reviewing a wide range of information from management and external data sources and considering among other factors the fees DeAM charges other clients, the fees charged by other fund managers, DeAM's costs and profits associated with managing the Funds, economies of scale, possible fall-out benefits, and the nature and quality of services provided, in my opinion the management fees charged the DWS Funds are reasonable.

Thomas H. Mack

Thomas H. Mack

# Board Members and Officers

The following table presents certain information regarding the Board Members and Officers of the Trust as of December 31, 2010. Each Board Member's year of birth is set forth in parentheses after his or her name. Unless otherwise noted, (i) each Board Member has engaged in the principal occupation(s) noted in the table for at least the most recent five years, although not necessarily in the same capacity; and (ii) the address of each Independent Board Member is c/o Paul K. Freeman, Independent Chairman, DWS Funds, PO Box 101833, Denver, CO 80250-1833. Except as otherwise noted below, the term of office for each Board Member is until the election and qualification of a successor, or until such Board Member sooner dies, resigns, is removed or as otherwise provided in the governing documents of the fund. Because the fund does not hold an annual meeting of shareholders, each Board Member will hold office for an indeterminate period. The Board Members may also serve in similar capacities with other funds in the fund complex. The Length of Time Served represents the year in which the Board Member joined the board of one or more DWS funds now overseen by the Board.

### Independent Board Members

| Name, Year of Birth, Position with the Fund and Length of Time Served[1] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Paul K. Freeman (1950)<br>Chairperson since 2009<br>Board Member since 1993 | Consultant, World Bank/Inter-American Development Bank; Executive and Governing Council of the Independent Directors Council (education committees); formerly, Project Leader, International Institute for Applied Systems Analysis (1998–2001); Chief Executive Officer, The Eric Group, Inc. (environmental insurance) (1986–1998) | 122 |
| John W. Ballantine (1946)<br>Board Member since 1999 | Retired; formerly, Executive Vice President and Chief Risk Management Officer, First Chicago NBD Corporation/The First National Bank of Chicago (1996–1998); Executive Vice President and Head of International Banking (1995–1996). Directorships: Healthways, Inc. (provider of disease and care management services); Portland General Electric (utility company); Stockwell Capital Investments PLC (private equity). Former Directorships: First Oak Brook Bancshares, Inc. and Oak Brook Bank; Prisma Energy International | 122 |
| Henry P. Becton, Jr. (1943)<br>Board Member since 1990 | Vice Chair and former President, WGBH Educational Foundation. Directorships: Association of Public Television Stations; Lead Director, Becton Dickinson and Company[3] (medical technology company); Lead Director, Belo Corporation[3] (media company); Public Radio International; Public Radio Exchange (PRX); The PBS Foundation. Former Directorships: Boston Museum of Science; American Public Television; Concord Academy; New England Aquarium; Mass. Corporation for Educational Telecommunications; Committee for Economic Development; Public Broadcasting Service | 122 |
| Dawn-Marie Driscoll (1946)<br>Board Member since 1987 | President, Driscoll Associates (consulting firm); Executive Fellow, Center for Business Ethics, Bentley University; formerly, Partner, Palmer & Dodge (1988–1990); Vice President of Corporate Affairs and General Counsel, Filene's (1978–1988). Directorships: Trustee of 22 open-end mutual funds managed by Sun Capital Advisers, Inc. (since 2007); Director of ICI Mutual Insurance Company (since 2007); Advisory Board, Center for Business Ethics, Bentley University; Trustee, Southwest Florida Community Foundation (charitable organization). Former Directorships: Investment Company Institute (audit, executive, nominating committees) and Independent Directors Council (governance, executive committees) | 122 |
| Keith R. Fox (1954)<br>Board Member since 1996 | Managing General Partner, Exeter Capital Partners (a series of private investment funds). Directorships: Progressive International Corporation (kitchen goods importer and distributor); BoxTop Media Inc. (advertising); The Kennel Shop (retailer); former Chairman, National Association of Small Business Investment Companies | 122 |
| Kenneth C. Froewiss (1945)<br>Board Member since 2001 | Adjunct Professor of Finance, NYU Stern School of Business (September 2009–present; Clinical Professor from 1997–September 2009); Member, Finance Committee, Association for Asian Studies (2002–present); Director, Mitsui Sumitomo Insurance Group (US) (2004–present); prior thereto, Managing Director, J.P. Morgan (investment banking firm) (until 1996) | 122 |
| Richard J. Herring (1946)<br>Board Member since 1990 | Jacob Safra Professor of International Banking and Professor, Finance Department, The Wharton School, University of Pennsylvania (since July 1972); Co-Director, Wharton Financial Institutions Center (since July 2000); Co-Chair, U.S. Shadow Financial Regulatory Committee; Executive Director, Financial Economists Roundtable; Director, Japan Equity Fund, Inc. (since September 2007), Thai Capital Fund, Inc. (since September 2007), Singapore Fund, Inc. (since September 2007); Independent Director of Barclays Bank Delaware (since September 2010). Formerly, Vice Dean and Director, Wharton Undergraduate Division (July 1995–June 2000); Director, Lauder Institute of International Management Studies (July 2000–June 2006) | 122 |
| William McClayton (1944)<br>Board Member since 2004+ | Private equity investor (since October 2009); previously, Managing Director, Diamond Management & Technology Consultants, Inc. (global consulting firm) (2001–2009); Directorship: Board of Managers, YMCA of Metropolitan Chicago; formerly: Senior Partner, Arthur Andersen LLP (accounting) (1966–2001); Trustee, Ravinia Festival | 122 |

| Name, Year of Birth, Position with the Fund and Length of Time Served[1] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Rebecca W. Rimel (1951)<br>Board Member since 1995 | President and Chief Executive Officer, The Pew Charitable Trusts (charitable organization) (1994 to present); Trustee, Thomas Jefferson Foundation (charitable organization) (1994 to present); Trustee, Executive Committee, Philadelphia Chamber of Commerce (2001–2007); Director, CardioNet, Inc.[2] (2009–present) (health care). Formerly, Executive Vice President, The Glenmede Trust Company (investment trust and wealth management) (1983–2004); Board Member, Investor Education (charitable organization) (2004–2005); Director, Viasys Health Care[2] (January 2007–June 2007); Trustee, Pro Publica (charitable organization) (2007–2010) | 122 |
| William N. Searcy, Jr. (1946)<br>Board Member since 1993 | Private investor since October 2003; Trustee of 22 open-end mutual funds managed by Sun Capital Advisers, Inc. (since October 1998). Formerly, Pension & Savings Trust Officer, Sprint Corporation[2] (telecommunications) (November 1989–September 2003) | 122 |
| Jean Gleason Stromberg (1943)<br>Board Member since 1997 | Retired. Formerly, Consultant (1997–2001); Director, Financial Markets US Government Accountability Office (1996–1997); Partner, Fulbright & Jaworski, L.L.P. (law firm) (1978–1996). Directorships: The William and Flora Hewlett Foundation. Former Directorships: Service Source, Inc., Mutual Fund Directors Forum (2002–2004), American Bar Retirement Association (funding vehicle for retirement plans) (1987–1990 and 1994–1996) | 122 |
| Robert H. Wadsworth (1940)<br>Board Member since 1999 | President, Robert H. Wadsworth & Associates, Inc. (consulting firm) (1983 to present); Director, The Phoenix Boys Choir Association | 125 |

## Interested Board Member and Officer[4]

| Name, Year of Birth, Position with the Trust/ Corporation and Length of Time Served[1,5] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Ingo Gefeke[7] (1967)<br>Board Member since 2010<br>Executive Vice President since 2010 | Managing Director[3], Deutsche Asset Management; Global Head of Distribution and Product Management, DWS Global Head of Trading and Securities Lending. Member of the Board of Directors of DWS Investment GmbH Frankfurt (since July 2009) and DWS Holding & Service GmbH Frankfurt (since January 2010); formerly, Global Chief Administrative Officer, Deutsche Asset Management (2004–2009); Global Chief Operating Officer, Global Transaction Banking, Deutsche Bank AG, New York (2001–2004); Chief Operating Officer, Global Banking Division Americas, Deutsche Bank AG, New York (1999–2001); Central Management, Global Banking Services, Deutsche Bank AG, Frankfurt (1998–1999); Relationship Management, Deutsche Bank AG, Tokyo, Japan (1997–1998) | 55 |

## Officers[4]

| Name, Year of Birth, Position with the Fund and Length of Time Served[5] | Principal Occupation(s) During Past 5 Years and Other Directorships Held |
|---|---|
| Michael G. Clark[6] (1965)<br>President, 2006–present | Managing Director[3], Deutsche Asset Management (2006–present); President of DWS family of funds; Director, ICI Mutual Insurance Company (since October 2007); formerly, Director of Fund Board Relations (2004–2006) and Director of Product Development (2000–2004), Merrill Lynch Investment Managers; Senior Vice President Operations, Merrill Lynch Asset Management (1999–2000) |
| John Millette[8] (1962)<br>Vice President and Secretary, 1999–present | Director[3], Deutsche Asset Management |
| Paul H. Schubert[6] (1963)<br>Chief Financial Officer, 2004–present<br>Treasurer, 2005–present | Managing Director[3], Deutsche Asset Management (since July 2004); formerly, Executive Director, Head of Mutual Fund Services and Treasurer for UBS Family of Funds (1998–2004); Vice President and Director of Mutual Fund Finance at UBS Global Asset Management (1994–1998) |
| Caroline Pearson[8] (1962)<br>Chief Legal Officer, April 2010–present | Managing Director[3], Deutsche Asset Management; formerly, Assistant Secretary for DWS family of funds (1997–2010) |
| Rita Rubin[9] (1970)<br>Assistant Secretary, 2009–present | Vice President and Counsel, Deutsche Asset Management (since October 2007); formerly, Vice President, Morgan Stanley Investment Management (2004–2007) |
| Paul Antosca[8] (1957)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management (since 2006); Vice President, The Manufacturers Life Insurance Company (U.S.A.) (1990–2006) |
| Jack Clark[8] (1967)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management (since 2007); formerly, Vice President, State Street Corporation (2002–2007) |

| Name, Year of Birth, Position with the Fund and Length of Time Served[5] | Principal Occupation(s) During Past 5 Years and Other Directorships Held |
|---|---|
| Diane Kenneally[8] (1966)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management |
| John Caruso[9] (1965)<br>Anti-Money Laundering Compliance Officer, 2010–present | Managing Director[3], Deutsche Asset Management |
| Robert Kloby[9] (1962)<br>Chief Compliance Officer, 2006–present | Managing Director[3], Deutsche Asset Management |

1 *The length of time served represents the year in which the Board Member joined the board of one or more DWS funds currently overseen by the Board.*

2 *A publicly held company with securities registered pursuant to Section 12 of the Securities Exchange Act of 1934.*

3 *Executive title, not a board directorship.*

4 *As a result of their respective positions held with the Advisor, these individuals are considered "interested persons" of the Advisor within the meaning of the 1940 Act. Interested persons receive no compensation from the fund.*

5 *The length of time served represents the year in which the officer was first elected in such capacity for one or more DWS funds.*

6 *Address: 100 Plaza One, Jersey City, NJ 07311.*

7 *Effective January 11, 2011, Mr. Gefeke, an interested Board Member and Executive Vice President, resigned from the fund's Board and as an officer.*

*The mailing address of Mr. Gefeke is 345 Park Avenue, New York, New York 10154. Mr. Gefeke was an interested Board Member of certain DWS funds by virtue of his positions with Deutsche Asset Management. As an interested person, Mr. Gefeke received no compensation from the fund.*

8 *Address: One Beacon Street, Boston, MA 02108.*

9 *Address: 60 Wall Street, New York, New York 10005.*

*The fund's Statement of Additional Information ("SAI") includes additional information about the Board Members. The SAI is available, without charge, upon request. If you would like to request a copy of the SAI, you may do so by calling the following toll-free number: (800) 728-3337.*

## Notes

DWS Investments is part of Deutsche Bank's Asset Management division and, within the US, represents the retail asset management activities of Deutsche Bank AG, Deutsche Bank Trust Company Americas, Deutsche Investment Management Americas Inc. and DWS Trust Company.

The views expressed in this report reflect those of the portfolio managers only through the end of the period of the report as stated on the cover. The managers' views are subject to change at any time based on market and other conditions and should not be construed as a recommendation.

This information must be preceded or accompanied by a current prospectus.

Portfolio changes should not be considered recommendations for action by individual investors.

DWS Investments Distributors, Inc.
222 South Riverside Plaza
Chicago, IL 60606
(800) 621-1148

VS2CFI-2 (2/11)

DWS INVESTMENTS
Deutsche Bank Group

DECEMBER 31, 2010

# ANNUAL REPORT

## DWS VARIABLE SERIES II

## DWS Diversified International Equity VIP

**This report must be preceded or accompanied by a prospectus. To obtain an additional prospectus or summary prospectus, if available, call (800) 728-3337 or your financial representative. We advise you to consider the Fund's objectives, risks, charges and expenses carefully before investing. The summary prospectus and prospectus contain this and other important information about the Fund. Please read the prospectus carefully before you invest.**



DWS INVESTMENTS
Deutsche Bank Group

# Performance Summary

## DWS Diversified International Equity VIP

**All performance shown is historical, assumes reinvestment of all dividend and capital gain distributions and does not guarantee future results. Investment return and principal value fluctuate with changing market conditions so that, when redeemed, shares may be worth more or less than their original cost. Current performance may be lower or higher than the performance data quoted. Please contact your participating insurance company for the Fund's most recent month-end performance. Performance doesn't reflect charges and fees ("contract charges") associated with the separate account that invests in the Fund or any variable life insurance policy or variable annuity contract for which the Fund is an investment option. These charges and fees will reduce returns.**

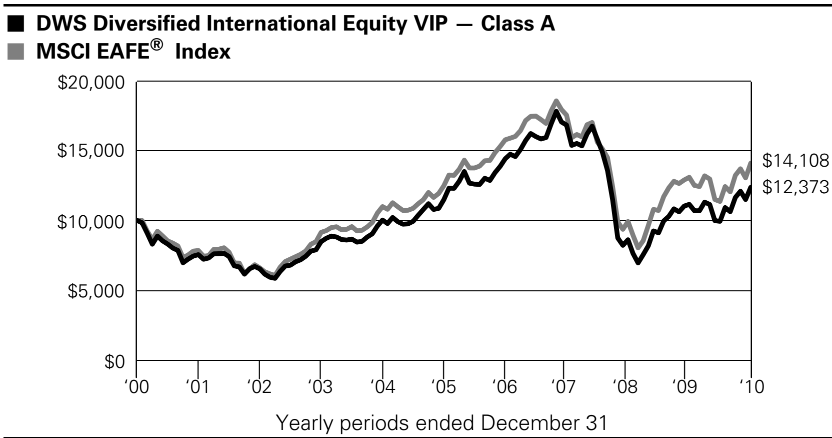
**The gross expense ratio of the Fund, as stated in the fee table of the prospectus dated May 1, 2010 is 0.96% for Class A shares and may differ from the expense ratio disclosed in the Financial Highlights table in this report.**

### Risk Considerations

Investing in foreign securities, particularly those of emerging markets, presents certain risks, such as currency fluctuations, political and economic changes, and market risks. Stocks may decline in value. See the prospectus for details.

Fund returns for the 3-year, 5-year and 10-year periods shown reflect a fee waiver and/or expense reimbursement. Without this waiver/reimbursement, returns would have been lower.

### Growth of an Assumed $10,000 Investment in DWS Diversified International Equity VIP




*The Morgan Stanley Capital International (MSCI) EAFE® Index is an unmanaged, free float-adjusted, market capitalization index that tracks international stock performance in the 21 developed markets of Europe, Australasia and the Far East. The MSCI indices are calculated using closing local market prices and translates into US dollars using the London close foreign exchange rates.*

*Index returns assume reinvestment of dividends and, unlike fund returns, do not reflect any fees or expenses. It is not possible to invest directly into an index.*

### Comparative Results

| DWS Diversified International Equity VIP | | 1-Year | 3-Year | 5-Year | 10-Year |
|---|---|---|---|---|---|
| **Class A** | Growth of $10,000 | $11,093 | $7,346 | $10,765 | $12,373 |
| | Average annual total return | 10.93% | –9.77% | 1.48% | 2.15% |
| MSCI EAFE Index | Growth of $10,000 | $10,775 | $8,040 | $11,292 | $14,108 |
| | Average annual total return | 7.75% | –7.02% | 2.46% | 3.50% |

*The growth of $10,000 is cumulative.*

# Information About Your Fund's Expenses

## DWS Diversified International Equity VIP

As an investor of the Fund, you incur two types of costs: ongoing expenses and transaction costs. Ongoing expenses include management fees and other Fund expenses. Examples of transaction costs include contract charges, redemption fees and account maintenance fees, which are not shown in this section. The following tables are intended to help you understand your ongoing expenses (in dollars) of investing in the Fund and to help you compare these expenses with the ongoing expenses of investing in other mutual funds. The example in the table is based on an investment of $1,000 invested at the beginning of the six-month period and held for the entire period (July 1, 2010 to December 31, 2010).

The tables illustrate your Fund's expenses in two ways:

- **Actual Fund Return.** This helps you estimate the actual dollar amount of ongoing expenses (but not transaction costs) paid on a $1,000 investment in the Fund using the Fund's actual return during the period. To estimate the expenses you paid over the period, simply divide your account value by $1,000 (for example, an $8,600 account value divided by $1,000 = 8.6), then multiply the result by the number in the "Expenses Paid per $1,000" line under the share class you hold.
- **Hypothetical 5% Fund Return.** This helps you to compare your Fund's ongoing expenses (but not transaction costs) with those of other mutual funds using the Fund's actual expense ratio and a hypothetical rate of return of 5% per year before expenses. Examples using a 5% hypothetical Fund return may be found in the shareholder reports of other mutual funds. The hypothetical account values and expenses may not be used to estimate the actual ending account balance or expenses you paid for the period.

Please note that the expenses shown in these tables are meant to highlight your ongoing expenses only and do not reflect any transaction costs. The "Expenses Paid per $1,000" line of the tables is useful in comparing ongoing expenses only and will not help you determine the relative total expense of owning different funds. If these transaction costs had been included, your costs would have been higher.

**Expenses and Value of a $1,000 Investment** for the six months ended December 31, 2010

| Actual Fund Return | Class A |
|---|---|
| Beginning Account Value 7/1/10 | $1,000.00 |
| Ending Account Value 12/31/10 | $1,245.00 |
| Expenses Paid per $1,000* | $ 5.21 |
| **Hypothetical 5% Fund Return** | **Class A** |
| Beginning Account Value 7/1/10 | $1,000.00 |
| Ending Account Value 12/31/10 | $1,020.57 |
| Expenses Paid per $1,000* | $ 4.69 |

* *Expenses are equal to the Fund's annualized expense ratio, multiplied by the average account value over the period, multiplied by the number of days in the most recent six-month period, then divided by 365.*

| Annualized Expense Ratio | Class A |
|---|---|
| DWS Variable Series II — DWS Diversified International Equity VIP | .92% |

For more information, please refer to the Fund's prospectus.

These tables do not reflect charges and fees ("contract charges") associated with the separate account that invests in the Fund or any variable life insurance policy or variable annuity contract for which the Fund is an investment option.

## DWS Diversified International Equity VIP

International equities withstood both the European debt crisis and the sluggish growth in Japan to finish 2010 with a gain of 7.75%, as measured by the MSCI EAFE Index. The Class A shares of the Fund returned 10.93% (unadjusted for contract charges), comfortably outpacing the benchmark.

In managing the Fund, we use a top-down approach based on the principle that country and sector, rather than stock selection, are the primary drivers of return. We divide the universe of international stocks into "risk units" according to sector and country: "UK Financials," for example. We assign these units weights to maximize diversification potential, and we rebalance the portfolio on a quarterly basis to maintain diversification.

The Fund's underweight in the financial sector made a substantial contribution to its return.[1] Our overall weighting in financials was less than 40% of the benchmark weight, which added substantial value at a time in which financials were one of the worst-performing sectors in the index. The primary reason for the sector's shortfall was the concern about European banks' exposure to the poor-performing debt of the region's smaller economies. Accordingly, our underweights in the financial sectors of Spain, France and Italy boosted our return.

Our position in the emerging markets also made a positive contribution to the Fund's return. The Fund is invested in two exchanged-traded funds, or ETFs — Vanguard Emerging Markets and iShares MSCI Emerging Markets Index — that together provide the Fund with diversified emerging-markets exposure.[2] The MCSI Emerging Markets Index returned 18.88% during 2010, well ahead of the MSCI EAFE Index.

The Fund's largest detractors were generally its underweights in the most economically sensitive sectors of the market, such as the materials, industrials and consumer discretionary sectors. Among risk units, the largest negative contributions came from our underweights in UK materials, Japan industrials and Australia materials.

We believe our proprietary investment process makes this a unique product within the universe of international investments. For investors looking for a way to diversify their domestic portfolios, DWS Diversified International Equity VIP offers a compelling combination of extensive diversification, low turnover and an approach that looks beyond market capitalization to structure a more optimized portfolio.

Robert Wang
Russell Shtern, CFA
*Portfolio Managers, QS Investors, LLC*
*Subadvisor to the Fund*

*The Morgan Stanley Capital International (MSCI) EAFE Index is an unmanaged, free float-adjusted, market capitalization index that tracks international stock performance in the 21 developed markets of Europe, Australasia and the Far East. The index is calculated using closing local market prices and translates into US dollars using the London close foreign exchange rates.*

*The Vanguard Emerging Markets invests in stocks of companies located in emerging markets around the world, such as Brazil, Russia, China, Korea and Taiwan. The fund seeks to closely track the return of the MSCI Emerging Markets Index over the long term.*

*The iShares MSCI Emerging Markets Index seeks to provide investment results that correspond generally to the price and yield performance, before fees and expenses, of publicly traded securities in emerging markets, as represented by the MSCI Emerging Markets Index.*

*The Morgan Stanley Capital International (MSCI) Emerging Markets Index is an unmanaged, capitalization-weighted index of companies in a universe of 26 emerging markets. The index is calculated using closing local market prices and translates into US dollars using the London close foreign exchange rates.*

*Index returns assume reinvested dividends and, unlike fund returns, do not reflect any fees or expenses. It is not possible to invest directly into an index.*

1 *"Overweight" means the Fund holds a higher weighting in a given sector or security than the benchmark. "Underweight" means the Fund holds a lower weighting.*

2 *An exchange-traded fund (ETF) is a security that tracks an index, a commodity or a basket of assets like an index fund, but trades like a stock on an exchange.*

*Portfolio management market commentary is as of December 31, 2010, and may not come to pass. This information is subject to change at any time based on market and other conditions. Past performance does not guarantee future results. Current and future portfolio holdings are subject to risk.*

# Portfolio Summary

## DWS Diversified International Equity VIP

| **Asset Allocation** (As a % of Investment Portfolio excluding Securities Lending Collateral) | **12/31/10** | **12/31/09** |
|---|---|---|
| Common Stocks | 87% | 87% |
| Exchange-Traded Funds | 9% | 9% |
| Cash Equivalents* | 3% | 3% |
| Preferred Stocks | 1% | 1% |
| Government & Agency Obligations | — | 0% |
| | 100% | 100% |

| **Sector Diversification** (As a % of Common Stocks, Preferred Stocks and Rights) | **12/31/10** | **12/31/09** |
|---|---|---|
| Telecommunication Services | 16% | 15% |
| Consumer Staples | 12% | 14% |
| Materials | 11% | 9% |
| Industrials | 11% | 9% |
| Financials | 10% | 10% |
| Health Care | 9% | 13% |
| Energy | 9% | 6% |
| Utilities | 8% | 9% |
| Consumer Discretionary | 8% | 9% |
| Information Technology | 6% | 6% |
| | 100% | 100% |

| **Geographical Diversification** (As a % of Investment Portfolio excluding Cash Equivalents and Securities Lending Collateral) | **12/31/10** | **12/31/09** |
|---|---|---|
| Continental Europe | 49% | 53% |
| Japan | 21% | 16% |
| Emerging Markets | 10% | 9% |
| United Kingdom | 7% | 7% |
| Canada | 5% | 5% |
| Australia | 4% | 6% |
| Asia (excluding Japan) | 4% | 4% |
| Other | — | 0% |
| | 100% | 100% |

* *In order to keep cash on hand to meet shareholder redemptions or other needs while maintaining exposure to the market, the Fund invests in futures contracts.*

*Asset allocation, sector and geographical diversifications are subject to change.*

*For more complete details about the Fund's investment portfolio, see page 6.*

Following the Fund's fiscal first and third quarter-end, a complete portfolio holdings listing is filed with the SEC on Form N-Q. The form will be available on the SEC's Web site at www.sec.gov, and it also may be reviewed and copied at the SEC's Public Reference Room in Washington, D.C. Information on the operation of the SEC's Public Reference Room may be obtained by calling (800) SEC-0330. The Fund's portfolio holdings are also posted on www.dws-investments.com from time to time. Please see the Fund's current prospectus for more information.

## DWS Diversified International Equity VIP

| | Shares | Value ($) |
|---|---|---|
| **Common Stocks 86.4%** | | |
| **Australia 4.3%** | | |
| Asciano Ltd.* | 17,279 | 28,188 |
| Australia & New Zealand Banking Group Ltd. | 2,823 | 67,420 |
| BHP Billiton Ltd. | 9,579 | 443,332 |
| Brambles Ltd. | 13,105 | 95,435 |
| Coca-Cola Amatil Ltd. | 3,584 | 39,810 |
| Cochlear Ltd. | 862 | 70,894 |
| Commonwealth Bank of Australia | 1,574 | 81,734 |
| Crown Ltd. | 9,187 | 77,521 |
| CSL Ltd. | 8,694 | 322,699 |
| Fairfax Media Ltd. | 54,011 | 77,339 |
| Foster's Group Ltd. | 10,776 | 62,603 |
| Leighton Holdings Ltd. | 1,643 | 51,725 |
| National Australia Bank Ltd. | 2,600 | 63,025 |
| Newcrest Mining Ltd. | 1,579 | 65,311 |
| Origin Energy Ltd. | 8,027 | 136,779 |
| Paladin Energy Ltd.* | 7,326 | 36,941 |
| Qantas Airways Ltd.* | 18,444 | 47,916 |
| QBE Insurance Group Ltd. | 2,063 | 38,297 |
| Rio Tinto Ltd. | 900 | 78,677 |
| Santos Ltd. | 9,683 | 130,235 |
| Sonic Healthcare Ltd. | 5,537 | 65,694 |
| TABCORP Holdings Ltd. | 15,130 | 110,027 |
| Tatts Group Ltd. | 24,689 | 65,150 |
| Telstra Corp., Ltd. | 144,475 | 412,276 |
| Toll Holdings Ltd. | 7,945 | 46,563 |
| Transurban Group (Units) | 14,907 | 78,064 |
| Wesfarmers Ltd. | 5,593 | 183,057 |
| Westfield Group (REIT) (Units) | 3,912 | 38,331 |
| Westfield Retail Trust (REIT)* | 3,912 | 10,283 |
| Westpac Banking Corp. | 2,569 | 58,358 |
| Woodside Petroleum Ltd. | 5,329 | 231,973 |
| Woolworths Ltd. | 6,442 | 177,702 |
| WorleyParsons Ltd. | 2,509 | 68,620 |
| (Cost $2,231,498) | | **3,561,979** |
| **Austria 0.5%** | | |
| Erste Group Bank AG | 3,997 | 187,838 |
| Immofinanz AG* | 21,500 | 91,676 |
| Raiffeisen Bank International AG | 1,267 | 69,401 |
| Vienna Insurance Group AG Wiener Versicherung Gruppe | 1,323 | 68,751 |
| (Cost $249,456) | | **417,666** |
| **Belgium 1.3%** | | |
| Ageas | 27,095 | 61,914 |
| Anheuser-Busch InBev NV | 6,331 | 362,093 |
| Compagnie Nationale a Portefeuille | 907 | 44,360 |
| Delhaize Group | 1,198 | 88,481 |
| Dexia SA* | 9,616 | 33,409 |
| Groupe Bruxelles Lambert SA | 588 | 49,447 |
| KBC Groep NV* | 1,952 | 66,516 |
| Solvay SA | 1,904 | 202,909 |
| Umicore | 3,759 | 195,501 |
| (Cost $778,860) | | **1,104,630** |
| **Bermuda 0.2%** | | |
| Seadrill Ltd. (Cost $63,651) | 4,800 | **162,369** |

| | Shares | Value ($) |
|---|---|---|
| **Canada 4.9%** | | |
| Agnico-Eagle Mines Ltd. | 700 | 53,927 |
| Bank of Montreal | 700 | 40,467 |
| Bank of Nova Scotia | 1,100 | 63,170 |
| Barrick Gold Corp. | 2,600 | 138,904 |
| BCE, Inc. | 4,300 | 152,833 |
| Bombardier, Inc. "B" | 8,400 | 42,325 |
| Canadian Imperial Bank of Commerce | 400 | 31,512 |
| Canadian National Railway Co. | 3,100 | 206,864 |
| Canadian Natural Resources Ltd. | 2,800 | 124,892 |
| Canadian Pacific Railway Ltd. | 1,200 | 77,989 |
| Canadian Tire Corp., Ltd. "A" | 1,000 | 68,581 |
| Canadian Utilities Ltd. "A" | 2,800 | 153,193 |
| CGI Group, Inc. "A"* | 4,600 | 79,574 |
| EnCana Corp. | 1,500 | 43,885 |
| Fortis, Inc. | 5,800 | 198,214 |
| George Weston Ltd. | 800 | 67,746 |
| Gildan Activewear, Inc.* | 900 | 25,661 |
| Goldcorp, Inc. | 1,800 | 83,057 |
| Imperial Oil Ltd. | 2,100 | 85,707 |
| Kinross Gold Corp. | 2,300 | 43,742 |
| Loblaw Companies Ltd. | 2,100 | 85,263 |
| Magna International, Inc. "A" | 1,906 | 99,508 |
| Manulife Financial Corp. | 2,800 | 48,295 |
| Metro, Inc. "A" | 1,700 | 77,280 |
| Open Text Corp.* | 700 | 32,195 |
| Potash Corp. of Saskatchewan, Inc. | 700 | 108,748 |
| Research In Motion Ltd.* | 7,100 | 414,661 |
| Rogers Communications, Inc. "B" (a) | 5,000 | 173,992 |
| Royal Bank of Canada | 1,400 | 73,668 |
| Saputo, Inc. | 2,200 | 87,575 |
| Shaw Communications, Inc. "B" | 3,800 | 81,595 |
| Shoppers Drug Mart Corp. | 2,900 | 115,294 |
| SNC-Lavalin Group, Inc. | 1,200 | 72,135 |
| Suncor Energy, Inc. | 3,520 | 135,518 |
| Teck Resources Ltd. "B" | 1,500 | 93,216 |
| Telus Corp. | 1,700 | 73,946 |
| Thomson Reuters Corp. (b) | 3,000 | 112,360 |
| Thomson Reuters Corp. (b) | 1,158 | 43,159 |
| Tim Hortons, Inc. | 2,400 | 99,205 |
| Toronto-Dominion Bank | 1,000 | 74,676 |
| TransAlta Corp. | 8,100 | 172,297 |
| Viterra, Inc.* | 4,900 | 45,733 |
| (Cost $2,788,578) | | **4,102,562** |
| **Cyprus 0.0%** | | |
| Bank of Cyprus Public Co., Ltd. (Cost $60,706) | 11,062 | **38,138** |
| **Denmark 2.2%** | | |
| A P Moller-Maersk AS "A" | 10 | 88,121 |
| A P Moller-Maersk AS "B" | 25 | 226,448 |
| Carlsberg AS "B" | 5,037 | 504,084 |
| Coloplast AS "B" | 299 | 40,638 |
| Danske Bank AS* | 12,075 | 309,525 |
| DSV AS | 3,456 | 76,339 |
| Novo Nordisk AS "B" | 3,809 | 428,722 |
| Tryg AS | 621 | 28,673 |
| Vestas Wind Systems AS* | 3,931 | 124,142 |

*The accompanying notes are an integral part of the financial statements.*

| | Shares | Value ($) |
|---|---|---|
| William Demant Holding AS* | 427 | 31,543 |
| (Cost $1,278,483) | | **1,858,235** |
| **Finland 3.1%** | | |
| Fortum Oyj | 22,604 | 685,753 |
| Kone Oyj "B" | 3,962 | 220,119 |
| Metso Corp. | 3,040 | 169,715 |
| Nokia Oyj | 37,878 | 392,071 |
| Outokumpu Oyj | 4,027 | 74,775 |
| Pohjola Bank PLC | 5,199 | 62,309 |
| Rautaruukki Oyj | 2,774 | 64,975 |
| Sampo Oyj "A" | 9,439 | 253,037 |
| Stora Enso Oyj "R" | 19,919 | 204,757 |
| UPM-Kymmene Oyj | 16,621 | 293,846 |
| Wartsila Corp. | 1,893 | 144,496 |
| (Cost $1,735,409) | | **2,565,853** |
| **France 7.2%** | | |
| Air Liquide SA | 2,497 | 315,789 |
| Alcatel-Lucent* | 27,533 | 80,207 |
| Atos Origin SA* | 697 | 37,107 |
| AXA SA | 3,081 | 51,258 |
| BNP Paribas | 1,550 | 98,613 |
| Bouygues SA | 1,062 | 45,775 |
| Cap Gemini | 1,723 | 80,425 |
| Carrefour SA | 6,517 | 268,662 |
| Casino Guichard-Perrachon SA | 996 | 97,093 |
| Compagnie de Saint-Gobain | 1,739 | 89,467 |
| Compagnie Generale de Geophysique-Veritas* | 1,118 | 34,026 |
| Credit Agricole SA | 3,149 | 39,993 |
| DANONE SA | 6,358 | 399,491 |
| Dassault Systemes SA | 1,112 | 83,838 |
| Electricite de France | 964 | 39,541 |
| Essilor International SA | 3,351 | 215,725 |
| France Telecom SA | 50,588 | 1,054,234 |
| GDF Suez | 6,014 | 215,780 |
| Iliad SA | 426 | 46,338 |
| L'Oreal SA | 2,731 | 303,195 |
| Lafarge SA | 1,526 | 95,679 |
| LVMH Moet Hennessy Louis Vuitton SA | 420 | 69,089 |
| Pernod Ricard SA | 2,240 | 210,610 |
| Sanofi-Aventis | 13,946 | 891,735 |
| Schneider Electric SA | 627 | 93,840 |
| Societe Generale | 1,401 | 75,298 |
| Suez Environnement Co. | 1,869 | 38,587 |
| Technip SA | 213 | 19,668 |
| Total SA | 10,370 | 549,447 |
| Unibail-Rodamco SE (REIT) | 265 | 52,410 |
| Vallourec SA | 689 | 72,368 |
| Veolia Environnement | 2,122 | 62,015 |
| Vinci SA | 1,171 | 63,656 |
| Vivendi | 3,089 | 83,382 |
| (Cost $5,022,648) | | **5,974,341** |
| **Germany 4.9%** | | |
| Allianz SE (Registered) | 1,458 | 173,254 |
| BASF SE | 2,590 | 206,619 |
| Bayer AG | 2,784 | 205,730 |
| Bayerische Motoren Werke (BMW) AG | 649 | 51,004 |
| Beiersdorf AG | 3,770 | 209,184 |
| Daimler AG (Registered)* | 1,906 | 129,162 |
| Deutsche Boerse AG | 688 | 47,619 |
| Deutsche Post AG (Registered) | 3,555 | 60,295 |
| Deutsche Telekom AG (Registered) | 81,553 | 1,053,208 |
| E.ON AG | 6,205 | 190,309 |
| HeidelbergCement AG | 833 | 52,233 |
| Henkel AG & Co. KGaA | 4,251 | 219,399 |
| Infineon Technologies AG* | 8,199 | 76,227 |
| K+S AG | 629 | 47,406 |
| Linde AG | 769 | 116,725 |
| MAN SE | 245 | 29,130 |
| Merck KGaA | 430 | 34,415 |
| Metro AG | 4,361 | 313,982 |
| Muenchener Rueckversicherungs-Gesellschaft AG (Registered) | 598 | 90,704 |
| RWE AG | 1,021 | 68,116 |
| SAP AG | 5,623 | 286,324 |
| Siemens AG (Registered) | 2,260 | 279,799 |
| Suedzucker AG | 3,769 | 100,244 |
| ThyssenKrupp AG | 1,086 | 44,993 |
| (Cost $2,921,913) | | **4,086,081** |
| **Greece 0.3%** | | |
| Alpha Bank AE* | 9,054 | 45,976 |
| EFG Eurobank Ergasias* | 4,435 | 22,224 |
| National Bank of Greece SA* | 18,976 | 153,414 |
| Piraeus Bank SA* | 7,558 | 36,864 |
| (Cost $428,467) | | **258,478** |
| **Hong Kong 2.2%** | | |
| Cheung Kong (Holdings) Ltd. | 5,000 | 77,064 |
| Cheung Kong Infrastructure Holdings Ltd. | 7,000 | 32,060 |
| CLP Holdings Ltd. | 19,500 | 158,804 |
| Esprit Holdings Ltd. | 18,495 | 87,802 |
| Genting Singapore PLC* | 116,000 | 197,951 |
| Hang Seng Bank Ltd. | 2,200 | 36,116 |
| Hong Kong & China Gas Co., Ltd. | 51,500 | 122,310 |
| Hong Kong Exchanges & Clearing Ltd. | 3,500 | 79,386 |
| HongKong Electric Holdings Ltd. | 17,500 | 110,320 |
| Hutchison Whampoa Ltd. | 26,000 | 268,269 |
| Li & Fung Ltd. | 26,000 | 152,030 |
| MTR Corp., Ltd. | 28,500 | 103,766 |
| Noble Group Ltd. | 29,363 | 49,649 |
| NWS Holdings Ltd. | 30,000 | 45,466 |
| Shangri-La Asia Ltd. | 24,000 | 65,150 |
| SJM Holdings Ltd. | 16,000 | 25,401 |
| Sun Hung Kai Properties Ltd. | 5,000 | 82,724 |
| Swire Pacific Ltd. "A" | 3,500 | 57,547 |
| Yue Yuen Industrial (Holdings) Ltd. | 14,500 | 52,047 |
| (Cost $1,126,048) | | **1,803,862** |
| **Ireland 0.7%** | | |
| CRH PLC (b) | 20,956 | 434,054 |
| CRH PLC (b) | 1,456 | 30,449 |
| Experian PLC | 6,430 | 80,000 |
| (Cost $437,178) | | **544,503** |
| **Italy 3.7%** | | |
| A2A SpA | 20,926 | 28,791 |
| Assicurazioni Generali SpA | 3,242 | 61,622 |
| Atlantia SpA | 5,502 | 112,337 |
| Enel SpA | 46,072 | 230,142 |
| Eni SpA | 20,641 | 451,027 |
| Fiat SpA | 12,889 | 265,393 |
| Finmeccanica SpA | 12,332 | 140,217 |
| Intesa Sanpaolo | 25,029 | 67,876 |

*The accompanying notes are an integral part of the financial statements.*

| | Shares | Value ($) |
|---|---|---|
| Luxottica Group SpA | 2,649 | 80,626 |
| Mediaset SpA | 10,870 | 65,803 |
| Prysmian SpA | 6,182 | 105,278 |
| Saipem SpA | 2,103 | 103,613 |
| Snam Rete Gas SpA | 9,753 | 48,499 |
| Telecom Italia SpA | 552,428 | 714,199 |
| Telecom Italia SpA (RSP) | 372,172 | 404,058 |
| Terna — Rete Elettrica Nationale SpA | 14,939 | 63,103 |
| UBI Banca — Unione di Banche Italiane ScpA | 3,919 | 34,330 |
| UniCredit SpA | 41,574 | 85,980 |
| (Cost $2,699,436) | | **3,062,894** |
| **Japan 20.1%** | | |
| AEON Co., Ltd. | 11,300 | 141,313 |
| Ajinomoto Co., Inc. | 11,000 | 114,568 |
| Alfresa Holdings Corp. | 1,000 | 44,374 |
| Asahi Breweries Ltd. | 7,000 | 135,513 |
| Asahi Glass Co., Ltd. | 8,000 | 93,400 |
| Asahi Kasei Corp. | 14,000 | 91,320 |
| Astellas Pharma, Inc. | 5,900 | 224,755 |
| Canon, Inc. | 6,200 | 317,841 |
| Central Japan Railway Co. | 5 | 41,861 |
| Chubu Electric Power Co., Inc. | 8,600 | 211,388 |
| Chugai Pharmaceutical Co., Ltd. | 3,700 | 67,859 |
| Chugoku Electric Power Co., Inc. | 3,500 | 71,127 |
| Cosmo Oil Co., Ltd. | 43,000 | 140,754 |
| Dai-ichi Life Insurance Co., Ltd. | 47 | 76,280 |
| Daiichi Sankyo Co., Ltd. | 9,500 | 207,835 |
| Daikin Industries Ltd. | 1,100 | 38,978 |
| Daiwa House Industry Co., Ltd. | 3,000 | 36,766 |
| Daiwa Securities Group, Inc. | 10,000 | 51,423 |
| Denso Corp. | 1,100 | 37,930 |
| East Japan Railway Co. | 926 | 60,196 |
| Eisai Co., Ltd. (a) | 3,700 | 133,913 |
| Electric Power Development Co., Ltd. | 2,600 | 81,558 |
| FamilyMart Co., Ltd. | 1,400 | 52,743 |
| FANUC Corp. | 900 | 138,066 |
| FUJIFILM Holdings Corp. | 2,300 | 83,088 |
| Fujitsu Ltd. | 13,000 | 90,394 |
| Hisamitsu Pharmaceutical Co., Inc. | 900 | 37,898 |
| Hitachi Ltd. | 18,000 | 96,042 |
| Hokkaido Electric Power Co., Inc. | 2,400 | 49,068 |
| Hokuriku Electric Power Co. | 2,800 | 68,793 |
| Honda Motor Co., Ltd. | 2,900 | 114,619 |
| HOYA | 2,100 | 50,957 |
| Idemitsu Kosan Co., Ltd. | 1,500 | 159,151 |
| INPEX Corp. | 102 | 596,635 |
| ITOCHU Corp. | 6,000 | 60,680 |
| Japan Petroleum Exploration Co., Ltd. | 2,300 | 87,453 |
| Japan Prime Realty Investment Corp. (REIT) | 10 | 30,790 |
| Japan Retail Fund Investment Corp. (REIT) | 20 | 38,352 |
| Japan Tobacco, Inc. | 73 | 269,810 |
| JFE Holdings, Inc. | 5,300 | 184,414 |
| JX Holdings, Inc. | 106,320 | 720,011 |
| Kansai Electric Power Co., Inc. | 9,900 | 244,348 |
| Kao Corp. | 7,800 | 210,059 |
| KDDI Corp. | 69 | 398,341 |
| Keyence Corp. | 200 | 57,822 |
| Kikkoman Corp. | 4,000 | 44,753 |
| Kirin Holdings Co., Ltd. | 14,000 | 196,265 |
| Kobe Steel Ltd. | 33,000 | 83,641 |
| Komatsu Ltd. | 4,200 | 126,962 |
| Kubota Corp. | 10,000 | 94,620 |
| Kuraray Co., Ltd. | 6,000 | 85,941 |
| Kyocera Corp. | 800 | 81,591 |
| Kyowa Hakko Kirin Co., Ltd. | 5,000 | 51,447 |
| Kyushu Electric Power Co., Inc. | 4,800 | 107,579 |
| Lawson, Inc. | 900 | 44,503 |
| MEIJI Holdings Co., Ltd. | 1,200 | 54,215 |
| Miraca Holdings, Inc. | 1,000 | 40,261 |
| Mitsubishi Chemical Holdings Corp. | 12,000 | 81,380 |
| Mitsubishi Corp. | 6,300 | 170,369 |
| Mitsubishi Electric Corp. | 11,000 | 115,331 |
| Mitsubishi Estate Co., Ltd. | 5,000 | 92,668 |
| Mitsubishi Heavy Industries Ltd. | 18,000 | 67,574 |
| Mitsubishi Materials Corp.* | 29,000 | 92,404 |
| Mitsubishi Tanabe Pharma Corp. | 3,000 | 50,656 |
| Mitsubishi UFJ Financial Group, Inc. | 51,400 | 277,722 |
| Mitsui & Co., Ltd. | 5,000 | 82,495 |
| Mitsui Fudosan Co., Ltd. | 3,000 | 59,759 |
| Mitsui O.S.K Lines Ltd. | 7,000 | 47,717 |
| Mizuho Financial Group, Inc. | 88,000 | 165,702 |
| MS&AD Insurance Group Holdings, Inc. | 2,400 | 60,114 |
| Murata Manufacturing Co., Ltd. | 1,300 | 91,029 |
| NEC Corp. | 26,000 | 78,070 |
| Nidec Corp. | 500 | 50,417 |
| Nintendo Co., Ltd. | 500 | 146,692 |
| Nippon Steel Corp. | 58,000 | 208,407 |
| Nippon Telegraph & Telephone Corp. | 12,109 | 553,990 |
| Nishi-Nippon City Bank Ltd. | 13,000 | 39,521 |
| Nissan Motor Co., Ltd. | 6,000 | 57,065 |
| Nisshin Seifun Group, Inc. | 4,000 | 50,755 |
| Nissin Foods Holdings Co., Ltd. | 1,100 | 39,414 |
| Nitto Denko Corp. | 1,900 | 89,405 |
| NKSJ Holdings, Inc.* | 12,000 | 88,289 |
| Nomura Holdings, Inc. | 12,000 | 76,048 |
| Nomura Real Estate Office Fund, Inc. (REIT) | 7 | 50,506 |
| NTT DoCoMo, Inc. | 354 | 618,098 |
| OJI Paper Co., Ltd. | 11,000 | 53,224 |
| Olympus Corp. | 3,500 | 105,835 |
| Ono Pharmaceutical Co., Ltd. | 1,500 | 70,003 |
| Oriental Land Co., Ltd. | 700 | 64,821 |
| ORIX Corp. | 260 | 25,562 |
| Osaka Gas Co., Ltd. | 30,000 | 116,371 |
| Panasonic Corp. | 4,600 | 64,934 |
| Resona Holdings, Inc. (a) | 2,600 | 15,595 |
| Ricoh Co., Ltd. | 4,000 | 58,556 |
| ROHM Co., Ltd. | 1,100 | 71,796 |
| Santen Pharmaceutical Co., Ltd. | 1,300 | 45,151 |
| Sapporo Hokuyo Holdings, Inc. | 10,400 | 48,644 |
| Sapporo Holdings Ltd. | 7,000 | 31,715 |
| Seven & I Holdings Co., Ltd. | 12,000 | 320,512 |
| Sharp Corp. | 3,000 | 30,896 |
| Shikoku Electric Power Co., Inc. | 2,400 | 70,587 |
| Shin-Etsu Chemical Co., Ltd. | 4,100 | 221,962 |
| Shionogi & Co., Ltd. | 5,000 | 98,446 |
| Shiseido Co., Ltd. | 5,000 | 109,169 |
| Showa Shell Sekiyu KK | 14,800 | 135,502 |
| SOFTBANK Corp. | 17,300 | 598,557 |
| Sony Corp. | 2,100 | 75,629 |
| Sumitomo Chemical Co., Ltd. | 14,000 | 68,912 |

*The accompanying notes are an integral part of the financial statements.*

| | Shares | Value ($) |
|---|---|---|
| Sumitomo Corp. | 5,300 | 74,925 |
| Sumitomo Electric Industries Ltd. | 6,500 | 90,214 |
| Sumitomo Metal Industries Ltd. | 26,000 | 63,987 |
| Sumitomo Metal Mining Co., Ltd. | 4,000 | 69,812 |
| Sumitomo Mitsui Financial Group, Inc. | 5,700 | 202,892 |
| Sumitomo Realty & Development Co., Ltd. | 2,000 | 47,715 |
| Sumitomo Trust & Banking Co., Ltd. | 9,000 | 56,720 |
| Suzuken Co., Ltd. | 1,300 | 39,690 |
| Sysmex Corp. | 1,100 | 76,235 |
| T&D Holdings, Inc. | 1,800 | 45,599 |
| Taisho Pharmaceutical Co., Ltd. | 2,000 | 43,759 |
| Takeda Pharmaceutical Co., Ltd. | 10,200 | 501,659 |
| TDK Corp. | 1,200 | 83,399 |
| Terumo Corp. | 2,300 | 129,328 |
| Tohoku Electric Power Co., Inc. | 5,600 | 124,836 |
| Tokio Marine Holdings, Inc. | 2,200 | 65,711 |
| Tokyo Electric Power Co., Inc. | 21,600 | 527,510 |
| Tokyo Electron Ltd. | 900 | 56,898 |
| Tokyo Gas Co., Ltd. | 31,000 | 137,415 |
| TonenGeneral Sekiyu KK | 19,000 | 207,743 |
| Toray Industries, Inc. | 10,000 | 59,696 |
| Toshiba Corp. | 25,000 | 136,079 |
| Toyo Suisan Kaisha Ltd. | 2,000 | 44,482 |
| Toyota Motor Corp. | 4,600 | 181,144 |
| Tsumura & Co. | 1,500 | 48,553 |
| Unicharm Corp. | 1,500 | 59,585 |
| UNY Co., Ltd. | 5,600 | 56,576 |
| Yakult Honsha Co., Ltd. | 1,700 | 48,948 |
| Yamaguchi Financial Group, Inc. | 3,000 | 30,368 |
| (Cost $13,501,410) | | **16,687,718** |
| **Luxembourg 0.5%** | | |
| ArcelorMittal | 6,320 | 239,681 |
| Millicom International Cellular SA (SDR) | 943 | 90,465 |
| Tenaris SA | 4,211 | 103,183 |
| (Cost $232,092) | | **433,329** |
| **Macau 0.2%** | | |
| Sands China Ltd.* | 32,000 | 70,811 |
| Wynn Macau Ltd. | 30,000 | 67,003 |
| (Cost $91,291) | | **137,814** |
| **Netherlands 5.2%** | | |
| AEGON NV* | 13,839 | 84,624 |
| Akzo Nobel NV | 4,125 | 256,236 |
| ASML Holding NV | 11,111 | 429,097 |
| Heineken Holding NV | 913 | 39,682 |
| Heineken NV | 3,364 | 164,933 |
| ING Groep NV (CVA)* | 22,591 | 219,771 |
| Koninklijke (Royal) KPN NV | 73,369 | 1,070,630 |
| Koninklijke Ahold NV | 14,948 | 197,273 |
| Koninklijke DSM NV | 2,400 | 136,639 |
| Koninklijke Philips Electronics NV | 8,829 | 270,415 |
| Randstad Holding NV* | 1,215 | 64,132 |
| Reed Elsevier NV | 17,980 | 222,415 |
| Royal Dutch Shell PLC "A" | 3,949 | 131,665 |
| Royal Dutch Shell PLC "B" | 3,179 | 104,827 |
| TNT NV | 4,235 | 111,770 |
| Unilever NV (CVA) | 21,114 | 657,401 |
| Wolters Kluwer NV | 9,269 | 203,133 |
| (Cost $3,155,279) | | **4,364,643** |

| | Shares | Value ($) |
|---|---|---|
| **Norway 2.7%** | | |
| Aker Solutions ASA | 3,600 | 61,310 |
| DnB NOR ASA | 24,684 | 346,421 |
| Norsk Hydro ASA | 35,480 | 259,456 |
| Orkla ASA | 33,980 | 330,413 |
| Renewable Energy Corp. ASA* | 6,626 | 20,237 |
| Statoil ASA | 17,400 | 413,572 |
| Telenor ASA | 25,300 | 411,353 |
| Yara International ASA | 7,642 | 442,069 |
| (Cost $1,356,007) | | **2,284,831** |
| **Portugal 0.3%** | | |
| EDP — Energias de Portugal SA (Cost $266,681) | 79,204 | **263,648** |
| **Singapore 1.7%** | | |
| CapitaLand Ltd. | 20,000 | 57,817 |
| DBS Group Holdings Ltd. | 10,000 | 111,583 |
| Fraser & Neave Ltd. | 15,000 | 74,921 |
| Jardine Cycle & Carriage Ltd. | 2,000 | 57,038 |
| Keppel Corp., Ltd. | 14,000 | 123,489 |
| Oversea-Chinese Banking Corp., Ltd. | 14,000 | 107,780 |
| SembCorp Industries Ltd. | 19,000 | 76,098 |
| Singapore Airlines Ltd. | 6,000 | 71,532 |
| Singapore Exchange Ltd. | 7,000 | 45,927 |
| Singapore Press Holdings Ltd. | 37,000 | 114,747 |
| Singapore Technologies Engineering Ltd. | 15,000 | 39,974 |
| Singapore Telecommunications Ltd. | 167,000 | 396,891 |
| United Overseas Bank Ltd. | 7,000 | 99,271 |
| (Cost $773,177) | | **1,377,068** |
| **Spain 3.8%** | | |
| Abertis Infraestructuras SA | 5,893 | 106,010 |
| ACS, Actividades de Construccion y Servicios SA (a) | 2,437 | 114,277 |
| Banco Bilbao Vizcaya Argentaria SA | 9,332 | 94,405 |
| Banco Santander SA | 14,432 | 153,345 |
| EDP Renovaveis SA* | 11,598 | 67,217 |
| Enagas | 2,258 | 44,983 |
| Ferrovial SA | 9,049 | 89,992 |
| Gas Natural SDG SA | 2,049 | 31,759 |
| Gestevision Telecinco SA | 3,887 | 42,760 |
| Iberdrola Renovables | 11,066 | 39,296 |
| Iberdrola SA | 31,585 | 243,338 |
| Iberia Lineas Aereas de Espana SA* | 8,829 | 37,697 |
| Industria de Diseno Textil SA | 4,356 | 326,437 |
| Red Electrica Corporacion SA | 1,144 | 53,788 |
| Repsol YPF SA | 22,674 | 632,404 |
| Telefonica SA | 45,620 | 1,036,077 |
| Zardoya Otis SA | 3,050 | 42,985 |
| (Cost $2,508,005) | | **3,156,770** |
| **Sweden 3.1%** | | |
| AB SKF "B" | 2,358 | 67,923 |
| Assa Abloy AB "B" | 2,544 | 71,733 |
| Atlas Copco AB "A" | 3,215 | 81,187 |
| Boliden AB | 7,309 | 148,741 |
| Electrolux AB "B" | 3,335 | 94,669 |
| Hennes & Mauritz AB "B" | 11,314 | 376,974 |
| Holmen AB "B" | 2,160 | 71,148 |
| Husqvarna AB "B" | 7,799 | 65,087 |
| Nordea Bank AB | 12,273 | 133,467 |
| Sandvik AB | 5,637 | 109,770 |
| Skandinaviska Enskilda Banken AB "A" | 6,486 | 54,090 |

*The accompanying notes are an integral part of the financial statements.*

| | Shares | Value ($) |
|---|---|---|
| Skanska AB "B" | 3,667 | 72,717 |
| SSAB AB "A" | 5,874 | 98,701 |
| Svenska Cellulosa AB "B" | 18,870 | 297,735 |
| Svenska Handelsbanken AB "A" | 2,807 | 89,680 |
| Tele2 AB "B" | 4,023 | 84,051 |
| Telefonaktiebolaget LM Ericsson "B" | 28,799 | 333,484 |
| TeliaSonera AB | 21,657 | 171,703 |
| Volvo AB "B"* | 7,507 | 133,796 |
| (Cost $1,485,950) | | **2,556,656** |
| **Switzerland 6.6%** | | |
| ABB Ltd. (Registered)* | 11,048 | 246,740 |
| Adecco SA (Registered) | 824 | 53,911 |
| Aryzta AG* | 543 | 25,085 |
| Compagnie Financiere Richemont SA "A" | 4,125 | 242,678 |
| Credit Suisse Group AG (Registered) | 1,994 | 80,455 |
| Geberit AG (Registered) | 332 | 76,769 |
| Givaudan SA (Registered) | 102 | 110,133 |
| Holcim Ltd. (Registered) | 2,786 | 210,546 |
| Lonza Group AG (Registered) | 466 | 37,382 |
| Nestle SA (Registered) | 19,171 | 1,122,990 |
| Novartis AG (Registered) | 9,930 | 584,327 |
| Roche Holding AG (Genusschein) | 3,411 | 500,027 |
| Sika AG | 27 | 59,255 |
| Sonova Holding AG (Registered) | 289 | 37,430 |
| STMicroelectronics NV | 7,073 | 73,146 |
| Swatch Group AG (Bearer) | 301 | 134,189 |
| Swiss Reinsurance Co., Ltd. (Registered) | 1,091 | 59,420 |
| Swisscom AG (Registered) | 2,760 | 1,214,110 |
| Syngenta AG (Registered) | 861 | 252,195 |
| UBS AG (Registered)* | 7,534 | 123,650 |
| Wolseley PLC* | 2,345 | 74,804 |
| Xstrata PLC | 2,858 | 67,084 |
| Zurich Financial Services AG | 398 | 103,083 |
| (Cost $3,299,178) | | **5,489,409** |
| **United Kingdom 6.7%** | | |
| Anglo American PLC | 3,286 | 170,884 |
| ARM Holdings PLC | 29,996 | 197,964 |
| AstraZeneca PLC | 8,391 | 382,268 |
| Autonomy Corp. PLC* | 5,572 | 130,744 |
| BAE Systems PLC | 18,633 | 95,867 |
| Barclays PLC | 8,467 | 34,540 |
| BG Group PLC | 5,435 | 109,819 |
| BHP Billiton PLC | 4,437 | 176,471 |
| BP PLC | 25,484 | 184,973 |
| British American Tobacco PLC | 2,268 | 87,110 |
| British Sky Broadcasting Group PLC | 4,941 | 56,698 |
| BT Group PLC | 57,356 | 161,678 |
| Cable & Wireless Communications PLC | 24,059 | 18,204 |
| Capita Group PLC | 5,549 | 60,257 |
| Centrica PLC | 28,642 | 148,078 |
| Compass Group PLC | 11,814 | 107,016 |
| Diageo PLC | 2,849 | 52,636 |
| GlaxoSmithKline PLC | 27,730 | 536,099 |
| HSBC Holdings PLC | 12,924 | 131,195 |
| Imperial Tobacco Group PLC | 881 | 27,032 |
| Inmarsat PLC | 5,084 | 53,385 |
| International Power PLC | 9,966 | 67,994 |
| Kingfisher PLC | 14,696 | 60,352 |
| Lloyds Banking Group PLC* | 35,330 | 36,190 |
| Marks & Spencer Group PLC | 8,450 | 48,613 |
| National Grid PLC | 13,726 | 118,343 |
| Next PLC | 1,325 | 40,800 |
| Pearson PLC | 4,110 | 64,592 |
| Reed Elsevier PLC | 7,134 | 60,229 |
| Rio Tinto PLC | 2,348 | 164,240 |
| Rolls-Royce Group PLC* | 12,478 | 121,201 |
| SABMiller PLC | 1,731 | 60,898 |
| Scottish & Southern Energy PLC | 5,665 | 108,196 |
| Severn Trent PLC | 2,133 | 49,152 |
| Shire PLC | 4,174 | 100,413 |
| Smith & Nephew PLC | 6,163 | 65,003 |
| Smiths Group PLC | 3,914 | 75,974 |
| Standard Chartered PLC | 1,687 | 45,384 |
| Tesco PLC | 11,554 | 76,559 |
| The Sage Group PLC | 36,069 | 153,747 |
| Unilever PLC | 1,529 | 46,795 |
| United Utilities Group PLC | 6,323 | 58,360 |
| Vodafone Group PLC | 342,837 | 886,229 |
| William Morrison Supermarkets PLC | 8,072 | 33,678 |
| WPP PLC | 7,538 | 92,786 |
| (Cost $3,894,272) | | **5,558,646** |
| **Total Common Stocks** (Cost $52,385,673) | | **71,852,123** |

## Preferred Stocks 0.6%

### Germany

| | Shares | Value ($) |
|---|---|---|
| Fresenius SE | 632 | 54,108 |
| Henkel AG & Co. KGaA | 5,783 | 359,427 |
| Volkswagen AG | 396 | 64,171 |
| **Total Preferred Stocks** (Cost $216,838) | | **477,706** |

## Exchange-Traded Funds 9.6%

### Emerging Markets

| | Shares | Value ($) |
|---|---|---|
| iShares MSCI Emerging Markets Index (a) | 83,800 | 3,990,556 |
| Vanguard Emerging Markets (a) | 82,600 | 3,977,190 |
| **Total Exchange-Traded Funds** (Cost $5,469,338) | | **7,967,746** |

## Securities Lending Collateral 7.9%

| | Shares | Value ($) |
|---|---|---|
| Daily Assets Fund Institutional, 0.27% (c) (d) (Cost $6,610,195) | 6,610,195 | **6,610,195** |

## Cash Equivalents 3.2%

| | Shares | Value ($) |
|---|---|---|
| Central Cash Management Fund, 0.19% (c) (Cost $2,661,762) | 2,661,762 | **2,661,762** |

| | % of Net Assets | Value ($) |
|---|---|---|
| **Total Investment Portfolio** (Cost $67,343,806)† | 107.7 | **89,569,532** |
| **Other Assets and Liabilities, Net** | (7.7) | **(6,397,099)** |
| **Net Assets** | 100.0 | **83,172,433** |

*The accompanying notes are an integral part of the financial statements.*

* *Non-income producing security.*

† *The cost for federal income tax purposes was $67,805,906. At December 31, 2010, net unrealized appreciation for all securities based on tax cost was $21,763,626. This consisted of aggregate gross unrealized appreciation for all securities in which there was an excess of value over tax cost of $22,921,273 and aggregate gross unrealized depreciation for all securities in which there was an excess of tax cost over value of $1,157,647.*

(a) *All or a portion of these securities were on loan (see Notes to Financial Statements). The value of all securities loaned at December 31, 2010 amounted to $6,491,313, which is 7.8% of net assets.*

(b) *Securities with the same description are the same corporate entity but trade on different stock exchanges.*

(c) *Affiliated fund managed by Deutsche Investment Management Americas Inc. The rate shown is the annualized seven-day yield at period end.*

(d) *Represents collateral held in connection with securities lending. Income earned by the Fund is net of borrower rebates.*

*CVA: Certificaten Van Aandelen*

*MSCI: Morgan Stanley Capital International*

*REIT: Real Estate Investment Trust*

*RSP: Risparmio (Convertible Savings Shares)*

*SDR: Swedish Depositary Receipt*

*At December 31, 2010, open futures contracts purchased were as follows:*

| Futures | Currency | Expiration Date | Contracts | Notional Value ($) | Unrealized Appreciation (Depreciation) ($) |
|---|---|---|---|---|---|
| ASX SPI 200 Index | AUD | 3/17/2011 | 2 | 241,892 | (3,375) |
| DJ Euro Stoxx 50 Index | EUR | 3/18/2011 | 42 | 1,568,121 | (38,726) |
| FTSE 100 Index | GBP | 3/18/2011 | 3 | 275,633 | 1,684 |
| Nikkei 225 Index | USD | 3/10/2011 | 13 | 664,950 | (450) |
| S&P TSX 60 Index | CAD | 3/17/2011 | 1 | 154,300 | 1,840 |
| **Total net unrealized depreciation** | | | | | **(39,027)** |

**Currency Abbreviations**

| | | | | | |
|---|---|---|---|---|---|
| AUD | Australian Dollar | EUR | Euro | USD | United States Dollar |
| CAD | Canadian Dollar | GBP | British Pound | | |

*For information on the Fund's policy and additional disclosures regarding futures contracts, please refer to Note B in the accompanying Notes to Financial Statements.*

*The accompanying notes are an integral part of the financial statements.*

## Fair Value Measurements

*Various inputs are used in determining the value of the Fund's investments. These inputs are summarized in three broad levels. Level 1 includes quoted prices in active markets for identical securities. Level 2 includes other significant observable inputs (including quoted prices for similar securities, interest rates, prepayment speeds, and credit risk). Level 3 includes significant unobservable inputs (including the Fund's own assumptions in determining the fair value of investments). The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities.*

*The following is a summary of the inputs used as of December 31, 2010 in valuing the Fund's investments. For information on the Fund's policy regarding the valuation of investments, please refer to the Security Valuation section of Note A in the accompanying Notes to Financial Statements.*

| **Assets** | **Level 1** | **Level 2** | **Level 3** | **Total** |
|---|---|---|---|---|
| Common and Preferred Stocks | | | | |
| Australia | $ — | $ 3,561,979 | $ — | $ 3,561,979 |
| Austria | — | 417,666 | — | 417,666 |
| Belgium | — | 1,104,630 | — | 1,104,630 |
| Bermuda | — | 162,369 | — | 162,369 |
| Canada | 4,102,562 | — | — | 4,102,562 |
| Cyprus | — | 38,138 | — | 38,138 |
| Denmark | — | 1,858,235 | — | 1,858,235 |
| Finland | — | 2,565,853 | — | 2,565,853 |
| France | — | 5,974,341 | — | 5,974,341 |
| Germany | — | 4,563,787 | — | 4,563,787 |
| Greece | — | 258,478 | — | 258,478 |
| Hong Kong | — | 1,803,862 | — | 1,803,862 |
| Ireland | — | 544,503 | — | 544,503 |
| Italy | — | 3,062,894 | — | 3,062,894 |
| Japan | — | 16,687,718 | — | 16,687,718 |
| Luxembourg | — | 433,329 | — | 433,329 |
| Macau | — | 137,814 | — | 137,814 |
| Netherlands | — | 4,364,643 | — | 4,364,643 |
| Norway | — | 2,284,831 | — | 2,284,831 |
| Portugal | — | 263,648 | — | 263,648 |
| Singapore | — | 1,377,068 | — | 1,377,068 |
| Spain | — | 3,156,770 | — | 3,156,770 |
| Sweden | — | 2,556,656 | — | 2,556,656 |
| Switzerland | — | 5,489,409 | — | 5,489,409 |
| United Kingdom | — | 5,558,646 | — | 5,558,646 |
| Exchange-Traded Funds | 7,967,746 | — | — | 7,967,746 |
| Short-Term Investments (e) | 9,271,957 | — | — | 9,271,957 |
| **Total** | **$ 21,342,265** | **$ 68,227,267** | **$ —** | **$ 89,569,532** |

| **Liabilities** | | | | |
|---|---|---|---|---|
| Derivatives (f) | $ (39,027) | $ — | $ — | $ (39,027) |
| **Total** | **$ (39,027)** | $ — | $ — | **$ (39,027)** |

*There have been no significant transfers between Level 1 and Level 2 fair value measurements during the year ended December 31, 2010.*

(e) *See Investment Portfolio for additional detailed categorizations.*

(f) *Derivatives include unrealized appreciation (depreciation) on open futures contracts.*

*The accompanying notes are an integral part of the financial statements.*

## Statement of Assets and Liabilities

as of December 31, 2010

| | | |
|---|---|---|
| **Assets** | | |
| Investments: | | |
| Investments in unaffiliated securities, at value (cost $58,071,849) — including $6,491,313 of securities loaned | $ | 80,297,575 |
| Investment in Daily Assets Fund Institutional (cost $6,610,195)* | | 6,610,195 |
| Investment in Central Cash Management Fund (cost $2,661,762) | | 2,661,762 |
| Total investments, at value (cost $67,343,806) | | 89,569,532 |
| Foreign currency, at value (cost $87,151) | | 88,902 |
| Deposits with broker for open futures contracts | | 281,548 |
| Receivable for investments sold | | 1,245 |
| Receivable for Fund shares sold | | 14,646 |
| Dividends receivable | | 70,486 |
| Interest receivable | | 1,119 |
| Foreign taxes recoverable | | 10,924 |
| Other assets | | 459 |
| Total assets | | 90,038,861 |
| **Liabilities** | | |
| Payable upon return of securities loaned | | 6,610,195 |
| Payable for Fund shares redeemed | | 60,107 |
| Payable for daily variation margin on open futures contracts | | 39,027 |
| Accrued management fee | | 55,970 |
| Other accrued expenses and payables | | 101,129 |
| Total liabilities | | 6,866,428 |
| **Net assets, at value** | **$** | **83,172,433** |
| **Net Assets Consist of** | | |
| Undistributed net investment income | | 1,336,930 |
| Net unrealized appreciation (depreciation) on: | | |
| Investments | | 22,225,726 |
| Futures | | (39,027) |
| Foreign currency | | 2,382 |
| Accumulated net realized gain (loss) | | (69,565,313) |
| Paid-in capital | | 129,211,735 |
| **Net assets, at value** | **$** | **83,172,433** |
| **Class A** | | |
| **Net Asset Value,** offering and redemption price per share ($83,172,433 ÷ 10,297,508 outstanding shares of beneficial interest, no par value, unlimited number of shares authorized) | **$** | **8.08** |

* *Represents collateral on securities loaned.*

## Statement of Operations

for the year ended December 31, 2010

| | | |
|---|---|---|
| **Investment Income** | | |
| Income: | | |
| Dividends (net of foreign taxes withheld of $330,003) | $ | 2,216,179 |
| Interest | | 585 |
| Income distributions — Central Cash Management Fund | | 1,903 |
| Securities lending income, including income from Daily Assets Fund Institutional, net of borrower rebates | | 94,036 |
| Total income | | 2,312,703 |
| Expenses: | | |
| Management fee | | 519,737 |
| Administration fee | | 79,960 |
| Services to shareholders | | 2,094 |
| Custodian fee | | 68,980 |
| Legal fees | | 8,349 |
| Audit and tax fees | | 60,810 |
| Trustees' fees and expenses | | 5,193 |
| Reports to shareholders | | 11,959 |
| Other | | 35,847 |
| Total expenses | | 792,929 |
| **Net investment income (loss)** | | **1,519,774** |
| **Realized and Unrealized Gain (Loss)** | | |
| Net realized gain (loss) from: | | |
| Investments | | 2,946,085 |
| Futures | | 139,952 |
| Foreign currency | | (29,672) |
| | | 3,056,365 |
| Change in net unrealized appreciation (depreciation) on: | | |
| Investments | | 3,584,528 |
| Futures | | (169,560) |
| Foreign currency | | (17,721) |
| | | 3,397,247 |
| **Net gain (loss)** | | **6,453,612** |
| **Net increase (decrease) in net assets resulting from operations** | **$** | **7,973,386** |

*The accompanying notes are an integral part of the financial statements.*

# Statement of Changes in Net Assets

| Increase (Decrease) in Net Assets | Years Ended December 31, 2010 | 2009 |
|---|---|---|
| Operations: | | |
| Net investment income (loss) | $ 1,519,774 | $ 1,533,993 |
| Net realized gain (loss) | 3,056,365 | (23,604,083) |
| Change in net unrealized appreciation (depreciation) | 3,397,247 | 41,842,935 |
| Net increase (decrease) in net assets resulting from operations | 7,973,386 | 19,772,845 |
| Distributions to shareholders from: | | |
| Net investment income: | | |
| Class A | (1,843,687) | (5,187,036) |
| Total distributions | (1,843,687) | (5,187,036) |
| Fund share transactions: | | |
| **Class A** | | |
| Proceeds from shares sold | 3,841,591 | 1,865,488 |
| Reinvestment of distributions | 1,843,687 | 5,187,036 |
| Payments for shares redeemed | (14,779,706) | (26,149,949) |
| Shares converted* | — | 72,862 |
| Net increase (decrease) in net assets from Class A share transactions | (9,094,428) | (19,024,563) |
| **Class B** | | |
| Payments for shares redeemed | — | (294) |
| Shares converted* | — | (72,862) |
| Net increase (decrease) in net assets from Class B share transactions | — | (73,156) |
| **Increase (decrease) in net assets** | (2,964,729) | (4,511,910) |
| Net assets at beginning of period | 86,137,162 | 90,649,072 |
| Net assets at end of period (including undistributed net investment income of $1,336,930 and $1,659,097, respectively) | **$ 83,172,433** | **$ 86,137,162** |

| Other Information | | |
|---|---|---|
| **Class A** | | |
| Shares outstanding at beginning of period | 11,562,525 | 14,554,587 |
| Shares sold | 508,055 | 283,708 |
| Shares issued to shareholders in reinvestment of distributions | 252,215 | 1,027,136 |
| Shares redeemed | (2,025,287) | (4,318,475) |
| Shares converted* | — | 15,569 |
| Net increase (decrease) in Class A shares | (1,265,017) | (2,992,062) |
| Shares outstanding at end of period | **10,297,508** | **11,562,525** |
| **Class B** | | |
| Shares outstanding at beginning of period | — | 15,672 |
| Shares issued to shareholders in reinvestment of distributions | — | — |
| Shares redeemed | — | (53) |
| Shares converted* | — | (15,619) |
| Net increase (decrease) in Class B shares | — | (15,672) |
| Shares outstanding at end of period | **—** | **—** |

* *On March 6, 2009, Class B shares converted into Class A shares.*

*The accompanying notes are an integral part of the financial statements.*

# Financial Highlights

## Class A

| Years Ended December 31, | 2010 | 2009 | 2008 | 2007 | 2006 |
|---|---|---|---|---|---|
| **Selected Per Share Data** | | | | | |
| **Net asset value, beginning of period** | **$ 7.45** | **$ 6.22** | **$16.76** | **$16.31** | **$13.25** |
| *Income (loss) from investment operations:* | | | | | |
| Net investment income[a] | .14 | .12 | .33[d] | .25 | .24[b] |
| Net realized and unrealized gain (loss) | .66 | 1.51 | (6.67) | 2.24 | 3.11 |
| **Total from investment operations** | .80 | 1.63 | (6.34) | 2.49 | 3.35 |
| *Less distributions from:* | | | | | |
| Net investment income | (.17) | (.40) | (.13) | (.46) | (.29) |
| Net realized gains | — | — | (4.07) | (1.58) | — |
| **Total distributions** | (.17) | (.40) | (4.20) | (2.04) | (.29) |
| **Net asset value, end of period** | **$ 8.08** | **$ 7.45** | **$ 6.22** | **$16.76** | **$16.31** |
| Total Return (%) | 10.93 | 29.36 | (48.81)[c,e] | 16.71 | 25.56 |
| **Ratios to Average Net Assets and Supplemental Data** | | | | | |
| Net assets, end of period ($ millions) | 83 | 86 | 91 | 236 | 223 |
| Ratio of expenses before expense reductions (%) | .99 | .94 | 1.02 | .93 | .88 |
| Ratio of expenses after expense reductions (%) | .99 | .94 | 1.01 | .93 | .88 |
| Ratio of net investment income (%) | 1.90 | 1.89 | 3.04[d] | 1.53 | 1.65[b] |
| Portfolio turnover rate (%) | 14 | 139 | 132 | 117 | 122 |

[a] *Based on average shares outstanding during the period.*

[b] *Net investment income per share and the ratio of net investment income without non-recurring dividend income amounting to $0.20 per share and 1.39% of average daily net assets, respectively.*

[c] *Total return would have been lower had certain expenses not been reimbursed.*

[d] *Net investment income per share and ratio of net investment income include non-recurring dividend income amounting to $0.16 per share and 1.49% of average daily net assets, respectively.*

[e] *Includes a reimbursement from the Advisor to reimburse the effect of losses incurred as the result of certain operation errors during the period. Excluding this reimbursement, total return would have been 0.14% lower.*

# Notes to Financial Statements

## A. Organization and Significant Accounting Policies

DWS Variable Series II (the "Trust") is registered under the Investment Company Act of 1940, as amended (the "1940 Act"), as an open-end management investment company organized as a Massachusetts business trust. The Trust offers seventeen funds (hereinafter referred to individually as "Fund" or collectively as "Funds"). The Fund is classified as a diversified open-end management investment company.

The Trust's financial statements are prepared in accordance with accounting principles generally accepted in the United States of America which require the use of management estimates. Actual results could differ from those estimates. The policies described below are followed consistently by the Trust in the preparation of its financial statements.

**Security Valuation.** Investments are stated at value determined as of the close of regular trading on the New York Stock Exchange on each day the exchange is open for trading.

Various inputs are used in determining the value of the Fund's investments. These inputs are summarized in three broad levels. Level 1 includes quoted prices in active markets for identical securities. Level 2 includes other significant observable inputs (including quoted prices for similar securities, interest rates, prepayment speeds, and credit risk). Level 3 includes significant unobservable inputs (including the Fund's own assumptions in determining the fair value of investments). The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities.

Equity securities and exchange-traded funds ("ETFs") are valued at the most recent sale price or official closing price reported on the exchange (US or foreign) or over-the-counter market on which they trade and are categorized as Level 1 securities. Securities or ETFs for which no sales are reported are valued at the calculated mean between the most recent bid and asked quotations on the relevant market or, if a mean cannot be determined, at the most recent bid quotation. For certain international equity securities, in order to adjust for events which may occur between the close of the foreign exchanges and the close of the New York Stock Exchange, a fair valuation model may be used. This fair valuation model takes into account comparisons to the valuation of American Depository Receipts (ADRs), exchange-traded funds, futures contracts and certain indices and these securities are categorized as Level 2.

Futures contracts are generally valued at the settlement prices established each day on the exchange on which they are traded and are categorized as Level 1.

Money market instruments purchased with an original or remaining maturity of sixty days or less, maturing at par, are valued at amortized cost, which approximates value, and are categorized as Level 2. Investments in open-end investment companies are valued at their net asset value each business day and are categorized as Level 1.

Securities and other assets for which market quotations are not readily available or for which the above valuation procedures are deemed not to reflect fair value are valued in a manner that is intended to reflect their fair value as determined in accordance with procedures approved by the Board and are generally categorized as Level 3. In accordance with the Fund's valuation procedures, factors used in determining value may include, but are not limited to, the type of the security; the size of the holding; the initial cost of the security; the existence of any contractual restrictions on the security's disposition; the price and extent of public trading in similar securities of the issuer or of comparable companies; quotations or evaluated prices from broker-dealers and/or pricing services; information obtained from the issuer, analysts, and/or the appropriate stock exchange (for exchange-traded securities); an analysis of the company's or issuer's financial statements; an evaluation of the forces that influence the issuer and the market(s) in which the security is purchased and sold and with respect to debt securities; the maturity, coupon, creditworthiness, currency denomination and the movement of the market in which the security is normally traded. The value determined under these procedures may differ from published values for the same securities.

Disclosure about the classification of fair value measurements is included in a table following the Fund's Investment Portfolio.

**Foreign Currency Translations.** The books and records of the Trust are maintained in US dollars. Investment securities and other assets and liabilities denominated in a foreign currency are translated into US dollars at the prevailing exchange rates at period end. Purchases and sales of investment securities, income and expenses are translated into US dollars at the prevailing exchange rates on the respective dates of the transactions.

Net realized and unrealized gains and losses on foreign currency transactions represent net gains and losses between trade and settlement dates on securities transactions, the disposition of forward foreign currency exchange contracts and foreign currencies, and the difference between the amount of net investment income accrued and the US dollar amount actually received. That portion of both realized and unrealized gains and losses on investments that results from fluctuations in foreign currency exchange rates is not separately disclosed but is included with net realized and unrealized gain/appreciation and loss/depreciation on investments.

**Securities Lending.** The Fund lends securities to certain financial institutions. The Fund retains beneficial ownership of the securities it has loaned and continues to receive interest and dividends paid by the issuer of securities and to participate in any changes in their market value. The Fund requires the borrowers of the securities to maintain collateral with the Fund consisting of either cash or liquid, unencumbered assets having a value at least equal to the value of the securities loaned. When the collateral falls below specified amounts, the lending agent will use its best effort to obtain additional collateral on the next business day to meet required amounts under the security lending agreement. The Fund may invest the cash collateral into a joint trading account in an affiliated money market fund pursuant to Exemptive Orders issued by the SEC. The Fund receives compensation for lending its securities either in the form of fees or by earning interest on invested cash collateral net of borrower rebates and fees paid to a lending agent. Either the Fund or the borrower may terminate the loan. There may be risks of delay and costs in recovery of securities or even loss of rights in the collateral should the borrower of the securities fail financially. The Fund is also subject to all investment risks associated with the reinvestment of any cash collateral received, including, but not limited to, interest rate, credit and liquidity risk associated with such investments.

**Taxes.** The Fund's policy is to comply with the requirements of the Internal Revenue Code, as amended, which are applicable to regulated investment companies and to distribute all of its taxable income to its shareholders.

Additionally, based on the Fund's understanding of the tax rules and rates related to income, gains and transactions for the foreign jurisdictions in which it invests, the Fund will provide for foreign taxes, and where appropriate, deferred foreign taxes.

At December 31, 2010, the Fund had an approximate net tax basis capital loss carryforward which may be applied against any realized net taxable capital gains of each succeeding year until fully utilized or until the following expiration dates, whichever occurs first:

| Fund | Capital Loss Carryforward ($) | Expiration Date | Capital Loss Carryforward Utilized ($) |
|---|---|---|---|
| DWS Diversified International Equity VIP | 30,075,000 | 12/31/2016 | 2,858,000 |
| | 39,164,000 | 12/31/2017 | |

The Fund has reviewed the tax positions for the open tax years as of December 31, 2010 and has determined that no provision for income tax is required in the Fund's financial statements. The Fund's federal tax returns for the prior three fiscal years remain open subject to examination by the Internal Revenue Service.

**Distribution of Income and Gains.** Distributions of net investment income of the Fund, if any, are made annually. Net realized gains from investment transactions, in excess of available capital loss carryforwards, would be taxable to the Fund if not distributed and, therefore, will be distributed to shareholders at least annually. The Fund may also make additional distributions for tax purposes if necessary.

The timing and characterization of certain income and capital gains distributions are determined annually in accordance with federal tax regulations which may differ from accounting principles generally accepted in the United States of America. These differences primarily relate to investments in foreign denominated investments, investments in futures contracts, income received from Passive Foreign Investment Companies and and certain securities sold at a loss. As a result, net investment income (loss) and net realized gain (loss) on investment transactions for a reporting period may differ significantly from distributions during such period. Accordingly, the Fund may periodically make reclassifications among certain of its capital accounts without impacting the net asset value of the Fund.

At December 31, 2010, the Fund's components of distributable earnings on a tax basis were as follows:

| Fund | Undistributed Ordinary Income ($)* | Capital Loss Carryforwards ($) | Unrealized Appreciation (Depreciation) on Investments ($) |
|---|---|---|---|
| DWS Diversified International Equity VIP | 1,473,946 | (69,239,000) | 21,763,626 |

In addition, the tax character of distributions paid by the Fund is summarized as follows:

| Fund | Distributions from Ordinary Income ($)* Years Ended December 31, 2010 | 2009 |
|---|---|---|
| DWS Diversified International Equity VIP | 1,843,687 | 5,187,036 |

* *For tax purposes, short-term capital gain distributions are considered ordinary income distributions.*

**Expenses.** Expenses of the Trust arising in connection with a specific fund are allocated to that fund. Other Trust expenses which cannot be directly attributed to a fund are apportioned among the funds in the Trust.

**Contingencies.** In the normal course of business, the Fund may enter into contracts with service providers that contain general indemnification clauses. The Fund's maximum exposure under these arrangements is unknown as this would involve future claims that may be made against the Fund that have not yet been made. However, based on experience, the Fund expects the risk of loss to be remote.

**Other.** Investment transactions are accounted for on a trade date plus one basis for daily net asset value calculations. However, for financial reporting purposes, investment transactions are reported on trade date. Interest income is recorded on the accrual basis. Dividend income is recorded on the ex-dividend date net of foreign withholding taxes. Certain dividends from foreign securities may be recorded subsequent to the ex-dividend date as soon as the Fund is informed of such dividends. Realized gains and losses from investment transactions are recorded on an identified cost basis.

## B. Derivative Instruments

**Futures Contracts.** A futures contract is an agreement between a buyer or seller and an established futures exchange or its clearinghouse in which the buyer or seller agrees to take or make a delivery of a specific amount of a financial instrument at a specified price on a specific date (settlement date). For the year ended December 31, 2010, the Fund entered into futures contracts to keep cash on hand to meet shareholder redemptions or other needs while maintaining exposure to the market. The Fund also entered into futures contracts as a means of gaining exposure to a particular asset class.

Futures contracts are valued at the most recent settlement price. Upon entering into a futures contract, the Fund is required to deposit with a financial intermediary cash or securities ("initial margin") in an amount equal to a certain percentage of the face value indicated in the futures contract. Subsequent payments ("variation margin") are made or received by the Fund dependent upon the daily fluctuations in the value and are recorded for financial reporting purposes as unrealized gains or losses by the Fund. Gains or losses are realized when the contract expires or is closed. Since all futures contracts are exchange-traded, counterparty risk is minimized as the exchange's clearinghouse acts as the counterparty, and guarantees the futures against default.

Certain risks may arise upon entering into futures contracts, including the risk that an illiquid market will limit the Fund's ability to close out a futures contract prior to the settlement date and that a change in the value of a futures contract may not correlate exactly with the changes in the value of the underlying hedged security, index or currency. Risk of loss may exceed amounts recognized in the Statement of Assets and Liabilities.

A summary of the open futures contracts as of December 31, 2010 is included in a table following the Fund's Investment Portfolio. For the year ended December 31, 2010, the Fund's investment in futures contracts purchased had a total notional value generally indicative of a range from approximately $676,000 to $2,958,000.

The following table summarizes the value of the Fund's derivative instruments held as of December 31, 2010 and the related location in the accompanying Statement of Assets and Liabilities, presented by primary underlying risk exposure:

| Liability Derivative | Futures Contracts |
|---|---|
| Equity Contracts (a) | $ (39,027) |

*The above derivative is located in the following Statement of Assets and Liabilities account:*

(a) *Net unrealized appreciation (depreciation) on futures. Liability of payable for daily variation margin on open futures contracts reflects unsettled variation margin.*

Additionally, the amount of unrealized and realized gains and losses on derivative instruments recognized in Fund earnings during the year ended December 31, 2010 and the related location in the accompanying Statement of Operations is summarized in the following tables by primary underlying risk exposure:

| Realized Gain (Loss) | Futures Contracts |
|---|---|
| Equity Contracts (a) | $ 139,952 |

*The above derivative is located in the following Statement of Operations account:*

(a) *Net realized gain (loss) from futures*

| Change in Net Unrealized Appreciation (Depreciation) | Futures Contracts |
|---|---|
| Equity Contracts (a) | $ (169,560) |

*The above derivative is located in the following Statement of Operations account:*

(a) *Change in net unrealized appreciation (depreciation) on futures*

## C. Purchases and Sales of Securities

During the year ended December 31, 2010, purchases and sales of investment transactions (excluding short-term investments) were as follows:

| Fund | Purchases ($) | Sales ($) |
|---|---|---|
| DWS Diversified International Equity VIP | 10,585,084 | 20,213,690 |

## D. Related Parties

**Management Agreement.** Under the Investment Management Agreement with Deutsche Investment Management Americas Inc. ("DIMA" or the "Advisor"), an indirect, wholly owned subsidiary of Deutsche Bank AG, the Advisor directs the investments of the Fund in accordance with its investment objectives, policies and restrictions. The Advisor determines the securities, instruments and other contracts relating to investments to be purchased, sold or entered into by the Fund or delegates such responsibility to the Fund's subadvisor.

QS Investors, LLC ("QS Investors") acts as an investment sub-advisor to the Fund. On August 1, 2010, members of the Advisor's Quantitative Strategies Group, including some members of the Fund's portfolio management team, separated from the Advisor and formed QS Investors as a separate investment advisory firm unaffiliated with the Advisor (the "Separation"). As an investment sub-advisor to the Fund, QS Investors makes investment decisions and buys and sells securities for the Fund. QS Investors is paid by the Advisor, not the Fund, for the services QS Investors provides to the Fund.

Under the Investment Management Agreement with the Advisor, the fee is equivalent to the annual rates shown below of the Fund's average daily net assets, computed and accrued daily and payable monthly:

| Fund | Annual Management Fee Rate |
|---|---|
| DWS Diversified International Equity VIP | |
| $0–$1.5 billion | .650% |
| next $1.75 billion | .635% |
| next $1.75 billion | .620% |
| over $5 billion | .605% |

Accordingly, for the year ended December 31, 2010, the total management fee and effective management fee rate were as follows:

| Fund | Total Aggregated ($) | Annual Effective Rate |
|---|---|---|
| DWS Diversified International Equity VIP | 519,737 | .65% |

**Administration Fee.** Pursuant to an Administrative Services Agreement, DIMA provides most administrative services to the Fund. For all services provided under the Administrative Services Agreement, the Fund pays DIMA an annual fee ("Administration Fee") of 0.10% of the Fund's average daily net assets, computed and accrued daily and payable monthly. For the year ended December 31, 2010, the Administration Fee was as follows:

| Fund | Total Aggregated ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS Diversified International Equity VIP | 79,960 | 6,963 |

**Service Provider Fees.** DWS Investments Service Company ("DISC"), an affiliate of the Advisor, is the transfer agent, dividend-paying agent and shareholder service agent for the Fund. Pursuant to a sub-transfer agency agreement between DISC and DST Systems, Inc. ("DST"), DISC has delegated certain transfer agent, dividend-paying agent and shareholder service agent functions to DST. DISC compensates DST out of the shareholder servicing fee it receives from the Fund. For the year ended December 31, 2010, the amounts charged to the Fund by DISC were as follows:

| Fund | Total Aggregated ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS Diversified International Equity VIP Class A | 138 | 34 |

**Typesetting and Filing Service Fees.** Under an agreement with DIMA, DIMA is compensated for providing typesetting and certain regulatory filing services to the Fund. For the year ended December 31, 2010, the amount charged to the Fund by DIMA included in the Statement of Operations under "reports to shareholders" was as follows:

| Fund | Amount ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS Diversified International Equity VIP | 11,959 | 2,922 |

**Trustees' Fees and Expenses.** The Fund paid each Trustee not affiliated with the Advisor retainer fees plus specified amounts for various committee services and for the Board Chairperson.

**Affiliated Cash Management Vehicles.** The Fund may invest uninvested cash balances in Central Cash Management Fund, which is managed by the Advisor. The Fund indirectly bears their proportionate share of the expenses of the underlying money market funds. Central Cash Management Fund does not pay the Advisor an investment management fee. Central Cash Management Fund seeks a high level of current income consistent with liquidity and the preservation of capital.

## E. Investing in Emerging Markets

Investing in emerging markets may involve special risks and considerations not typically associated with investing in developed markets. These risks include revaluation of currencies, high rates of inflation or deflation, repatriation restrictions on income and capital, and future adverse political, social and economic developments. Moreover, securities issued in these markets may be less liquid, subject to government ownership controls or delayed settlements, and may have prices that are more volatile or less easily assessed than those of comparable securities of issuers in developed markets.

## F. Ownership of the Fund

At December 31, 2010, the beneficial ownership in the Fund was as follows:

**DWS Diversified International Equity VIP:** Three Participating Insurance Companies were owners of record of 10% or more of the total outstanding Class A shares of the Fund, each owning 42%, 29% and 28%.

## G. Line of Credit

The Trust and other affiliated fund (the "Participants") share in a $450 million revolving credit facility provided by a syndication of banks. The Fund may borrow for temporary or emergency purposes, including the meeting of redemption requests that otherwise might require the untimely disposition of securities. The Participants are charged an annual commitment fee which is allocated based on net assets, among each of the Participants. Interest is calculated at a rate per annum equal to the sum of the Federal Funds Rate plus 1.25 percent plus if LIBOR exceeds the Federal Funds Rate the amount of such excess. The Fund may borrow up to a maximum of 33 percent of its net assets under the agreement.

# Report of Independent Registered Public Accounting Firm

**To the Board of Trustees and Shareholders of DWS Variable Series II:**

We have audited the accompanying statement of assets and liabilities of DWS Diversified International Equity VIP, one of the funds constituting the DWS Variable Series II (the "Trust"), including the investment portfolio, as of December 31, 2010, and the related statement of operations, the statement of changes in net assets and the financial highlights for each of the periods indicated therein. These financial statements and financial highlights are the responsibility of the Trust's management. Our responsibility is to express an opinion on these financial statements and financial highlights based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements and financial highlights are free of material misstatement. We were not engaged to perform an audit of the Trust's internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Trust's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements and financial highlights, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our procedures included confirmation of securities owned as of December 31, 2010, by correspondence with the custodian and brokers or by other appropriate auditing procedures where replies from brokers were not received. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements and financial highlights referred to above present fairly, in all material respects, the financial position of the aforementioned fund of the DWS Variable Series II at December 31, 2010, the results of its operations, the changes in its net assets and the financial highlights for each of the periods indicated therein, in conformity with U.S. generally accepted accounting principles.

Ernst + Young LLP

Boston, Massachusetts
February 14, 2011

# Tax Information

**(Unaudited)**

For corporate shareholders, the following percentage of income dividends paid during the Fund's fiscal year ended December 31, 2010 qualified for the dividends received deduction:

| Fund | Dividends Received % |
|---|---|
| DWS Diversified International Equity VIP | 4 |

The Fund paid foreign taxes of $274,450 and earned $1,655,652 of foreign source income during the year ended December 31, 2010. Pursuant to Section 853 of the Internal Revenue Code, the Fund designates $0.03 per share as foreign taxes paid and $0.16 per share as income earned from foreign sources for the year ended December 31, 2010.

Please consult a tax advisor if you have questions about federal or state income tax laws, or on how to prepare your tax returns. If you have specific questions about your account, please contact your insurance provider.

# Proxy Voting

The Trust's policies and procedures for voting proxies for portfolio securities and information about how the Trust voted proxies related to its portfolio securities during the 12-month period ended June 30 are available on our Web site — www.dws-investments.com (click on "proxy voting" at the bottom of the page) — or on the SEC's Web site — www.sec.gov. To obtain a written copy of the Trust's policies and procedures without charge, upon request, call us toll free at (800) 728-3337.

# Investment Management Agreement Approval

## DWS Diversified International Equity VIP

The Board of Trustees, including the Independent Trustees, approved the renewal of your Fund's investment management agreement (the "Agreement") with Deutsche Investment Management Americas Inc. ("DWS") and sub-advisory agreement (the "Sub-Advisory Agreement" and together with the Agreement the "Agreements") between DWS and QS Investors, LLC ("QS Investors") in September 2010.

In terms of the process that the Board followed prior to approving the Agreements, shareholders should know that:

- In September 2010, all but one of the Fund's Trustees were independent of DWS and its affiliates.
- The Trustees meet frequently to discuss fund matters. Each year, the Trustees dedicate substantial time to contract review matters. Over the course of several months, the Board's Contract Committee, in coordination with the Board's Fixed Income and Quant Oversight Committee, reviewed comprehensive materials received from DWS, independent third parties and independent counsel. These materials included an analysis of the Fund's performance, fees and expenses, and profitability compiled by the Fund's independent fee consultant. The Board also received extensive information throughout the year regarding performance of the Fund.
- The Independent Trustees regularly meet privately with their independent counsel to discuss contract review and other matters. In addition, the Independent Trustees were also advised by the Fund's independent fee consultant in the course of their review of the Fund's contractual arrangements and considered a comprehensive report prepared by the independent fee consultant in connection with their deliberations (the "IFC Report").
- In connection with reviewing the Agreements, the Board also reviewed the terms of the Fund's distribution agreement, administrative services agreement, transfer agency agreement and other material service agreements.
- Based on its evaluation of the information provided, the Contract Committee presented its findings and recommendations to the Independent Trustees as a group. The Independent Trustees reviewed the Contract Committee's findings and recommendations and presented their recommendations to the full Board.

In connection with the contract review process, the Contract Committee and the Board considered the factors discussed below, among others. The Board also considered that DWS and its predecessors have managed the Fund since its inception, and the Board believes that a long-term relationship with a capable, conscientious advisor is in the best interests of the Fund. The Board considered, generally, that shareholders chose to invest or remain invested in the Fund knowing that DWS managed the Fund, and that the Agreement was approved by the Fund's shareholders. DWS is part of Deutsche Bank, a major global banking institution that is engaged in a wide range of financial services. The Board believes that there are significant advantages to being part of a global asset management business that offers a wide range of investing expertise and resources, including hundreds of portfolio managers and analysts with research capabilities in many countries throughout the world.

While shareholders may focus primarily on fund performance and fees, the Fund's Board considers these and many other factors, including the quality and integrity of DWS's and QS Investors' personnel and such other issues as back-office operations, fund valuations, and compliance policies and procedures. In addition, in connection with approving the continuation of the Fund's Sub-Advisory Agreement, the Board noted it had engaged in a comprehensive review of the agreement in connection with its initial approval in May 2010.

**Nature, Quality and Extent of Services.** The Board considered the terms of the Agreements, including the scope of advisory services provided under the Agreements. The Board noted that, under the Agreements, DWS and QS Investors provide portfolio management services to the Fund and that, pursuant to a separate administrative services agreement, DWS provides administrative services to the Fund. The Board considered the experience and skills of senior management and investment personnel, the resources made available to such personnel, the ability of DWS to attract and retain high-quality personnel, and the organizational depth and stability of DWS. The Board reviewed the Fund's performance over short-term and long-term periods and compared those returns to various agreed-upon performance measures, including market indices and a peer universe compiled by the independent fee consultant using information supplied by Lipper Inc. ("Lipper"). The Board also noted that it has put into place a process of identifying "Focus Funds" (e.g., funds performing poorly relative to their benchmark or a peer universe compiled by Lipper), and receives more frequent reporting and information from DWS regarding such funds, along with DWS's remedial plans to address underperformance. The Board believes this process is an effective manner of identifying and addressing underperforming funds. Based on the information provided, the Board noted that for the one-, three- and five-year periods ended December 31, 2009, the Fund's performance (Class A shares) was in the 3rd quartile, 4th quartile and 4th quartile, respectively, of the applicable Lipper universe (the 1st quartile being the best performers and the 4th quartile being the worst performers). The Board also observed that the Fund has underperformed its benchmark in the one-, three- and five-year periods ended December 31, 2009. The Board noted the disappointing investment performance of the Fund in recent periods and continued to discuss with senior management of DWS and QS Investors the factors contributing to such underperformance and actions being taken to improve performance. The Board recognized that DWS has made significant changes in its investment personnel and processes in recent years in an effort to improve long-term performance.

On the basis of this evaluation and the ongoing review of investment results by the Board, the Board concluded that the nature, quality and extent of services provided by DWS and QS Investors historically have been and continue to be satisfactory.

**Fees and Expenses.** The Board considered the Fund's investment management fee schedule, sub-advisory fee schedule, operating expenses, and total expense ratios, and comparative information provided by Lipper and the independent fee consultant regarding investment management fee rates paid to other investment advisors by similar funds (1st quartile being the most favorable and 4th quartile being the least favorable). With respect to management fees paid to other investment advisors by similar funds, the Board noted that the contractual fee rates paid by the Fund, which include the 0.10% fee paid to DWS under the Fund's administrative services agreement, were lower than the median (1st quartile) of the applicable Lipper peer group (based on Lipper data provided as of December 31, 2009). With respect to the sub-advisory fee paid to QS Investors, the Board noted that the fee is paid by DWS out of its fee and not directly by the Fund. The Board noted that the Fund's Class A shares total (net) operating expenses were expected to be higher than the median (3rd quartile) of the applicable Lipper expense universe (based on Lipper data provided as of December 31, 2009, and analyzing Lipper expense universe Class A expenses less any applicable 12b-1 fees) ("Lipper Universe Expenses"). The Board considered the Fund's management fee rate as compared to fees charged by DWS and certain of its affiliates for comparable mutual funds and considered differences in fund and fee structures between the DWS Funds. The Board also considered how the Fund's total (net) operating expenses compared to the total (net) operating expenses of a more customized peer group selected by Lipper (based on such factors as asset size).

The information considered by the Board as part of its review of management fees included information regarding fees charged by DWS and its affiliates to similar institutional accounts and to similar funds offered primarily to European investors ("DWS Europe funds"), in each case as applicable. The Board observed that advisory fee rates for institutional accounts generally were lower than the management fees charged by similarly managed DWS US mutual funds ("DWS Funds"), but also took note of the differences in services provided to DWS Funds as compared to institutional accounts. In the case of DWS Europe funds, the Board observed that fee rates for DWS Europe funds generally were higher than for similarly managed DWS Funds, but noted that differences in the types of services provided to DWS Funds relative to DWS Europe funds made it difficult to compare such fees.

On the basis of the information provided, the Board concluded that management fees were reasonable and appropriate in light of the nature, quality and extent of services provided by DWS and QS Investors.

**Profitability.** The Board reviewed detailed information regarding revenues received by DWS under the Agreement. The Board considered the estimated costs and pre-tax profits realized by DWS from advising the DWS Funds, as well as estimates of the pre-tax profits attributable to managing the Fund in particular. The Board also received information regarding the estimated enterprise-wide profitability of DWS and its affiliates with respect to all fund services in totality and by fund. The Board reviewed DWS's methodology in allocating its costs to the management of the Fund. Based on the information provided, the Board concluded that the pre-tax profits realized by DWS in connection with the management of the Fund were not unreasonable. The Board also reviewed information regarding the profitability of certain similar investment management firms. The Board noted that while information regarding the profitability of such firms is limited (and in some cases is not necessarily prepared on a comparable basis), DWS and its affiliates' overall profitability with respect to the DWS fund complex (after taking into account distribution and other services provided to the funds by DWS and its affiliates) was lower than the overall profitability levels of many comparable firms for which such data was available. The Board did not consider the profitability of QS Investors with respect to the Fund. The Board noted that DWS pays QS Investors' fee out of its management fee, and its understanding that the Fund's sub-advisory fee schedule was the product of an arm's length negotiation with DWS.

**Economies of Scale.** The Board considered whether there are economies of scale with respect to the management of the Fund and whether the Fund benefits from any economies of scale. The Board noted that the Fund's management fee schedule includes fee breakpoints. The Board concluded that the Fund's fee schedule represents an appropriate sharing between the Fund and DWS of such economies of scale as may exist in the management of the Fund at current asset levels.

**Other Benefits to DWS and QS Investors and Their Affiliates.** The Board also considered the character and amount of other incidental benefits received by DWS and QS Investors and their affiliates, including any fees received by DWS for administrative services provided to the Fund and any fees received by an affiliate of DWS for distribution services. The Board also considered benefits to DWS and QS Investors related to brokerage and soft-dollar allocations, including allocating brokerage to pay for research generated by parties other than the executing broker dealers, which pertain primarily to funds investing in equity securities, along with the incidental public relations benefits to DWS and QS Investors related to DWS Funds advertising and cross-selling opportunities among DWS products and services. The Board concluded that management fees were reasonable in light of these fallout benefits.

**Compliance.** The Board considered the significant attention and resources dedicated by DWS to documenting and enhancing its compliance processes in recent years. The Board noted in particular (i) the experience and seniority of both DWS's chief compliance officer and the Fund's chief compliance officer; (ii) the large number of DWS compliance personnel; and (iii) the substantial commitment of resources by DWS and its affiliates to compliance matters. The Board also considered the attention and resources dedicated by DWS to the oversight of the investment sub-advisor's compliance program and compliance with the applicable fund policies and procedures.

Based on all of the information considered and the conclusions reached, the Board unanimously (including the Independent Trustees) determined that the continuation of the Agreements is in the best interests of the Fund. In making this determination, the Board did not give particular weight to any single factor identified above. The Board considered these factors over the course of numerous meetings, certain of which were in executive session with only the Independent Trustees and their counsel present. It is possible that individual Trustees may have weighed these factors differently in reaching their individual decisions to approve the continuation of the Agreements.

# Summary of Management Fee Evaluation by Independent Fee Consultant

October 3, 2010

Pursuant to an Order entered into by Deutsche Investment Management Americas and affiliates (collectively, "DeAM") with the Attorney General of New York, I, Thomas H. Mack, have been appointed the Independent Fee Consultant for the DWS Funds (formerly the DWS Scudder Funds). My duties include preparing an annual written evaluation of the management fees DeAM charges the Funds, considering among other factors the management fees charged by other mutual fund companies for like services, management fees DeAM charges other clients for like services, DeAM's costs of supplying services under the management agreements and related profit margins, possible economies of scale if a Fund grows larger, and the nature and quality of DeAM's services, including fund performance. This report summarizes my evaluation for 2010, including my qualifications, the evaluation process for each of the DWS Funds, consideration of certain complex-level factors, and my conclusions. I served in substantially the same capacity in 2007, 2008, and 2009.

## Qualifications

For more than 35 years I have served in various professional capacities within the investment management business. I have held investment analysis and advisory positions, including securities analyst, portfolio strategist and director of investment policy with a large investment firm. I have also performed business management functions, including business development, financial management and marketing research and analysis.

Since 1991, I have been an independent consultant within the asset management industry. I have provided services to over 125 client organizations, including investment managers, mutual fund boards, product distributors and related organizations. Over the past ten years I have completed a number of assignments for mutual fund boards, specifically including assisting boards with management contract renewal.

I hold a Master of Business Administration degree, with highest honors, from Harvard University and Master of Science and Bachelor of Science (highest honors) degrees from the University of California at Berkeley. I am an independent director and audit committee financial expert for two closed-end mutual funds and have served in various leadership and financial oversight capacities with non-profit organizations.

## Evaluation of Fees for each DWS Fund

My work focused primarily on evaluating, fund-by-fund, the fees charged to each of the 118 publicly offered Fund portfolios in the DWS Fund family. For each Fund, I considered each of the key factors mentioned above, as well as any other relevant information. In doing so I worked closely with the Funds' Independent Directors in their annual contract renewal process, as well as in their approval of contracts for several new funds (documented separately).

In evaluating each Fund's fees, I reviewed comprehensive materials provided by or on behalf of DeAM, including expense information prepared by Lipper Analytical, comparative performance information, profitability data, manager histories, and other materials. I also accessed certain additional information from the Lipper and Morningstar databases and drew on my industry knowledge and experience.

To facilitate evaluating this considerable body of information, I prepared for each Fund a document summarizing the key data elements in each area as well as additional analytics discussed below. This made it possible to consider each key data element in the context of the others.

In the course of contract renewal, DeAM agreed to implement a number of fee and expense adjustments requested by the Independent Directors which will favorably impact future fees and expenses, and my evaluation includes the effects of these changes.

### Fees and Expenses Compared with Other Funds

The competitive fee and expense evaluation for each fund focused on two primary comparisons:

- The Fund's contractual management fee (the advisory fee plus the administration fee where applicable) compared with those of a group of typically 12–15 funds in the same Lipper investment category (e.g. Large Capitalization Growth) having similar distribution arrangements and being of similar size.
- The Fund's total expenses compared with a broader universe of funds from the same Lipper investment category and having similar distribution arrangements.

These two comparisons provide a view of not only the level of the fee compared with funds of similar scale but also the total expense the Fund bears for all the services it receives, in comparison with the investment choices available in the Fund's investment category and distribution channel. The principal figure-of-merit used in these comparisons was the subject Fund's percentile ranking against peers.

### DeAM's Fees for Similar Services to Others

DeAM provided management fee schedules for all of its US domiciled fund and non-fund investment management accounts in any of the investment categories where there is a DWS Fund. These similar products included the other DWS Funds, non-fund pooled accounts, institutional accounts and sub-advisory accounts. Using this information, I calculated for each Fund the fee that would be charged to each similar product, at the subject Fund's asset level.

Evaluating information regarding non-fund products is difficult because there are varying levels of services required for different types of accounts, with mutual funds generally requiring considerably more regulatory and administrative types of service as well as having more frequent cash flows than other types of accounts. Also, while mutual fund fees for similar fund products can be expected to be similar, there will be some differences due to different pricing conditions in different distribution channels (e.g. retail funds versus those used in variable insurance products), differences in underlying investment processes and other factors.

**Costs and Profit Margins**

DeAM provided a detailed profitability analysis for each Fund. After making some adjustments so that the presentation would be more comparable to the available industry figures, I reviewed profit margins from investment management alone, from investment management plus other fund services (excluding distribution) provided to the Funds by DeAM (principally shareholder services), and DeAM profits from all sources, including distribution. A later section comments on overall profitability.

**Economies of Scale**

Economies of scale — an expected decline in management cost per dollar of fund assets as fund assets grow — are very rarely quantified and documented because of inherent difficulties in collecting and analyzing relevant data. However, in virtually every investment category that I reviewed, larger funds tend to have lower fees and lower total expenses than smaller funds. To see how each DWS Fund compares with this industry observation, I reviewed:

- The trend in Fund assets over the last five years and the accompanying trend in total expenses. This shows if the Fund has grown and, if so, whether total expense (management fees as well as other expenses) have declined as a percent of assets.
- Whether the Fund has break-points in its management fee schedule, the extent of the fee reduction built into the schedule and the asset levels where the breaks take effect, and in the case of a sub-advised Fund how the Fund's break-points compare with those of the sub-advisory fee schedule.
- How the Fund's contractual fee schedule compares with trends in the industry data. To accomplish this, I constructed a chart showing how actual latest-fiscal-year contractual fees of the Fund and of other similar funds relate to average fund assets, with the subject Fund's contractual fee schedule superimposed.

**Quality of Service — Performance**

The quality-of-service evaluation focused on investment performance, which is the principal result of the investment management service. Each Fund's performance was reviewed over the past 1, 3, 5 and 10 years, as applicable, and compared with that of other funds in the same investment category and with a suitable market index.

In addition, I calculated and reviewed risk-adjusted returns relative to an index of similar mutual funds' returns and a suitable market index. The risk-adjusted returns analysis provides a way of determining the extent to which the Fund's return comparisons are mainly the product of investment value-added (or lack thereof) or alternatively taking considerably more or less risk than is typical in its investment category.

I also received and considered the history of portfolio manager changes for each Fund, as this provided an important context for evaluating the performance results.

## Complex-Level Considerations

While this evaluation was conducted mainly at the individual fund level, there are some issues relating to the reasonableness of fees that can alternatively be considered across the whole fund complex:

- I reviewed DeAM's profitability analysis for all DWS Funds, with a view toward determining if the allocation procedures used were reasonable and how profit levels compared with public data for other investment managers.
- I considered whether DeAM and affiliates receive any significant ancillary or "fall-out" benefits that should be considered in interpreting the direct profitability results. These would be situations where serving as the investment manager of the Funds is beneficial to another part of the Deutsche Bank organization.
- I considered how aggregated DWS Fund expenses had varied over the years, by asset class and in the context of trends in asset levels.
- I reviewed the structure of the DeAM organization, trends in staffing levels, and information on compensation of investment management and other professionals compared with industry data.

## Findings

Based on the process and analysis discussed above, which included reviewing a wide range of information from management and external data sources and considering among other factors the fees DeAM charges other clients, the fees charged by other fund managers, DeAM's costs and profits associated with managing the Funds, economies of scale, possible fall-out benefits, and the nature and quality of services provided, in my opinion the management fees charged the DWS Funds are reasonable.

Thomas H. Mack

# Board Members and Officers

The following table presents certain information regarding the Board Members and Officers of the Trust as of December 31, 2010. Each Board Member's year of birth is set forth in parentheses after his or her name. Unless otherwise noted, (i) each Board Member has engaged in the principal occupation(s) noted in the table for at least the most recent five years, although not necessarily in the same capacity; and (ii) the address of each Independent Board Member is c/o Paul K. Freeman, Independent Chairman, DWS Funds, PO Box 101833, Denver, CO 80250-1833. Except as otherwise noted below, the term of office for each Board Member is until the election and qualification of a successor, or until such Board Member sooner dies, resigns, is removed or as otherwise provided in the governing documents of the fund. Because the fund does not hold an annual meeting of shareholders, each Board Member will hold office for an indeterminate period. The Board Members may also serve in similar capacities with other funds in the fund complex. The Length of Time Served represents the year in which the Board Member joined the board of one or more DWS funds now overseen by the Board.

**Independent Board Members**

| Name, Year of Birth, Position with the Fund and Length of Time Served[1] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Paul K. Freeman (1950)<br>Chairperson since 2009<br>Board Member since 1993 | Consultant, World Bank/Inter-American Development Bank; Executive and Governing Council of the Independent Directors Council (education committees); formerly, Project Leader, International Institute for Applied Systems Analysis (1998–2001); Chief Executive Officer, The Eric Group, Inc. (environmental insurance) (1986–1998) | 122 |
| John W. Ballantine (1946)<br>Board Member since 1999 | Retired; formerly, Executive Vice President and Chief Risk Management Officer, First Chicago NBD Corporation/The First National Bank of Chicago (1996–1998); Executive Vice President and Head of International Banking (1995–1996). Directorships: Healthways, Inc. (provider of disease and care management services); Portland General Electric (utility company); Stockwell Capital Investments PLC (private equity). Former Directorships: First Oak Brook Bancshares, Inc. and Oak Brook Bank; Prisma Energy International | 122 |
| Henry P. Becton, Jr. (1943)<br>Board Member since 1990 | Vice Chair and former President, WGBH Educational Foundation. Directorships: Association of Public Television Stations; Lead Director, Becton Dickinson and Company[3] (medical technology company); Lead Director, Belo Corporation[3] (media company); Public Radio International; Public Radio Exchange (PRX); The PBS Foundation. Former Directorships: Boston Museum of Science; American Public Television; Concord Academy; New England Aquarium; Mass. Corporation for Educational Telecommunications; Committee for Economic Development; Public Broadcasting Service | 122 |
| Dawn-Marie Driscoll (1946)<br>Board Member since 1987 | President, Driscoll Associates (consulting firm); Executive Fellow, Center for Business Ethics, Bentley University; formerly, Partner, Palmer & Dodge (1988–1990); Vice President of Corporate Affairs and General Counsel, Filene's (1978–1988). Directorships: Trustee of 22 open-end mutual funds managed by Sun Capital Advisers, Inc. (since 2007); Director of ICI Mutual Insurance Company (since 2007); Advisory Board, Center for Business Ethics, Bentley University; Trustee, Southwest Florida Community Foundation (charitable organization). Former Directorships: Investment Company Institute (audit, executive, nominating committees) and Independent Directors Council (governance, executive committees) | 122 |
| Keith R. Fox (1954)<br>Board Member since 1996 | Managing General Partner, Exeter Capital Partners (a series of private investment funds). Directorships: Progressive International Corporation (kitchen goods importer and distributor); BoxTop Media Inc. (advertising); The Kennel Shop (retailer); former Chairman, National Association of Small Business Investment Companies | 122 |
| Kenneth C. Froewiss (1945)<br>Board Member since 2001 | Adjunct Professor of Finance, NYU Stern School of Business (September 2009–present; Clinical Professor from 1997–September 2009); Member, Finance Committee, Association for Asian Studies (2002–present); Director, Mitsui Sumitomo Insurance Group (US) (2004–present); prior thereto, Managing Director, J.P. Morgan (investment banking firm) (until 1996) | 122 |
| Richard J. Herring (1946)<br>Board Member since 1990 | Jacob Safra Professor of International Banking and Professor, Finance Department, The Wharton School, University of Pennsylvania (since July 1972); Co-Director, Wharton Financial Institutions Center (since July 2000); Co-Chair, U.S. Shadow Financial Regulatory Committee; Executive Director, Financial Economists Roundtable; Director, Japan Equity Fund, Inc. (since September 2007), Thai Capital Fund, Inc. (since September 2007), Singapore Fund, Inc. (since September 2007); Independent Director of Barclays Bank Delaware (since September 2010). Formerly, Vice Dean and Director, Wharton Undergraduate Division (July 1995–June 2000); Director, Lauder Institute of International Management Studies (July 2000–June 2006) | 122 |
| William McClayton (1944)<br>Board Member since 2004+ | Private equity investor (since October 2009); previously, Managing Director, Diamond Management & Technology Consultants, Inc. (global consulting firm) (2001–2009); Directorship: Board of Managers, YMCA of Metropolitan Chicago; formerly: Senior Partner, Arthur Andersen LLP (accounting) (1966–2001); Trustee, Ravinia Festival | 122 |

| Name, Year of Birth, Position with the Fund and Length of Time Served[1] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Rebecca W. Rimel (1951)<br>Board Member since 1995 | President and Chief Executive Officer, The Pew Charitable Trusts (charitable organization) (1994 to present); Trustee, Thomas Jefferson Foundation (charitable organization) (1994 to present); Trustee, Executive Committee, Philadelphia Chamber of Commerce (2001–2007); Director, CardioNet, Inc.[2] (2009–present) (health care). Formerly, Executive Vice President, The Glenmede Trust Company (investment trust and wealth management) (1983–2004); Board Member, Investor Education (charitable organization) (2004–2005); Director, Viasys Health Care[2] (January 2007–June 2007); Trustee, Pro Publica (charitable organization) (2007–2010) | 122 |
| William N. Searcy, Jr. (1946)<br>Board Member since 1993 | Private investor since October 2003; Trustee of 22 open-end mutual funds managed by Sun Capital Advisers, Inc. (since October 1998). Formerly, Pension & Savings Trust Officer, Sprint Corporation[2] (telecommunications) (November 1989–September 2003) | 122 |
| Jean Gleason Stromberg (1943)<br>Board Member since 1997 | Retired. Formerly, Consultant (1997–2001); Director, Financial Markets US Government Accountability Office (1996–1997); Partner, Fulbright & Jaworski, L.L.P. (law firm) (1978–1996). Directorships: The William and Flora Hewlett Foundation. Former Directorships: Service Source, Inc., Mutual Fund Directors Forum (2002–2004), American Bar Retirement Association (funding vehicle for retirement plans) (1987–1990 and 1994–1996) | 122 |
| Robert H. Wadsworth (1940)<br>Board Member since 1999 | President, Robert H. Wadsworth & Associates, Inc. (consulting firm) (1983 to present); Director, The Phoenix Boys Choir Association | 125 |

## Interested Board Member and Officer[4]

| Name, Year of Birth, Position with the Trust/ Corporation and Length of Time Served[1,5] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Ingo Gefeke[7] (1967)<br>Board Member since 2010<br>Executive Vice President since 2010 | Managing Director[3], Deutsche Asset Management; Global Head of Distribution and Product Management, DWS Global Head of Trading and Securities Lending. Member of the Board of Directors of DWS Investment GmbH Frankfurt (since July 2009) and DWS Holding & Service GmbH Frankfurt (since January 2010); formerly, Global Chief Administrative Officer, Deutsche Asset Management (2004–2009); Global Chief Operating Officer, Global Transaction Banking, Deutsche Bank AG, New York (2001–2004); Chief Operating Officer, Global Banking Division Americas, Deutsche Bank AG, New York (1999–2001); Central Management, Global Banking Services, Deutsche Bank AG, Frankfurt (1998–1999); Relationship Management, Deutsche Bank AG, Tokyo, Japan (1997–1998) | 55 |

## Officers[4]

| Name, Year of Birth, Position with the Fund and Length of Time Served[5] | Principal Occupation(s) During Past 5 Years and Other Directorships Held |
|---|---|
| Michael G. Clark[6] (1965)<br>President, 2006–present | Managing Director[3], Deutsche Asset Management (2006–present); President of DWS family of funds; Director, ICI Mutual Insurance Company (since October 2007); formerly, Director of Fund Board Relations (2004–2006) and Director of Product Development (2000–2004), Merrill Lynch Investment Managers; Senior Vice President Operations, Merrill Lynch Asset Management (1999–2000) |
| John Millette[8] (1962)<br>Vice President and Secretary, 1999–present | Director[3], Deutsche Asset Management |
| Paul H. Schubert[6] (1963)<br>Chief Financial Officer, 2004–present<br>Treasurer, 2005–present | Managing Director[3], Deutsche Asset Management (since July 2004); formerly, Executive Director, Head of Mutual Fund Services and Treasurer for UBS Family of Funds (1998–2004); Vice President and Director of Mutual Fund Finance at UBS Global Asset Management (1994–1998) |
| Caroline Pearson[8] (1962)<br>Chief Legal Officer, April 2010–present | Managing Director[3], Deutsche Asset Management; formerly, Assistant Secretary for DWS family of funds (1997–2010) |
| Rita Rubin[9] (1970)<br>Assistant Secretary, 2009–present | Vice President and Counsel, Deutsche Asset Management (since October 2007); formerly, Vice President, Morgan Stanley Investment Management (2004–2007) |
| Paul Antosca[8] (1957)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management (since 2006); Vice President, The Manufacturers Life Insurance Company (U.S.A.) (1990–2006) |
| Jack Clark[8] (1967)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management (since 2007); formerly, Vice President, State Street Corporation (2002–2007) |

| Name, Year of Birth, Position with the Fund and Length of Time Served[5] | Principal Occupation(s) During Past 5 Years and Other Directorships Held |
|---|---|
| Diane Kenneally[8] (1966)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management |
| John Caruso[9] (1965)<br>Anti-Money Laundering Compliance Officer, 2010–present | Managing Director[3], Deutsche Asset Management |
| Robert Kloby[9] (1962)<br>Chief Compliance Officer, 2006–present | Managing Director[3], Deutsche Asset Management |

1 *The length of time served represents the year in which the Board Member joined the board of one or more DWS funds currently overseen by the Board.*

2 *A publicly held company with securities registered pursuant to Section 12 of the Securities Exchange Act of 1934.*

3 *Executive title, not a board directorship.*

4 *As a result of their respective positions held with the Advisor, these individuals are considered "interested persons" of the Advisor within the meaning of the 1940 Act. Interested persons receive no compensation from the fund.*

5 *The length of time served represents the year in which the officer was first elected in such capacity for one or more DWS funds.*

6 *Address: 100 Plaza One, Jersey City, NJ 07311.*

7 *Effective January 11, 2011, Mr. Gefeke, an interested Board Member and Executive Vice President, resigned from the fund's Board and as an officer.*

*The mailing address of Mr. Gefeke is 345 Park Avenue, New York, New York 10154. Mr. Gefeke was an interested Board Member of certain DWS funds by virtue of his positions with Deutsche Asset Management. As an interested person, Mr. Gefeke received no compensation from the fund.*

8 *Address: One Beacon Street, Boston, MA 02108.*

9 *Address: 60 Wall Street, New York, New York 10005.*

*The fund's Statement of Additional Information ("SAI") includes additional information about the Board Members. The SAI is available, without charge, upon request. If you would like to request a copy of the SAI, you may do so by calling the following toll-free number: (800) 728-3337.*

## Notes

DWS Investments is part of Deutsche Bank's Asset Management division and, within the US, represents the retail asset management activities of Deutsche Bank AG, Deutsche Bank Trust Company Americas, Deutsche Investment Management Americas Inc. and DWS Trust Company.

The views expressed in this report reflect those of the portfolio managers only through the end of the period of the report as stated on the cover. The managers' views are subject to change at any time based on market and other conditions and should not be construed as a recommendation.

This information must be preceded or accompanied by a current prospectus.

Portfolio changes should not be considered recommendations for action by individual investors.

DWS Investments Distributors, Inc.
222 South Riverside Plaza
Chicago, IL 60606
(800) 621-1148

VS2DIE-2 (2/11)

DWS INVESTMENTS
Deutsche Bank Group

DECEMBER 31, 2010

# ANNUAL REPORT

## DWS VARIABLE SERIES II

DWS Dreman Small Mid Cap Value VIP

**This report must be preceded or accompanied by a prospectus. To obtain an additional prospectus or summary prospectus, if available, call (800) 728-3337 or your financial representative. We advise you to consider the Fund's objectives, risks, charges and expenses carefully before investing. The summary prospectus and prospectus contain this and other important information about the Fund. Please read the prospectus carefully before you invest.**

*Investments in variable insurance portfolios (VIPs) involve risk. Stocks may decline in value. Bond investments are subject to interest-rate and credit risks. When interest rates rise, bond prices generally fall. Credit risk refers to the ability of an issuer to make timely payments of principal and interest. Investing in derivatives entails special risks relating to liquidity, leverage and credit that may reduce returns and/or increased volatility. Investing in foreign securities, particularly those of emerging markets, presents certain risks, such as currency fluctuations, political and economic changes, and market risks. There are additional risks associated with investing in commodities, high-yield bonds, aggressive growth stocks, non-diversified/ concentrated funds and small- and mid-cap stocks which are more fully explained in the prospectuses. Please read the prospectus for more information.*

*DWS Investments is part of Deutsche Bank's Asset Management division and, within the US, represents the retail asset management activities of Deutsche Bank AG, Deutsche Bank Trust Company Americas, Deutsche Investment Management Americas Inc. and DWS Trust Company.*

*NOT FDIC/NCUA INSURED   NO BANK GUARANTEE   MAY LOSE VALUE   NOT A DEPOSIT*
*NOT INSURED BY ANY FEDERAL GOVERNMENT AGENCY*

DWS INVESTMENTS
Deutsche Bank Group

# Performance Summary

**December 31, 2010**

## DWS Dreman Small Mid Cap Value VIP

**All performance shown is historical, assumes reinvestment of all dividend and capital gain distributions and does not guarantee future results. Investment return and principal value fluctuate with changing market conditions so that, when redeemed, shares may be worth more or less than their original cost. Current performance may be lower or higher than the performance data quoted. Please contact your participating insurance company for the Fund's most recent month-end performance. Performance doesn't reflect charges and fees ("contract charges") associated with the separate account that invests in the Fund or any variable life insurance policy or variable annuity contract for which the Fund is an investment option. These charges and fees will reduce returns. While all share classes have the same underlying portfolio, their performance will differ.**

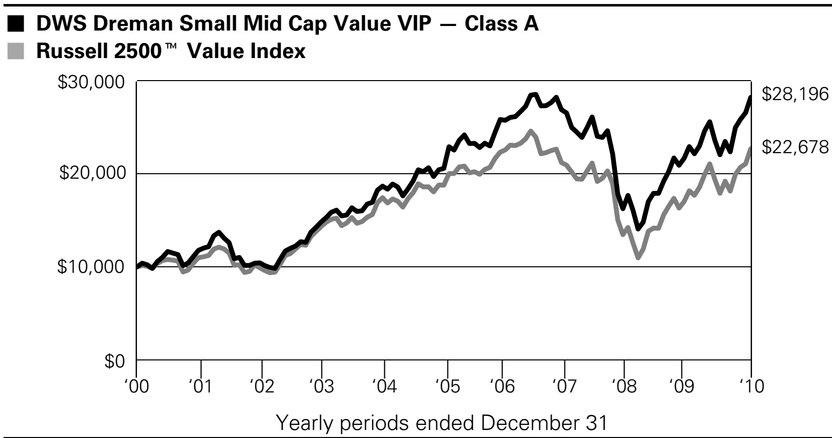
**The gross expense ratios of the Fund, as stated in the fee table of the prospectus dated May 1, 2010 are 0.79% and 1.14% for Class A and Class B shares, respectively, and may differ from the expense ratios disclosed in the Financial Highlights tables in this report.**

### Risk Considerations

Any Fund that focuses in a particular segment of the market will generally be more volatile than a fund that invests more broadly. Stocks of small and medium-sized companies involve greater risk than securities of larger, more-established companies. Any decline in value of a Fund security that is out on loan by the Fund will adversely affect performance. Financial failure of the borrower may mean a delay in recovery or loss of rights in the collateral. Stocks may decline in value. See the prospectus for details.

Fund returns shown for the 3-year, 5-year and 10-year/Life of Class periods reflect a fee waiver and/or expense reimbursement. Without this waiver/reimbursement, returns would have been lower.

### Growth of an Assumed $10,000 Investment in DWS Dreman Small Mid Cap Value VIP




*The Russell 2500 ™ Value Index is an unmanaged Index of those securities in the Russell 3000® Index with lower price-to-book ratios and lower forecasted growth values.*

*Index returns assume reinvestment of dividends and, unlike fund returns, do not reflect any fees or expenses. It is not possible to invest directly into an index.*

### Comparative Results

| DWS Dreman Small Mid Cap Value VIP | | 1-Year | 3-Year | 5-Year | 10-Year |
|---|---|---|---|---|---|
| **Class A** | Growth of $10,000 | $12,307 | $10,628 | $13,698 | $28,196 |
| | Average annual total return | 23.07% | 2.05% | 6.50% | 10.92% |
| Russell 2500 Value Index | Growth of $10,000 | $12,482 | $10,839 | $12,079 | $22,678 |
| | Average annual total return | 24.82% | 2.72% | 3.85% | 8.53% |

| DWS Dreman Small Mid Cap Value VIP | | 1-Year | 3-Year | 5-Year | Life of Class* |
|---|---|---|---|---|---|
| **Class B** | Growth of $10,000 | $12,266 | $10,518 | $13,454 | $22,074 |
| | Average annual total return | 22.66% | 1.70% | 6.11% | 9.76% |
| Russell 2500 Value Index | Growth of $10,000 | $12,482 | $10,839 | $12,079 | $19,734 |
| | Average annual total return | 24.82% | 2.72% | 3.85% | 8.33% |

*The growth of $10,000 is cumulative.*

* *The Fund commenced offering Class B shares on July 1, 2002. Index returns began on June 30, 2002.*

# Information About Your Fund's Expenses

## DWS Dreman Small Mid Cap Value VIP

As an investor of the Fund, you incur two types of costs: ongoing expenses and transaction costs. Ongoing expenses include management fees, distribution and service (12b-1) fees and other Fund expenses. Examples of transaction costs include contract charges, redemption fees and account maintenance fees, which are not shown in this section. The following tables are intended to help you understand your ongoing expenses (in dollars) of investing in the Fund and to help you compare these expenses with the ongoing expenses of investing in other mutual funds. The example in the table is based on an investment of $1,000 invested at the beginning of the six-month period and held for the entire period (July 1, 2010 to December 31, 2010).

The tables illustrate your Fund's expenses in two ways:

- **Actual Fund Return.** This helps you estimate the actual dollar amount of ongoing expenses (but not transaction costs) paid on a $1,000 investment in the Fund using the Fund's actual return during the period. To estimate the expenses you paid over the period, simply divide your account value by $1,000 (for example, an $8,600 account value divided by $1,000 = 8.6), then multiply the result by the number in the "Expenses Paid per $1,000" line under the share class you hold.
- **Hypothetical 5% Fund Return.** This helps you to compare your Fund's ongoing expenses (but not transaction costs) with those of other mutual funds using the Fund's actual expense ratio and a hypothetical rate of return of 5% per year before expenses. Examples using a 5% hypothetical Fund return may be found in the shareholder reports of other mutual funds. The hypothetical account values and expenses may not be used to estimate the actual ending account balance or expenses you paid for the period.

Please note that the expenses shown in these tables are meant to highlight your ongoing expenses only and do not reflect any transaction costs. The "Expenses Paid per $1,000" line of the tables is useful in comparing ongoing expenses only and will not help you determine the relative total expense of owning different funds. If these transaction costs had been included, your costs would have been higher.

**Expenses and Value of a $1,000 Investment** for the six months ended December 31, 2010

| **Actual Fund Return** | **Class A** | **Class B** |
|---|---|---|
| Beginning Account Value 7/1/10 | $1,000.00 | $1,000.00 |
| Ending Account Value 12/31/10 | $1,279.90 | $1,277.50 |
| Expenses Paid per $1,000* | $ 4.65 | $ 6.72 |
| **Hypothetical 5% Fund Return** | **Class A** | **Class B** |
| Beginning Account Value 7/1/10 | $1,000.00 | $1,000.00 |
| Ending Account Value 12/31/10 | $1,021.12 | $1,019.31 |
| Expenses Paid per $1,000* | $ 4.13 | $ 5.96 |

* *Expenses are equal to the Fund's annualized expense ratio for each share class, multiplied by the average account value over the period, multiplied by the number of days in the most recent six-month period, then divided by 365.*

| **Annualized Expense Ratios** | **Class A** | **Class B** |
|---|---|---|
| DWS Variable Series II — DWS Dreman Small Mid Cap Value VIP | .81% | 1.17% |

For more information, please refer to the Fund's prospectus.

These tables do not reflect charges and fees ("contract charges") associated with the separate account that invests in the Fund or any variable life insurance policy or variable annuity contract for which the Fund is an investment option.

## DWS Dreman Small Mid Cap Value VIP

Small- and mid-cap stocks performed very well in 2010, reflecting an environment of positive investor sentiment and gradually improving economic growth. The Class A shares of the Fund returned 23.07% for the year (unadjusted for contract charges), but lagged the 24.82% return of the fund's benchmark, the Russell 2500™ Value Index. Although the Fund underperformed, we are gratified that it largely kept pace with the index at a time in which the market's best performers were generally the type of richly valued, momentum-driven stocks that we seek to avoid.

We believe it is important to note that our value-focused approach has contributed to strong outperformance for the Fund over the long term, as it has outpaced the benchmark during both the 5- and 10-year periods ended December 31, 2010.

Our bottom-up stock selection process worked well in the information technology, materials and financial sectors during 2010, but we underperformed in the consumer discretionary segment. Our top individual performer in 2010 was CBL & Associates Properties, Inc., a real estate investment trust whose focus on retail properties positioned it to benefit from the improvement in consumer spending. Endo Pharmaceuticals Holdings, Inc., Pan American Silver Corp.* and Forest Oil Corp. also added significant value for the Fund. On the negative side, our leading detractors were ITT Educational Services, Inc.* and Alliant Techsystems, Inc.

We retain a reasonably optimistic outlook as we enter the new year. While the broader market is nowhere near as inexpensive as it was 12–18 months ago, there are still plenty of opportunities for bottom-up stock pickers. We continue to focus on companies with valuations that do not fully reflect their strong fundamentals, which in our view provide a margin of safety in the event of a market downturn.[1] We believe this disciplined, value-based approach — together with our conscious decision to avoid chasing overvalued stocks when they rally — has been the key to our success over the past decade.

David N. Dreman
*Lead Portfolio Manager*

E. Clifton Hoover, Jr., CFA
Mark Roach
*Portfolio Managers*
*Dreman Value Management, L.L.C., Subadvisor to the Fund*

*The Russell 2500 Value Index is an unmanaged index of those securities in the Russell 3000® Index with lower price-to-book ratio and lower forecasted growth values.*

*Index returns assume reinvestment of dividends and, unlike fund returns, do not reflect any fees or expenses. It is not possible to invest directly into an index.*

1 *"Valuation" refers to the price investors pay for a given security. An asset can be undervalued, meaning that it trades for less than its intrinsic value, or overvalued, which means that it trades at a more expensive price than its underlying worth.*

* *Not held in the Fund as of December 31, 2010.*

*Portfolio management market commentary is as of December 31, 2010, and may not come to pass. This information is subject to change at any time based on market and other conditions. Past performance does not guarantee future results. Current and future portfolio holdings are subject to risk.*

# Portfolio Summary

## DWS Dreman Small Mid Cap Value VIP

| **Asset Allocation** (As a % of Investment Portfolio excluding Securities Lending Collateral) | **12/31/10** | **12/31/09** |
|---|---|---|
| Common Stocks | 98% | 100% |
| Closed-End Investment Company | 1% | — |
| Cash Equivalents | 1% | 0% |
| | 100% | 100% |

| **Sector Diversification** (As a % of Common Stocks) | **12/31/10** | **12/31/09** |
|---|---|---|
| Financials | 19% | 15% |
| Information Technology | 14% | 15% |
| Industrials | 13% | 16% |
| Energy | 11% | 9% |
| Health Care | 11% | 9% |
| Consumer Discretionary | 11% | 14% |
| Materials | 9% | 6% |
| Utilities | 6% | 7% |
| Consumer Staples | 6% | 8% |
| Telecommunications Services | — | 1% |
| | 100% | 100% |

*Asset allocation and sector diversification are subject to change.*

*For more complete details about the Fund's investment portfolio, see page 6.*

Following the Fund's fiscal first and third quarter-end, a complete portfolio holdings listing is filed with the SEC on Form N-Q. The form will be available on the SEC's Web site at www.sec.gov, and it also may be reviewed and copied at the SEC's Public Reference Room in Washington, D.C. Information on the operation of the SEC's Public Reference Room may be obtained by calling (800) SEC-0330. The Fund's portfolio holdings are also posted on www.dws-investments.com from time to time. Please see the Fund's current prospectus for more information.

# Investment Portfolio

December 31, 2010

## DWS Dreman Small Mid Cap Value VIP

| | Shares | Value ($) |
|---|---|---|
| **Common Stocks 97.8%** | | |
| **Consumer Discretionary 11.0%** | | |
| **Auto Components 0.6%** | | |
| Cooper Tire & Rubber Co. (a) | 70,654 | **1,666,021** |
| **Diversified Consumer Services 1.1%** | | |
| Regis Corp. (a) | 187,925 | **3,119,555** |
| **Hotels Restaurants & Leisure 3.3%** | | |
| Brinker International, Inc. (a) | 192,550 | 4,020,444 |
| International Speedway Corp. "A" (a) | 113,475 | 2,969,641 |
| LIFE TIME FITNESS, Inc.* (a) | 48,596 | 1,991,950 |
| | | **8,982,035** |
| **Leisure Equipment & Products 1.2%** | | |
| Mattel, Inc. | 131,425 | **3,342,138** |
| **Multiline Retail 1.0%** | | |
| Big Lots, Inc.* (a) | 91,179 | **2,777,312** |
| **Specialty Retail 1.2%** | | |
| Aaron's, Inc. (a) | 153,987 | **3,139,795** |
| **Textiles, Apparel & Luxury Goods 2.6%** | | |
| Hanesbrands, Inc.* (a) | 129,900 | 3,299,460 |
| The Jones Group, Inc. | 239,790 | 3,726,337 |
| | | **7,025,797** |
| **Consumer Staples 5.7%** | | |
| **Beverages 1.6%** | | |
| Constellation Brands, Inc. "A"* (a) | 195,975 | **4,340,846** |
| **Food Products 2.7%** | | |
| Del Monte Foods Co. (a) | 214,750 | 4,037,300 |
| Ralcorp Holdings, Inc.* (a) | 53,300 | 3,465,033 |
| | | **7,502,333** |
| **Household Products 1.4%** | | |
| Energizer Holdings, Inc.* | 50,975 | **3,716,078** |
| **Energy 11.2%** | | |
| **Energy Equipment & Services 5.9%** | | |
| Atwood Oceanics, Inc.* (a) | 90,490 | 3,381,612 |
| Cal Dive International, Inc.* | 481,725 | 2,731,381 |
| McDermott International, Inc.* | 126,125 | 2,609,526 |
| Superior Energy Services, Inc.* (a) | 111,975 | 3,918,005 |
| Tidewater, Inc. (a) | 65,875 | 3,546,710 |
| | | **16,187,234** |
| **Oil, Gas & Consumable Fuels 5.3%** | | |
| Arch Coal, Inc. (a) | 123,000 | 4,312,380 |
| Forest Oil Corp.* (a) | 102,800 | 3,903,316 |
| Frontline Ltd. (a) | 113,375 | 2,876,324 |
| Newfield Exploration Co.* | 46,915 | 3,383,040 |
| | | **14,475,060** |
| **Financials 17.5%** | | |
| **Capital Markets 1.3%** | | |
| Raymond James Financial, Inc. (a) | 104,600 | **3,420,420** |
| **Commercial Banks 2.2%** | | |
| Bank of Hawaii Corp. (a) | 60,100 | 2,837,321 |
| BOK Financial Corp. (a) | 61,025 | 3,258,735 |
| | | **6,096,056** |
| **Insurance 6.3%** | | |
| Allied World Assurance Co. Holdings Ltd. (a) | 62,450 | 3,712,028 |
| Argo Group International Holdings Ltd. | 104,813 | 3,925,247 |
| Axis Capital Holdings Ltd. | 93,800 | 3,365,544 |
| Endurance Specialty Holdings Ltd. (a) | 60,075 | 2,767,655 |
| Everest Re Group Ltd. | 40,225 | 3,411,885 |
| | | **17,182,359** |
| **Real Estate Investment Trusts 7.7%** | | |
| CBL & Associates Properties, Inc. (REIT) (a) | 225,500 | 3,946,250 |
| CommonWealth REIT (REIT) (a) | 126,756 | 3,233,545 |
| Hospitality Properties Trust (REIT) | 146,750 | 3,381,120 |
| Medical Properties Trust, Inc. (REIT) (a) | 341,500 | 3,698,445 |
| MFA Financial, Inc. (REIT) | 411,975 | 3,361,716 |
| Weingarten Realty Investors (REIT) (a) | 149,400 | 3,549,744 |
| | | **21,170,820** |
| **Health Care 11.2%** | | |
| **Biotechnology 1.2%** | | |
| Cephalon, Inc.* | 52,450 | **3,237,214** |
| **Health Care Equipment & Supplies 3.8%** | | |
| Alere, Inc.* (a) | 107,275 | 3,926,265 |
| Beckman Coulter, Inc. (a) | 47,700 | 3,588,471 |
| Teleflex, Inc. (a) | 54,200 | 2,916,502 |
| | | **10,431,238** |
| **Health Care Providers & Services 3.7%** | | |
| Healthspring, Inc.* (a) | 125,175 | 3,320,893 |
| LifePoint Hospitals, Inc.* (a) | 88,825 | 3,264,319 |
| Owens & Minor, Inc. | 114,350 | 3,365,320 |
| | | **9,950,532** |
| **Life Sciences Tools & Services 1.2%** | | |
| Charles River Laboratories International, Inc.* (a) | 93,375 | **3,318,547** |
| **Pharmaceuticals 1.3%** | | |
| Endo Pharmaceuticals Holdings, Inc.* (a) | 100,625 | **3,593,319** |
| **Industrials 12.4%** | | |
| **Aerospace & Defense 2.4%** | | |
| Alliant Techsystems, Inc.* | 45,250 | 3,367,958 |
| Spirit AeroSystems Holdings, Inc. "A"* | 155,000 | 3,225,550 |
| | | **6,593,508** |
| **Commercial Services & Supplies 2.1%** | | |
| Pitney Bowes, Inc. (a) | 124,950 | 3,021,291 |
| The Brink's Co. | 101,475 | 2,727,648 |
| | | **5,748,939** |
| **Construction & Engineering 1.2%** | | |
| Tutor Perini Corp. | 155,900 | **3,337,819** |
| **Electrical Equipment 2.9%** | | |
| GrafTech International Ltd.* | 183,925 | 3,649,072 |
| Hubbell, Inc. "B" (a) | 69,050 | 4,151,976 |
| | | **7,801,048** |
| **Machinery 2.6%** | | |
| Crane Co. | 89,925 | 3,693,219 |
| Joy Global, Inc. | 39,385 | 3,416,649 |
| | | **7,109,868** |
| **Trading Companies & Distributors 1.2%** | | |
| Textainer Group Holdings Ltd. (a) | 118,450 | **3,374,641** |
| **Information Technology 14.3%** | | |
| **Communications Equipment 2.0%** | | |
| Arris Group, Inc.* (a) | 260,450 | 2,922,249 |

*The accompanying notes are an integral part of the financial statements.*

| | Shares | Value ($) |
|---|---|---|
| CommScope, Inc.* (a) | 85,450 | 2,667,749 |
| | | **5,589,998** |
| **Computers & Peripherals 1.6%** | | |
| NCR Corp.* | 89,728 | 1,379,119 |
| Synaptics, Inc.* (a) | 103,375 | 3,037,158 |
| | | **4,416,277** |
| **Electronic Equipment, Instruments & Components 2.9%** | | |
| Arrow Electronics, Inc.* | 119,375 | 4,088,594 |
| Jabil Circuit, Inc. (a) | 196,500 | 3,947,685 |
| | | **8,036,279** |
| **IT Services 3.1%** | | |
| Amdocs Ltd.* | 114,125 | 3,135,014 |
| DST Systems, Inc. | 77,050 | 3,417,167 |
| Jack Henry & Associates, Inc. (a) | 69,381 | 2,022,456 |
| | | **8,574,637** |
| **Semiconductors & Semiconductor Equipment 2.6%** | | |
| Microsemi Corp.* | 156,150 | 3,575,835 |
| Teradyne, Inc.* (a) | 245,425 | 3,445,767 |
| | | **7,021,602** |
| **Software 2.1%** | | |
| Net 1 UEPS Technologies, Inc.* | 156,665 | 1,920,713 |
| Synopsys, Inc.* | 138,575 | 3,729,053 |
| | | **5,649,766** |
| **Materials 8.5%** | | |
| **Chemicals 3.0%** | | |
| CF Industries Holdings, Inc. | 34,200 | 4,622,130 |
| Lubrizol Corp. (a) | 32,900 | 3,516,352 |
| | | **8,138,482** |
| **Containers & Packaging 1.1%** | | |
| Owens-Illinois, Inc.* | 98,125 | **3,012,438** |
| **Metals & Mining 4.4%** | | |
| Coeur d'Alene Mines Corp.* (a) | 194,375 | 5,310,325 |
| IAMGOLD Corp. (a) | 188,575 | 3,356,635 |
| Reliance Steel & Aluminum Co. (a) | 68,800 | 3,515,680 |
| | | **12,182,640** |
| **Utilities 6.0%** | | |
| **Electric Utilities 2.5%** | | |
| Allegheny Energy, Inc. | 142,100 | 3,444,504 |
| Portland General Electric Co. | 150,350 | 3,262,595 |
| | | **6,707,099** |
| **Gas Utilities 1.0%** | | |
| AGL Resources, Inc. | 78,575 | **2,816,914** |
| **Independent Power Producers & Energy Traders 1.2%** | | |
| Constellation Energy Group, Inc. | 109,825 | **3,363,940** |
| **Multi-Utilities 1.3%** | | |
| Ameren Corp. (a) | 121,650 | **3,429,313** |
| **Total Common Stocks** (Cost $206,930,389) | | **267,579,917** |

## Closed-End Investment Company 1.2%

| | Shares | Value ($) |
|---|---|---|
| **Financials** | | |
| Apollo Investment Corp. (Cost $3,305,969) | 302,775 | **3,351,719** |

## Securities Lending Collateral 35.9%

| | Shares | Value ($) |
|---|---|---|
| Daily Assets Fund Institutional, 0.27% (b) (c) (Cost $98,280,070) | 98,280,070 | **98,280,070** |

## Cash Equivalents 0.6%

| | Shares | Value ($) |
|---|---|---|
| Central Cash Management Fund, 0.19% (b) (Cost $1,698,867) | 1,698,867 | **1,698,867** |

| | % of Net Assets | Value ($) |
|---|---|---|
| **Total Investment Portfolio** (Cost $310,215,295)† | 135.5 | **370,910,573** |
| **Other Assets and Liabilities, Net** | (35.5) | **(97,205,361)** |
| **Net Assets** | 100.0 | **273,705,212** |

* *Non-income producing security.*

† *The cost for federal income tax purposes was $311,177,875. At December 31, 2010, net unrealized appreciation for all securities based on tax cost was $59,732,698. This consisted of aggregate gross unrealized appreciation for all securities in which there was an excess of value over tax cost of $69,554,187 and aggregate gross unrealized depreciation for all securities in which there was an excess of tax cost over value of $9,821,489.*

(a) *All or a portion of these securities were on loan (see Notes to Financial Statements). The value of all securities loaned at December 31, 2010 amounted to $95,671,560, which is 35.0% of net assets.*

(b) *Affiliated fund managed by Deutsche Investment Management Americas Inc. The rate shown is the annualized seven-day yield at period end.*

(c) *Represents collateral held in connection with securities lending. Income earned by the Fund is net of borrower rebates.*

*REIT: Real Estate Investment Trust*

### Fair Value Measurements

*Various inputs are used in determining the value of the Fund's investments. These inputs are summarized in three broad levels. Level 1 includes quoted prices in active markets for identical securities. Level 2 includes other significant observable inputs (including quoted prices for similar securities, interest rates, prepayment speeds, and credit risk). Level 3 includes significant unobservable inputs (including the Fund's own assumptions in determining the fair value of investments). The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities.*

*The following is a summary of the inputs used as of December 31, 2010 in valuing the Fund's investments. For information on the Fund's policy regarding the valuation of investments, please refer to the Security Valuation section of Note A in the accompanying Notes to Financial Statements.*

| Assets | Level 1 | Level 2 | Level 3 | Total |
|---|---|---|---|---|
| Common Stocks (d) | $ 267,579,917 | $ — | $ — | $ 267,579,917 |
| Closed-End Investment Company | 3,351,719 | — | — | 3,351,719 |
| Short-Term Investments (d) | 99,978,937 | — | — | 99,978,937 |
| **Total** | **$ 370,910,573** | **$ —** | **$ —** | **$ 370,910,573** |

*There have been no significant transfers between Level 1 and Level 2 fair value measurements during the year ended December 31, 2010.*

(d) *See Investment Portfolio for additional detailed categorizations.*

*The accompanying notes are an integral part of the financial statements.*

# Statement of Assets and Liabilities

as of December 31, 2010

| | | |
|---|---|---|
| **Assets** | | |
| Investments: | | |
| Investments in unaffiliated securities, at value (cost $210,236,358) — including $95,671,560 of securities loaned | $ | 270,931,636 |
| Investment in Daily Assets Fund Institutional (cost $98,280,070)* | | 98,280,070 |
| Investment in Central Cash Management Fund (cost $1,698,867) | | 1,698,867 |
| Total investments, at value (cost $310,215,295) | | 370,910,573 |
| Cash | | 18,356 |
| Receivable for investments sold | | 1,419,033 |
| Receivable for Fund shares sold | | 291,039 |
| Dividends receivable | | 398,083 |
| Interest receivable | | 9,566 |
| Other assets | | 1,379 |
| Total assets | | 373,048,029 |
| **Liabilities** | | |
| Payable upon return of securities loaned | | 98,280,070 |
| Payable for investments purchased | | 528,674 |
| Payable for Fund shares redeemed | | 245,511 |
| Accrued management fee | | 162,677 |
| Accrued expenses and payables | | 125,885 |
| Total liabilities | | 99,342,817 |
| **Net assets, at value** | **$** | **273,705,212** |
| **Net Assets Consist of:** | | |
| Undistributed net investment income | | 2,636,612 |
| Net unrealized appreciation (depreciation) on investments | | 60,695,278 |
| Accumulated net realized gain (loss) | | (104,463,786) |
| Paid-in capital | | 314,837,108 |
| **Net assets, at value** | **$** | **273,705,212** |
| **Class A** | | |
| **Net Asset Value,** offering and redemption price per share ($247,497,040 ÷ 20,271,172 outstanding shares of beneficial interest, no par value, unlimited number of shares authorized) | **$** | **12.21** |
| **Class B** | | |
| **Net Asset Value,** offering and redemption price per share ($26,208,172 ÷ 2,147,844 outstanding shares of beneficial interest, no par value, unlimited number of shares authorized) | **$** | **12.20** |

* *Represents collateral on securities loaned.*

# Statement of Operations

for the year ended December 31, 2010

| | | |
|---|---|---|
| **Investment Income** | | |
| Income: | | |
| Dividends (net of foreign taxes witheld of $18) | $ | 4,702,210 |
| Income distributions — Central Cash Management Fund | | 13,649 |
| Securities lending income, including income from Daily Assets Fund Institutional, net of borrower rebates | | 274,403 |
| Total income | | 4,990,262 |
| Expenses: | | |
| Management fee | | 1,653,319 |
| Administration fee | | 254,770 |
| Services to shareholders | | 8,397 |
| Distribution service fee (Class B) | | 59,943 |
| Record keeping fees (Class B) | | 24,599 |
| Custodian fee | | 13,570 |
| Professional fees | | 67,753 |
| Trustees fees and expenses | | 10,622 |
| Reports to shareholders | | 58,443 |
| Other | | 12,400 |
| Total expenses | | 2,163,816 |
| **Net investment income (loss)** | | **2,826,446** |
| **Realized and Unrealized Gain (Loss)** | | |
| Net realized gain (loss) from investments | | 30,809,807 |
| Change in net unrealized appreciation (depreciation) on investments | | 18,581,828 |
| **Net gain (loss)** | | **49,391,635** |
| **Net increase (decrease) in net assets resulting from operations** | **$** | **52,218,081** |

*The accompanying notes are an integral part of the financial statements.*

# Statement of Changes in Net Assets

| Increase (Decrease) in Net Assets | Years Ended December 31, 2010 | 2009 |
|---|---|---|
| Operations: | | |
| Net investment income (loss) | $ 2,826,446 | $ 4,311,793 |
| Net realized gain (loss) | 30,809,807 | (70,986,842) |
| Change in net unrealized appreciation (depreciation) | 18,581,828 | 125,626,581 |
| Net increase (decrease) in net assets resulting from operations | 52,218,081 | 58,951,532 |
| Distributions to shareholders from: | | |
| Net investment income: | | |
| Class A | (3,068,046) | (4,046,857) |
| Class B | (217,515) | (395,321) |
| Total distributions | (3,285,561) | (4,442,178) |
| Fund share transactions: | | |
| **Class A** | | |
| Proceeds from shares sold | 28,003,012 | 23,798,898 |
| Reinvestment of distributions | 3,068,046 | 4,046,857 |
| Payments for shares redeemed | (62,437,627) | (65,465,868) |
| Net increase (decrease) in net assets from Class A share transactions | (31,366,569) | (37,620,113) |
| **Class B** | | |
| Proceeds from shares sold | 3,472,987 | 3,195,894 |
| Reinvestment of distributions | 217,515 | 395,321 |
| Payments for shares redeemed | (5,804,013) | (9,987,772) |
| Net increase (decrease) in net assets from Class B share transactions | (2,113,511) | (6,396,557) |
| **Increase (decrease) in net assets** | 15,452,440 | 10,492,684 |
| Net assets at beginning of period | 258,252,772 | 247,760,088 |
| Net assets at end of period (including undistributed net investment income of $2,636,612 and $3,095,726, respectively) | **$ 273,705,212** | **$ 258,252,772** |
| **Other Information** | | |
| **Class A** | | |
| Shares outstanding at beginning of period | 23,383,684 | 28,178,465 |
| Shares sold | 2,611,387 | 2,960,168 |
| Shares issued to shareholders in reinvestment of distributions | 271,509 | 624,515 |
| Shares redeemed | (5,995,408) | (8,379,464) |
| Net increase (decrease) in Class A shares | (3,112,512) | (4,794,781) |
| Shares outstanding at end of period | **20,271,172** | **23,383,684** |
| **Class B** | | |
| Shares outstanding at beginning of period | 2,341,698 | 3,073,371 |
| Shares sold | 327,236 | 387,629 |
| Shares issued to shareholders in reinvestment of distributions | 19,214 | 60,912 |
| Shares redeemed | (540,304) | (1,180,214) |
| Net increase (decrease) in Class B shares | (193,854) | (731,673) |
| Shares outstanding at end of period | **2,147,844** | **2,341,698** |

*The accompanying notes are an integral part of the financial statements.*

# Financial Highlights

## Class A

| Years Ended December 31, | 2010 | 2009 | 2008 | 2007 | 2006 |
|---|---|---|---|---|---|
| **Selected Per Share Data** | | | | | |
| **Net asset value, beginning of period** | **$10.04** | **$ 7.93** | **$20.12** | **$22.93** | **$19.98** |
| *Income (loss) from investment operations:* | | | | | |
| Net investment income[a] | .12 | .16 | .13 | .18 | .15 |
| Net realized and unrealized gain (loss) | 2.19 | 2.11 | (4.92) | .54 | 4.69 |
| **Total from investment operations** | 2.31 | 2.27 | (4.79) | .72 | 4.84 |
| *Less distributions from:* | | | | | |
| Net investment income | (.14) | (.16) | (.29) | (.23) | (.18) |
| Net realized gains | — | — | (7.11) | (3.30) | (1.71) |
| **Total distributions** | (.14) | (.16) | (7.40) | (3.53) | (1.89) |
| **Net asset value, end of period** | **$12.21** | **$10.04** | **$ 7.93** | **$20.12** | **$22.93** |
| Total Return (%) | 23.07 | 29.70 | (33.42)[b] | 3.06 | 25.06 |
| **Ratios to Average Net Assets and Supplemental Data** | | | | | |
| Net assets, end of period ($ millions) | 247 | 235 | 223 | 468 | 562 |
| Ratio of expenses before expense reductions (%) | .82 | .79 | .83 | .78 | .79 |
| Ratio of expenses after expense reductions (%) | .82 | .79 | .82 | .78 | .79 |
| Ratio of net investment income (%) | 1.14 | 1.92 | 1.13 | .85 | .71 |
| Portfolio turnover rate (%) | 38 | 72 | 49 | 110 | 52 |

a *Based on average shares outstanding during the period.*
b *Total return would have been lower had certain expenses not been reduced.*

## Class B

| Years Ended December 31, | 2010 | 2009 | 2008 | 2007 | 2006 |
|---|---|---|---|---|---|
| **Selected Per Share Data** | | | | | |
| **Net asset value, beginning of period** | **$10.03** | **$ 7.92** | **$20.08** | **$22.88** | **$19.93** |
| *Income (loss) from investment operations:* | | | | | |
| Net investment income[a] | .08 | .13 | .09 | .10 | .07 |
| Net realized and unrealized gain (loss) | 2.19 | 2.12 | (4.92) | .54 | 4.67 |
| **Total from investment operations** | 2.27 | 2.25 | (4.83) | .64 | 4.74 |
| *Less distributions from:* | | | | | |
| Net investment income | (.10) | (.14) | (.22) | (.14) | (.08) |
| Net realized gains | — | — | (7.11) | (3.30) | (1.71) |
| **Total distributions** | (.10) | (.14) | (7.33) | (3.44) | (1.79) |
| **Net asset value, end of period** | **$12.20** | **$10.03** | **$ 7.92** | **$20.08** | **$22.88** |
| Total Return (%) | 22.66 | 29.28 | (33.67)[b] | 2.67 | 24.59 |
| **Ratios to Average Net Assets and Supplemental Data** | | | | | |
| Net assets, end of period ($ millions) | 26 | 23 | 24 | 34 | 90 |
| Ratio of expenses before expense reductions (%) | 1.17 | 1.14 | 1.18 | 1.16 | 1.17 |
| Ratio of expenses after expense reductions (%) | 1.17 | 1.14 | 1.17 | 1.16 | 1.17 |
| Ratio of net investment income (%) | .79 | 1.57 | .78 | .47 | .33 |
| Portfolio turnover rate (%) | 38 | 72 | 49 | 110 | 52 |

a *Based on average shares outstanding during the period.*
b *Total return would have been lower had certain expenses not been reduced.*

# Notes to Financial Statements

## A. Organization and Significant Accounting Policies

DWS Variable Series II (the "Trust") is registered under the Investment Company Act of 1940, as amended (the "1940 Act"), as an open-end management investment company organized as a Massachusetts business trust. The Trust offers seventeen funds (hereinafter referred to individually as "Fund" or collectively as "Funds"). The Fund is classified as a diversified open-end management investment company.

**Multiple Classes of Shares of Beneficial Interest.** Certain Funds of the Trust offer two classes of shares (Class A shares and Class B shares). Sales of Class B shares are subject to record keeping fees up to 0.15% and Rule 12b-1 fees under the 1940 Act equal to an annual rate of 0.25%, of the average daily net assets of the Class B shares of the applicable Fund. Class A shares are not subject to such fees.

Investment income, realized and unrealized gains and losses, and certain fund-level expenses and expense reductions, if any, are borne pro rata on the basis of relative net assets by the holders of all classes of shares except that each class bears certain expenses unique to that class (including the applicable Rule 12b-1 fee and record keeping fees). Differences in class-level expenses may result in payment of different per share dividends by class. All shares have equal rights with respect to voting subject to class-specific arrangements.

The Trust's financial statements are prepared in accordance with accounting principles generally accepted in the United States of America which require the use of management estimates. Actual results could differ from those estimates. The policies described below are followed consistently by the Trust in the preparation of its financial statements.

**Security Valuation.** Investments are stated at value determined as of the close of regular trading on the New York Stock Exchange on each day the exchange is open for trading.

Various inputs are used in determining the value of the Fund's investments. These inputs are summarized in three broad levels. Level 1 includes quoted prices in active markets for identical securities. Level 2 includes other significant observable inputs (including quoted prices for similar securities, interest rates, prepayment speeds, and credit risk). Level 3 includes significant unobservable inputs (including the Fund's own assumptions in determining the fair value of investments). The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities.

Equity securities are valued at the most recent sale price or official closing price reported on the exchange (US or foreign) or over-the-counter market on which they trade and are categorized as Level 1 securities. Securities for which no sales are reported are valued at the calculated mean between the most recent bid and asked quotations on the relevant market or, if a mean cannot be determined, at the most recent bid quotation.

Money market instruments purchased with an original or remaining maturity of sixty days or less, maturing at par, are valued at amortized cost, which approximates value, and are categorized as Level 2. Investments in open-end investment companies are valued at their net asset value each business day and are categorized as Level 1.

Securities and other assets for which market quotations are not readily available or for which the above valuation procedures are deemed not to reflect fair value are valued in a manner that is intended to reflect their fair value as determined in accordance with procedures approved by the Board and are generally categorized as Level 3. In accordance with the Fund's valuation procedures, factors used in determining value may include, but are not limited to, the type of the security; the size of the holding; the initial cost of the security; the existence of any contractual restrictions on the security's disposition; the price and extent of public trading in similar securities of the issuer or of comparable companies; quotations or evaluated prices from broker-dealers and/or pricing services; information obtained from the issuer, analysts, and/or the appropriate stock exchange (for exchange-traded securities); an analysis of the company's or issuer's financial statements; an evaluation of the forces that influence the issuer and the market(s) in which the security is purchased and sold and with respect to debt securities; the maturity, coupon, creditworthiness, currency denomination and the movement of the market in which the security is normally traded. The value determined under these procedures may differ from published values for the same securities.

Disclosure about the classification of fair value measurements is included in a table following the Fund's Investment Portfolio.

**Foreign Currency Translations.** The books and records of the Trust are maintained in US dollars. Investment securities and other assets and liabilities denominated in a foreign currency are translated into US dollars at the prevailing exchange rates at period end. Purchases and sales of investment securities, income and expenses are translated into US dollars at the prevailing exchange rates on the respective dates of the transactions.

Net realized and unrealized gains and losses on foreign currency transactions represent net gains and losses between trade and settlement dates on securities transactions, the disposition of forward foreign currency exchange contracts and foreign currencies, and the difference between the amount of net investment income accrued and the US dollar amount actually received. That portion of both realized and unrealized gains and losses on investments that results from fluctuations in foreign currency exchange rates is not separately disclosed but is included with net realized and unrealized gain/appreciation and loss/depreciation on investments.

**Securities Lending.** The Fund lends securities to certain financial institutions. The Fund retains beneficial ownership of the securities it has loaned and continues to receive interest and dividends paid by the issuer of securities and to participate in any changes in their market value. The Fund requires the borrowers of the securities to maintain collateral with the Fund consisting of either cash or liquid, unencumbered assets having a value at least equal to the value of the securities loaned. When the collateral falls below specified amounts, the lending agent will use its best effort to obtain additional collateral on the next business day to meet required amounts under the security lending agreement. The Fund may invest the cash collateral into a joint trading account in an affiliated money market fund pursuant to Exemptive Orders issued by the SEC. The Fund receives compensation for lending its securities either in the form of fees or by earning interest on invested cash collateral net of borrower rebates and fees paid to a lending agent. Either the Fund or the borrower may terminate the loan. There may be risks of delay and costs in recovery of securities or even loss of rights in the collateral should the borrower of the securities fail financially. The Fund is also subject to all investment risks associated with the reinvestment of any cash collateral received, including, but not limited to, interest rate, credit and liquidity risk associated with such investments.

**Taxes.** The Fund's policy is to comply with the requirements of the Internal Revenue Code, as amended, which are applicable to regulated investment companies and to distribute all of its taxable income to its shareholders.

At December 31, 2010, the Fund had an approximate net tax basis capital loss carryforward which may be applied against any realized net taxable capital gains of each succeeding year until fully utilized or until the following expiration dates, whichever occurs first:

| Fund | Capital Loss Carryforward ($) | Expiration Date | Capital Loss Carryforward Utilized ($) |
|---|---|---|---|
| DWS Dreman Small Mid Cap Value VIP | 10,090,000 | 12/31/2016 | 30,517,000 |
| | 93,411,000 | 12/31/2017 | |

The Fund has reviewed the tax positions for the open tax years as of December 31, 2010 and has determined that no provision for income tax is required in the Fund's financial statements. The Fund's federal tax returns for the prior three fiscal years remain open subject to examination by the Internal Revenue Service.

**Distribution of Income and Gains.** Distributions of net investment income of the Fund, if any, are made annually. Net realized gains from investment transactions, in excess of available capital loss carryforwards, would be taxable to the Fund if not distributed and, therefore, will be distributed to shareholders at least annually. The Fund may also make additional distributions for tax purposes if necessary.

The timing and characterization of certain income and capital gains distributions are determined annually in accordance with federal tax regulations which may differ from accounting principles generally accepted in the United States of America. These differences primarily relate to income received from Real Estate Investment Trusts and certain securities sold at a loss. As a result, net investment income (loss) and net realized gain (loss) on investment transactions for a reporting period may differ significantly from distributions during such period. Accordingly, the Fund may periodically make reclassifications among certain of its capital accounts without impacting the net asset value of the Fund.

At December 31, 2010, the Fund's components of distributable earnings on a tax basis were as follows:

| Fund | Undistributed Ordinary Income ($)* | Capital Loss Carryforwards ($) | Unrealized Appreciation (Depreciation) on Investments ($) |
|---|---|---|---|
| DWS Dreman Small Mid Cap Value VIP | 2,636,612 | (103,501,000) | 59,732,698 |

In addition, the tax character of distributions paid by the Fund is summarized as follows:

| | Distributions from Ordinary Income ($)* | |
|---|---|---|
| | Years Ended December 31, | |
| Fund | 2010 | 2009 |
| DWS Dreman Small Mid Cap Value VIP | 3,285,561 | 4,442,178 |

* *For tax purposes, short-term capital gain distributions are considered ordinary income distributions.*

**Expenses.** Expenses of the Trust arising in connection with a specific fund are allocated to that fund. Other Trust expenses which cannot be directly attributed to a fund are apportioned among the funds in the Trust.

**Contingencies.** In the normal course of business, the Fund may enter into contracts with service providers that contain general indemnification clauses. The Fund's maximum exposure under these arrangements is unknown as this would involve future claims that may be made against the Fund that have not yet been made. However, based on experience, the Fund expects the risk of loss to be remote.

**Real Estate Investment Trusts.** The Fund periodically recharacterize distributions received from a Real Estate Investment Trust ("REIT") investment based on information provided by the REIT into the following categories: ordinary income, long-term and short-term capital gains, and return of capital. If information is not available timely from a REIT, the recharacterization will be estimated for financial reporting purposes and a recharacterization will be made to the accounting records in the following year when such information becomes available. Distributions received from REITs in excess of income are recorded as either a reduction of cost of investments or realized gains. The Fund distinguishes between dividends on a tax basis and a financial reporting basis and only distributions in excess of tax basis earnings and profits are reported in the financial statements as a return of capital.

**Other.** Investment transactions are accounted for on a trade date plus one basis for daily net asset value calculations. However, for financial reporting purposes, investment transactions are reported on trade date. Interest income is recorded on the accrual basis. Dividend income is recorded on the ex-dividend date net of foreign withholding taxes. Realized gains and losses from investment transactions are recorded on an identified cost basis.

## B. Purchases and Sales of Securities

During the year ended December 31, 2010, purchases and sales of investment transactions (excluding short-term investments) were as follows:

| Fund | Purchases ($) | Sales ($) |
|---|---|---|
| DWS Dreman Small Mid Cap Value VIP | 93,395,395 | 129,147,757 |

## C. Related Parties

**Management Agreement.** Under the Investment Management Agreement with Deutsche Investment Management Americas Inc. ("DIMA" or the "Advisor"), an indirect, wholly owned subsidiary of Deutsche Bank AG, the Advisor directs the investments of the Fund in accordance with its investment objectives, policies and restrictions. The Advisor determines the securities, instruments and other contracts relating to investments to be purchased, sold or entered into by the Fund or delegates such responsibility to the Fund's subadvisor.

Dreman Value Management, L.L.C. ("DVM") serves as subadvisor to the Fund and is paid by the Advisor for its services.

Under the Investment Management Agreement with the Advisor, the fee is equivalent to the annual rates shown below of the Fund's average daily net assets, computed and accrued daily and payable monthly:

| Fund | Annual Management Fee Rate |
|---|---|
| DWS Dreman Small Mid Cap Value VIP | |
| $0–$250 million | .650% |
| next $750 million | .620% |
| next $1.5 billion | .600% |
| next $2.5 billion | .580% |
| next $2.5 billion | .550% |
| next $2.5 billion | .540% |
| next $2.5 billion | .530% |
| over $12.5 billion | .520% |

Accordingly, for the year ended December 31, 2010, the total management fee and effective management fee rate were as follows:

| Fund | Total Aggregated ($) | Annual Effective Rate |
|---|---|---|
| DWS Dreman Small Mid Cap Value VIP | 1,653,319 | .65% |

**Administration Fee.** Pursuant to an Administrative Services Agreement, DIMA provides most administrative services to the Fund. For all services provided under the Administrative Services Agreement, the Fund pays DIMA an annual fee ("Administration Fee") of 0.10% of the Fund's average daily net assets, computed and accrued daily and payable monthly. For the year ended December 31, 2010, the Administration Fee was as follows:

| Fund | Total Aggregated ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS Dreman Small Mid Cap Value VIP | 254,770 | 23,011 |

**Service Provider Fees.** DWS Investments Service Company ("DISC"), an affiliate of the Advisor, is the transfer agent, dividend-paying agent and shareholder service agent for the Fund. Pursuant to a sub-transfer agency agreement between DISC and DST Systems, Inc. ("DST"), DISC has delegated certain transfer agent, dividend-paying agent and shareholder service agent functions to DST. DISC compensates DST out of the shareholder servicing fee it receives from the Fund. For the year ended December 31, 2010, the amounts charged to the Fund by DISC were as follows:

| Fund | Total Aggregated ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS Dreman Small Mid Cap Value VIP Class A | 678 | 168 |
| DWS Dreman Small Mid Cap Value VIP Class B | 390 | 102 |

**Distribution Service Agreement**. Under the Fund's Class B 12b-1 plans, DWS Investments Distributors, Inc. ("DIDI") received a fee ("Distribution Service Fee") of 0.25% of average daily net assets of Class B shares. For the year ended December 31, 2010, the Distribution Service Fee was as follows:

| Fund | Total Aggregated ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS Dreman Small Mid Cap Value VIP | 59,943 | 5,482 |

**Typesetting and Filing Service Fees.** Under an agreement with DIMA, DIMA is compensated for providing typesetting and certain regulatory filing services to the Fund. For the year ended December 31, 2010, the amount charged to the Fund by DIMA included in the Statement of Operations under "reports to shareholders" was as follows:

| Fund | Amount ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS Dreman Small Mid Cap Value VIP | 12,427 | 3,129 |

**Trustees' Fees and Expenses.** The Fund paid each Trustee not affiliated with the Advisor retainer fees plus specified amounts for various committee services and for the Board Chairperson.

**Affiliated Cash Management Vehicles.** The Fund may invest uninvested cash balances in Central Cash Management Fund, which is managed by the Advisor. The Fund indirectly bears their proportionate share of the expenses of the underlying money market funds. Central Cash Management Fund does not pay the Advisor an investment management fee. Central Cash Management Fund seeks a high level of current income consistent with liquidity and the preservation of capital.

## D. Ownership of the Fund

At December 31, 2010, the beneficial ownership in the Fund was as follows:

**DWS Dreman Small Mid Cap Value VIP:** Three Participating Insurance Companies were owners of record of 10% or more of the total outstanding Class A shares of the Fund, each owning 39%, 26% and 15%. Three Participating Insurance Companies were owners of record of 10% or more of the total outstanding Class B shares of the Fund, each owning 41%, 19% and 11%.

## E. Line of Credit

The Trust and other affiliated fund (the "Participants") share in a $450 million revolving credit facility provided by a syndication of banks. The Fund may borrow for temporary or emergency purposes, including the meeting of redemption requests that otherwise might require the untimely disposition of securities. The Participants are charged an annual commitment fee which is allocated based on net assets, among each of the Participants. Interest is calculated at a rate per annum equal to the sum of the Federal Funds Rate plus 1.25 percent plus if LIBOR exceeds the Federal Funds Rate the amount of such excess. The Fund may borrow up to a maximum of 33 percent of its net assets under the agreement.

# Report of Independent Registered Public Accounting Firm

**To the Board of Trustees and Shareholders of DWS Variable Series II:**

We have audited the accompanying statement of assets and liabilities of DWS Dreman Small Mid Cap Value VIP, one of the funds constituting the DWS Variable Series II (the "Trust"), including the investment portfolio, as of December 31, 2010, and the related statement of operations, the statement of changes in net assets and the financial highlights for each of the periods indicated therein. These financial statements and financial highlights are the responsibility of the Trust's management. Our responsibility is to express an opinion on these financial statements and financial highlights based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements and financial highlights are free of material misstatement. We were not engaged to perform an audit of the Trust's internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Trust's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements and financial highlights, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our procedures included confirmation of securities owned as of December 31, 2010, by correspondence with the custodian and brokers or by other appropriate auditing procedures where replies from brokers were not received. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements and financial highlights referred to above present fairly, in all material respects, the financial position of the aforementioned fund of the DWS Variable Series II at December 31, 2010, the results of its operations, the changes in its net assets and the financial highlights for each of the periods indicated therein, in conformity with U.S. generally accepted accounting principles.

Ernst & Young LLP

Boston, Massachusetts
February 14, 2011

# Tax Information

**(Unaudited)**

For corporate shareholders, the following percentage of income dividends paid during the Fund's fiscal year ended December 31, 2010 qualified for the dividends received deduction:

| Fund | Dividends Received % |
|---|---|
| DWS Dreman Small Mid Cap Value VIP | 100 |

Please consult a tax advisor if you have questions about federal or state income tax laws, or on how to prepare your tax returns. If you have specific questions about your account, please contact your insurance provider.

# Proxy Voting

The Trust's policies and procedures for voting proxies for portfolio securities and information about how the Trust voted proxies related to its portfolio securities during the 12-month period ended June 30 are available on our Web site — www.dws-investments.com (click on "proxy voting" at the bottom of the page) — or on the SEC's Web site — www.sec.gov. To obtain a written copy of the Trust's policies and procedures without charge, upon request, call us toll free at (800) 728-3337.

# Investment Management Agreement Approval

## DWS Dreman Small Mid Cap Value VIP

The Board of Trustees, including the Independent Trustees, approved the renewal of your Fund's investment management agreement (the "Agreement") with Deutsche Investment Management Americas Inc. ("DWS") and sub-advisory agreement (the "Sub-Advisory Agreement" and together with the Agreement, the "Agreements") between DWS and Dreman Value Management L.L.C. ("DVM") in September 2010.

In terms of the process that the Board followed prior to approving the Agreements, shareholders should know that:

- In September 2010, all but one of the Fund's Trustees were independent of DWS and its affiliates.
- The Trustees meet frequently to discuss fund matters. Each year, the Trustees dedicate substantial time to contract review matters. Over the course of several months, the Board's Contract Committee, in coordination with the Board's Equity Oversight Committee, reviewed comprehensive materials received from DWS, independent third parties and independent counsel. These materials included an analysis of the Fund's performance, fees and expenses, and profitability compiled by the Fund's independent fee consultant. The Board also received extensive information throughout the year regarding performance of the Fund.
- The Independent Trustees regularly meet privately with their independent counsel to discuss contract review and other matters. In addition, the Independent Trustees were also advised by the Fund's independent fee consultant in the course of their review of the Fund's contractual arrangements and considered a comprehensive report prepared by the independent fee consultant in connection with their deliberations (the "IFC Report").
- In connection with reviewing the Agreements, the Board also reviewed the terms of the Fund's Rule 12b-1 plan, distribution agreement, administrative services agreement, transfer agency agreement and other material service agreements.
- Based on its evaluation of the information provided, the Contract Committee presented its findings and recommendations to the Independent Trustees as a group. The Independent Trustees reviewed the Contract Committee's findings and recommendations and presented their recommendations to the full Board.

In connection with the contract review process, the Contract Committee and the Board considered the factors discussed below, among others. The Board also considered that DWS and its predecessors have managed the Fund since its inception, and the Board believes that a long-term relationship with a capable, conscientious advisor is in the best interests of the Fund. The Board considered, generally, that shareholders chose to invest or remain invested in the Fund knowing that DWS managed the Fund, and that the Agreement was approved by the Fund's shareholders. DWS is part of Deutsche Bank, a major global banking institution that is engaged in a wide range of financial services. The Board believes that there are significant advantages to being part of a global asset management business that offers a wide range of investing expertise and resources, including hundreds of portfolio managers and analysts with research capabilities in many countries throughout the world.

While shareholders may focus primarily on fund performance and fees, the Fund's Board considers these and many other factors, including the quality and integrity of DWS's and DVM's personnel and such other issues as back-office operations, fund valuations, and compliance policies and procedures.

**Nature, Quality and Extent of Services.** The Board considered the terms of the Agreements, including the scope of advisory services provided under the Agreements. The Board noted that, under the Agreements, DWS and DVM provide portfolio management services to the Fund and that, pursuant to a separate administrative services agreement, DWS provides administrative services to the Fund. The Board considered the experience and skills of senior management and investment personnel, the resources made available to such personnel, the ability of DWS to attract and retain high-quality personnel, and the organizational depth and stability of DWS. The Board reviewed the Fund's performance over short-term and long-term periods and compared those returns to various agreed-upon performance measures, including market indices and a peer universe compiled by the independent fee consultant using information supplied by Lipper Inc. ("Lipper"). The Board also noted that it has put into place a process of identifying "Focus Funds" (e.g., funds performing poorly relative to their benchmark or a peer universe compiled by Lipper), and receives more frequent reporting and information from DWS regarding such funds, along with DWS's remedial plans to address underperformance. The Board believes this process is an effective manner of identifying and addressing underperforming funds. Based on the information provided, the Board noted that for the one-, three- and five-year periods ended December 31, 2009, the Fund's performance (Class A shares) was in the 2nd quartile, 1st quartile and 1st quartile, respectively, of the applicable Lipper universe (the 1st quartile being the best performers and the 4th quartile being the worst performers). The Board also observed that the Fund has outperformed its benchmark in the one-, three- and five-year periods ended December 31, 2009.

On the basis of this evaluation and the ongoing review of investment results by the Board, the Board concluded that the nature, quality and extent of services provided by DWS and DVM historically have been and continue to be satisfactory.

**Fees and Expenses.** The Board considered the Fund's investment management fee schedule, sub-advisory fee schedule, operating expenses, and total expense ratios, and comparative information provided by Lipper and the independent fee consultant regarding investment management fee rates paid to other investment advisors by similar funds (1st quartile being the most favorable and 4th quartile being the least favorable). With respect to management fees paid to other investment advisors by similar funds, the Board noted that the contractual fee rates paid by the Fund, which include the 0.10% fee paid to DWS under the Fund's administrative services agreement, were lower than the median (1st quartile) of the applicable Lipper peer group (based on Lipper data provided as of December 31, 2009). With respect to the sub-advisory fee paid to DVM, the Board noted that the fee is paid by DWS out of its fee and not directly by the Fund. The Board noted that the Fund's Class A shares total (net) operating expenses were expected to be lower than the median (1st quartile) of the applicable Lipper expense universe (based on Lipper data provided as of December 31, 2009, and analyzing Lipper expense universe Class A expenses less any applicable 12b-1 fees) ("Lipper Universe Expenses"). The Board also reviewed data comparing each share class's total (net) operating expenses to the applicable Lipper Universe Expenses. The Board considered the Fund's management fee rate as compared to fees charged by DWS and certain of its affiliates for comparable mutual funds and considered differences in fund and fee structures between the DWS Funds. The Board also considered how the Fund's total (net) operating expenses compared to the total (net) operating expenses of a more customized peer group selected by Lipper (based on such factors as asset size).

The information considered by the Board as part of its review of management fees included information regarding fees charged by DWS and its affiliates to similar institutional accounts and to similar funds offered primarily to European investors ("DWS Europe funds"), in each case as applicable. The Board observed that advisory fee rates for institutional accounts generally were lower than the management fees charged by similarly managed DWS US mutual funds ("DWS Funds"), but also took note of the differences in services provided to DWS Funds as compared to institutional accounts. In the case of DWS Europe funds, the Board observed that fee rates for DWS Europe funds generally were higher than for similarly managed DWS Funds, but noted that differences in the types of services provided to DWS Funds relative to DWS Europe funds made it difficult to compare such fees.

On the basis of the information provided, the Board concluded that management fees were reasonable and appropriate in light of the nature, quality and extent of services provided by DWS and DVM.

**Profitability.** The Board reviewed detailed information regarding revenues received by DWS under the Agreement. The Board considered the estimated costs and pre-tax profits realized by DWS from advising the DWS Funds, as well as estimates of the pre-tax profits attributable to managing the Fund in particular. The Board also received information regarding the estimated enterprise-wide profitability of DWS and its affiliates with respect to all fund services in totality and by fund. The Board reviewed DWS's methodology in allocating its costs to the management of the Fund. Based on the information provided, the Board concluded that the pre-tax profits realized by DWS in connection with the management of the Fund were not unreasonable. The Board also reviewed information regarding the profitability of certain similar investment management firms. The Board noted that while information regarding the profitability of such firms is limited (and in some cases is not necessarily prepared on a comparable basis), DWS and its affiliates' overall profitability with respect to the DWS fund complex (after taking into account distribution and other services provided to the funds by DWS and its affiliates) was lower than the overall profitability levels of many comparable firms for which such data was available. The Board did not consider the profitability of DVM with respect to the Fund. The Board noted that DWS pays DVM's fee out of its management fee, and its understanding that the Fund's sub-advisory fee schedule was the product of an arm's length negotiation with DWS.

**Economies of Scale.** The Board considered whether there are economies of scale with respect to the management of the Fund and whether the Fund benefits from any economies of scale. The Board noted that the Fund's management fee schedule includes fee breakpoints. The Board concluded that the Fund's fee schedule represents an appropriate sharing between the Fund and DWS of such economies of scale as may exist in the management of the Fund at current asset levels.

**Other Benefits to DWS and DVM and Their Affiliates.** The Board also considered the character and amount of other incidental benefits received by DWS and DVM and their affiliates, including any fees received by DWS for administrative services provided to the Fund and any fees received by an affiliate of DWS for distribution services. The Board also considered the incidental public relations benefits to DWS and DVM related to DWS Funds

advertising and cross-selling opportunities among DWS products and services. The Board concluded that management fees were reasonable in light of these fallout benefits.

**Compliance.** The Board considered the significant attention and resources dedicated by DWS to documenting and enhancing its compliance processes in recent years. The Board noted in particular (i) the experience and seniority of both DWS's chief compliance officer and the Fund's chief compliance officer; (ii) the large number of DWS compliance personnel; and (iii) the substantial commitment of resources by DWS and its affiliates to compliance matters. The Board also considered the attention and resources dedicated by DWS to the oversight of the investment sub-advisor's compliance program and compliance with the applicable fund policies and procedures.

Based on all of the information considered and the conclusions reached, the Board unanimously (including the Independent Trustees) determined that the continuation of the Agreements is in the best interests of the Fund. In making this determination, the Board did not give particular weight to any single factor identified above. The Board considered these factors over the course of numerous meetings, certain of which were in executive session with only the Independent Trustees and their counsel present. It is possible that individual Trustees may have weighed these factors differently in reaching their individual decisions to approve the continuation of the Agreements.

# Summary of Management Fee Evaluation by Independent Fee Consultant

October 3, 2010

Pursuant to an Order entered into by Deutsche Investment Management Americas and affiliates (collectively, "DeAM") with the Attorney General of New York, I, Thomas H. Mack, have been appointed the Independent Fee Consultant for the DWS Funds (formerly the DWS Scudder Funds). My duties include preparing an annual written evaluation of the management fees DeAM charges the Funds, considering among other factors the management fees charged by other mutual fund companies for like services, management fees DeAM charges other clients for like services, DeAM's costs of supplying services under the management agreements and related profit margins, possible economies of scale if a Fund grows larger, and the nature and quality of DeAM's services, including fund performance. This report summarizes my evaluation for 2010, including my qualifications, the evaluation process for each of the DWS Funds, consideration of certain complex-level factors, and my conclusions. I served in substantially the same capacity in 2007, 2008, and 2009.

## Qualifications

For more than 35 years I have served in various professional capacities within the investment management business. I have held investment analysis and advisory positions, including securities analyst, portfolio strategist and director of investment policy with a large investment firm. I have also performed business management functions, including business development, financial management and marketing research and analysis.

Since 1991, I have been an independent consultant within the asset management industry. I have provided services to over 125 client organizations, including investment managers, mutual fund boards, product distributors and related organizations. Over the past ten years I have completed a number of assignments for mutual fund boards, specifically including assisting boards with management contract renewal.

I hold a Master of Business Administration degree, with highest honors, from Harvard University and Master of Science and Bachelor of Science (highest honors) degrees from the University of California at Berkeley. I am an independent director and audit committee financial expert for two closed-end mutual funds and have served in various leadership and financial oversight capacities with non-profit organizations.

## Evaluation of Fees for each DWS Fund

My work focused primarily on evaluating, fund-by-fund, the fees charged to each of the 118 publicly offered Fund portfolios in the DWS Fund family. For each Fund, I considered each of the key factors mentioned above, as well as any other relevant information. In doing so I worked closely with the Funds' Independent Directors in their annual contract renewal process, as well as in their approval of contracts for several new funds (documented separately).

In evaluating each Fund's fees, I reviewed comprehensive materials provided by or on behalf of DeAM, including expense information prepared by Lipper Analytical, comparative performance information, profitability data, manager histories, and other materials. I also accessed certain additional information from the Lipper and Morningstar databases and drew on my industry knowledge and experience.

To facilitate evaluating this considerable body of information, I prepared for each Fund a document summarizing the key data elements in each area as well as additional analytics discussed below. This made it possible to consider each key data element in the context of the others.

In the course of contract renewal, DeAM agreed to implement a number of fee and expense adjustments requested by the Independent Directors which will favorably impact future fees and expenses, and my evaluation includes the effects of these changes.

### Fees and Expenses Compared with Other Funds

The competitive fee and expense evaluation for each fund focused on two primary comparisons:

- The Fund's contractual management fee (the advisory fee plus the administration fee where applicable) compared with those of a group of typically 12–15 funds in the same Lipper investment category (e.g. Large Capitalization Growth) having similar distribution arrangements and being of similar size.
- The Fund's total expenses compared with a broader universe of funds from the same Lipper investment category and having similar distribution arrangements.

These two comparisons provide a view of not only the level of the fee compared with funds of similar scale but also the total expense the Fund bears for all the services it receives, in comparison with the investment choices available in the Fund's investment category and distribution channel. The principal figure-of-merit used in these comparisons was the subject Fund's percentile ranking against peers.

### DeAM's Fees for Similar Services to Others

DeAM provided management fee schedules for all of its US domiciled fund and non-fund investment management accounts in any of the investment categories where there is a DWS Fund. These similar products included the other DWS Funds, non-fund pooled accounts, institutional accounts and sub-advisory accounts. Using this information, I calculated for each Fund the fee that would be charged to each similar product, at the subject Fund's asset level.

Evaluating information regarding non-fund products is difficult because there are varying levels of services required for different types of accounts, with mutual funds generally requiring considerably more regulatory and administrative types of service as well as having more frequent cash flows than other types of accounts. Also, while mutual fund fees for similar fund products can be expected to be similar, there will be some differences due to different pricing conditions in different distribution channels (e.g. retail funds versus those used in variable insurance products), differences in underlying investment processes and other factors.

**Costs and Profit Margins**

DeAM provided a detailed profitability analysis for each Fund. After making some adjustments so that the presentation would be more comparable to the available industry figures, I reviewed profit margins from investment management alone, from investment management plus other fund services (excluding distribution) provided to the Funds by DeAM (principally shareholder services), and DeAM profits from all sources, including distribution. A later section comments on overall profitability.

**Economies of Scale**

Economies of scale — an expected decline in management cost per dollar of fund assets as fund assets grow — are very rarely quantified and documented because of inherent difficulties in collecting and analyzing relevant data. However, in virtually every investment category that I reviewed, larger funds tend to have lower fees and lower total expenses than smaller funds. To see how each DWS Fund compares with this industry observation, I reviewed:

- The trend in Fund assets over the last five years and the accompanying trend in total expenses. This shows if the Fund has grown and, if so, whether total expense (management fees as well as other expenses) have declined as a percent of assets.
- Whether the Fund has break-points in its management fee schedule, the extent of the fee reduction built into the schedule and the asset levels where the breaks take effect, and in the case of a sub-advised Fund how the Fund's break-points compare with those of the sub-advisory fee schedule.
- How the Fund's contractual fee schedule compares with trends in the industry data. To accomplish this, I constructed a chart showing how actual latest-fiscal-year contractual fees of the Fund and of other similar funds relate to average fund assets, with the subject Fund's contractual fee schedule superimposed.

**Quality of Service — Performance**

The quality-of-service evaluation focused on investment performance, which is the principal result of the investment management service. Each Fund's performance was reviewed over the past 1, 3, 5 and 10 years, as applicable, and compared with that of other funds in the same investment category and with a suitable market index.

In addition, I calculated and reviewed risk-adjusted returns relative to an index of similar mutual funds' returns and a suitable market index. The risk-adjusted returns analysis provides a way of determining the extent to which the Fund's return comparisons are mainly the product of investment value-added (or lack thereof) or alternatively taking considerably more or less risk than is typical in its investment category.

I also received and considered the history of portfolio manager changes for each Fund, as this provided an important context for evaluating the performance results.

## Complex-Level Considerations

While this evaluation was conducted mainly at the individual fund level, there are some issues relating to the reasonableness of fees that can alternatively be considered across the whole fund complex:

- I reviewed DeAM's profitability analysis for all DWS Funds, with a view toward determining if the allocation procedures used were reasonable and how profit levels compared with public data for other investment managers.
- I considered whether DeAM and affiliates receive any significant ancillary or "fall-out" benefits that should be considered in interpreting the direct profitability results. These would be situations where serving as the investment manager of the Funds is beneficial to another part of the Deutsche Bank organization.
- I considered how aggregated DWS Fund expenses had varied over the years, by asset class and in the context of trends in asset levels.
- I reviewed the structure of the DeAM organization, trends in staffing levels, and information on compensation of investment management and other professionals compared with industry data.

## Findings

Based on the process and analysis discussed above, which included reviewing a wide range of information from management and external data sources and considering among other factors the fees DeAM charges other clients, the fees charged by other fund managers, DeAM's costs and profits associated with managing the Funds, economies of scale, possible fall-out benefits, and the nature and quality of services provided, in my opinion the management fees charged the DWS Funds are reasonable.

Thomas H. Mack

Thomas H. Mack

# Board Members and Officers

The following table presents certain information regarding the Board Members and Officers of the Trust as of December 31, 2010. Each Board Member's year of birth is set forth in parentheses after his or her name. Unless otherwise noted, (i) each Board Member has engaged in the principal occupation(s) noted in the table for at least the most recent five years, although not necessarily in the same capacity; and (ii) the address of each Independent Board Member is c/o Paul K. Freeman, Independent Chairman, DWS Funds, PO Box 101833, Denver, CO 80250-1833. Except as otherwise noted below, the term of office for each Board Member is until the election and qualification of a successor, or until such Board Member sooner dies, resigns, is removed or as otherwise provided in the governing documents of the fund. Because the fund does not hold an annual meeting of shareholders, each Board Member will hold office for an indeterminate period. The Board Members may also serve in similar capacities with other funds in the fund complex. The Length of Time Served represents the year in which the Board Member joined the board of one or more DWS funds now overseen by the Board.

### Independent Board Members

| Name, Year of Birth, Position with the Fund and Length of Time Served[1] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Paul K. Freeman (1950)<br>Chairperson since 2009<br>Board Member since 1993 | Consultant, World Bank/Inter-American Development Bank; Executive and Governing Council of the Independent Directors Council (education committees); formerly, Project Leader, International Institute for Applied Systems Analysis (1998–2001); Chief Executive Officer, The Eric Group, Inc. (environmental insurance) (1986–1998) | 122 |
| John W. Ballantine (1946)<br>Board Member since 1999 | Retired; formerly, Executive Vice President and Chief Risk Management Officer, First Chicago NBD Corporation/The First National Bank of Chicago (1996–1998); Executive Vice President and Head of International Banking (1995–1996). Directorships: Healthways, Inc. (provider of disease and care management services); Portland General Electric (utility company); Stockwell Capital Investments PLC (private equity). Former Directorships: First Oak Brook Bancshares, Inc. and Oak Brook Bank; Prisma Energy International | 122 |
| Henry P. Becton, Jr. (1943)<br>Board Member since 1990 | Vice Chair and former President, WGBH Educational Foundation. Directorships: Association of Public Television Stations; Lead Director, Becton Dickinson and Company[3] (medical technology company); Lead Director, Belo Corporation[3] (media company); Public Radio International; Public Radio Exchange (PRX); The PBS Foundation. Former Directorships: Boston Museum of Science; American Public Television; Concord Academy; New England Aquarium; Mass. Corporation for Educational Telecommunications; Committee for Economic Development; Public Broadcasting Service | 122 |
| Dawn-Marie Driscoll (1946)<br>Board Member since 1987 | President, Driscoll Associates (consulting firm); Executive Fellow, Center for Business Ethics, Bentley University; formerly, Partner, Palmer & Dodge (1988–1990); Vice President of Corporate Affairs and General Counsel, Filene's (1978–1988). Directorships: Trustee of 22 open-end mutual funds managed by Sun Capital Advisers, Inc. (since 2007); Director of ICI Mutual Insurance Company (since 2007); Advisory Board, Center for Business Ethics, Bentley University; Trustee, Southwest Florida Community Foundation (charitable organization). Former Directorships: Investment Company Institute (audit, executive, nominating committees) and Independent Directors Council (governance, executive committees) | 122 |
| Keith R. Fox (1954)<br>Board Member since 1996 | Managing General Partner, Exeter Capital Partners (a series of private investment funds). Directorships: Progressive International Corporation (kitchen goods importer and distributor); BoxTop Media Inc. (advertising); The Kennel Shop (retailer); former Chairman, National Association of Small Business Investment Companies | 122 |
| Kenneth C. Froewiss (1945)<br>Board Member since 2001 | Adjunct Professor of Finance, NYU Stern School of Business (September 2009–present; Clinical Professor from 1997–September 2009); Member, Finance Committee, Association for Asian Studies (2002–present); Director, Mitsui Sumitomo Insurance Group (US) (2004–present); prior thereto, Managing Director, J.P. Morgan (investment banking firm) (until 1996) | 122 |
| Richard J. Herring (1946)<br>Board Member since 1990 | Jacob Safra Professor of International Banking and Professor, Finance Department, The Wharton School, University of Pennsylvania (since July 1972); Co-Director, Wharton Financial Institutions Center (since July 2000); Co-Chair, U.S. Shadow Financial Regulatory Committee; Executive Director, Financial Economists Roundtable; Director, Japan Equity Fund, Inc. (since September 2007), Thai Capital Fund, Inc. (since September 2007), Singapore Fund, Inc. (since September 2007); Independent Director of Barclays Bank Delaware (since September 2010). Formerly, Vice Dean and Director, Wharton Undergraduate Division (July 1995–June 2000); Director, Lauder Institute of International Management Studies (July 2000–June 2006) | 122 |
| William McClayton (1944)<br>Board Member since 2004+ | Private equity investor (since October 2009); previously, Managing Director, Diamond Management & Technology Consultants, Inc. (global consulting firm) (2001–2009); Directorship: Board of Managers, YMCA of Metropolitan Chicago; formerly: Senior Partner, Arthur Andersen LLP (accounting) (1966–2001); Trustee, Ravinia Festival | 122 |

| Name, Year of Birth, Position with the Fund and Length of Time Served[1] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Rebecca W. Rimel (1951)<br>Board Member since 1995 | President and Chief Executive Officer, The Pew Charitable Trusts (charitable organization) (1994 to present); Trustee, Thomas Jefferson Foundation (charitable organization) (1994 to present); Trustee, Executive Committee, Philadelphia Chamber of Commerce (2001–2007); Director, CardioNet, Inc.[2] (2009–present) (health care). Formerly, Executive Vice President, The Glenmede Trust Company (investment trust and wealth management) (1983–2004); Board Member, Investor Education (charitable organization) (2004–2005); Director, Viasys Health Care[2] (January 2007–June 2007); Trustee, Pro Publica (charitable organization) (2007–2010) | 122 |
| William N. Searcy, Jr. (1946)<br>Board Member since 1993 | Private investor since October 2003; Trustee of 22 open-end mutual funds managed by Sun Capital Advisers, Inc. (since October 1998). Formerly, Pension & Savings Trust Officer, Sprint Corporation[2] (telecommunications) (November 1989–September 2003) | 122 |
| Jean Gleason Stromberg (1943)<br>Board Member since 1997 | Retired. Formerly, Consultant (1997–2001); Director, Financial Markets US Government Accountability Office (1996–1997); Partner, Fulbright & Jaworski, L.L.P. (law firm) (1978–1996). Directorships: The William and Flora Hewlett Foundation. Former Directorships: Service Source, Inc., Mutual Fund Directors Forum (2002–2004), American Bar Retirement Association (funding vehicle for retirement plans) (1987–1990 and 1994–1996) | 122 |
| Robert H. Wadsworth (1940)<br>Board Member since 1999 | President, Robert H. Wadsworth & Associates, Inc. (consulting firm) (1983 to present); Director, The Phoenix Boys Choir Association | 125 |

## Interested Board Member and Officer[4]

| Name, Year of Birth, Position with the Trust/ Corporation and Length of Time Served[1,5] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Ingo Gefeke[7] (1967)<br>Board Member since 2010<br>Executive Vice President since 2010 | Managing Director[3], Deutsche Asset Management; Global Head of Distribution and Product Management, DWS Global Head of Trading and Securities Lending. Member of the Board of Directors of DWS Investment GmbH Frankfurt (since July 2009) and DWS Holding & Service GmbH Frankfurt (since January 2010); formerly, Global Chief Administrative Officer, Deutsche Asset Management (2004–2009); Global Chief Operating Officer, Global Transaction Banking, Deutsche Bank AG, New York (2001–2004); Chief Operating Officer, Global Banking Division Americas, Deutsche Bank AG, New York (1999–2001); Central Management, Global Banking Services, Deutsche Bank AG, Frankfurt (1998–1999); Relationship Management, Deutsche Bank AG, Tokyo, Japan (1997–1998) | 55 |

## Officers[4]

| Name, Year of Birth, Position with the Fund and Length of Time Served[5] | Principal Occupation(s) During Past 5 Years and Other Directorships Held |
|---|---|
| Michael G. Clark[6] (1965)<br>President, 2006–present | Managing Director[3], Deutsche Asset Management (2006–present); President of DWS family of funds; Director, ICI Mutual Insurance Company (since October 2007); formerly, Director of Fund Board Relations (2004–2006) and Director of Product Development (2000–2004), Merrill Lynch Investment Managers; Senior Vice President Operations, Merrill Lynch Asset Management (1999–2000) |
| John Millette[8] (1962)<br>Vice President and Secretary, 1999–present | Director[3], Deutsche Asset Management |
| Paul H. Schubert[6] (1963)<br>Chief Financial Officer, 2004–present<br>Treasurer, 2005–present | Managing Director[3], Deutsche Asset Management (since July 2004); formerly, Executive Director, Head of Mutual Fund Services and Treasurer for UBS Family of Funds (1998–2004); Vice President and Director of Mutual Fund Finance at UBS Global Asset Management (1994–1998) |
| Caroline Pearson[8] (1962)<br>Chief Legal Officer, April 2010–present | Managing Director[3], Deutsche Asset Management; formerly, Assistant Secretary for DWS family of funds (1997–2010) |
| Rita Rubin[9] (1970)<br>Assistant Secretary, 2009–present | Vice President and Counsel, Deutsche Asset Management (since October 2007); formerly, Vice President, Morgan Stanley Investment Management (2004–2007) |
| Paul Antosca[8] (1957)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management (since 2006); Vice President, The Manufacturers Life Insurance Company (U.S.A.) (1990–2006) |
| Jack Clark[8] (1967)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management (since 2007); formerly, Vice President, State Street Corporation (2002–2007) |

| Name, Year of Birth, Position with the Fund and Length of Time Served[5] | Principal Occupation(s) During Past 5 Years and Other Directorships Held |
|---|---|
| Diane Kenneally[8] (1966)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management |
| John Caruso[9] (1965)<br>Anti-Money Laundering Compliance Officer, 2010–present | Managing Director[3], Deutsche Asset Management |
| Robert Kloby[9] (1962)<br>Chief Compliance Officer, 2006–present | Managing Director[3], Deutsche Asset Management |

1 *The length of time served represents the year in which the Board Member joined the board of one or more DWS funds currently overseen by the Board.*

2 *A publicly held company with securities registered pursuant to Section 12 of the Securities Exchange Act of 1934.*

3 *Executive title, not a board directorship.*

4 *As a result of their respective positions held with the Advisor, these individuals are considered "interested persons" of the Advisor within the meaning of the 1940 Act. Interested persons receive no compensation from the fund.*

5 *The length of time served represents the year in which the officer was first elected in such capacity for one or more DWS funds.*

6 *Address: 100 Plaza One, Jersey City, NJ 07311.*

7 *Effective January 11, 2011, Mr. Gefeke, an interested Board Member and Executive Vice President, resigned from the fund's Board and as an officer.*

*The mailing address of Mr. Gefeke is 345 Park Avenue, New York, New York 10154. Mr. Gefeke was an interested Board Member of certain DWS funds by virtue of his positions with Deutsche Asset Management. As an interested person, Mr. Gefeke received no compensation from the fund.*

8 *Address: One Beacon Street, Boston, MA 02108.*

9 *Address: 60 Wall Street, New York, New York 10005.*

*The fund's Statement of Additional Information ("SAI") includes additional information about the Board Members. The SAI is available, without charge, upon request. If you would like to request a copy of the SAI, you may do so by calling the following toll-free number: (800) 728-3337.*

# Notes

DWS Investments is part of Deutsche Bank's Asset Management division and, within the US, represents the retail asset management activities of Deutsche Bank AG, Deutsche Bank Trust Company Americas, Deutsche Investment Management Americas Inc. and DWS Trust Company.

The views expressed in this report reflect those of the portfolio managers only through the end of the period of the report as stated on the cover. The managers' views are subject to change at any time based on market and other conditions and should not be construed as a recommendation.

This information must be preceded or accompanied by a current prospectus.

Portfolio changes should not be considered recommendations for action by individual investors.

DWS Investments Distributors, Inc.
222 South Riverside Plaza
Chicago, IL 60606
(800) 621-1148

VS2DSMC-2 (2/11)

DWS INVESTMENTS
Deutsche Bank Group

DECEMBER 31, 2010

# ANNUAL REPORT

## DWS VARIABLE SERIES II

## DWS Global Thematic VIP

**This report must be preceded or accompanied by a prospectus. To obtain an additional prospectus or summary prospectus, if available, call (800) 728-3337 or your financial representative. We advise you to consider the Fund's objectives, risks, charges and expenses carefully before investing. The summary prospectus and prospectus contain this and other important information about the Fund. Please read the prospectus carefully before you invest.**

*Investments in variable insurance portfolios (VIPs) involve risk. Stocks may decline in value. Bond investments are subject to interest-rate and credit risks. When interest rates rise, bond prices generally fall. Credit risk refers to the ability of an issuer to make timely payments of principal and interest. Investing in derivatives entails special risks relating to liquidity, leverage and credit that may reduce returns and/or increased volatility. Investing in foreign securities, particularly those of emerging markets, presents certain risks, such as currency fluctuations, political and economic changes, and market risks. There are additional risks associated with investing in commodities, high-yield bonds, aggressive growth stocks, non-diversified/ concentrated funds and small- and mid-cap stocks which are more fully explained in the prospectuses. Please read the prospectus for more information.*

*DWS Investments is part of Deutsche Bank's Asset Management division and, within the US, represents the retail asset management activities of Deutsche Bank AG, Deutsche Bank Trust Company Americas, Deutsche Investment Management Americas Inc. and DWS Trust Company.*



DWS INVESTMENTS
Deutsche Bank Group

# Performance Summary

**December 31, 2010**

## DWS Global Thematic VIP

**All performance shown is historical, assumes reinvestment of all dividend and capital gain distributions and does not guarantee future results. Investment return and principal value fluctuate with changing market conditions so that, when redeemed, shares may be worth more or less than their original cost. Current performance may be lower or higher than the performance data quoted. Please contact your participating insurance company for the Fund's most recent month-end performance. Performance doesn't reflect charges and fees ("contract charges") associated with the separate account that invests in the Fund or any variable life insurance policy or variable annuity contract for which the Fund is an investment option. These charges and fees will reduce returns. While all share classes have the same underlying portfolio, their performance will differ.**

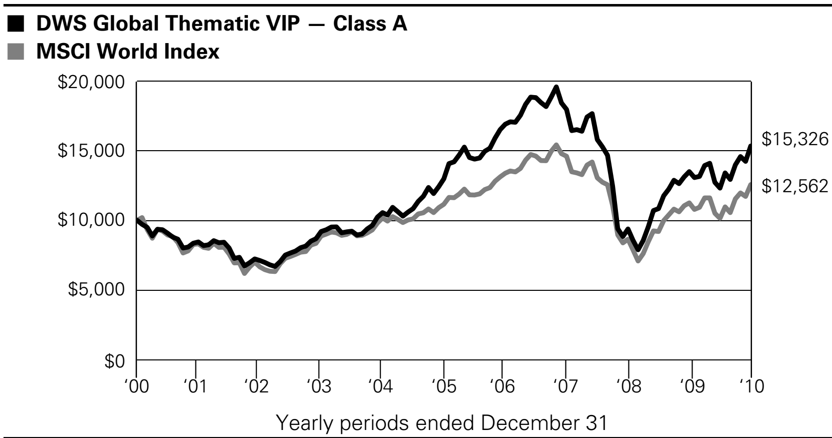
**The gross expense ratios of the Fund, as stated in the fee table of the prospectus dated May 1, 2010 are 1.39% and 1.74% for Class A and Class B shares, respectively, and may differ from the expense ratios disclosed in the Financial Highlights tables in this report.**

### Risk Considerations

Investing in derivatives entails special risks relating to liquidity, leverage and credit that may reduce returns and/or increase volatility. Investing in foreign securities, particularly those of emerging markets, presents certain risks, such as currency fluctuations, political and economic changes, and market risks. Any decline in value of a Fund security that is out on loan by the Fund will adversely affect performance. Financial failure of the borrower may mean a delay in recovery or loss of rights in the collateral. Stocks may decline in value. See the prospectus for details.

Fund returns shown for all periods reflect a fee waiver and/or expense reimbursement. Without this waiver/reimbursement, returns would have been lower.

### Growth of an Assumed $10,000 Investment in DWS Global Thematic VIP




*The Morgan Stanley Capital International (MSCI) World Index is an unmanaged, capitalization-weighted measure of global stock markets including the US, Canada, Europe, Australia and the Far East. The index is calculated using closing local market prices and translates into US dollars using the London close foreign exchange rates.*

*Index returns assume reinvestment of dividends and, unlike fund returns, do not reflect any fees or expenses. It is not possible to invest directly into an index.*

### Comparative Results

| DWS Global Thematic VIP | | 1-Year | 3-Year | 5-Year | 10-Year |
|---|---|---|---|---|---|
| **Class A** | Growth of $10,000 | $11,365 | $8,541 | $11,815 | $15,326 |
| | Average annual total return | 13.65% | –5.12% | 3.39% | 4.36% |
| MSCI World Index | Growth of $10,000 | $11,176 | $8,613 | $11,276 | $12,562 |
| | Average annual total return | 11.76% | –4.85% | 2.43% | 2.31% |

| DWS Global Thematic VIP | | 1-Year | 3-Year | 5-Year | Life of Class* |
|---|---|---|---|---|---|
| **Class B** | Growth of $10,000 | $11,324 | $8,455 | $11,603 | $18,809 |
| | Average annual total return | 13.24% | –5.44% | 3.02% | 7.71% |
| MSCI World Index | Growth of $10,000 | $11,176 | $8,613 | $11,276 | $16,563 |
| | Average annual total return | 11.76% | –4.85% | 2.43% | 6.12% |

*The growth of $10,000 is cumulative.*

* *The Fund commenced offering Class B shares on July 1, 2002. Index returns began on June 30, 2002.*

# Information About Your Fund's Expenses

## DWS Global Thematic VIP

As an investor of the Fund, you incur two types of costs: ongoing expenses and transaction costs. Ongoing expenses include management fees, distribution and service (12b-1) fees and other Fund expenses. Examples of transaction costs include contract charges, redemption fees and account maintenance fees, which are not shown in this section. The following tables are intended to help you understand your ongoing expenses (in dollars) of investing in the Fund and to help you compare these expenses with the ongoing expenses of investing in other mutual funds. In the most recent six-month period, the Fund limited these expenses; had it not done so, expenses would have been higher. The example in the table is based on an investment of $1,000 invested at the beginning of the six-month period and held for the entire period (July 1, 2010 to December 31, 2010).

The tables illustrate your Fund's expenses in two ways:

- **Actual Fund Return.** This helps you estimate the actual dollar amount of ongoing expenses (but not transaction costs) paid on a $1,000 investment in the Fund using the Fund's actual return during the period. To estimate the expenses you paid over the period, simply divide your account value by $1,000 (for example, an $8,600 account value divided by $1,000 = 8.6), then multiply the result by the number in the "Expenses Paid per $1,000" line under the share class you hold.
- **Hypothetical 5% Fund Return.** This helps you to compare your Fund's ongoing expenses (but not transaction costs) with those of other mutual funds using the Fund's actual expense ratio and a hypothetical rate of return of 5% per year before expenses. Examples using a 5% hypothetical Fund return may be found in the shareholder reports of other mutual funds. The hypothetical account values and expenses may not be used to estimate the actual ending account balance or expenses you paid for the period.

Please note that the expenses shown in these tables are meant to highlight your ongoing expenses only and do not reflect any transaction costs. The "Expenses Paid per $1,000" line of the tables is useful in comparing ongoing expenses only and will not help you determine the relative total expense of owning different funds. If these transaction costs had been included, your costs would have been higher.

**Expenses and Value of a $1,000 Investment** for the six months ended December 31, 2010

| **Actual Fund Return** | **Class A** | **Class B** |
|---|---|---|
| Beginning Account Value 7/1/10 | $1,000.00 | $1,000.00 |
| Ending Account Value 12/31/10 | $1,245.60 | $1,243.60 |
| Expenses Paid per $1,000* | $ 5.94 | $ 7.92 |
| **Hypothetical 5% Fund Return** | **Class A** | **Class B** |
| Beginning Account Value 7/1/10 | $1,000.00 | $1,000.00 |
| Ending Account Value 12/31/10 | $1,019.91 | $1,018.15 |
| Expenses Paid per $1,000* | $ 5.35 | $ 7.12 |

* *Expenses are equal to the Fund's annualized expense ratio for each share class, multiplied by the average account value over the period, multiplied by the number of days in the most recent six-month period, then divided by 365.*

| **Annualized Expense Ratios** | **Class A** | **Class B** |
|---|---|---|
| DWS Variable Series II — DWS Global Thematic VIP | 1.05% | 1.40% |

For more information, please refer to the Fund's prospectus.

These tables do not reflect charges and fees ("contract charges") associated with the separate account that invests in the Fund or any variable life insurance policy or variable annuity contract for which the Fund is an investment option.

## DWS Global Thematic VIP

The Fund's Class A shares returned 13.65% during 2010, outpacing the 11.76% return of the MSCI World Index. The Fund also has outperformed its benchmark during the 5- and 10-year periods ended December 31, 2010.

In managing the Fund, we strive to identify the themes that we believe will be the important long-term drivers of the global business environment, then we use intensive fundamental research and a wide array of quantitative tools to invest in companies that can benefit as these themes unfold. All 13 of the Fund's themes produced positive absolute returns during 2010. On a relative basis, nine themes outperformed the broader market while just three lagged.

Three of our best-performing themes of 2010 were those with heavy exposure to the emerging markets: Large Units, which invests in companies that are benefiting from the growth of middle classes and consumerism in emerging-markets countries; Global Agribusiness, where we seek companies that stand to benefit from the rapidly changing dietary needs of a growing global population; and Indian Ocean, which seeks to capitalize on the need for China and India to secure agricultural and energy supply routes in the region. Also performing very well was our theme Disequilibria, in which we hunt for situations where investors do not fully understand the capacity of an industry or a company to adapt to a structural change. Many industries experienced significant changes in the wake of the global recession of 2008–2009, creating abundant opportunities to capitalize on companies that were able to benefit from industry flux.

The smallest gain came from our theme Personalized Medicine, which is invested entirely in health care stocks — a sector that underperformed amid the momentum-driven market environment. We remain enthusiastic on the long-term prospects of this theme despite its recent underperformance, and we continue to add to the Fund's holdings in this area.

While we believe there is a good case for global equities as we move into 2011, we continue to spend time analyzing the potential adverse outcomes of various economic scenarios. Our investment framework remains guided by our well-researched themes and the core principle that investment management is a marathon and not a sprint.

Oliver Kratz, PhD
*Portfolio Manager, Global Thematic Partners, LLC*
*Subadvisor to the Fund*

*The Morgan Stanley Capital International (MSCI) World Index is an unmanaged, capitalization-weighted measure of global stock markets including the US, Canada, Europe, Australia and the Far East. The index is calculated using closing local market prices and translates into US dollars using the London close foreign exchange rates.*

*Index returns assume reinvestment of dividends and, unlike fund returns, do not reflect any fees of expenses. It is not possible to invest directly into an index.*

*Portfolio management market commentary is as of December 31, 2010, and may not come to pass. This information is subject to change at any time based on market and other conditions. Past performance does not guarantee future results. Current and future portfolio holdings are subject to risk.*

# Portfolio Summary

## DWS Global Thematic VIP

| **Asset Allocation** (As a % of Investment Portfolio excluding Securities Lending Collateral) | **12/31/10** | **12/31/09** |
|---|---|---|
| Common Stocks | 94% | 95% |
| Participatory Notes | 3% | 2% |
| Cash Equivalents | 2% | 1% |
| Preferred Stocks | 1% | — |
| Exchange-Traded Funds | — | 2% |
| | 100% | 100% |

| **Sector Diversification** (As a % of Investment Portfolio excluding Exchange-Traded Funds, Cash Equivalents and Securities Lending Collateral) | **12/31/10** | **12/31/09** |
|---|---|---|
| Financials | 21% | 23% |
| Information Technology | 14% | 11% |
| Health Care | 12% | 14% |
| Consumer Staples | 11% | 11% |
| Industrials | 11% | 14% |
| Materials | 9% | 2% |
| Telecommunication Services | 7% | 6% |
| Consumer Discretionary | 6% | 8% |
| Energy | 5% | 9% |
| Utilities | 4% | 2% |
| | 100% | 100% |

| **Geographical Diversification** (As a % of Investment Portfolio excluding Cash Equivalents and Securities Lending Collateral) | **12/31/10** | **12/31/09** |
|---|---|---|
| United States | 32% | 44% |
| Continental Europe | 23% | 23% |
| Japan | 9% | 9% |
| Latin America | 8% | 5% |
| Asia (excluding Japan) | 8% | 5% |
| United Kingdom | 8% | 7% |
| Africa | 4% | 2% |
| Middle East | 4% | 3% |
| Bermuda | 1% | 1% |
| Other | 3% | 1% |
| | 100% | 100% |

*Asset allocation, sector and geographical diversification are subject to change.*

*For more complete details about the Fund's investment portfolio, see page 6.*

Following the Fund's fiscal first and third quarter-end, a complete portfolio holdings listing is filed with the SEC on Form N-Q. The form will be available on the SEC's Web site at www.sec.gov, and it also may be reviewed and copied at the SEC's Public Reference Room in Washington, D.C. Information on the operation of the SEC's Public Reference Room may be obtained by calling (800) SEC-0330. The Fund's portfolio holdings are also posted on www.dws-investments.com from time to time. Please see the Fund's current prospectus for more information.

# Investment Portfolio

December 31, 2010

## DWS Global Thematic VIP

| | Shares | Value ($) |
|---|---|---|
| **Common Stocks 95.6%** | | |
| **Austria 3.4%** | | |
| Erste Group Bank AG | 40,781 | 1,916,496 |
| Raiffeisen Bank International AG | 6,427 | 352,042 |
| Wienerberger AG* | 10,111 | 193,193 |
| (Cost $1,834,682) | | **2,461,731** |
| **Bahrain 0.3%** | | |
| Aluminium Bahrain 144A (GDR)* (Cost $262,586) | 21,937 | **245,694** |
| **Bermuda 0.6%** | | |
| Lazard Ltd. "A" (Cost $323,175) | 11,956 | **472,143** |
| **Brazil 4.5%** | | |
| All America Latina Logistica | 41,745 | 377,342 |
| Banco Bradesco SA (ADR) (Preferred) | 16,875 | 342,394 |
| Banco Santander Brasil SA (ADR) | 32,906 | 447,522 |
| Brasil Telecom SA (ADR) | 4,401 | 96,514 |
| Petroleo Brasileiro SA (ADR) | 18,094 | 684,677 |
| Santos Brasil Participacoes SA (Units) | 34,497 | 477,684 |
| SLC Agricola SA | 63,320 | 839,453 |
| (Cost $2,784,368) | | **3,265,586** |
| **Cayman Islands 0.3%** | | |
| Herbalife Ltd. (Cost $153,889) | 3,749 | **256,319** |
| **China 2.1%** | | |
| Bank of China Ltd. "H" | 938,871 | 496,444 |
| China Metal Recycling Holdings Ltd. | 199,352 | 211,078 |
| Li Ning Co., Ltd. | 89,245 | 189,448 |
| Mindray Medical International Ltd. (ADR) (a) | 23,089 | 609,550 |
| (Cost $1,632,015) | | **1,506,520** |
| **Denmark 1.2%** | | |
| Vestas Wind Systems AS* (Cost $875,294) | 27,897 | **880,998** |
| **Egypt 0.5%** | | |
| Orascom Telecom Holding SAE (GDR) REG S* (Cost $185,988) | 96,576 | **352,502** |
| **France 0.8%** | | |
| Carrefour SA (Cost $747,206) | 14,437 | **595,163** |
| **Germany 6.3%** | | |
| Axel Springer AG | 3,028 | 493,655 |
| Deutsche Lufthansa AG (Registered)* | 18,558 | 405,585 |
| Deutsche Post AG (Registered) | 42,056 | 713,297 |
| E.ON AG | 67,902 | 2,082,574 |
| HeidelbergCement AG | 14,027 | 879,566 |
| (Cost $4,117,461) | | **4,574,677** |
| **Greece 0.3%** | | |
| Hellenic Exchanges SA (Cost $230,675) | 31,318 | **205,066** |
| **Hong Kong 1.3%** | | |
| China Mobile Ltd. (ADR) | 6,721 | 333,496 |
| Esprit Holdings Ltd. | 116,286 | 552,048 |
| Yingde Gases* (b) | 69,766 | 61,483 |
| (Cost $1,019,783) | | **947,027** |
| **India 0.2%** | | |
| Deccan Chronicle Holdings Ltd. (Cost $240,432) | 67,247 | **164,828** |
| **Indonesia 1.9%** | | |
| PT Semen Gresik (Persero) Tbk | 377,454 | 395,662 |
| PT Telekomunikasi Indonesia Tbk (ADR) | 26,780 | 954,707 |
| (Cost $1,244,304) | | **1,350,369** |
| **Israel 1.7%** | | |
| NICE Systems Ltd. (ADR)* | 5,989 | 209,016 |
| Teva Pharmaceutical Industries Ltd. (ADR) | 19,106 | 995,996 |
| (Cost $1,141,082) | | **1,205,012** |
| **Italy 1.0%** | | |
| Parmalat SpA | 165,995 | 454,527 |
| UniCredit SpA | 124,822 | 258,146 |
| (Cost $791,529) | | **712,673** |
| **Japan 9.3%** | | |
| FANUC Corp. | 3,300 | 506,241 |
| Fujitsu Ltd. | 74,000 | 514,552 |
| Hitachi Ltd. | 110,000 | 586,922 |
| INPEX Corp. | 171 | 1,000,241 |
| Kirin Holdings Co., Ltd. | 37,000 | 518,701 |
| Mitsubishi UFJ Financial Group, Inc. | 66,200 | 357,689 |
| Mizuho Financial Group, Inc. | 196,800 | 370,569 |
| Nomura Holdings, Inc. | 104,514 | 662,339 |
| Seven & I Holdings Co., Ltd. | 13,000 | 347,222 |
| Sumitomo Mitsui Financial Group, Inc. | 11,000 | 391,545 |
| Takeda Pharmaceutical Co., Ltd. | 6,000 | 295,094 |
| Toyota Motor Corp. | 24,000 | 945,101 |
| Yamada Denki Co., Ltd. | 4,020 | 274,124 |
| (Cost $5,930,147) | | **6,770,340** |
| **Kazakhstan 0.1%** | | |
| Kazakhstan Kagazy PLC 144A (GDR)* (Cost $916,872) | 181,200 | **45,300** |
| **Korea 3.1%** | | |
| KT&G Corp.* | 15,968 | 920,365 |
| Samsung Electronics Co., Ltd. | 1,571 | 1,312,832 |
| (Cost $1,940,032) | | **2,233,197** |
| **Malaysia 0.4%** | | |
| Axiata Group Bhd.* (Cost $214,993) | 185,900 | **286,203** |
| **Mexico 0.7%** | | |
| Grupo Aeroportuario del Sureste SAB de CV (ADR) (a) (Cost $379,121) | 8,482 | **478,809** |
| **Netherlands 2.5%** | | |
| QIAGEN NV* | 32,654 | 638,694 |
| Unilever NV (CVA) | 11,806 | 367,589 |
| VimpelCom Ltd. (ADR) (c) | 53,834 | 809,663 |
| (Cost $1,699,907) | | **1,815,946** |
| **Norway 0.2%** | | |
| Statoil Fuel & Retail ASA* (Cost $129,742) | 19,358 | **176,926** |

*The accompanying notes are an integral part of the financial statements.*

| | Shares | Value ($) |
|---|---|---|
| **Panama 1.5%** | | |
| Copa Holdings SA "A" (Cost $841,944) | 18,635 | **1,096,483** |
| **Puerto Rico 1.4%** | | |
| Popular, Inc.* (Cost $920,104) | 316,838 | **994,871** |
| **Russia 1.1%** | | |
| Aeroflot-Russian Airlines | 107,905 | 280,553 |
| Gazprom (ADR) | 15,660 | 395,415 |
| Sistema JSFC (GDR) (REG S) | 5,253 | 130,957 |
| (Cost $736,335) | | **806,925** |
| **South Africa 3.7%** | | |
| Aquarius Platinum Ltd. | 43,863 | 240,721 |
| MTN Group Ltd. | 37,788 | 771,076 |
| Murray & Roberts Holdings Ltd. | 47,792 | 291,431 |
| Standard Bank Group Ltd. | 68,349 | 1,115,892 |
| Tiger Brands Ltd. | 9,361 | 275,153 |
| (Cost $2,311,096) | | **2,694,273** |
| **Spain 1.1%** | | |
| Telefonica SA (Cost $794,722) | 34,493 | **783,371** |
| **Sweden 2.8%** | | |
| Telefonaktiebolaget LM Ericsson "B" (Cost $1,861,198) | 174,404 | **2,019,548** |
| **Switzerland 2.2%** | | |
| EFG International AG | 17,204 | 235,630 |
| Roche Holding AG (Genusschein) | 6,133 | 899,052 |
| Syngenta AG (Registered) | 1,600 | 468,654 |
| (Cost $1,496,506) | | **1,603,336** |
| **Thailand 0.1%** | | |
| Seamico Securities PCL (Foreign Registered)* (Cost $153,906) | 1,403,300 | **84,724** |
| **United Kingdom 7.4%** | | |
| African Minerals Ltd.* (d) | 19,586 | 128,559 |
| Anglo American PLC | 13,249 | 688,998 |
| BAE Systems PLC | 54,188 | 278,799 |
| Barratt Developments PLC* | 331,333 | 457,949 |
| Diageo PLC | 57,956 | 1,070,756 |
| GlaxoSmithKline PLC | 35,913 | 694,300 |
| Imperial Tobacco Group PLC | 21,678 | 665,147 |
| Tesco PLC | 109,726 | 727,063 |
| Vodafone Group PLC | 255,016 | 659,213 |
| (Cost $4,884,794) | | **5,370,784** |
| **United States 31.6%** | | |
| Abbott Laboratories | 18,197 | 871,818 |
| Advanced Micro Devices, Inc.* | 102,758 | 840,560 |
| Air Products & Chemicals, Inc. | 4,995 | 454,295 |
| Apache Corp. | 3,790 | 451,882 |
| Bank of America Corp. | 112,710 | 1,503,551 |
| Calpine Corp.* | 39,059 | 521,047 |
| Cisco Systems, Inc.* | 44,299 | 896,169 |
| Electronic Arts, Inc.* | 26,791 | 438,837 |
| EMC Corp.* | 21,348 | 488,869 |
| General Dynamics Corp. | 12,234 | 868,125 |
| General Electric Co. | 45,728 | 836,365 |
| General Motors Co.* | 10,233 | 377,188 |
| GSI Commerce, Inc.* | 14,323 | 332,294 |
| Harris Corp. | 12,034 | 545,140 |
| JPMorgan Chase & Co. | 41,332 | 1,753,303 |
| Kinetic Concepts, Inc.* | 13,074 | 547,539 |
| Laboratory Corp. of America Holdings* | 13,043 | 1,146,741 |
| Life Technologies Corp.* | 20,262 | 1,124,541 |
| MasterCard, Inc. "A" | 4,650 | 1,042,111 |
| Medco Health Solutions, Inc.* | 19,659 | 1,204,507 |
| Monsanto Co. | 5,794 | 403,494 |
| Morgan Stanley | 46,133 | 1,255,279 |
| New York Times Co. "A"* (a) | 37,641 | 368,882 |
| Owens-Illinois, Inc.* | 21,550 | 661,585 |
| Rock-Tenn Co. "A" | 2,966 | 160,016 |
| Schweitzer-Mauduit International, Inc. | 8,692 | 546,901 |
| The NASDAQ OMX Group, Inc.* | 29,036 | 688,444 |
| Wal-Mart Stores, Inc. | 21,281 | 1,147,684 |
| Williams Companies, Inc. | 24,851 | 614,317 |
| World Fuel Services Corp. | 7,879 | 284,905 |
| Yahoo!, Inc.* | 35,219 | 585,693 |
| (Cost $20,218,099) | | **22,962,082** |
| **Total Common Stocks** (Cost $63,013,987) | | **69,419,426** |

## Preferred Stocks 0.5%

| | Shares | Value ($) |
|---|---|---|
| **Germany 0.3%** | | |
| Porsche Automobil Holding SE (Cost $135,727) | 2,664 | **212,334** |
| **Russia 0.2%** | | |
| Surgutneftegas (Cost $132,021) | 281,496 | **140,748** |
| **Total Preferred Stocks** (Cost $267,748) | | **353,082** |

## Participatory Notes 2.9%

| | Shares | Value ($) |
|---|---|---|
| **Jordan 0.2%** | | |
| Arab Bank PLC (issuer HSBC Bank PLC), Expiration Date 4/12/2013* (Cost $183,726) | 11,543 | **162,756** |
| **Nigeria 0.9%** | | |
| Bank of Nigeria (issuer HSBC Bank PLC), Expiration Date 11/15/2013* | 2,922,113 | 263,952 |
| Guaranty Trust Bank PLC (issuer Morgan Stanley BV), Expiration Date 3/18/2011* | 2,479,865 | 289,752 |
| Zenith Bank Ltd. (issuer Morgan Stanley BV), Expiration Date 3/18/2011* | 1,015,714 | 100,302 |
| (Cost $601,105) | | **654,006** |
| **Pakistan 0.5%** | | |
| National Bank of Pakistan (issuer Merrill Lynch International & Co.), Expiration Date 2/25/2015* (Cost $347,029) | 398,560 | **356,611** |
| **Saudi Arabia 1.3%** | | |
| Saudi Basic Industrial Corp. (issuer HSBC Bank PLC), Expiration Date 3/26/2012* | 13,086 | 365,511 |
| Yanbu National Petrochemicals Co. (issuer HSBC Bank PLC), Expiration Date 1/7/2013 | 47,967 | 608,821 |
| (Cost $888,354) | | **974,332** |
| **Total Participatory Notes** (Cost $2,020,214) | | **2,147,705** |

## Securities Lending Collateral 1.3%

| | Shares | Value ($) |
|---|---|---|
| Daily Assets Fund Institutional, 0.27% (e) (f) (Cost $960,500) | 960,500 | **960,500** |

*The accompanying notes are an integral part of the financial statements.*

| | Shares | Value ($) |
|---|---|---|
| **Cash Equivalents 2.2%** | | |
| Central Cash Management Fund, 0.19% (e) (Cost $1,583,896) | 1,583,896 | **1,583,896** |

| | % of Net Assets | Value ($) |
|---|---|---|
| **Total Investment Portfolio** (Cost $67,846,345)† | 102.5 | **74,464,609** |
| **Other Assets and Liabilities, Net** | (2.5) | **(1,846,982)** |
| **Net Assets** | 100.0 | **72,617,627** |

* *Non-income producing security.*

† *The cost for federal income tax purposes was $68,246,019. At December 31, 2010, net unrealized appreciation for all securities based on tax cost was $6,218,590. This consisted of aggregate gross unrealized appreciation for all securities in which there was an excess of value over tax cost of $8,508,835 and aggregate gross unrealized depreciation for all securities in which there was an excess of tax cost over value of $2,290,245.*

(a) *All or a portion of these securities were on loan (see Notes to Financial Statements). The value of all securities loaned at December 31, 2010 amounted to $932,405, which is 1.3% of net assets.*

(b) *Security is listed in country of domicile. Significant business activities of company are in China.*

(c) *Security is listed in country of domicile. Significant business activities of company are in Eastern Europe and South Asia.*

(d) *Security is listed in country of domicile. Significant business activities of company are in Africa.*

(e) *Affiliated fund managed by Deutsche Investment Management Americas Inc. The rate shown is the annualized seven-day yield at period end.*

(f) *Represents collateral held in connection with securities lending. Income earned by the Fund is net of borrower rebates.*

*144A: Security exempt from registration under Rule 144A of the Securities Act of 1933. These securities may be resold in transactions exempt from registration, normally to qualified institutional buyers.*

*ADR: American Depositary Receipt*

*CVA: Certificaten Van Aandelen*

*GDR: Global Depositary Receipt*

*REG S: Securities sold under Regulation S may not be offered, sold or delivered within the United States or to, or for the account or benefit of, US persons, except pursuant to an exemption from, or in a transaction not subject to, the registration requirements of the Securities Act of 1933.*

## Fair Value Measurements

*Various inputs are used in determining the value of the Fund's investments. These inputs are summarized in three broad levels. Level 1 includes quoted prices in active markets for identical securities. Level 2 includes other significant observable inputs (including quoted prices for similar securities, interest rates, prepayment speeds, and credit risk). Level 3 includes significant unobservable inputs (including the Fund's own assumptions in determining the fair value of investments). The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities.*

*The following is a summary of the inputs used as of December 31, 2010 in valuing the Fund's investments. For information on the Fund's policy regarding the valuation of investments, please refer to the Security Valuation section of Note A in the accompanying Notes to Financial Statements.*

| Assets | Level 1 | Level 2 | Level 3 | Total |
|---|---|---|---|---|
| Common Stocks & Preferred Stocks (g) | | | | |
| Austria | $ — | $ 2,461,731 | $ — | $ 2,461,731 |
| Bahrain | — | 245,694 | — | 245,694 |
| Bermuda | 472,143 | — | — | 472,143 |
| Brazil | 3,265,586 | — | — | 3,265,586 |
| Cayman Islands | 256,319 | — | — | 256,319 |
| China | 609,550 | 896,970 | — | 1,506,520 |
| Denmark | — | 880,998 | — | 880,998 |
| Egypt | — | 352,502 | — | 352,502 |
| France | — | 595,163 | — | 595,163 |
| Germany | — | 4,787,011 | — | 4,787,011 |
| Greece | — | 205,066 | — | 205,066 |
| Hong Kong | 333,496 | 613,531 | — | 947,027 |
| India | — | 164,828 | — | 164,828 |
| Indonesia | 954,707 | 395,662 | — | 1,350,369 |
| Israel | 1,205,012 | — | — | 1,205,012 |
| Italy | — | 712,673 | — | 712,673 |
| Japan | — | 6,770,340 | — | 6,770,340 |
| Kazakhstan | — | 45,300 | — | 45,300 |
| Korea | — | 2,233,197 | — | 2,233,197 |
| Malaysia | — | 286,203 | — | 286,203 |
| Mexico | 478,809 | — | — | 478,809 |
| Netherlands | 809,663 | 1,006,283 | — | 1,815,946 |
| Norway | — | 176,926 | — | 176,926 |
| Panama | 1,096,483 | — | — | 1,096,483 |
| Puerto Rico | 994,871 | — | — | 994,871 |
| Russia | — | 947,673 | — | 947,673 |

*The accompanying notes are an integral part of the financial statements.*

| Assets | Level 1 | Level 2 | Level 3 | Total |
|---|---|---|---|---|
| South Africa | — | 2,694,273 | — | 2,694,273 |
| Spain | — | 783,371 | — | 783,371 |
| Sweden | — | 2,019,548 | — | 2,019,548 |
| Switzerland | — | 1,603,336 | — | 1,603,336 |
| Thailand | — | 84,724 | — | 84,724 |
| United Kingdom | — | 5,370,784 | — | 5,370,784 |
| United States | 22,962,082 | — | — | 22,962,082 |
| Participatory Notes (g) | — | 2,147,705 | — | 2,147,705 |
| Short-Term Investments (g) | 2,544,396 | — | — | 2,544,396 |
| **Total** | **$ 35,983,117** | **$ 38,481,492** | **$ —** | **$ 74,464,609** |

*There have been no significant transfers between Level 1 and Level 2 fair value measurements during the year ended December 31, 2010.*

(g) *See Investment Portfolio for additional detailed categorizations.*

*The accompanying notes are an integral part of the financial statements.*

# Statement of Assets and Liabilities

as of December 31, 2010

| | | |
|---|---|---|
| **Assets** | | |
| Investments: | | |
| Investments in unaffiliated securities, at value (cost $65,301,949) — including $932,405 of securities loaned | $ | 71,920,213 |
| Investment in Daily Assets Fund Institutional (cost $960,500)* | | 960,500 |
| Investment in Central Cash Management Fund (cost $1,583,896) | | 1,583,896 |
| Total investments, at value (cost $67,846,345) | | 74,464,609 |
| Foreign currency, at value (cost $129,430) | | 129,932 |
| Receivable for investments sold | | 421,035 |
| Receivable for Fund shares sold | | 92 |
| Dividends receivable | | 66,283 |
| Interest receivable | | 1,147 |
| Foreign taxes recoverable | | 15,438 |
| Due from Advisor | | 6,316 |
| Other assets | | 325 |
| Total assets | | 75,105,177 |
| **Liabilities** | | |
| Payable for investments purchased | | 1,362,763 |
| Payable for Fund shares redeemed | | 33,107 |
| Payable upon return of securities loaned | | 960,500 |
| Accrued expenses and payables | | 131,180 |
| Total liabilities | | 2,487,550 |
| **Net assets, at value** | **$** | **72,617,627** |
| **Net Assets Consist of** | | |
| Undistributed net investment income | | 361,169 |
| Net unrealized appreciation (depreciation) on: | | |
| Investments | | 6,618,264 |
| Foreign currency | | 2,108 |
| Accumulated net realized gain (loss) | | (53,454,008) |
| Paid-in capital | | 119,090,094 |
| **Net assets, at value** | **$** | **72,617,627** |
| **Class A** | | |
| **Net Asset Value,** offering and redemption price per share ($67,788,512 ÷ 7,301,949 outstanding shares of beneficial interest, no par value, unlimited number of shares authorized) | **$** | **9.28** |
| **Class B** | | |
| **Net Asset Value,** offering and redemption price per share ($4,829,115 ÷ 519,624 outstanding shares of beneficial interest, no par value, unlimited number of shares authorized) | **$** | **9.29** |

* *Represents collateral on securities loaned.*

# Statement of Operations

for the year ended December 31, 2010

| | | |
|---|---|---|
| **Investment Income** | | |
| Income: | | |
| Dividends (net of foreign taxes withheld of $75,539) | $ | 1,226,438 |
| Income distributions — Central Cash Management Fund | | 2,453 |
| Securities lending income, including income from Daily Assets Fund Institutional, net of borrower rebates | | 23,173 |
| Total income | | 1,252,064 |
| Expenses: | | |
| Management fee | | 626,939 |
| Administration fee | | 68,518 |
| Services to shareholders | | 3,860 |
| Distribution service fee (Class B) | | 11,552 |
| Record keeping fees (Class B) | | 4,575 |
| Custodian fee | | 142,829 |
| Legal fees | | 9,737 |
| Audit and tax fees | | 65,395 |
| Trustees' fees and expenses | | 5,102 |
| Reports to shareholders | | 10,208 |
| Other | | 34,743 |
| Total expenses before expense reductions | | 983,458 |
| Expense reductions | | (245,517) |
| Total expenses after expense reductions | | 737,941 |
| **Net investment income (loss)** | | **514,123** |
| **Realized and Unrealized Gain (Loss)** | | |
| Net realized gain (loss) from: | | |
| Investments (net of foreign taxes of $41,882) | | 7,284,942 |
| Foreign currency | | (78,627) |
| | | 7,206,315 |
| Change in net unrealized appreciation (depreciation) on: | | |
| Investments | | 897,676 |
| Foreign currency | | 1,793 |
| | | 899,469 |
| **Net gain (loss)** | | **8,105,784** |
| **Net increase (decrease) in net assets resulting from operations** | **$** | **8,619,907** |

*The accompanying notes are an integral part of the financial statements.*

# Statement of Changes in Net Assets

| Increase (Decrease) in Net Assets | Years Ended December 31, 2010 | 2009 |
|---|---|---|
| Operations: | | |
| Net investment income (loss) | $ 514,123 | $ 748,747 |
| Net realized gain (loss) | 7,206,315 | (3,218,906) |
| Change in net unrealized appreciation (depreciation) | 899,469 | 24,610,274 |
| Net increase (decrease) in net assets resulting from operations | 8,619,907 | 22,140,115 |
| Distributions to shareholders from: | | |
| Net investment income: | | |
| Class A | (621,927) | (911,359) |
| Class B | (28,358) | (54,811) |
| Total distributions | (650,285) | (966,170) |
| Fund share transactions: | | |
| **Class A** | | |
| Proceeds from shares sold | 5,854,566 | 5,051,406 |
| Reinvestment of distributions | 621,927 | 911,359 |
| Payments for shares redeemed | (12,215,497) | (18,301,405) |
| Net increase (decrease) in net assets from Class A share transactions | (5,739,004) | (12,338,640) |
| **Class B** | | |
| Proceeds from shares sold | 308,827 | 438,509 |
| Reinvestment of distributions | 28,358 | 54,811 |
| Payments for shares redeemed | (1,123,823) | (1,021,786) |
| Net increase (decrease) in net assets from Class B share transactions | (786,638) | (528,466) |
| **Increase (decrease) in net assets** | 1,443,980 | 8,306,839 |
| Net assets at beginning of period | 71,173,647 | 62,866,808 |
| Net assets at end of period (including undistributed net investment income of $361,169 and $607,015, respectively) | **$ 72,617,627** | **$ 71,173,647** |

| Other Information | | |
|---|---|---|
| **Class A** | | |
| Shares outstanding at beginning of period | 8,018,621 | 10,056,541 |
| Shares sold | 692,269 | 725,805 |
| Shares issued to shareholders in reinvestment of distributions | 72,065 | 174,256 |
| Shares redeemed | (1,481,006) | (2,937,981) |
| Net increase (decrease) in Class A shares | (716,672) | (2,037,920) |
| Shares outstanding at end of period | **7,301,949** | **8,018,621** |
| **Class B** | | |
| Shares outstanding at beginning of period | 617,302 | 702,064 |
| Shares sold | 36,659 | 66,888 |
| Shares issued to shareholders in reinvestment of distributions | 3,275 | 10,440 |
| Shares redeemed | (137,612) | (162,090) |
| Net increase (decrease) in Class B shares | (97,678) | (84,762) |
| Shares outstanding at end of period | **519,624** | **617,302** |

*The accompanying notes are an integral part of the financial statements.*

# Financial Highlights

## Class A

| Years Ended December 31, | 2010 | 2009 | 2008 | 2007 | 2006 |
|---|---|---|---|---|---|
| **Selected Per Share Data** | | | | | |
| **Net asset value, beginning of period** | **$ 8.24** | **$ 5.84** | **$15.66** | **$17.39** | **$14.44** |
| *Income (loss) from investment operations:* | | | | | |
| Net investment income[a] | .06 | .08 | .11 | .14 | .15[c] |
| Net realized and unrealized gain (loss) | 1.06 | 2.42 | (5.83) | .88 | 4.02 |
| **Total from investment operations** | 1.12 | 2.50 | (5.72) | 1.02 | 4.17 |
| *Less distributions from:* | | | | | |
| Net investment income | (.08) | (.10) | (.19) | (.11) | (.09) |
| Net realized gains | — | — | (3.91) | (2.64) | (1.13) |
| **Total distributions** | (.08) | (.10) | (4.10) | (2.75) | (1.22) |
| **Net asset value, end of period** | **$ 9.28** | **$ 8.24** | **$ 5.84** | **$15.66** | **$17.39** |
| Total Return (%)[b] | 13.65 | 43.82 | (47.75) | 6.29 | 30.14[c] |
| **Ratios to Average Net Assets and Supplemental Data** | | | | | |
| Net assets, end of period ($ millions) | 68 | 66 | 59 | 151 | 143 |
| Ratio of expenses before expense reductions (%) | 1.41 | 1.38 | 1.47 | 1.44 | 1.38 |
| Ratio of expenses after expense reductions (%) | 1.05 | 1.04 | 1.09 | 1.11 | 1.04 |
| Ratio of net investment income (%) | .77 | 1.23 | 1.09 | .82 | .92[c] |
| Portfolio turnover rate (%) | 165 | 190 | 229 | 191 | 136 |

a *Based on average shares outstanding during the period.*

b *Total return would have been lower had certain expenses not been reduced.*

c *Includes non-recurring income from the Advisor recorded as a result of an administrative proceeding regarding disclosure of brokerage allocation practices in connection with sales of DWS Funds. The non-recurring income resulted in an increase in net investment income of $0.004 per share and an increase in the ratio of net investment income of 0.03%. Excluding this non-recurring income, total return would have been 0.02% lower.*

## Class B

| Years Ended December 31, | 2010 | 2009 | 2008 | 2007 | 2006 |
|---|---|---|---|---|---|
| **Selected Per Share Data** | | | | | |
| **Net asset value, beginning of period** | **$ 8.25** | **$ 5.85** | **$15.66** | **$17.38** | **$14.43** |
| *Income (loss) from investment operations:* | | | | | |
| Net investment income[a] | .04 | .06 | .07 | .07 | .09[c] |
| Net realized and unrealized gain (loss) | 1.05 | 2.42 | (5.83) | .90 | 4.02 |
| **Total from investment operations** | 1.09 | 2.48 | (5.76) | .97 | 4.11 |
| *Less distributions from:* | | | | | |
| Net investment income | (.05) | (.08) | (.14) | (.05) | (.03) |
| Net realized gains | — | — | (3.91) | (2.64) | (1.13) |
| **Total distributions** | (.05) | (.08) | (4.05) | (2.69) | (1.16) |
| **Net asset value, end of period** | **$ 9.29** | **$ 8.25** | **$ 5.85** | **$15.66** | **$17.38** |
| Total Return (%)[b] | 13.24 | 43.23 | (47.87) | 5.84 | 29.65[c] |
| **Ratios to Average Net Assets and Supplemental Data** | | | | | |
| Net assets, end of period ($ millions) | 5 | 5 | 4 | 10 | 25 |
| Ratio of expenses before expense reductions (%) | 1.76 | 1.73 | 1.82 | 1.81 | 1.76 |
| Ratio of expenses after expense reductions (%) | 1.40 | 1.39 | 1.45 | 1.47 | 1.43 |
| Ratio of net investment income (%) | .42 | .88 | .73 | .46 | .53[c] |
| Portfolio turnover rate (%) | 165 | 190 | 229 | 191 | 136 |

a *Based on average shares outstanding during the period.*

b *Total return would have been lower had certain expenses not been reduced.*

c *Includes non-recurring income from the Advisor recorded as a result of an administrative proceeding regarding disclosure of brokerage allocation practices in connection with sales of DWS Funds. The non-recurring income resulted in an increase in net investment income of $0.004 per share and an increase in the ratio of net investment income of 0.03%. Excluding this non-recurring income, total return would have been 0.02% lower.*

# Notes to Financial Statements

## A. Organization and Significant Accounting Policies

DWS Variable Series II (the "Trust") is registered under the Investment Company Act of 1940, as amended (the "1940 Act"), as an open-end management investment company organized as a Massachusetts business trust. The Trust offers seventeen funds (hereinafter referred to individually as "Fund" or collectively as "Funds"). The Fund is classified as a diversified open-end management investment company.

**Multiple Classes of Shares of Beneficial Interest.** Certain Funds of the Trust offer two classes of shares (Class A shares and Class B shares). Sales of Class B shares are subject to record keeping fees up to 0.15% and Rule 12b-1 fees under the 1940 Act equal to an annual rate of 0.25%, of the average daily net assets of the Class B shares of the applicable Fund. Class A shares are not subject to such fees.

Investment income, realized and unrealized gains and losses, and certain fund-level expenses and expense reductions, if any, are borne pro rata on the basis of relative net assets by the holders of all classes of shares except that each class bears certain expenses unique to that class (including the applicable Rule 12b-1 fee and record keeping fees). Differences in class-level expenses may result in payment of different per share dividends by class. All shares have equal rights with respect to voting subject to class-specific arrangements.

The Trust's financial statements are prepared in accordance with accounting principles generally accepted in the United States of America which require the use of management estimates. Actual results could differ from those estimates. The policies described below are followed consistently by the Trust in the preparation of its financial statements.

**Security Valuation.** Investments are stated at value determined as of the close of regular trading on the New York Stock Exchange on each day the exchange is open for trading.

Various inputs are used in determining the value of the Fund's investments. These inputs are summarized in three broad levels. Level 1 includes quoted prices in active markets for identical securities. Level 2 includes other significant observable inputs (including quoted prices for similar securities, interest rates, prepayment speeds, and credit risk). Level 3 includes significant unobservable inputs (including the Fund's own assumptions in determining the fair value of investments). The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities.

Equity securities and exchange-traded funds ("ETFs") are valued at the most recent sale price or official closing price reported on the exchange (US or foreign) or over-the-counter market on which they trade and are categorized as Level 1 securities. Securities or ETFs for which no sales are reported are valued at the calculated mean between the most recent bid and asked quotations on the relevant market or, if a mean cannot be determined, at the most recent bid quotation. For certain international equity securities, in order to adjust for events which may occur between the close of the foreign exchanges and the close of the New York Stock Exchange, a fair valuation model may be used. This fair valuation model takes into account comparisons to the valuation of American Depository Receipts (ADRs), exchange-traded funds, futures contracts and certain indices and these securities are categorized as Level 2.

Exchange-traded options are valued at the last sale price or, in the absence of a sale, the mean between the closing bid and asked prices or at the most recent asked price (bid for purchased options) if no bid or asked price are available. Exchange-traded options are categorized as Level 1. Over-the-counter written or purchased options are valued based upon a price provided by the broker-dealer with which the option, was traded and are generally categorized as Level 3.

Money market instruments purchased with an original or remaining maturity of sixty days or less, maturing at par, are valued at amortized cost, which approximates value, and are categorized as Level 2. Investments in open-end investment companies are valued at their net asset value each business day and are categorized as Level 1.

Securities and other assets for which market quotations are not readily available or for which the above valuation procedures are deemed not to reflect fair value are valued in a manner that is intended to reflect their fair value as determined in accordance with procedures approved by the Board and are generally categorized as Level 3. In accordance with the Fund's valuation procedures, factors used in determining value may include, but are not limited to, the type of the security; the size of the holding; the initial cost of the security; the existence of any contractual restrictions on the security's disposition; the price and extent of public trading in similar securities of the issuer or of comparable companies; quotations or evaluated prices from broker-dealers and/or pricing services; information obtained from the issuer, analysts, and/or the appropriate stock exchange (for exchange-traded securities); an analysis of the company's or issuer's financial statements; an evaluation of the forces that influence the issuer and the market(s) in which the security is purchased and sold and with respect to debt securities; the maturity, coupon, creditworthiness, currency denomination and the movement of the market

in which the security is normally traded. The value determined under these procedures may differ from published values for the same securities.

Disclosure about the classification of fair value measurements is included in a table following the Fund's Investment Portfolio.

**Foreign Currency Translations.** The books and records of the Trust are maintained in US dollars. Investment securities and other assets and liabilities denominated in a foreign currency are translated into US dollars at the prevailing exchange rates at period end. Purchases and sales of investment securities, income and expenses are translated into US dollars at the prevailing exchange rates on the respective dates of the transactions.

Net realized and unrealized gains and losses on foreign currency transactions represent net gains and losses between trade and settlement dates on securities transactions, the disposition of forward foreign currency exchange contracts and foreign currencies, and the difference between the amount of net investment income accrued and the US dollar amount actually received. That portion of both realized and unrealized gains and losses on investments that results from fluctuations in foreign currency exchange rates is not separately disclosed but is included with net realized and unrealized gain/appreciation and loss/depreciation on investments.

**Securities Lending.** The Fund lends securities to certain financial institutions. The Fund retains beneficial ownership of the securities it has loaned and continues to receive interest and dividends paid by the issuer of securities and to participate in any changes in their market value. The Fund requires the borrowers of the securities to maintain collateral with the Fund consisting of either cash or liquid, unencumbered assets having a value at least equal to the value of the securities loaned. When the collateral falls below specified amounts, the lending agent will use its best effort to obtain additional collateral on the next business day to meet required amounts under the security lending agreement. The Fund may invest the cash collateral into a joint trading account in an affiliated money market fund pursuant to Exemptive Orders issued by the SEC. The Fund receives compensation for lending its securities either in the form of fees or by earning interest on invested cash collateral net of borrower rebates and fees paid to a lending agent. Either the Fund or the borrower may terminate the loan. There may be risks of delay and costs in recovery of securities or even loss of rights in the collateral should the borrower of the securities fail financially. The Fund is also subject to all investment risks associated with the reinvestment of any cash collateral received, including, but not limited to, interest rate, credit and liquidity risk associated with such investments.

**Participatory Notes.** The Fund invests in Participatory Notes (P-Notes). P-Notes are promissory notes designed to offer a return linked to the performance of a particular underlying equity security or market. P-Notes are issued by banks or broker-dealers and allow the Fund to gain exposure to local shares in foreign markets. Investments in P-Notes involve the same risks associated with a direct investment in the underlying foreign companies or foreign markets that they seek to replicate. Although each participation note is structured with a defined maturity date, early redemption may be possible. Risks associated with participation notes include the possible failure of a counterparty to perform in accordance with the terms of the agreement and potential delays or an inability to redeem before maturity under certain market conditions.

**Taxes.** The Fund's policy is to comply with the requirements of the Internal Revenue Code, as amended, which are applicable to regulated investment companies and to distribute all of its taxable income to its shareholders.

Additionally, based on the Fund's understanding of the tax rules and rates related to income, gains and transactions for the foreign jurisdictions in which it invests, the Fund will provide for foreign taxes, and where appropriate, deferred foreign taxes.

At December 31, 2010, the Fund had an approximate net tax basis capital loss carryforward which may be applied against any realized net taxable capital gains of each succeeding year until fully utilized or until the following expiration dates, whichever occurs first:

| Fund | Capital Loss Carryforward ($) | Expiration Date | Capital Loss Carryforward Utilized ($) |
|---|---|---|---|
| DWS Global Thematic VIP | 35,242,000 | 12/31/2016 | 6,786,000 |
| | 17,811,000 | 12/31/2017 | |

In addition, from November 1, 2010 through December 31, 2010, the Fund incurred net realized capital losses. As permitted by tax regulations, the Fund intends to elect to defer these losses and treat them as arising in the fiscal year ended December 31, 2011.

| Fund | |
|---|---|
| DWS Global Thematic VIP | $ 43,000 |

The Fund has reviewed the tax positions for the open tax years as of December 31, 2010 and has determined that no provision for income tax is required in the Fund's financial statements. The Fund's federal tax returns for the prior three fiscal years remain open subject to examination by the Internal Revenue Service.

**Distribution of Income and Gains.** Distributions of net investment income of the Fund, if any, are made annually. Net realized gains from investment transactions, in excess of available capital loss carryforwards, would be taxable to the Fund if not distributed and, therefore, will be distributed to shareholders at least annually. The Fund may also make additional distributions for tax purposes if necessary.

The timing and characterization of certain income and capital gains distributions are determined annually in accordance with federal tax regulations which may differ from accounting principles generally accepted in the United States of America. These differences primarily relate to investments in foreign denominated investments, income received from Passive Foreign Investment Companies and certain securities sold at a loss. As a result, net investment income (loss) and net realized gain (loss) on investment transactions for a reporting period may differ significantly from distributions during such period. Accordingly, the Fund may periodically make reclassifications among certain of its capital accounts without impacting the net asset value of the Fund.

At December 31, 2010, the Fund's components of distributable earnings on a tax basis were as follows:

| Fund | Undistributed Ordinary Income ($)* | Capital Loss Carryforwards ($) | Unrealized Appreciation (Depreciation) on Investments ($) |
|---|---|---|---|
| DWS Global Thematic VIP | 363,173 | (53,053,000) | 6,218,590 |

In addition, the tax character of distributions paid by the Fund is summarized as follows:

| | Distributions from Ordinary Income ($)* | |
|---|---|---|
| | Years Ended December 31, | |
| Fund | 2010 | 2009 |
| DWS Global Thematic VIP | 650,285 | 966,170 |

* *For tax purposes, short-term capital gain distributions are considered ordinary income distributions.*

**Expenses.** Expenses of the Trust arising in connection with a specific fund are allocated to that fund. Other Trust expenses which cannot be directly attributed to a fund are apportioned among the funds in the Trust.

**Contingencies.** In the normal course of business, the Fund may enter into contracts with service providers that contain general indemnification clauses. The Fund's maximum exposure under these arrangements is unknown as this would involve future claims that may be made against the Fund that have not yet been made. However, based on experience, the Fund expects the risk of loss to be remote.

**Other.** Investment transactions are accounted for on a trade date plus one basis for daily net asset value calculations. However, for financial reporting purposes, investment transactions are reported on trade date. Interest income is recorded on the accrual basis. Dividend income is recorded on the ex-dividend date net of foreign withholding taxes. Certain dividends from foreign securities may be recorded subsequent to the ex-dividend date as soon as the Fund is informed of such dividends. Realized gains and losses from investment transactions are recorded on an identified cost basis.

## B. Derivative Instruments

**Options.** An option contract is a contract in which the writer (seller) of the option grants the buyer of the option, upon payment of a premium, the right to purchase from (call option), or sell to (put option), the writer a designated instrument at a specified price within a specified period of time. Certain options, including options on indices, will require cash settlement by the Fund if the option is exercised. For the year ended December 31, 2010, the Fund entered into option contracts in order to enhance potential gain.

The liability representing the Fund's obligation under an exchange-traded written option or investment in a purchased option is valued at the last sale price or, in the absence of a sale, the mean between the closing bid and asked prices or at the most recent asked price (bid for purchased options) if no bid and asked price are available. Over-the-counter written or purchased options are valued using dealer-supplied quotations. Gain or loss is recognized when the option contract expires, exercised or is closed.

If the Fund writes a covered call option, the Fund foregoes, in exchange for the premium, the opportunity to profit during the option period from an increase in the market value of the underlying security above the exercise price. If the Fund writes a put option it accepts the risk of a decline in the value of the underlying security below the exercise price. Over-the-counter options have the risk of the potential inability of counterparties to meet the terms of their contracts. The Fund's maximum exposure to purchased options is limited to the premium initially paid. In addition, certain risks may arise upon entering into option contracts including the risk that an illiquid secondary market will limit the Fund's ability to close out an option contract prior to the expiration date and that a change in the value of the option contract may not correlate exactly with changes in the value of the securities or currencies hedged.

There are no open option contracts as of December 31, 2010 for the Fund. During the year ended December 31, 2010, the Fund's investment in purchased option contracts had a total value generally indicative of a range from $0 to approximately $1,000.

The following tables summarize the amount of unrealized and realized gains and losses on derivative instruments recognized in Fund earnings during the year ended December 31, 2010 and the related location in the accompanying Statement of Operations, presented by primary underlying risk exposure:

| **Realized Gain (Loss)** | **Purchased Options** |
|---|---|
| Equity Contracts (a) | $ (212,772) |

*The above derivative is located in the following Statement of Operations account:*

(a) *Net realized gain (loss) from investments (includes purchased options)*

| **Change in Net Unrealized Appreciation (Depreciation)** | **Purchased Options** |
|---|---|
| Equity Contracts (a) | $ 212,262 |

*The above derivative is located in the following Statement of Operations account:*

(a) *Change in net unrealized appreciation (depreciation) on investments (includes purchased options)*

## C. Purchases and Sales of Securities

During the year ended December 31, 2010, purchases and sales of investment transactions (excluding short-term investments) were as follows:

| **Fund** | **Purchases ($)** | **Sales ($)** |
|---|---|---|
| DWS Global Thematic VIP | 110,185,987 | 116,147,618 |

## D. Related Parties

**Management Agreement.** Under the Investment Management Agreement with Deutsche Investment Management Americas Inc. ("DIMA" or the "Advisor"), an indirect, wholly owned subsidiary of Deutsche Bank AG, the Advisor directs the investments of the Fund in accordance with its investment objectives, policies and restrictions. The Advisor determines the securities, instruments and other contracts relating to investments to be purchased, sold or entered into by the Fund or delegates such responsibility to the Fund's subadvisor.

Global Thematic Partners, LLC ("GTP") acts as investment sub-advisor to the Fund. On July 1, 2010, members of the Advisor's Global Equity Team, including members of the Fund's portfolio management team, separated from the Advisor and formed GTP as a separate investment advisory firm unaffiliated with the Advisor (the "Separation"). As an investment sub-advisor to the Fund, GTP makes investment decisions and buys and sells securities for the Fund. GTP is paid by the Advisor, not the Fund, for the services GTP provides to the Fund.

Under the Investment Management Agreement with the Advisor, the fee is equivalent to the annual rates shown below of the Fund's average daily net assets, computed and accrued daily and payable monthly:

| **Fund** | **Annual Management Fee Rate** |
|---|---|
| DWS Global Thematic VIP | |
| $0–$250 million | .915% |
| next $500 million | .865% |
| next $750 million | .815% |
| next $1.5 billion | .765% |
| over $3 billion | .715% |

For the period from January 1, 2010 through September 30, 2010, the Advisor had contractually agreed to waive its fee and/or reimburse certain operating expenses to the extent necessary to maintain the operating expenses (excluding certain expenses such as extraordinary expenses, taxes, brokerage and interest expense) of each class as follows:

| Fund | Annual Rate |
|---|---|
| DWS Global Thematic VIP | |
| Class A | 1.06% |
| Class B | 1.46% |

For the period from October 1, 2010 through September 30, 2011, the Advisor has contractually agreed to waive its fee and/or reimburse certain operating expenses to the extent necessary to maintain the operating expenses (excluding certain expenses such as extraordinary expenses, taxes, brokerage and interest expense) of each class as follows:

| Fund | Annual Rate |
|---|---|
| DWS Global Thematic VIP | |
| Class A | 1.03% |
| Class B | 1.43% |

Accordingly, for the year ended December 31, 2010, the total management fee, management fee waived and effective management fee rate were as follows:

| Fund | Total Aggregated ($) | Waived ($) | Annual Effective Rate |
|---|---|---|---|
| DWS Global Thematic VIP | 626,939 | 245,154 | .56% |

**Administration Fee.** Pursuant to an Administrative Services Agreement, DIMA provides most administrative services to the Fund. For all services provided under the Administrative Services Agreement, the Fund pays DIMA an annual fee ("Administration Fee") of 0.10% of the Fund's average daily net assets, computed and accrued daily and payable monthly. For the year ended December 31, 2010, the Administration Fee was as follows:

| Fund | Total Aggregated ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS Global Thematic VIP | 68,518 | 6,051 |

**Service Provider Fees.** DWS Investments Service Company ("DISC"), an affiliate of the Advisor, is the transfer agent, dividend-paying agent and shareholder service agent for the Fund. Pursuant to a sub-transfer agency agreement between DISC and DST Systems, Inc. ("DST"), DISC has delegated certain transfer agent, dividend-paying agent and shareholder service agent functions to DST. DISC compensates DST out of the shareholder servicing fee it receives from the Fund. For the year ended December 31, 2010, the amounts charged to the Fund by DISC were as follows:

| Fund | Total Aggregated ($) | Waived ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|---|
| DWS Global Thematic VIP Class A | 363 | 363 | — |
| DWS Global Thematic VIP Class B | 83 | — | 18 |

**Distribution Service Agreement**. Under the Fund's Class B 12b-1 plans, DWS Investments Distributors, Inc. ("DIDI") received a fee ("Distribution Service Fee") of 0.25% of average daily net assets of Class B shares. For the year ended December 31, 2010, the Distribution Service Fee was as follows:

| Fund | Total Aggregated ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS Global Thematic VIP | 11,552 | 1,002 |

**Typesetting and Filing Service Fees.** Under an agreement with DIMA, DIMA is compensated for providing typesetting and certain regulatory filing services to the Fund. For the year ended December 31, 2010, the amount charged to the Fund by DIMA included in the Statement of Operations under "reports to shareholders" was as follows:

| Fund | Amount ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS Global Thematic VIP | 10,208 | 1,734 |

**Trustees' Fees and Expenses.** The Fund paid each Trustee not affiliated with the Advisor retainer fees plus specified amounts for various committee services and for the Board Chairperson.

**Affiliated Cash Management Vehicles.** The Fund may invest uninvested cash balances in Central Cash Management Fund, which is managed by the Advisor. The Fund indirectly bears their proportionate share of the expenses of the underlying money market funds. Central Cash Management Fund does not pay the Advisor an investment management fee. Central Cash Management Fund seeks a high level of current income consistent with liquidity and the preservation of capital.

### E. Investing in Emerging Markets

Investing in emerging markets may involve special risks and considerations not typically associated with investing in developed markets. These risks include revaluation of currencies, high rates of inflation or deflation, repatriation restrictions on income and capital, and future adverse political, social and economic developments. Moreover, securities issued in these markets may be less liquid, subject to government ownership controls or delayed settlements, and may have prices that are more volatile or less easily assessed than those of comparable securities of issuers in developed markets.

### F. Ownership of the Fund

At December 31, 2010, the beneficial ownership in the Fund was as follows:

**DWS Global Thematic VIP:** Two Participating Insurance Companies were owners of record of 10% or more of the total outstanding Class A shares of the Fund, each owning 57% and 33%. One Participating Insurance Company was the owner of record of 10% or more of the total outstanding Class B shares of the Fund, owning 98%.

### G. Line of Credit

The Trust and other affiliated fund (the "Participants") share in a $450 million revolving credit facility provided by a syndication of banks. The Fund may borrow for temporary or emergency purposes, including the meeting of redemption requests that otherwise might require the untimely disposition of securities. The Participants are charged an annual commitment fee which is allocated based on net assets, among each of the Participants. Interest is calculated at a rate per annum equal to the sum of the Federal Funds Rate plus 1.25 percent plus if LIBOR exceeds the Federal Funds Rate the amount of such excess. The Fund may borrow up to a maximum of 33 percent of its net assets under the agreement.

# Report of Independent Registered Public Accounting Firm

**To the Board of Trustees and Shareholders of DWS Variable Series II:**

We have audited the accompanying statement of assets and liabilities of DWS Global Thematic VIP, one of the funds constituting the DWS Variable Series II (the "Trust"), including the investment portfolio, as of December 31, 2010, and the related statement of operations, the statement of changes in net assets and the financial highlights for each of the periods indicated therein. These financial statements and financial highlights are the responsibility of the Trust's management. Our responsibility is to express an opinion on these financial statements and financial highlights based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements and financial highlights are free of material misstatement. We were not engaged to perform an audit of the Trust's internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Trust's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements and financial highlights, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our procedures included confirmation of securities owned as of December 31, 2010, by correspondence with the custodian and brokers or by other appropriate auditing procedures where replies from brokers were not received. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements and financial highlights referred to above present fairly, in all material respects, the financial position of the aforementioned fund of the DWS Variable Series II at December 31, 2010, the results of its operations, the changes in its net assets and the financial highlights for each of the periods indicated therein, in conformity with U.S. generally accepted accounting principles.

Ernst + Young LLP

Boston, Massachusetts
February 14, 2011

# Tax Information

**(Unaudited)**

For corporate shareholders, the following percentage of income dividends paid during the Fund's fiscal year ended December 31, 2010 qualified for the dividends received deduction:

| Fund | Dividends Received % |
|---|---|
| DWS Global Thematic VIP | 59 |

The Fund paid foreign taxes of $117,000 and earned $347,000 of foreign source income during the year ended December 31, 2010. Pursuant to Section 853 of the International Revenue Code, the Fund designates $0.02 per share as foreign taxes paid and $0.04 per share as income earned from foreign sources for the year ended December 31, 2010.

Please consult a tax advisor if you have questions about federal or state income tax laws, or on how to prepare your tax returns. If you have specific questions about your account, please contact your insurance provider.

# Proxy Voting

The Trust's policies and procedures for voting proxies for portfolio securities and information about how the Trust voted proxies related to its portfolio securities during the 12-month period ended June 30 are available on our Web site — www.dws-investments.com (click on "proxy voting" at the bottom of the page) — or on the SEC's Web site — www.sec.gov. To obtain a written copy of the Trust's policies and procedures without charge, upon request, call us toll free at (800) 728-3337.

# Investment Management Agreement Approval

## DWS Global Thematic VIP

The Board of Trustees, including the Independent Trustees, approved the renewal of your Fund's investment management agreement (the "Agreement") with Deutsche Investment Management Americas Inc. ("DWS") and sub-advisory agreement (the "Sub-Advisory Agreement" and together with the Agreement the "Agreements") between DWS and Global Thematic Partners, LLC ("Global Thematic") in September 2010.

In terms of the process that the Board followed prior to approving the Agreements, shareholders should know that:

- In September 2010, all but one of the Fund's Trustees were independent of DWS and its affiliates.
- The Trustees meet frequently to discuss fund matters. Each year, the Trustees dedicate substantial time to contract review matters. Over the course of several months, the Board's Contract Committee, in coordination with the Board's Equity Oversight Committee, reviewed comprehensive materials received from DWS, independent third parties and independent counsel. These materials included an analysis of the Fund's performance, fees and expenses, and profitability compiled by the Fund's independent fee consultant. The Board also received extensive information throughout the year regarding performance of the Fund.
- The Independent Trustees regularly meet privately with their independent counsel to discuss contract review and other matters. In addition, the Independent Trustees were also advised by the Fund's independent fee consultant in the course of their review of the Fund's contractual arrangements and considered a comprehensive report prepared by the independent fee consultant in connection with their deliberations (the "IFC Report").
- In connection with reviewing the Agreements, the Board also reviewed the terms of the Fund's Rule 12b-1 plan, distribution agreement, administrative services agreement, transfer agency agreement and other material service agreements.
- Based on its evaluation of the information provided, the Contract Committee presented its findings and recommendations to the Independent Trustees as a group. The Independent Trustees reviewed the Contract Committee's findings and recommendations and presented their recommendations to the full Board.

In connection with the contract review process, the Contract Committee and the Board considered the factors discussed below, among others. The Board also considered that DWS and its predecessors have managed the Fund since its inception, and the Board believes that a long-term relationship with a capable, conscientious advisor is in the best interests of the Fund. The Board considered, generally, that shareholders chose to invest or remain invested in the Fund knowing that DWS managed the Fund, and that the Agreement was approved by the Fund's shareholders. DWS is part of Deutsche Bank, a major global banking institution that is engaged in a wide range of financial services. The Board believes that there are significant advantages to being part of a global asset management business that offers a wide range of investing expertise and resources, including hundreds of portfolio managers and analysts with research capabilities in many countries throughout the world.

While shareholders may focus primarily on fund performance and fees, the Fund's Board considers these and many other factors, including the quality and integrity of DWS's and Global Thematic's personnel and such other issues as back-office operations, fund valuations, and compliance policies and procedures. In addition, in connection with approving the continuation of the Fund's Sub-Advisory Agreement, the Board noted it had engaged in a comprehensive review of the agreement in connection with its initial approval in May 2010.

**Nature, Quality and Extent of Services.** The Board considered the terms of the Agreements, including the scope of advisory services provided under the Agreements. The Board noted that, under the Agreements, DWS and Global Thematic provide portfolio management services to the Fund and that, pursuant to a separate administrative services agreement, DWS provides administrative services to the Fund. The Board considered the experience and skills of senior management and investment personnel, the resources made available to such personnel, the ability of DWS to attract and retain high-quality personnel, and the organizational depth and stability of DWS. The Board reviewed the Fund's performance over short-term and long-term periods and compared those returns to various agreed-upon performance measures, including market indices and a peer universe compiled by the independent fee consultant using information supplied by Lipper Inc. ("Lipper"). The Board also noted that it has put into place a process of identifying "Focus Funds" (e.g., funds performing poorly relative to their benchmark or a peer universe compiled by Lipper), and receives more frequent reporting and information from DWS regarding such funds, along with DWS's remedial plans to address underperformance. The Board believes this process is an effective manner of identifying and addressing underperforming funds. Based on the information provided, the Board noted that for the one-, three- and five-year periods ended December 31, 2009, the Fund's performance (Class A shares) was in the 1st quartile, 4th quartile and 1st quartile, respectively, of the applicable Lipper universe (the 1st quartile being the best performers and the 4th quartile being the worst performers). The Board also observed that the Fund has outperformed its benchmark in the one- and five-year periods and has underperformed its benchmark in the three-year period ended December 31, 2009.

On the basis of this evaluation and the ongoing review of investment results by the Board, the Board concluded that the nature, quality and extent of services provided by DWS and Global Thematic historically have been and continue to be satisfactory.

**Fees and Expenses.** The Board considered the Fund's investment management fee schedule, sub-advisory fee schedule, operating expenses, and total expense ratios, and comparative information provided by Lipper and the independent fee consultant regarding investment management fee rates paid to other investment advisors by similar funds (1st quartile being the most favorable and 4th quartile being the least favorable). With respect to management fees paid to other investment advisors by similar funds, the Board noted that the contractual fee rates paid by the Fund, which include the 0.10% fee paid to DWS under the Fund's administrative services agreement, were higher than the median (4th quartile) of the applicable Lipper peer group (based on Lipper data provided as of December 31, 2009). With respect to the sub-advisory fee paid to Global Thematic, the Board noted that the fee is paid by DWS out of its fee and not directly by the Fund. The Board noted that the Fund's Class A shares total (net) operating expenses were expected to be higher than the median (4th quartile) of the applicable Lipper expense universe (based on Lipper data provided as of December 31, 2009, and analyzing Lipper expense universe Class A expenses less any applicable 12b-1 fees) ("Lipper Universe Expenses"). The Board also reviewed data comparing each share class's total (net) operating expenses to the applicable Lipper Universe Expenses. The Board considered the Fund's management fee rate as compared to fees charged by DWS and certain of its affiliates for comparable mutual funds and considered differences in fund and fee structures between the DWS Funds. The Board also considered how the Fund's total (net) operating expenses compared to the total (net) operating expenses of a more customized peer group selected by Lipper (based on such factors as asset size). The Board also noted that the expense limitations agreed to by DWS helped to ensure that the Fund's total (net) operating expenses would remain competitive.

The information considered by the Board as part of its review of management fees included information regarding fees charged by DWS and its affiliates to similar institutional accounts and to similar funds offered primarily to European investors ("DWS Europe funds"), in each case as applicable. The Board observed that advisory fee rates for institutional accounts generally were lower than the management fees charged by similarly managed DWS US mutual funds ("DWS Funds"), but also took note of the differences in services provided to DWS Funds as compared to institutional accounts. In the case of DWS Europe funds, the Board observed that fee rates for DWS Europe funds generally were higher than for similarly managed DWS Funds, but noted that differences in the types of services provided to DWS Funds relative to DWS Europe funds made it difficult to compare such fees.

On the basis of the information provided, the Board concluded that management fees were reasonable and appropriate in light of the nature, quality and extent of services provided by DWS and Global Thematic.

**Profitability.** The Board reviewed detailed information regarding revenues received by DWS under the Agreement. The Board considered the estimated costs and pre-tax profits realized by DWS from advising the DWS Funds, as well as estimates of the pre-tax profits attributable to managing the Fund in particular. The Board also received information regarding the estimated enterprise-wide profitability of DWS and its affiliates with respect to all fund services in totality and by fund. The Board reviewed DWS's methodology in allocating its costs to the management of the Fund. Based on the information provided, the Board concluded that the pre-tax profits realized by DWS in connection with the management of the Fund were not unreasonable. The Board also reviewed information regarding the profitability of certain similar investment management firms. The Board noted that while information regarding the profitability of such firms is limited (and in some cases is not necessarily prepared on a comparable basis), DWS and its affiliates' overall profitability with respect to the DWS fund complex (after taking into account distribution and other services provided to the funds by DWS and its affiliates) was lower than the overall profitability levels of many comparable firms for which such data was available. The Board did not consider the profitability of Global Thematic with respect to the Fund. The Board noted that DWS pays Global Thematic's fee out of its management fee, and its understanding that the Fund's sub-advisory fee schedule was the product of an arm's length negotiation with DWS.

**Economies of Scale.** The Board considered whether there are economies of scale with respect to the management of the Fund and whether the Fund benefits from any economies of scale. The Board noted that the Fund's management fee schedule includes fee breakpoints. The Board concluded that the Fund's fee schedule represents an appropriate sharing between the Fund and DWS of such economies of scale as may exist in the management of the Fund at current asset levels.

**Other Benefits to DWS and Global Thematic and Their Affiliates.** The Board also considered the character and amount of other incidental benefits received by DWS and Global Thematic and their affiliates, including any fees received by DWS for administrative services provided to the Fund and any fees received by an affiliate of DWS for distribution services. The Board also considered benefits to DWS and Global Thematic related to brokerage and soft-dollar allocations, including allocating brokerage to pay for research generated by parties other than the executing broker dealers, which pertain primarily to funds investing in equity securities, along with the incidental public relations benefits to DWS and Global Thematic related to DWS Funds advertising and cross-selling opportunities among DWS products and services. The Board concluded that management fees were reasonable in light of these fallout benefits.

**Compliance.** The Board considered the significant attention and resources dedicated by DWS to documenting and enhancing its compliance processes in recent years. The Board noted in particular (i) the experience and seniority of both DWS's chief compliance officer and the Fund's chief compliance officer; (ii) the large number of DWS compliance personnel; and (iii) the substantial commitment of resources by DWS and its affiliates to compliance matters. The Board also considered the attention and resources dedicated by DWS to the oversight of the investment sub-advisor's compliance program and compliance with the applicable fund policies and procedures.

Based on all of the information considered and the conclusions reached, the Board unanimously (including the Independent Trustees) determined that the continuation of the Agreements is in the best interests of the Fund. In making this determination, the Board did not give particular weight to any single factor identified above. The Board considered these factors over the course of numerous meetings, certain of which were in executive session with only the Independent Trustees and their counsel present. It is possible that individual Trustees may have weighed these factors differently in reaching their individual decisions to approve the continuation of the Agreements.

# Summary of Management Fee Evaluation by Independent Fee Consultant

October 3, 2010

Pursuant to an Order entered into by Deutsche Investment Management Americas and affiliates (collectively, "DeAM") with the Attorney General of New York, I, Thomas H. Mack, have been appointed the Independent Fee Consultant for the DWS Funds (formerly the DWS Scudder Funds). My duties include preparing an annual written evaluation of the management fees DeAM charges the Funds, considering among other factors the management fees charged by other mutual fund companies for like services, management fees DeAM charges other clients for like services, DeAM's costs of supplying services under the management agreements and related profit margins, possible economies of scale if a Fund grows larger, and the nature and quality of DeAM's services, including fund performance. This report summarizes my evaluation for 2010, including my qualifications, the evaluation process for each of the DWS Funds, consideration of certain complex-level factors, and my conclusions. I served in substantially the same capacity in 2007, 2008, and 2009.

## Qualifications

For more than 35 years I have served in various professional capacities within the investment management business. I have held investment analysis and advisory positions, including securities analyst, portfolio strategist and director of investment policy with a large investment firm. I have also performed business management functions, including business development, financial management and marketing research and analysis.

Since 1991, I have been an independent consultant within the asset management industry. I have provided services to over 125 client organizations, including investment managers, mutual fund boards, product distributors and related organizations. Over the past ten years I have completed a number of assignments for mutual fund boards, specifically including assisting boards with management contract renewal.

I hold a Master of Business Administration degree, with highest honors, from Harvard University and Master of Science and Bachelor of Science (highest honors) degrees from the University of California at Berkeley. I am an independent director and audit committee financial expert for two closed-end mutual funds and have served in various leadership and financial oversight capacities with non-profit organizations.

## Evaluation of Fees for each DWS Fund

My work focused primarily on evaluating, fund-by-fund, the fees charged to each of the 118 publicly offered Fund portfolios in the DWS Fund family. For each Fund, I considered each of the key factors mentioned above, as well as any other relevant information. In doing so I worked closely with the Funds' Independent Directors in their annual contract renewal process, as well as in their approval of contracts for several new funds (documented separately).

In evaluating each Fund's fees, I reviewed comprehensive materials provided by or on behalf of DeAM, including expense information prepared by Lipper Analytical, comparative performance information, profitability data, manager histories, and other materials. I also accessed certain additional information from the Lipper and Morningstar databases and drew on my industry knowledge and experience.

To facilitate evaluating this considerable body of information, I prepared for each Fund a document summarizing the key data elements in each area as well as additional analytics discussed below. This made it possible to consider each key data element in the context of the others.

In the course of contract renewal, DeAM agreed to implement a number of fee and expense adjustments requested by the Independent Directors which will favorably impact future fees and expenses, and my evaluation includes the effects of these changes.

### Fees and Expenses Compared with Other Funds

The competitive fee and expense evaluation for each fund focused on two primary comparisons:

- The Fund's contractual management fee (the advisory fee plus the administration fee where applicable) compared with those of a group of typically 12–15 funds in the same Lipper investment category (e.g. Large Capitalization Growth) having similar distribution arrangements and being of similar size.
- The Fund's total expenses compared with a broader universe of funds from the same Lipper investment category and having similar distribution arrangements.

These two comparisons provide a view of not only the level of the fee compared with funds of similar scale but also the total expense the Fund bears for all the services it receives, in comparison with the investment choices available in the Fund's investment category and distribution channel. The principal figure-of-merit used in these comparisons was the subject Fund's percentile ranking against peers.

### DeAM's Fees for Similar Services to Others

DeAM provided management fee schedules for all of its US domiciled fund and non-fund investment management accounts in any of the investment categories where there is a DWS Fund. These similar products included the other DWS Funds, non-fund pooled accounts, institutional accounts and sub-advisory accounts. Using this information, I calculated for each Fund the fee that would be charged to each similar product, at the subject Fund's asset level.

Evaluating information regarding non-fund products is difficult because there are varying levels of services required for different types of accounts, with mutual funds generally requiring considerably more regulatory and administrative types of service as well as having more frequent cash flows than other types of accounts. Also, while mutual fund fees for similar fund products can be expected to be similar, there will be some differences due to different pricing conditions in different distribution channels (e.g. retail funds versus those used in variable insurance products), differences in underlying investment processes and other factors.

**Costs and Profit Margins**

DeAM provided a detailed profitability analysis for each Fund. After making some adjustments so that the presentation would be more comparable to the available industry figures, I reviewed profit margins from investment management alone, from investment management plus other fund services (excluding distribution) provided to the Funds by DeAM (principally shareholder services), and DeAM profits from all sources, including distribution. A later section comments on overall profitability.

**Economies of Scale**

Economies of scale — an expected decline in management cost per dollar of fund assets as fund assets grow — are very rarely quantified and documented because of inherent difficulties in collecting and analyzing relevant data. However, in virtually every investment category that I reviewed, larger funds tend to have lower fees and lower total expenses than smaller funds. To see how each DWS Fund compares with this industry observation, I reviewed:

- The trend in Fund assets over the last five years and the accompanying trend in total expenses. This shows if the Fund has grown and, if so, whether total expense (management fees as well as other expenses) have declined as a percent of assets.
- Whether the Fund has break-points in its management fee schedule, the extent of the fee reduction built into the schedule and the asset levels where the breaks take effect, and in the case of a sub-advised Fund how the Fund's break-points compare with those of the sub-advisory fee schedule.
- How the Fund's contractual fee schedule compares with trends in the industry data. To accomplish this, I constructed a chart showing how actual latest-fiscal-year contractual fees of the Fund and of other similar funds relate to average fund assets, with the subject Fund's contractual fee schedule superimposed.

**Quality of Service — Performance**

The quality-of-service evaluation focused on investment performance, which is the principal result of the investment management service. Each Fund's performance was reviewed over the past 1, 3, 5 and 10 years, as applicable, and compared with that of other funds in the same investment category and with a suitable market index.

In addition, I calculated and reviewed risk-adjusted returns relative to an index of similar mutual funds' returns and a suitable market index. The risk-adjusted returns analysis provides a way of determining the extent to which the Fund's return comparisons are mainly the product of investment value-added (or lack thereof) or alternatively taking considerably more or less risk than is typical in its investment category.

I also received and considered the history of portfolio manager changes for each Fund, as this provided an important context for evaluating the performance results.

## Complex-Level Considerations

While this evaluation was conducted mainly at the individual fund level, there are some issues relating to the reasonableness of fees that can alternatively be considered across the whole fund complex:

- I reviewed DeAM's profitability analysis for all DWS Funds, with a view toward determining if the allocation procedures used were reasonable and how profit levels compared with public data for other investment managers.
- I considered whether DeAM and affiliates receive any significant ancillary or "fall-out" benefits that should be considered in interpreting the direct profitability results. These would be situations where serving as the investment manager of the Funds is beneficial to another part of the Deutsche Bank organization.
- I considered how aggregated DWS Fund expenses had varied over the years, by asset class and in the context of trends in asset levels.
- I reviewed the structure of the DeAM organization, trends in staffing levels, and information on compensation of investment management and other professionals compared with industry data.

## Findings

Based on the process and analysis discussed above, which included reviewing a wide range of information from management and external data sources and considering among other factors the fees DeAM charges other clients, the fees charged by other fund managers, DeAM's costs and profits associated with managing the Funds, economies of scale, possible fall-out benefits, and the nature and quality of services provided, in my opinion the management fees charged the DWS Funds are reasonable.

Thomas H. Mack

Thomas H. Mack

## Board Members and Officers

The following table presents certain information regarding the Board Members and Officers of the Trust as of December 31, 2010. Each Board Member's year of birth is set forth in parentheses after his or her name. Unless otherwise noted, (i) each Board Member has engaged in the principal occupation(s) noted in the table for at least the most recent five years, although not necessarily in the same capacity; and (ii) the address of each Independent Board Member is c/o Paul K. Freeman, Independent Chairman, DWS Funds, PO Box 101833, Denver, CO 80250-1833. Except as otherwise noted below, the term of office for each Board Member is until the election and qualification of a successor, or until such Board Member sooner dies, resigns, is removed or as otherwise provided in the governing documents of the fund. Because the fund does not hold an annual meeting of shareholders, each Board Member will hold office for an indeterminate period. The Board Members may also serve in similar capacities with other funds in the fund complex. The Length of Time Served represents the year in which the Board Member joined the board of one or more DWS funds now overseen by the Board.

### Independent Board Members

| Name, Year of Birth, Position with the Fund and Length of Time Served[1] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Paul K. Freeman (1950)<br>Chairperson since 2009<br>Board Member since 1993 | Consultant, World Bank/Inter-American Development Bank; Executive and Governing Council of the Independent Directors Council (education committees); formerly, Project Leader, International Institute for Applied Systems Analysis (1998–2001); Chief Executive Officer, The Eric Group, Inc. (environmental insurance) (1986–1998) | 122 |
| John W. Ballantine (1946)<br>Board Member since 1999 | Retired; formerly, Executive Vice President and Chief Risk Management Officer, First Chicago NBD Corporation/The First National Bank of Chicago (1996–1998); Executive Vice President and Head of International Banking (1995–1996). Directorships: Healthways, Inc. (provider of disease and care management services); Portland General Electric (utility company); Stockwell Capital Investments PLC (private equity). Former Directorships: First Oak Brook Bancshares, Inc. and Oak Brook Bank; Prisma Energy International | 122 |
| Henry P. Becton, Jr. (1943)<br>Board Member since 1990 | Vice Chair and former President, WGBH Educational Foundation. Directorships: Association of Public Television Stations; Lead Director, Becton Dickinson and Company[3] (medical technology company); Lead Director, Belo Corporation[3] (media company); Public Radio International; Public Radio Exchange (PRX); The PBS Foundation. Former Directorships: Boston Museum of Science; American Public Television; Concord Academy; New England Aquarium; Mass. Corporation for Educational Telecommunications; Committee for Economic Development; Public Broadcasting Service | 122 |
| Dawn-Marie Driscoll (1946)<br>Board Member since 1987 | President, Driscoll Associates (consulting firm); Executive Fellow, Center for Business Ethics, Bentley University; formerly, Partner, Palmer & Dodge (1988–1990); Vice President of Corporate Affairs and General Counsel, Filene's (1978–1988). Directorships: Trustee of 22 open-end mutual funds managed by Sun Capital Advisers, Inc. (since 2007); Director of ICI Mutual Insurance Company (since 2007); Advisory Board, Center for Business Ethics, Bentley University; Trustee, Southwest Florida Community Foundation (charitable organization). Former Directorships: Investment Company Institute (audit, executive, nominating committees) and Independent Directors Council (governance, executive committees) | 122 |
| Keith R. Fox (1954)<br>Board Member since 1996 | Managing General Partner, Exeter Capital Partners (a series of private investment funds). Directorships: Progressive International Corporation (kitchen goods importer and distributor); BoxTop Media Inc. (advertising); The Kennel Shop (retailer); former Chairman, National Association of Small Business Investment Companies | 122 |
| Kenneth C. Froewiss (1945)<br>Board Member since 2001 | Adjunct Professor of Finance, NYU Stern School of Business (September 2009–present; Clinical Professor from 1997–September 2009); Member, Finance Committee, Association for Asian Studies (2002–present); Director, Mitsui Sumitomo Insurance Group (US) (2004–present); prior thereto, Managing Director, J.P. Morgan (investment banking firm) (until 1996) | 122 |
| Richard J. Herring (1946)<br>Board Member since 1990 | Jacob Safra Professor of International Banking and Professor, Finance Department, The Wharton School, University of Pennsylvania (since July 1972); Co-Director, Wharton Financial Institutions Center (since July 2000); Co-Chair, U.S. Shadow Financial Regulatory Committee; Executive Director, Financial Economists Roundtable; Director, Japan Equity Fund, Inc. (since September 2007), Thai Capital Fund, Inc. (since September 2007), Singapore Fund, Inc. (since September 2007); Independent Director of Barclays Bank Delaware (since September 2010). Formerly, Vice Dean and Director, Wharton Undergraduate Division (July 1995–June 2000); Director, Lauder Institute of International Management Studies (July 2000–June 2006) | 122 |
| William McClayton (1944)<br>Board Member since 2004+ | Private equity investor (since October 2009); previously, Managing Director, Diamond Management & Technology Consultants, Inc. (global consulting firm) (2001–2009); Directorship: Board of Managers, YMCA of Metropolitan Chicago; formerly: Senior Partner, Arthur Andersen LLP (accounting) (1966–2001); Trustee, Ravinia Festival | 122 |

| Name, Year of Birth, Position with the Fund and Length of Time Served[1] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Rebecca W. Rimel (1951)<br>Board Member since 1995 | President and Chief Executive Officer, The Pew Charitable Trusts (charitable organization) (1994 to present); Trustee, Thomas Jefferson Foundation (charitable organization) (1994 to present); Trustee, Executive Committee, Philadelphia Chamber of Commerce (2001–2007); Director, CardioNet, Inc.[2] (2009–present) (health care). Formerly, Executive Vice President, The Glenmede Trust Company (investment trust and wealth management) (1983–2004); Board Member, Investor Education (charitable organization) (2004–2005); Director, Viasys Health Care[2] (January 2007–June 2007); Trustee, Pro Publica (charitable organization) (2007–2010) | 122 |
| William N. Searcy, Jr. (1946)<br>Board Member since 1993 | Private investor since October 2003; Trustee of 22 open-end mutual funds managed by Sun Capital Advisers, Inc. (since October 1998). Formerly, Pension & Savings Trust Officer, Sprint Corporation[2] (telecommunications) (November 1989–September 2003) | 122 |
| Jean Gleason Stromberg (1943)<br>Board Member since 1997 | Retired. Formerly, Consultant (1997–2001); Director, Financial Markets US Government Accountability Office (1996–1997); Partner, Fulbright & Jaworski, L.L.P. (law firm) (1978–1996). Directorships: The William and Flora Hewlett Foundation. Former Directorships: Service Source, Inc., Mutual Fund Directors Forum (2002–2004), American Bar Retirement Association (funding vehicle for retirement plans) (1987–1990 and 1994–1996) | 122 |
| Robert H. Wadsworth (1940)<br>Board Member since 1999 | President, Robert H. Wadsworth & Associates, Inc. (consulting firm) (1983 to present); Director, The Phoenix Boys Choir Association | 125 |

## Interested Board Member and Officer[4]

| Name, Year of Birth, Position with the Trust/ Corporation and Length of Time Served[1,5] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Ingo Gefeke[7] (1967)<br>Board Member since 2010<br>Executive Vice President since 2010 | Managing Director[3], Deutsche Asset Management; Global Head of Distribution and Product Management, DWS Global Head of Trading and Securities Lending. Member of the Board of Directors of DWS Investment GmbH Frankfurt (since July 2009) and DWS Holding & Service GmbH Frankfurt (since January 2010); formerly, Global Chief Administrative Officer, Deutsche Asset Management (2004–2009); Global Chief Operating Officer, Global Transaction Banking, Deutsche Bank AG, New York (2001–2004); Chief Operating Officer, Global Banking Division Americas, Deutsche Bank AG, New York (1999–2001); Central Management, Global Banking Services, Deutsche Bank AG, Frankfurt (1998–1999); Relationship Management, Deutsche Bank AG, Tokyo, Japan (1997–1998) | 55 |

## Officers[4]

| Name, Year of Birth, Position with the Fund and Length of Time Served[5] | Principal Occupation(s) During Past 5 Years and Other Directorships Held |
|---|---|
| Michael G. Clark[6] (1965)<br>President, 2006–present | Managing Director[3], Deutsche Asset Management (2006–present); President of DWS family of funds; Director, ICI Mutual Insurance Company (since October 2007); formerly, Director of Fund Board Relations (2004–2006) and Director of Product Development (2000–2004), Merrill Lynch Investment Managers; Senior Vice President Operations, Merrill Lynch Asset Management (1999–2000) |
| John Millette[8] (1962)<br>Vice President and Secretary, 1999–present | Director[3], Deutsche Asset Management |
| Paul H. Schubert[6] (1963)<br>Chief Financial Officer, 2004–present<br>Treasurer, 2005–present | Managing Director[3], Deutsche Asset Management (since July 2004); formerly, Executive Director, Head of Mutual Fund Services and Treasurer for UBS Family of Funds (1998–2004); Vice President and Director of Mutual Fund Finance at UBS Global Asset Management (1994–1998) |
| Caroline Pearson[8] (1962)<br>Chief Legal Officer, April 2010–present | Managing Director[3], Deutsche Asset Management; formerly, Assistant Secretary for DWS family of funds (1997–2010) |
| Rita Rubin[9] (1970)<br>Assistant Secretary, 2009–present | Vice President and Counsel, Deutsche Asset Management (since October 2007); formerly, Vice President, Morgan Stanley Investment Management (2004–2007) |
| Paul Antosca[8] (1957)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management (since 2006); Vice President, The Manufacturers Life Insurance Company (U.S.A.) (1990–2006) |
| Jack Clark[8] (1967)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management (since 2007); formerly, Vice President, State Street Corporation (2002–2007) |

| Name, Year of Birth, Position with the Fund and Length of Time Served[5] | Principal Occupation(s) During Past 5 Years and Other Directorships Held |
|---|---|
| Diane Kenneally[8] (1966)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management |
| John Caruso[9] (1965)<br>Anti-Money Laundering Compliance Officer, 2010–present | Managing Director[3], Deutsche Asset Management |
| Robert Kloby[9] (1962)<br>Chief Compliance Officer, 2006–present | Managing Director[3], Deutsche Asset Management |

1 *The length of time served represents the year in which the Board Member joined the board of one or more DWS funds currently overseen by the Board.*

2 *A publicly held company with securities registered pursuant to Section 12 of the Securities Exchange Act of 1934.*

3 *Executive title, not a board directorship.*

4 *As a result of their respective positions held with the Advisor, these individuals are considered "interested persons" of the Advisor within the meaning of the 1940 Act. Interested persons receive no compensation from the fund.*

5 *The length of time served represents the year in which the officer was first elected in such capacity for one or more DWS funds.*

6 *Address: 100 Plaza One, Jersey City, NJ 07311.*

7 *Effective January 11, 2011, Mr. Gefeke, an interested Board Member and Executive Vice President, resigned from the fund's Board and as an officer.*

*The mailing address of Mr. Gefeke is 345 Park Avenue, New York, New York 10154. Mr. Gefeke was an interested Board Member of certain DWS funds by virtue of his positions with Deutsche Asset Management. As an interested person, Mr. Gefeke received no compensation from the fund.*

8 *Address: One Beacon Street, Boston, MA 02108.*

9 *Address: 60 Wall Street, New York, New York 10005.*

*The fund's Statement of Additional Information ("SAI") includes additional information about the Board Members. The SAI is available, without charge, upon request. If you would like to request a copy of the SAI, you may do so by calling the following toll-free number: (800) 728-3337.*

# Notes

DWS Investments is part of Deutsche Bank's Asset Management division and, within the US, represents the retail asset management activities of Deutsche Bank AG, Deutsche Bank Trust Company Americas, Deutsche Investment Management Americas Inc. and DWS Trust Company.

The views expressed in this report reflect those of the portfolio managers only through the end of the period of the report as stated on the cover. The managers' views are subject to change at any time based on market and other conditions and should not be construed as a recommendation.

This information must be preceded or accompanied by a current prospectus.

Portfolio changes should not be considered recommendations for action by individual investors.

DWS Investments Distributors, Inc.
222 South Riverside Plaza
Chicago, IL 60606
(800) 621-1148

VS2GT-2 (2/11)

DWS INVESTMENTS
Deutsche Bank Group

DECEMBER 31, 2010

# ANNUAL REPORT

## DWS VARIABLE SERIES II

## DWS Government & Agency Securities VIP

**This report must be preceded or accompanied by a prospectus. To obtain an additional prospectus or summary prospectus, if available, call (800) 728-3337 or your financial representative. We advise you to consider the Fund's objectives, risks, charges and expenses carefully before investing. The summary prospectus and prospectus contain this and other important information about the Fund. Please read the prospectus carefully before you invest.**

*Investments in variable insurance portfolios (VIPs) involve risk. Stocks may decline in value. Bond investments are subject to interest-rate and credit risks. When interest rates rise, bond prices generally fall. Credit risk refers to the ability of an issuer to make timely payments of principal and interest. Investing in derivatives entails special risks relating to liquidity, leverage and credit that may reduce returns and/or increased volatility. Investing in foreign securities, particularly those of emerging markets, presents certain risks, such as currency fluctuations, political and economic changes, and market risks. There are additional risks associated with investing in commodities, high-yield bonds, aggressive growth stocks, non-diversified/ concentrated funds and small- and mid-cap stocks which are more fully explained in the prospectuses. Please read the prospectus for more information.*

*DWS Investments is part of Deutsche Bank's Asset Management division and, within the US, represents the retail asset management activities of Deutsche Bank AG, Deutsche Bank Trust Company Americas, Deutsche Investment Management Americas Inc. and DWS Trust Company.*

*NOT FDIC/NCUA INSURED    NO BANK GUARANTEE    MAY LOSE VALUE    NOT A DEPOSIT*
*NOT INSURED BY ANY FEDERAL GOVERNMENT AGENCY*

DWS INVESTMENTS
Deutsche Bank Group

# Performance Summary

**December 31, 2010**

## DWS Government & Agency Securities VIP

**All performance shown is historical, assumes reinvestment of all dividend and capital gain distributions and does not guarantee future results. Investment return and principal value fluctuate with changing market conditions so that, when redeemed, shares may be worth more or less than their original cost. Current performance may be lower or higher than the performance data quoted. Please contact your participating insurance company for the Fund's most recent month-end performance. Performance doesn't reflect charges and fees ("contract charges") associated with the separate account that invests in the Fund or any variable life insurance policy or variable annuity contract for which the Fund is an investment option. These charges and fees will reduce returns. While all share classes have the same underlying portfolio, their performance will differ.**

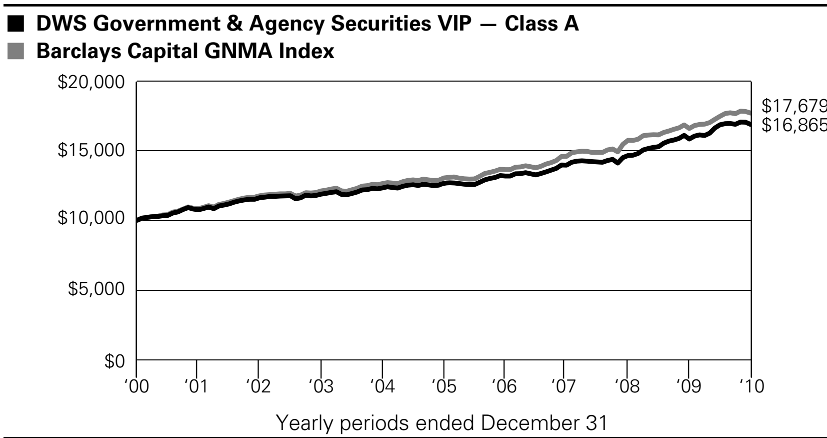
**The gross expense ratios of the Fund, as stated in the fee table of the prospectus dated May 1, 2010 are 0.58% and 0.92% for Class A and Class B shares, respectively, and may differ from the expense ratios disclosed in the Financial Highlights tables in this report.**

### Risk Considerations

Bond investments are subject to interest-rate and credit risks. When interest rates rise, bond prices generally fall. Credit risk refers to the ability of an issuer to make timely payments of principal and interest. In the current market environment, mortgage backed securities are experiencing increased volatility. The "full faith and credit" guarantee of the US government applies to the timely repayment of interest, and does not eliminate market risk. See the prospectus for details.

Fund returns shown for the 3-year, 5-year and 10-year/Life of Class periods reflect a fee waiver and/or expense reimbursement. Without this waiver/reimbursement, returns would have been lower.

### Growth of an Assumed $10,000 Investment in DWS Government & Agency Securities VIP




*The Barclays Capital GNMA Index is an unmanaged, market-value-weighted measure of all fixed-rate securities backed by mortgage pools of the Government National Mortgage Association.*

*Index returns, unlike fund returns, do not reflect any fees or expenses. It is not possible to invest directly into an index.*

### Comparative Results

| DWS Government & Agency Securities VIP | | 1-Year | 3-Year | 5-Year | 10-Year |
|---|---|---|---|---|---|
| **Class A** | Growth of $10,000 | $10,661 | $12,091 | $13,344 | $16,865 |
| | Average annual total return | 6.61% | 6.53% | 5.94% | 5.37% |
| Barclays Capital GNMA Index | Growth of $10,000 | $10,667 | $12,125 | $13,568 | $17,679 |
| | Average annual total return | 6.67% | 6.63% | 6.29% | 5.86% |

| DWS Government & Agency Securities VIP | | 1-Year | 3-Year | 5-Year | Life of Class* |
|---|---|---|---|---|---|
| **Class B** | Growth of $10,000 | $10,624 | $11,968 | $13,090 | $14,610 |
| | Average annual total return | 6.24% | 6.17% | 5.53% | 4.56% |
| Barclays Capital GNMA Index | Growth of $10,000 | $10,667 | $12,125 | $13,568 | $15,655 |
| | Average annual total return | 6.67% | 6.63% | 6.29% | 5.41% |

*The growth of $10,000 is cumulative.*

* *The Fund commenced offering Class B shares on July 1, 2002. Index returns began on June 30, 2002.*

# Information About Your Fund's Expenses

## DWS Government & Agency Securities VIP

As an investor of the Fund, you incur two types of costs: ongoing expenses and transaction costs. Ongoing expenses include management fees, distribution and service (12b-1) fees and other Fund expenses. Examples of transaction costs include contract charges, redemption fees and account maintenance fees, which are not shown in this section. The following tables are intended to help you understand your ongoing expenses (in dollars) of investing in the Fund and to help you compare these expenses with the ongoing expenses of investing in other mutual funds. The example in the table is based on an investment of $1,000 invested at the beginning of the six-month period and held for the entire period (July 1, 2010 to December 31, 2010).

The tables illustrate your Fund's expenses in two ways:

- **Actual Fund Return.** This helps you estimate the actual dollar amount of ongoing expenses (but not transaction costs) paid on a $1,000 investment in the Fund using the Fund's actual return during the period. To estimate the expenses you paid over the period, simply divide your account value by $1,000 (for example, an $8,600 account value divided by $1,000 = 8.6), then multiply the result by the number in the "Expenses Paid per $1,000" line under the share class you hold.
- **Hypothetical 5% Fund Return.** This helps you to compare your Fund's ongoing expenses (but not transaction costs) with those of other mutual funds using the Fund's actual expense ratio and a hypothetical rate of return of 5% per year before expenses. Examples using a 5% hypothetical Fund return may be found in the shareholder reports of other mutual funds. The hypothetical account values and expenses may not be used to estimate the actual ending account balance or expenses you paid for the period.

Please note that the expenses shown in these tables are meant to highlight your ongoing expenses only and do not reflect any transaction costs. The "Expenses Paid per $1,000" line of the tables is useful in comparing ongoing expenses only and will not help you determine the relative total expense of owning different funds. If these transaction costs had been included, your costs would have been higher.

**Expenses and Value of a $1,000 Investment** for the six months ended December 31, 2010

| **Actual Fund Return** | **Class A** | **Class B** |
|---|---|---|
| Beginning Account Value 7/1/10 | $1,000.00 | $1,000.00 |
| Ending Account Value 12/31/10 | $1,001.50 | $ 999.20 |
| Expenses Paid per $1,000* | $ 3.13 | $ 4.89 |
| **Hypothetical 5% Fund Return** | **Class A** | **Class B** |
| Beginning Account Value 7/1/10 | $1,000.00 | $1,000.00 |
| Ending Account Value 12/31/10 | $1,022.08 | $1,020.32 |
| Expenses Paid per $1,000* | $ 3.16 | $ 4.94 |

* *Expenses are equal to the Fund's annualized expense ratio for each share class, multiplied by the average account value over the period, multiplied by the number of days in the most recent six-month period, then divided by 365.*

| **Annualized Expense Ratios** | **Class A** | **Class B** |
|---|---|---|
| DWS Variable Series II — DWS Government & Agency Securities VIP | .62% | .97% |

For more information, please refer to the Fund's prospectus.

These tables do not reflect charges and fees ("contract charges") associated with the separate account that invests in the Fund or any variable life insurance policy or variable annuity contract for which the Fund is an investment option.

## DWS Government & Agency Securities VIP

During the 12-month period, the US Federal Reserve Board (the Fed) maintained the benchmark federal funds rate at near-zero levels and engaged in bond purchases designed to lower longer-term interest rates as it sought to stimulate economic growth.[1] Treasury yields fell for most of the year, before rising in the fourth quarter as market participants reacted to better economic data and the extension of Bush-era tax cuts. For the year, credit-sensitive sectors such as corporate bonds outperformed as investors sought yield in an environment of extraordinarily low interest rates. GNMAs, for which repayment of principal is backed by the full faith and credit of the US government, also provided attractive returns for the full period, helped by a declining rate environment and modest prepayments on underlying mortgages.

During the 12-month period ended December 31, 2010, the Fund provided a total return of 6.61% (Class A shares, unadjusted for contract charges), compared with the 6.67% return of its benchmark, the Barclays Capital GNMA Index.

During the year, investors tried to balance the potential impact of very low interest rates on mortgage prepayments against the implications of a tighter lending climate following the financial crisis and downturn in housing prices. The Fund held certain specified pools of seasoned and low-balance mortgages with favorable prepayment characteristics that held up well in the uncertain environment for mortgage-backed securities. We also had significant exposure to longer-duration mortgages, which performed well as interest rates continued to decline for most of the period. The Fund's exposure to higher-interest-rate mortgages was less favorable for relative performance. These issues trade at a premium, and trading in them was particularly impacted by proposals that emerged to enable underwater homeowners to prepay mortgages at par and refinance at lower rates. With refinancing continuing to be difficult for many homeowners, given underwater mortgages and tightened lending standards, we remain comfortable with our overall focus on generating income by holding bonds with higher coupons and steady cash flows. We will continue to closely monitor the refinancing environment and various policy proposals with the potential to increase prepayments. With 30-year mortgage rates still near historically low levels, we will continue to look for opportunities to add floating-rate issues where we can find attractive pricing and other ways to position the Fund ahead of an eventual rise in interest rates.

William Chepolis, CFA
*Co-Manager*

Ohn Choe, CFA
John D. Ryan
*Portfolio Managers*

*The Barclays Capital GNMA Index is an unmanaged, market-value-weighted measure of all fixed-rate securities backed by mortgage pools of the Government National Mortgage Association.*

*Index returns, unlike fund returns, do not reflect any fees or expenses. It is not possible to invest directly into an index.*

1 *The federal funds rate is the interest rate, set by the US Federal Reserve, at which banks lend money to each other, usually on an overnight basis.*

*Portfolio management market commentary is as of December 31, 2010, and may not come to pass. This information is subject to change at any time based on market and other conditions. Past performance does not guarantee future results. Current and future portfolio holdings are subject to risk.*

# Portfolio Summary

## DWS Government & Agency Securities VIP

| **Asset Allocation** (As a % of Investment Portfolio) | **12/31/10** | **12/31/09** |
|---|---|---|
| Mortgage-Backed Securities Pass-Throughs | 69% | 70% |
| Collateralized Mortgage Obligation | 15% | 16% |
| Government & Agency Obligations | 14% | 10% |
| Cash Equivalents | 2% | 4% |
| | 100% | 100% |

| **Coupons*** | **12/31/10** | **12/31/09** |
|---|---|---|
| Less than 4.5% | 4% | 18% |
| 4.5%–5.49% | 50% | 29% |
| 5.5%–6.49% | 40% | 42% |
| 6.5%–7.49% | 4% | 6% |
| 7.5% and Greater | 2% | 5% |
| | 100% | 100% |

| **Interest Rate Sensitivity** | **12/31/10** | **12/31/09** |
|---|---|---|
| Effective Maturity | 5.9 years | 5.7 years |
| Effective Duration | 5.0 years | 4.6 years |

* *Excludes Cash Equivalents, Securities Lending Collateral and US Treasury Bills.*

*Asset allocation, coupons and interest rate sensitivity are subject to change.*

*Effective maturity is the weighted average of the bonds held by the Fund taking into consideration any maturity shortening features.*

*Effective duration is an approximate measure of the Fund's sensitivity to interest rate changes taking into consideration any maturity shortening features.*

*For more complete details about the Fund's investment portfolio, see page 6.*

Following the Fund's fiscal first and third quarter-end, a complete portfolio holdings listing is filed with the SEC on Form N-Q. The form will be available on the SEC's Web site at www.sec.gov, and it also may be reviewed and copied at the SEC's Public Reference Room in Washington, D.C. Information on the operation of the SEC's Public Reference Room may be obtained by calling (800) SEC-0330. The Fund's portfolio holdings are also posted on www.dws-investments.com from time to time. Please see the Fund's current prospectus for more information.

## DWS Government & Agency Securities VIP

| | Principal Amount ($) | Value ($) |
|---|---|---|
| **Mortgage-Backed Securities Pass-Throughs 83.3%** | | |
| Federal Home Loan Mortgage Corp.: | | |
| 5.0%, 9/1/2036 (a) | 15,000,000 | 15,732,421 |
| 7.0%, with various maturities from 6/1/2032 until 8/1/2035 | 263,476 | 290,117 |
| Federal National Mortgage Association: | | |
| 4.5%, 12/1/2038 (a) | 10,000,000 | 10,266,406 |
| 5.0%, with various maturities from 10/1/2033 until 4/1/2036 (a) | 14,422,091 | 15,164,163 |
| Government National Mortgage Association: | | |
| 4.5%, with various maturities from 2/15/2039 until 10/15/2040 (a) | 3,438,403 | 3,584,194 |
| 5.0%, with various maturities from 12/15/2032 until 7/15/2040 (a) | 11,397,116 | 12,327,983 |
| 5.5%, with various maturities from 3/15/2029 until 3/20/2040 (a) | 46,206,832 | 49,986,154 |
| 6.0%, with various maturities from 7/15/2014 until 7/20/2039 (a) | 17,397,268 | 19,165,837 |
| 6.5%, with various maturities from 4/15/2031 until 2/15/2039 | 4,575,400 | 5,110,697 |
| 7.0%, with various maturities from 10/15/2026 until 2/20/2039 | 2,685,289 | 3,011,685 |
| 7.5%, with various maturities from 4/15/2026 until 1/15/2037 | 1,095,618 | 1,242,032 |
| **Total Mortgage-Backed Securities Pass-Throughs** (Cost $130,051,803) | | **135,881,689** |
| **Collateralized Mortgage Obligations 18.2%** | | |
| Fannie Mae Benchmark Remic, "ZA", Series 2007-B2, 5.5%, 6/25/2037 | 1,704,216 | 1,790,925 |
| Federal Home Loan Mortgage Corp.: | | |
| "OA", Series 3179, Principal Only, Zero Coupon, 7/15/2036 | 904,810 | 784,239 |
| "FO", Series 2418, 1.16%*, 2/15/2032 | 529,262 | 539,639 |
| "FA", Series 2419, 1.26%*, 2/15/2032 | 442,297 | 452,259 |
| "FA", Series 2436, 1.26%*, 3/15/2032 | 441,110 | 450,889 |
| "NI", Series 3657, Interest Only, 4.5%, 8/15/2027 | 2,467,460 | 271,639 |
| "ZK", Series 3382, 5.0%, 7/15/2037 | 1,166,312 | 1,201,332 |
| "22", Series 243, Interest Only, 5.325%**, 6/15/2021 | 2,429,666 | 301,574 |
| "PI", Series 2535, Interest Only, 6.0%, 9/15/2032 | 1,075,492 | 82,363 |
| "S17", Series 244, Interest Only, 6.19%**, 12/15/2036 | 3,774,462 | 480,009 |
| "WS", Series 2877, Interest Only, 6.34%**, 10/15/2034 | 1,106,464 | 94,741 |
| "A", Series 172, Interest Only, 6.5%, 1/1/2024 | 50,339 | 9,913 |
| "ST", Series 2411, Interest Only, 8.49%**, 6/15/2021 | 2,413,469 | 379,237 |
| Federal National Mortgage Association: | | |
| "FA", Series G92-53, 1.031%*, 9/25/2022 | 1,291,456 | 1,307,589 |
| "OF", Series 2001-60, 1.211%*, 10/25/2031 | 223,599 | 227,868 |
| "FB", Series 2002-30, 1.261%*, 8/25/2031 | 485,528 | 496,408 |
| "FG", Series 2002-66, 1.261%*, 9/25/2032 | 753,586 | 770,257 |
| "25", Series 351, Interest Only, 4.5%, 5/1/2019 | 510,823 | 54,370 |
| "HI", Series 2009-77, Interest Only, 4.5%, 9/25/2027 | 2,152,932 | 234,077 |
| "20", Series 334, Interest Only, 5.0%, 3/1/2018 | 373,251 | 38,881 |
| "21", Series 334, Interest Only, 5.0%, 3/1/2018 | 248,750 | 26,378 |
| ''23", Series 339, Interest Only, 5.0%, 7/1/2018 | 522,209 | 55,150 |
| "ZA", Series 2008-24, 5.0%, 4/25/2038 | 602,220 | 618,402 |
| "PI", Series 2009-14, Interest Only, 5.5%, 3/25/2024 | 1,843,156 | 226,232 |
| "ZQ", Series G93-39, 6.5%, 12/25/2023 | 457,372 | 502,399 |
| "SA", Series G92-57, IOette, 82.35%**, 10/25/2022 | 71,607 | 146,159 |
| Government National Mortgage Association: | | |
| "FB", Series 2001-28, 0.761%*, 6/16/2031 | 491,847 | 496,021 |
| "HI", Series 2010-H06, Interest Only, 1.15%**, 4/20/2060 | 1,022,799 | 49,913 |
| "BI", Series 2010-H01, Interest Only, 1.596%**, 1/20/2060 | 1,988,409 | 147,938 |
| "HI", Series 2010-H21, Interest Only, 1.785%**, 10/20/2060 | 2,048,263 | 166,589 |
| "FI", Series 2009-H01, Interest Only, 1.796%**, 11/20/2059 | 1,998,548 | 153,688 |
| "JY", Series 2010-20, 4.0%, 12/20/2033 | 1,786,472 | 1,647,685 |
| "LI", Series 2009-104, Interest Only, 4.5%, 12/16/2018 | 587,403 | 63,474 |
| "NI", Series 2010-44, Interest Only, 4.5%, 10/20/2037 | 963,539 | 140,720 |
| "CI", Series 2010-87, Interest Only, 4.5%, 11/20/2038 | 1,251,588 | 374,586 |
| "VB", Series 2010-26, 5.0%, 1/20/2024 | 600,000 | 641,071 |
| "KE", Series 2004-19, 5.0%, 3/16/2034 | 500,000 | 520,213 |
| "ZM", Series 2004-24, 5.0%, 4/20/2034 | 2,091,969 | 2,212,195 |
| "Z", Series 2004-61, 5.0%, 8/16/2034 | 1,028,732 | 1,030,343 |
| "LE", Series 2004-87, 5.0%, 10/20/2034 | 1,000,000 | 1,050,448 |
| "ZB", Series 2005-15, 5.0%, 2/16/2035 | 1,471,630 | 1,553,900 |
| "GZ", Series 2005-24, 5.0%, 3/20/2035 | 446,319 | 421,792 |
| "ZA", Series 2005-75, 5.0%, 10/16/2035 | 502,101 | 505,910 |

*The accompanying notes are an integral part of the financial statements.*

| | Principal Amount ($) | Value ($) |
|---|---|---|
| "CK", Series 2007-31, 5.0%, 5/16/2037 | 1,000,000 | 1,063,979 |
| "MZ", Series 2009-98, 5.0%, 10/16/2039 | 900,949 | 918,669 |
| "AI", Series 2008-46, Interest Only, 5.5%, 5/16/2023 | 563,141 | 70,675 |
| "AI", Series 2008-51, Interest Only, 5.5%, 5/16/2023 | 1,178,100 | 142,207 |
| "GI", Series 2003-19, Interest Only, 5.5%, 3/16/2033 | 1,090,909 | 223,861 |
| "ZA", Series 2006-7, 5.5%, 2/20/2036 | 2,216,333 | 2,382,304 |
| "IB", Series 2010-130, Interest Only, 5.5%, 2/20/2038 | 2,858,860 | 169,796 |
| "NZ", Series 2009-65, 5.5%, 8/20/2039 | 357,202 | 377,085 |
| "KZ", Series 2009-78, 5.5%, 9/16/2039 | 327,726 | 334,509 |
| "DI", Series 2009-10, Interest Only, 6.0%, 4/16/2038 | 577,014 | 86,183 |
| "PY", Series 2009-122, 6.0%, 12/20/2039 | 650,888 | 701,828 |
| "SJ", Series 2004-22, Interest Only, 6.339%**, 4/20/2034 | 590,550 | 4,362 |
| "SA", Series 2006-47, Interest Only, 6.539%**, 8/16/2036 | 400,205 | 65,259 |
| "SM", Series 2004-49, Interest Only, 6.889%**, 1/20/2034 | 1,154,062 | 129,137 |
| "IC", Series 1997-4, Interest Only, 7.5%, 3/16/2027 | 922,676 | 217,810 |
| "SA", Series 1999-30, Interest Only, 7.739%**, 4/16/2029 | 698,263 | 71,332 |
| **Total Collateralized Mortgage Obligations** (Cost $27,327,105) | | **29,678,411** |

| | Principal Amount ($) | Value ($) |
|---|---|---|
| **Government & Agency Obligations 17.0%** | | |
| **Other Government Related 2.3%** | | |
| Citibank NA, FDIC Guaranteed, 0.316%*, 5/7/2012 | 2,800,000 | 2,802,274 |
| JPMorgan Chase & Co.: | | |
| FDIC Guaranteed, 0.532%*, 6/15/2012 | 537,000 | 538,852 |
| Series 3, FDIC Guaranteed, 0.553%*, 12/26/2012 | 463,000 | 465,349 |
| | | **3,806,475** |
| **US Government Sponsored Agency 12.5%** | | |
| Federal Home Loan Bank, 5.0%, 11/17/2017 | 18,000,000 | **20,407,428** |
| **US Treasury Obligations 2.2%** | | |
| US Treasury Bill, 0.185%***, 3/17/2011 (b) | 1,045,000 | 1,044,767 |
| US Treasury Note, 0.875%, 2/29/2012 | 2,500,000 | 2,514,550 |
| | | **3,559,317** |
| **Total Government & Agency Obligations** (Cost $27,820,256) | | **27,773,220** |

| | Shares | Value ($) |
|---|---|---|
| **Cash Equivalents 2.5%** | | |
| Central Cash Management Fund, 0.19% (c) (Cost $3,978,480) | 3,978,480 | **3,978,480** |

| | % of Net Assets | Value ($) |
|---|---|---|
| **Total Investment Portfolio** (Cost $189,177,644)† | 121.0 | **197,311,800** |
| **Other Assets and Liabilities, Net** | (21.0) | **(34,184,750)** |
| **Net Assets** | 100.0 | **163,127,050** |

* *These securities are shown at their current rate as of December 31, 2010. Floating rate securities' yields vary with a designated market index or market rate, such as the coupon-equivalent of the US Treasury bill rate.*

** *These securities are shown at their current rate as of December 31, 2010.*

*** *Annualized yield at time of purchase; not a coupon rate.*

† *The cost for federal income tax purposes was $189,177,684. At December 31, 2010, net unrealized appreciation for all securities based on tax cost was $8,134,116. This consisted of aggregate gross unrealized appreciation for all securities in which there was an excess of value over tax cost of $8,765,237 and aggregate gross unrealized depreciation for all securities in which there was an excess of tax cost over value of $631,121.*

(a) *When-issued or delayed delivery securities included.*

(b) *At December 31, 2010, this security has been pledged, in whole or in part, to cover initial margin requirements for open futures contracts.*

(c) *Affiliated fund managed by Deutsche Investment Management Americas Inc. The rate shown is the annualized seven-day yield at period end.*

*FDIC: Federal Deposit Insurance Corp.*

*Interest Only: Interest Only (IO) bonds represent the "interest only" portion of payments on a pool of underlying mortgages or mortgage-backed securities. IO securities are subject to prepayment risk of the pool of underlying mortgages.*

*IOettes: These securities represent the right to receive interest payments on an underlying pool of mortgages with similar features as those associated with IO securities. Unlike IO's, a nominal amount of principal is assigned to an IOette which is small in relation to the interest flow that constitutes almost all of the IOette cash flow. The effective yield of this security is lower than the stated interest rate.*

*Principal Only: Principal Only (PO) bonds represent the "principal only" portion of payments on a pool of underlying mortgages or mortgage-backed securities.*

*Included in the portfolio are investments in mortgage or asset-backed securities which are interests in separate pools of mortgages or assets. Effective maturities of these investments may be shorter than stated maturities due to prepayments. Some separate investments in the Federal Home Loan Mortgage Corp., Federal National Mortgage Association and Government National Mortgage Association issues which have similar coupon rates have been aggregated for presentation purposes in this investment portfolio.*

*The accompanying notes are an integral part of the financial statements.*

*At December 31, 2010, open futures contracts purchased were as follows:*

| Futures | Currency | Expiration Date | Contracts | Notional Value ($) | Unrealized Depreciation ($) |
|---|---|---|---|---|---|
| Ultra Long Term US Treasury Bond | USD | 3/22/2011 | 18 | 2,287,688 | **(64,828)** |

*At December 31, 2010, open futures contracts sold were as follows:*

| Futures | Currency | Expiration Date | Contracts | Notional Value ($) | Unrealized Depreciation ($) |
|---|---|---|---|---|---|
| 10 Year US Treasury Note | USD | 3/22/2011 | 119 | 14,332,063 | **(80,855)** |

| Currency Abbreviation | |
|---|---|
| USD | United States Dollar |

*At December 31, 2010, open interest rate swap contracts were as follows:*

| Effective/ Expiration Dates | Notional Amount ($) | Cash Flows Paid by the Fund | Cash Flows Received by the Fund | Value ($) | Upfront Payments Paid/ (Received) ($) | Unrealized Depreciation ($) |
|---|---|---|---|---|---|---|
| 10/28/2010<br>10/28/2025 | 320,000[1] | Floating — LIBOR | Floating — 4.138%[††] | (10,086) | — | (10,086) |
| 11/1/2010<br>11/1/2025 | 540,000[2] | Floating — LIBOR | Floating — 4.292%[††] | (48,753) | — | (48,753) |
| 11/12/2010<br>11/12/2025 | 640,000[1] | Floating — LIBOR | Floating — 4.285%[††] | (18,640) | — | (18,640) |
| 11/15/2010<br>11/15/2025 | 640,000[2] | Floating — LIBOR | Floating — 4.585%[††] | (53,840) | — | (53,840) |
| 11/16/2010<br>11/16/2025 | 320,000[1] | Floating — LIBOR | Floating — 4.584%[††] | (6,437) | — | (6,437) |
| 11/19/2010<br>11/19/2025 | 320,000[2] | Floating — LIBOR | Floating — 4.784%[††] | (25,396) | — | (25,396) |
| 11/23/2010<br>11/23/2025 | 150,000[1] | Floating — LIBOR | Floating — 4.834%[††] | (1,981) | — | (1,981) |
| **Total unrealized depreciation** | | | | | | **(165,133)** |

†† *These interest rate swaps are shown at their current rate as of December 31, 2010.*

*At December 31, 2010, open total return swap contracts were as follows:*

| Effective/ Expiration Date | Notional Amount ($) | Fixed Cash Flows Paid | Reference Entity | Value ($) | Upfront Payments Paid/ (Received) ($) | Unrealized Appreciation ($) |
|---|---|---|---|---|---|---|
| 5/28/2010<br>6/1/2012 | 6,900,000[3] | 0.45% | Citi Global Interest Rate Strategy Index | 11,198 | 4,600 | **6,598** |

*Counterparties:*

1 *Morgan Stanley*

2 *Barclays Capital Securities, Inc.*

3 *Citigroup, Inc.*

*LIBOR: London InterBank Offered Rate*

*For information on the Fund's policy and additional disclosures regarding futures contracts, interest rate swap contracts and total return swap contracts, please refer to the Derivatives section of Note B in the accompanying Notes to Financial Statements.*

*The accompanying notes are an integral part of the financial statements.*

## Fair Value Measurements

*Various inputs are used in determining the value of the Fund's investments. These inputs are summarized in three broad levels. Level 1 includes quoted prices in active markets for identical securities. Level 2 includes other significant observable inputs (including quoted prices for similar securities, interest rates, prepayment speeds, and credit risk). Level 3 includes significant unobservable inputs (including the Fund's own assumptions in determining the fair value of investments). The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities.*

*The following is a summary of the inputs used as of December 31, 2010 in valuing the Fund's investments. For information on the Fund's policy regarding the valuation of investments, please refer to the Security Valuation section of Note A in the accompanying Notes to Financial Statements.*

| **Assets** | **Level 1** | **Level 2** | **Level 3** | **Total** |
|---|---|---|---|---|
| Fixed-Income Investments (d) | | | | |
| Mortgage-Backed Securities Pass-Throughs | $ — | $ 135,881,689 | $ — | $ 135,881,689 |
| Collateralized Mortgage Obligations | — | 29,160,283 | 518,128 | 29,678,411 |
| Government & Agency Obligations | — | 26,728,453 | — | 26,728,453 |
| Short-Term Investments | 3,978,480 | 1,044,767 | — | 5,023,247 |
| Derivatives (e) | — | 6,598 | — | 6,598 |
| **Total** | **$ 3,978,480** | **$ 192,821,790** | **$ 518,128** | **$ 197,318,398** |
| **Liabilities** | | | | |
| Derivatives (e) | $ (145,683) | $ (165,133) | $ — | $ (310,816) |
| **Total** | **$ (145,683)** | **$ (165,133)** | **$ —** | **$ (310,816)** |

*There have been no significant transfers between Level 1 and Level 2 fair value measurements during the year ended December 31, 2010.*

(d) *See Investment Portfolio for additional detailed categorizations.*

(e) *Derivatives include unrealized appreciation (depreciation) on open futures contracts, interest rate swap contracts and total return swap contracts.*

## Level 3 Reconciliation

*The following is a reconciliation of the Fund's Level 3 investments for which significant unobservable inputs were used in determining value:*

| | **Collateralized Mortgage Obligations** | **Government & Agency Obligations** | **Total** |
|---|---|---|---|
| **Balance as of December 31, 2009** | $ 135,301 | $ 523,600 | **$ 658,901** |
| Realized gains (loss) | (2,253) | — | **(2,253)** |
| Change in unrealized appreciation (depreciation) | 44,476 | 36,400 | **80,876** |
| Amortization premium/discount | (30,311) | — | **(30,311)** |
| Net purchases (sales) | 370,915 | (560,000) | **(189,085)** |
| Transfers into Level 3 | — | — | **—** |
| Transfers (out) of Level 3 | — | — | **—** |
| **Balance as of December 31, 2010** | **$ 518,218** | **$ —** | **$ 518,218** |
| **Net change in unrealized appreciation (depreciation) from investments still held as of December 31, 2010** | **$ 44,476** | **$ —** | **$ 44,476** |

*Transfers between price levels are recognized at the beginning of the reporting period.*

*The accompanying notes are an integral part of the financial statements.*

## Statement of Assets and Liabilities

as of December 31, 2010

| Assets | | |
|---|---|---|
| Investments | | |
| Investments in unaffiliated securities, at value (cost $185,199,164) | $ | 193,333,320 |
| Investment in Central Cash Management Fund (cost $3,978,480) | | 3,978,480 |
| Total investments, at value (cost $189,177,644) | | 197,311,800 |
| Cash | | 11,209 |
| Receivable for when-issued and delayed delivery securities sold | | 62,105,877 |
| Receivable for Fund shares sold | | 82 |
| Unrealized appreciation on open swap contracts | | 6,598 |
| Upfront payments paid on open swap contracts | | 4,600 |
| Interest receivable | | 663,286 |
| Other assets | | 1,039 |
| Total assets | | 260,104,491 |

| Liabilities | | |
|---|---|---|
| Payable for when-issued and delayed delivery securities purchased | | 96,492,907 |
| Payable for Fund shares redeemed | | 122,653 |
| Payable for daily variation margin on open futures contracts | | 22,421 |
| Unrealized depreciation on open swap contracts | | 165,133 |
| Accrued management fee | | 64,314 |
| Other accrued expenses and payables | | 110,013 |
| Total liabilities | | 96,977,441 |
| **Net assets, at value** | **$** | **163,127,050** |

| Net Assets Consist of | | |
|---|---|---|
| Undistributed net investment income | | 6,521,765 |
| Net unrealized appreciation (depreciation) on: | | |
| Investments | | 8,134,156 |
| Futures | | (145,683) |
| Swap contracts | | (158,535) |
| Accumulated net realized gain (loss) | | 2,570,629 |
| Paid-in capital | | 146,204,718 |
| **Net assets, at value** | **$** | **163,127,050** |
| **Class A** | | |
| **Net Asset Value,** offering and redemption price per share ($157,270,905 ÷ 12,120,178 outstanding shares of beneficial interest, no par value, unlimited number of shares authorized) | **$** | **12.98** |
| **Class B** | | |
| **Net Asset Value,** offering and redemption price per share ($5,856,145 ÷ 452,192 outstanding shares of beneficial interest, no par value, unlimited number of shares authorized) | **$** | **12.95** |

## Statement of Operations

for the year ended December 31, 2010

| Investment Income | | |
|---|---|---|
| Income: | | |
| Interest | $ | 7,879,825 |
| Income distributions — Central Cash Management Fund | | 11,105 |
| Total income | | 7,890,930 |
| Expenses: | | |
| Management fee | | 789,612 |
| Administration fee | | 175,469 |
| Services to shareholders | | 2,747 |
| Distribution service fee (Class B) | | 15,782 |
| Record keeping fees (Class B) | | 6,123 |
| Custodian fee | | 19,184 |
| Legal fees | | 10,450 |
| Audit and tax fees | | 67,125 |
| Trustees' fees and expenses | | 8,731 |
| Reports to shareholders | | 21,188 |
| Other | | 30,423 |
| Total expenses | | 1,146,834 |
| **Net investment income** | | **6,744,096** |

| Realized and Unrealized Gain (Loss) | | |
|---|---|---|
| Net realized gain (loss) from: | | |
| Investments | | 2,806,212 |
| Futures | | 950,817 |
| Written options | | 87,625 |
| Swap contracts | | (659,466) |
| | | 3,185,188 |
| Change in net unrealized appreciation (depreciation) on: | | |
| Investments | | 1,027,186 |
| Futures | | 475,938 |
| Swap contracts | | (95,677) |
| | | 1,407,447 |
| **Net gain (loss)** | | **4,592,635** |
| **Net increase (decrease) in net assets resulting from operations** | **$** | **11,336,731** |

*The accompanying notes are an integral part of the financial statements.*

# Statement of Changes in Net Assets

| Increase (Decrease) in Net Assets | Years Ended December 31, 2010 | 2009 |
|---|---|---|
| Operations: | | |
| Net investment income | $ 6,744,096 | $ 8,168,646 |
| Net realized gain (loss) | 3,185,188 | 2,256,128 |
| Change in net unrealized appreciation (depreciation) | 1,407,447 | 5,187,713 |
| Net increase (decrease) in net assets resulting from operations | 11,336,731 | 15,612,487 |
| Distributions to shareholders from: | | |
| Net investment income: | | |
| Class A | (7,785,441) | (9,576,836) |
| Class B | (277,185) | (337,035) |
| Total distributions | (8,062,626) | (9,913,871) |
| Fund share transactions: | | |
| **Class A** | | |
| Proceeds from shares sold | 38,574,553 | 23,250,916 |
| Reinvestment of distributions | 7,785,441 | 9,576,836 |
| Payments for shares redeemed | (61,339,038) | (80,587,867) |
| Net increase (decrease) in net assets from Class A share transactions | (14,979,044) | (47,760,115) |
| **Class B** | | |
| Proceeds from shares sold | 653,336 | 1,821,403 |
| Reinvestment of distributions | 277,185 | 337,035 |
| Payments for shares redeemed | (1,704,050) | (3,752,537) |
| Net increase (decrease) in net assets from Class B share transactions | (773,529) | (1,594,099) |
| **Increase (decrease) in net assets** | (12,478,468) | (43,655,598) |
| Net assets at beginning of period | 175,605,518 | 219,261,116 |
| Net assets at end of period (including undistributed net investment income of $6,521,765 and $7,761,196, respectively) | **$ 163,127,050** | **$ 175,605,518** |

| Other Information | 2010 | 2009 |
|---|---|---|
| **Class A** | | |
| Shares outstanding at beginning of period | 13,231,519 | 17,044,556 |
| Shares sold | 2,996,102 | 1,856,164 |
| Shares issued to shareholders in reinvestment of distributions | 623,833 | 788,217 |
| Shares redeemed | (4,731,276) | (6,457,418) |
| Net increase (decrease) in Class A shares | (1,111,341) | (3,813,037) |
| Shares outstanding at end of period | **12,120,178** | **13,231,519** |
| **Class B** | | |
| Shares outstanding at beginning of period | 510,999 | 639,523 |
| Shares sold | 50,683 | 144,579 |
| Shares issued to shareholders in reinvestment of distributions | 22,193 | 27,739 |
| Shares redeemed | (131,683) | (300,842) |
| Net increase (decrease) in Class B shares | (58,807) | (128,524) |
| Shares outstanding at end of period | **452,192** | **510,999** |

*The accompanying notes are an integral part of the financial statements.*

# Financial Highlights

## Class A

| Years Ended December 31, | 2010 | 2009 | 2008 | 2007 | 2006 |
|---|---|---|---|---|---|
| **Selected Per Share Data** | | | | | |
| **Net asset value, beginning of period** | **$12.78** | **$12.40** | **$12.38** | **$12.28** | **$12.26** |
| *Income (loss) from investment operations:* | | | | | |
| Net investment income[a] | .50 | .52 | .56 | .58 | .55 |
| Net realized and unrealized gain (loss) | .32 | .45 | .04 | .12 | (.06) |
| **Total from investment operations** | .82 | .97 | .60 | .70 | .49 |
| *Less distributions from:* | | | | | |
| Net investment income | (.62) | (.59) | (.58) | (.60) | (.47) |
| **Net asset value, end of period** | **$12.98** | **$12.78** | **$12.40** | **$12.38** | **$12.28** |
| Total Return (%) | 6.61 | 8.08 | 4.93[b] | 5.95[b] | 4.16 |
| **Ratios to Average Net Assets and Supplemental Data** | | | | | |
| Net assets, end of period ($ millions) | 157 | 169 | 211 | 199 | 211 |
| Ratio of expenses before expense reductions (%) | .64 | .58 | .66 | .66 | .67 |
| Ratio of expenses after expense reductions (%) | .64 | .58 | .65 | .63 | .67 |
| Ratio of net investment income (%) | 3.86 | 4.16 | 4.58 | 4.77 | 4.56 |
| Portfolio turnover rate (%) | 423 | 390 | 543 | 465 | 241 |

[a] *Based on average shares outstanding during the period.*

[b] *Total return would have been lower had certain expenses not been reduced.*

## Class B

| Years Ended December 31, | 2010 | 2009 | 2008 | 2007 | 2006 |
|---|---|---|---|---|---|
| **Selected Per Share Data** | | | | | |
| **Net asset value, beginning of period** | **$12.75** | **$12.37** | **$12.35** | **$12.25** | **$12.23** |
| *Income (loss) from investment operations:* | | | | | |
| Net investment income[a] | .46 | .48 | .52 | .53 | .50 |
| Net realized and unrealized gain (loss) | .31 | .45 | .03 | .12 | (.06) |
| **Total from investment operations** | .77 | .93 | .55 | .65 | .44 |
| *Less distributions from:* | | | | | |
| Net investment income | (.57) | (.55) | (.53) | (.55) | (.42) |
| **Net asset value, end of period** | **$12.95** | **$12.75** | **$12.37** | **$12.35** | **$12.25** |
| Total Return (%) | 6.24 | 7.70 | 4.60[b] | 5.43[b] | 3.74 |
| **Ratios to Average Net Assets and Supplemental Data** | | | | | |
| Net assets, end of period ($ millions) | 6 | 7 | 8 | 5 | 33 |
| Ratio of expenses before expense reductions (%) | .99 | .92 | 1.00 | 1.04 | 1.07 |
| Ratio of expenses after expense reductions (%) | .99 | .92 | 1.00 | 1.01 | 1.07 |
| Ratio of net investment income (%) | 3.51 | 3.81 | 4.24 | 4.39 | 4.16 |
| Portfolio turnover rate (%) | 423 | 390 | 543 | 465 | 241 |

[a] *Based on average shares outstanding during the period.*

[b] *Total return would have been lower had certain expenses not been reduced.*

# Notes to Financial Statements

## A. Organization and Significant Accounting Policies

DWS Variable Series II (the "Trust") is registered under the Investment Company Act of 1940, as amended (the "1940 Act"), as an open-end management investment company organized as a Massachusetts business trust. The Trust offers seventeen funds (hereinafter referred to individually as "Fund" or collectively as "Funds"). The Fund is classified as a diversified open-end management investment company.

**Multiple Classes of Shares of Beneficial Interest.** Certain Funds of the Trust offer two classes of shares (Class A shares and Class B shares). Sales of Class B shares are subject to record keeping fees up to 0.15% and Rule 12b-1 fees under the 1940 Act equal to an annual rate of 0.25%, of the average daily net assets of the Class B shares of the applicable Fund. Class A shares are not subject to such fees.

Investment income, realized and unrealized gains and losses, and certain fund-level expenses and expense reductions, if any, are borne pro rata on the basis of relative net assets by the holders of all classes of shares except that each class bears certain expenses unique to that class (including the applicable Rule 12b-1 fee and record keeping fees). Differences in class-level expenses may result in payment of different per share dividends by class. All shares have equal rights with respect to voting subject to class-specific arrangements.

The Trust's financial statements are prepared in accordance with accounting principles generally accepted in the United States of America which require the use of management estimates. Actual results could differ from those estimates. The policies described below are followed consistently by the Trust in the preparation of its financial statements.

**Security Valuation.** Investments are stated at value determined as of the close of regular trading on the New York Stock Exchange on each day the exchange is open for trading.

Various inputs are used in determining the value of the Fund's investments. These inputs are summarized in three broad levels. Level 1 includes quoted prices in active markets for identical securities. Level 2 includes other significant observable inputs (including quoted prices for similar securities, interest rates, prepayment speeds, and credit risk). Level 3 includes significant unobservable inputs (including the Fund's own assumptions in determining the fair value of investments). The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities.

Debt securities are valued by independent pricing services approved by the Fund's Board. If the pricing services are unable to provide valuations, securities are valued at the most recent bid quotation or evaluated price, as applicable, obtained from one or more broker-dealers. Such services may use various pricing techniques which take into account appropriate factors such as yield, quality, coupon rate, maturity, type of issue, trading characteristics and other data, as well as broker quotes. These securities are generally categorized as Level 2.

Futures contracts are generally valued at the settlement prices established each day on the exchange on which they are traded and are categorized as Level 1.

Swap contracts are valued daily based upon prices supplied by a Board approved pricing vendor, if available, and otherwise are valued at the price provided by the broker-dealer. Swap contracts are generally categorized as Level 2.

Exchange-traded options are valued at the last sale price or, in the absence of a sale, the mean between the closing bid and asked prices or at the most recent asked price (bid for purchased options) if no bid or asked price are available. Exchange-traded options are categorized as Level 1. Over-the-counter written or purchased options are valued based upon a price provided by the broker-dealer with which the option, was traded and are generally categorized as Level 3.

Money market instruments purchased with an original or remaining maturity of sixty days or less, maturing at par, are valued at amortized cost, which approximates value, and are categorized as Level 2. Investments in open-end investment companies are valued at their net asset value each business day and are categorized as Level 1.

Securities and other assets for which market quotations are not readily available or for which the above valuation procedures are deemed not to reflect fair value are valued in a manner that is intended to reflect their fair value as determined in accordance with procedures approved by the Board and are generally categorized as Level 3. In accordance with the Fund's valuation procedures, factors used in determining value may include, but are not limited to, the type of the security; the size of the holding; the initial cost of the security; the existence of any contractual restrictions on the security's disposition; the price and extent of public trading in similar securities of the issuer or of comparable companies; quotations or evaluated prices from broker-dealers and/or pricing services; information obtained from the issuer, analysts, and/or the appropriate stock exchange (for exchange-traded securities); an analysis of the company's or issuer's financial statements; an evaluation of the forces that influence the issuer and the market(s) in which the security is purchased and sold and with respect to debt securities; the maturity, coupon, creditworthiness, currency denomination and the movement of the market in which the security is normally traded. The value determined under these procedures may differ from published values for the same securities.

Disclosure about the classification of fair value measurements is included in a table following the Fund's Investment Portfolio.

**Securities Lending.** The Fund lends securities to certain financial institutions. The Fund retains beneficial ownership of the securities it has loaned and continues to receive interest and dividends paid by the issuer of securities and to participate in any changes in their market value. The Fund requires the borrowers of the securities to maintain collateral with the Fund consisting of either cash or liquid, unencumbered assets having a value at least equal to the value of the securities loaned. When the collateral falls below specified amounts, the lending agent will use its best effort to obtain additional collateral on the next business day to meet required amounts under the security lending agreement. The Fund may invest the cash collateral into a joint trading account in an affiliated money market fund pursuant to Exemptive Orders issued by the SEC. The Fund receives compensation for lending its securities either in the form of fees or by earning interest on invested cash collateral net of borrower rebates and fees paid to a lending agent. Either the Fund or the borrower may terminate the loan. There may be risks of delay and costs in recovery of securities or even loss of rights in the collateral should the borrower of the securities fail financially. The Fund is also subject to all investment risks associated with the reinvestment of any cash collateral received, including, but not limited to, interest rate, credit and liquidity risk associated with such investments. The Fund had no securities on loan as of December 31, 2010.

**Mortgage Dollar Rolls.** The Fund may enter into mortgage dollar rolls in which the Fund sells to a bank or broker/dealer (the "counterparty") mortgage-backed securities for delivery in the current month and simultaneously contracts to repurchase similar, but not identical, securities on a fixed date. The counterparty receives all principal and interest payments, including prepayments, made on the security while it is the holder. The Fund receives compensation as consideration for entering into the commitment to repurchase. The compensation is paid in the form of a lower price for the security upon its repurchase, or alternatively, a fee. Mortgage dollar rolls may be renewed with a new sale and repurchase price and a cash settlement made at each renewal without physical delivery of the securities subject to the contract.

Certain risks may arise upon entering into mortgage dollar rolls from the potential inability of counterparties to meet the terms of their commitments. Additionally, the value of such securities may change adversely before the Fund is able to repurchase them. There can be no assurance that the Fund's use of the cash that it receives from a mortgage dollar roll will provide a return that exceeds its costs.

**When-Issued/Delayed Delivery Securities.** The Fund may purchase securities with delivery or payment to occur at a later date beyond the normal settlement period. At the time the Fund enters into a commitment to purchase a security, the transaction is recorded and the value of the security is reflected in the net asset value. The price of such security and the date when the security will be delivered and paid for are fixed at the time the transaction is negotiated. The value of the security may vary with market fluctuations. No interest accrues to the Fund until payment takes place. At the time the Fund enters into this type of transaction it is required to segregate cash or other liquid assets at least equal to the amount of the commitment.

Certain risks may arise upon entering into when-issued or delayed delivery securities from the potential inability of counterparties to meet the terms of their contracts or if the issuer does not issue the securities due to political, economic, or other factors. Additionally, losses may arise due to changes in the value of the underlying securities.

**Taxes.** The Fund's policy is to comply with the requirements of the Internal Revenue Code, as amended, which are applicable to regulated investment companies and to distribute all of its taxable income to its shareholders.

At December 31, 2010, the Fund had an approximate net tax basis capital loss carryforward which may be applied against any realized net taxable capital gains of each succeeding year until fully utilized or until the following expiration dates, whichever occurs first:

| Fund | Capital Loss Carryforward Utilized ($) |
|---|---|
| DWS Government & Agency Securities VIP | 1,158,000 |

The Fund has reviewed the tax positions for the open tax years as of December 31, 2010 and has determined that no provision for income tax is required in the Fund's financial statements. The Fund's federal tax returns for the prior three fiscal years remain open subject to examination by the Internal Revenue Service.

**Distribution of Income and Gains.** Distributions of net investment income of the Fund, if any, are made annually. Net realized gains from investment transactions, in excess of available capital loss carryforwards, would be taxable to the Fund if not distributed and, therefore, will be distributed to shareholders at least annually. The Fund may also make additional distributions for tax purposes if necessary.

The timing and characterization of certain income and capital gains distributions are determined annually in accordance with federal tax regulations which may differ from accounting principles generally accepted in the United States of America. These differences primarily relate to investments in futures contracts, investments in swap contracts and certain securities sold at a loss. As a result, net investment income (loss) and net realized gain (loss) on investment transactions for a reporting period may differ significantly from distributions during such period. Accordingly, the Fund may periodically make reclassifications among certain of its capital accounts without impacting the net asset value of the Fund.

At December 31, 2010, the Fund's components of distributable earnings on a tax basis were as follows:

| Fund | Undistributed Ordinary Income ($)* | Undistributed Net Long-Term Capital gains | Unrealized Appreciation (Depreciation) on Investments ($) |
|---|---|---|---|
| DWS Government & Agency Securities VIP | 7,707,477 | 1,262,738 | 8,134,116 |

In addition, the tax character of distributions paid by the Fund is summarized as follows:

| | Distributions from Ordinary Income ($)* | |
|---|---|---|
| | Years Ended December 31, | |
| Fund | 2010 | 2009 |
| DWS Government & Agency Securities VIP | 8,062,626 | 9,913,871 |

* *For tax purposes, short-term capital gain distributions are considered ordinary income distributions.*

**Expenses.** Expenses of the Trust arising in connection with a specific fund are allocated to that fund. Other Trust expenses which cannot be directly attributed to a fund are apportioned among the funds in the Trust.

**Contingencies.** In the normal course of business, the Fund may enter into contracts with service providers that contain general indemnification clauses. The Fund's maximum exposure under these arrangements is unknown as this would involve future claims that may be made against the Fund that have not yet been made. However, based on experience, the Fund expects the risk of loss to be remote.

**Other.** Investment transactions are accounted for on a trade date plus one basis for daily net asset value calculations. However, for financial reporting purposes, investment transactions are reported on trade date. Interest income is recorded on the accrual basis. Realized gains and losses from investment transactions are recorded on an identified cost basis. All discounts and premiums are accreted/amortized for both tax and financial reporting purposes for the Fund.

## B. Derivative Instruments

**Interest Rate Swap Contracts.** For the year ended December 31, 2010, the Fund entered into interest rate swap transactions to gain exposure to different parts of the yield curve while managing overall duration. The use of interest rate swaps is a highly specialized activity that involves investment techniques and risks different from those associated with ordinary portfolio security transactions. In an interest rate swap, the Fund agrees to pay to the other party to the interest rate swap (which is known as the "counterparty") a fixed rate payment in exchange for the counterparty agreeing to pay to the Fund a variable rate payment, or the Fund agrees to receive from the counterparty a fixed rate payment in exchange for the counterparty agreeing to receive from the Fund a variable rate payment. The payment obligations are based on the notional amount of the swap. Certain risks may arise when entering into swap transactions including counterparty default, liquidity or unfavorable changes in interest rates. In connection with these agreements, securities and or cash may be identified as collateral in accordance with the terms of the swap agreements to provide assets of value and recourse in the event of default. The maximum counterparty credit risk is the net present value of the cash flows to be received from or paid to the counterparty over the term of the interest rate swap contract, to the extent that this amount is beneficial to the Fund, in addition to any related collateral posted to the counterparty by the Fund. This risk may be partially reduced by a master netting arrangement between the Fund and the counterparty. The value of the swap is adjusted daily and the change in value, if any, is recorded as unrealized appreciation or depreciation in the Statement of Assets and Liabilities. An upfront payment made by the Fund is recorded as an asset in the Statement of Assets and Liabilities. An upfront payment received by the Fund is recorded as a liability in the Statement of Assets and Liabilities. Payments received or made at the end of the measurement period are recorded as realized gain or loss in the Statement of Operations.

A summary of the open interest rate swap contracts as of December 31, 2010 is included in a table following the Fund's Investment Portfolio. For the year ended December 31, 2010, the Fund's investment in interest rate swap contracts had a total notional amount generally indicative of a range from approximately $2,930,000 to $12,800,000.

**Total Return Swap Contracts.** Total return swaps involve commitments to pay interest in exchange for a market-linked return based on a notional amount. For the year ended December 31, 2010, the Fund entered into total return swap transactions to enhance potential gain. To the extent the total return of the reference security or index underlying the total return swap exceeds or falls short of the offsetting interest rate obligation, the Fund will receive a payment or make a payment to the counterparty, respectively. Certain risks may arise when entering into swap transactions including counterparty default, liquidity or unfavorable changes in the value of underlying reference security or index. The value of the swap is adjusted daily and the change in value, if any, is recorded as unrealized appreciation or depreciation in the Statement of Assets and Liabilities. An upfront payment made by the Fund is recorded as an asset in the Statement of Assets and Liabilities. An upfront payment received by the Fund is recorded as a liability in the Statement of Assets and Liabilities. Payments received or made at the end of each measurement period are recorded as realized gain or loss in the Statement of Operations.

A summary of the open total return swap contracts as of December 31, 2010 is included in a table following the Fund's Investment Portfolio. For the year ended December 31, 2010, the Fund's investment in total return swap contracts had a total notional amount generally indicative of a range from approximately $6,900,000 to $9,000,000.

**Options.** An option contract is a contract in which the writer (seller) of the option grants the buyer of the option, upon payment of a premium, the right to purchase from (call option), or sell to (put option), the writer a designated instrument at a specified price within a specified period of time. Certain options, including options on indices, will require cash settlement by the Fund if the option is exercised. For the year ended December 31, 2010, the Fund entered into option contracts in order to enhance potential gain.

The liability representing the Fund's obligation under an exchange-traded written option or investment in a purchased option is valued at the last sale price or, in the absence of a sale, the mean between the closing bid and asked prices or at the most recent asked price (bid for purchased options) if no bid and asked price are available. Over-the-counter written or purchased options are valued using dealer-supplied quotations. Gain or loss is recognized when the option contract expires, exercised or is closed.

If the Fund writes a covered call option, the Fund foregoes, in exchange for the premium, the opportunity to profit during the option period from an increase in the market value of the underlying security above the exercise price. If the Fund writes a put option it accepts the risk of a decline in the value of the underlying security below the exercise price. Over-the-counter options have the risk of the potential inability of counterparties to meet the terms of their contracts. The Fund's maximum exposure to purchased options is limited to the premium initially paid. In addition, certain risks may arise upon entering into option contracts including the risk that an illiquid secondary market will limit the Fund's ability to close out an option contract prior to the expiration date and that a change in the value of the option contract may not correlate exactly with changes in the value of the securities or currencies hedged.

There are no open option contracts as of December 31, 2010 for the Fund. During the year ended December 31, 2010, the Fund's investment in written option contracts had a total value generally indicative of a range from $0 to approximately $197,000 and in purchased option contracts had a total value generally indicative of a range from $0 to approximately $49,000.

**Futures Contracts.** A futures contract is an agreement between a buyer or seller and an established futures exchange or its clearinghouse in which the buyer or seller agrees to take or make a delivery of a specific amount of a financial instrument at a specified price on a specific date (settlement date). For the year ended December 31, 2010, the Fund entered into interest rate futures to gain exposure to different parts of the yield curve while managing overall duration.

Futures contracts are valued at the most recent settlement price. Upon entering into a futures contract, the Fund is required to deposit with a financial intermediary cash or securities ("initial margin") in an amount equal to a certain percentage of the face value indicated in the futures contract. Subsequent payments ("variation margin") are made or received by the Fund dependent upon the daily fluctuations in the value and are recorded for financial reporting purposes as unrealized gains or losses by the Fund. Gains or losses are realized when the contract expires or is closed. Since all futures contracts are exchange-traded, counterparty risk is minimized as the exchange's clearinghouse acts as the counterparty, and guarantees the futures against default.

Certain risks may arise upon entering into futures contracts, including the risk that an illiquid market will limit the Fund's ability to close out a futures contract prior to the settlement date and that a change in the value of a futures contract may not correlate exactly with the changes in the value of the underlying hedged security, index or currency. Risk of loss may exceed amounts recognized in the Statement of Assets and Liabilities.

A summary of the open futures contracts as of December 31, 2010 is included in a table following the Fund's Investment Portfolio. For the year ended December 31, 2010, the Fund's investment in futures contracts purchased had a total notional value generally indicative of a range from $0 to approximately $33,947,000, and the Fund's investment in futures contracts sold had a total notional value generally indicative of a range from approximately $14,332,000 to $49,098,000.

The following tables summarize the value of the Fund's derivative instruments held as of December 31, 2010 and the related location in the accompanying Statement of Assets and Liabilities, presented by primary underlying risk exposure:

| **Asset Derivative** | **Swap Contracts** |
|---|---|
| Interest Rate Contracts (a) | $ 6,598 |

*The above derivative is located in the following Statement of Assets and Liabilities account:*

(a) *Unrealized appreciation on open swap contracts*

| **Liability Derivative** | **Futures Contracts** | **Swap Contracts** | **Total** |
|---|---|---|---|
| Interest Rate Contracts (a) | $ (145,683) | $ (165,133) | $ (310,816) |

*Each of the above derivatives is located in the following Statement of Assets and Liabilities accounts:*

(a) *Net unrealized appreciation (depreciation) on futures and unrealized depreciation on open swap contracts. Liability of payable for daily variation margin on open futures contracts reflects unsettled variation margin.*

Additionally, the amount of unrealized and realized gains and losses on derivative instruments recognized in Fund earnings during the year ended December 31, 2010 and the related location in the accompanying Statement of Operations is summarized in the following tables by primary underlying risk exposure:

| **Realized Gain (Loss)** | **Purchased Options** | **Written Options** | **Swap Contracts** | **Futures Contracts** | **Total** |
|---|---|---|---|---|---|
| Interest Rate Contracts (a) | $ (323,210) | $ 87,625 | $ (659,466) | $ 950,817 | $ 55,766 |

*Each of the above derivatives is located in the following Statement of Operations accounts:*

(a) *Net realized gain (loss) from investments (includes purchased options), written options, swap contracts and futures, respectively*

| **Change in Net Unrealized Appreciation (Depreciation)** | **Swap Contracts** | **Futures Contracts** | **Total** |
|---|---|---|---|
| Interest Rate Contracts (a) | $ (95,677) | $ 475,938 | $ 380,261 |

*Each of the above derivatives is located in the following Statement of Operations accounts:*

(a) *Change in net unrealized appreciation (depreciation) on swap contracts and futures, respectively*

## C. Purchases and Sales of Securities

During the year ended December 31, 2010, purchases and sales of investment transactions (excluding short-term investments) were as follows:

| **Fund** | **Purchases ($)** | **Sales ($)** |
|---|---|---|
| DWS Government & Agency Securities VIP | 814,547,329 | 814,973,550 |

For the year ended December 31, 2010, transactions for written options on futures were as follows:

| | **Number of Contracts** | **Premiums** |
|---|---|---|
| Outstanding, beginning of period | — | $ — |
| Options written | 636 | 202,702 |
| Options closed | (120) | (65,361) |
| Options exercised | (256) | (105,437) |
| Options expired | (260) | (31,904) |
| Outstanding, end of period | **—** | **$ —** |

## D. Related Parties

**Management Agreement.** Under the Investment Management Agreement with Deutsche Investment Management Americas Inc. ("DIMA" or the "Advisor"), an indirect, wholly owned subsidiary of Deutsche Bank

AG, the Advisor directs the investments of the Fund in accordance with its investment objectives, policies and restrictions. The Advisor determines the securities, instruments and other contracts relating to investments to be purchased, sold or entered into by the Fund.

Under the Investment Management Agreement with the Advisor, the fee is equivalent to the annual rates shown below of the Fund's average daily net assets, computed and accrued daily and payable monthly:

| Fund | Annual Management Fee Rate |
|---|---|
| DWS Government & Agency Securities VIP | |
| $0–$250 million | .450% |
| next $750 million | .430% |
| next $1.5 billion | .410% |
| next $2.5 billion | .400% |
| next $2.5 billion | .380% |
| next $2.5 billion | .360% |
| next $2.5 billion | .340% |
| over $12.5 billion | .320% |

Accordingly, for the year ended December 31, 2010, the total management fee and effective management fee rate were as follows:

| Fund | Total Aggregated ($) | Annual Effective Rate |
|---|---|---|
| DWS Government & Agency Securities VIP | 789,612 | .45% |

**Administration Fee.** Pursuant to an Administrative Services Agreement, DIMA provides most administrative services to the Fund. For all services provided under the Administrative Services Agreement, the Fund pays DIMA an annual fee ("Administration Fee") of 0.10% of the Fund's average daily net assets, computed and accrued daily and payable monthly. For the year ended December 31, 2010, the Administration Fee was as follows:

| Fund | Total Aggregated ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS Government & Agency Securities VIP | 175,469 | 13,991 |

**Service Provider Fees.** DWS Investments Service Company ("DISC"), an affiliate of the Advisor, is the transfer agent, dividend-paying agent and shareholder service agent for the Fund. Pursuant to a sub-transfer agency agreement between DISC and DST Systems, Inc. ("DST"), DISC has delegated certain transfer agent, dividend-paying agent and shareholder service agent functions to DST. DISC compensates DST out of the shareholder servicing fee it receives from the Fund. For the year ended December 31, 2010, the amounts charged to the Fund by DISC were as follows:

| Fund | Total Aggregated ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS Government & Agency Securities VIP Class A | 325 | 77 |
| DWS Government & Agency Securities VIP Class B | 56 | 12 |

**Distribution Service Agreement**. Under the Fund's Class B 12b-1 plans, DWS Investments Distributors, Inc. ("DIDI") received a fee ("Distribution Service Fee") of 0.25% of average daily net assets of Class B shares. For the year ended December 31, 2010, the Distribution Service Fee was as follows:

| Fund | Total Aggregated ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS Government & Agency Securities VIP | 15,782 | 1,330 |

**Typesetting and Filing Service Fees.** Under an agreement with DIMA, DIMA is compensated for providing typesetting and certain regulatory filing services to the Fund. For the year ended December 31, 2010, the amount charged to the Fund by DIMA included in the Statement of Operations under "reports to shareholders" was as follows:

| Fund | Amount ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS Government & Agency Securities VIP | 12,898 | 3,141 |

**Trustees' Fees and Expenses.** The Fund paid each Trustee not affiliated with the Advisor retainer fees plus specified amounts for various committee services and for the Board Chairperson.

**Affiliated Cash Management Vehicles.** The Fund may invest uninvested cash balances in Central Cash Management Fund, which is managed by the Advisor. The Fund indirectly bears their proportionate share of the expenses of the underlying money market funds. Central Cash Management Fund does not pay the Advisor an investment management fee. Central Cash Management Fund seeks a high level of current income consistent with liquidity and the preservation of capital.

## E. Ownership of the Fund

At December 31, 2010, the beneficial ownership in the Fund was as follows:

**DWS Government & Agency Securities VIP:** Three Participating Insurance Companies were owners of record of 10% or more of the total outstanding Class A shares of the Fund, each owning 40%, 38% and 16%. One Participating Insurance Company was the owner of record of 10% or more of the total outstanding Class B shares of the Fund, owning 96%.

## F. Line of Credit

The Trust and other affiliated fund (the "Participants") share in a $450 million revolving credit facility provided by a syndication of banks. The Fund may borrow for temporary or emergency purposes, including the meeting of redemption requests that otherwise might require the untimely disposition of securities. The Participants are charged an annual commitment fee which is allocated based on net assets, among each of the Participants. Interest is calculated at a rate per annum equal to the sum of the Federal Funds Rate plus 1.25 percent plus if LIBOR exceeds the Federal Funds Rate the amount of such excess. The Fund may borrow up to a maximum of 33 percent of its net assets under the agreement.

# Report of Independent Registered Public Accounting Firm

**To the Board of Trustees and Shareholders of DWS Variable Series II:**

We have audited the accompanying statement of assets and liabilities of DWS Government & Agency Securities VIP, one of the funds constituting the DWS Variable Series II (the "Trust"), including the investment portfolio, as of December 31, 2010, and the related statement of operations, the statement of changes in net assets and the financial highlights for each of the periods indicated therein. These financial statements and financial highlights are the responsibility of the Trust's management. Our responsibility is to express an opinion on these financial statements and financial highlights based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements and financial highlights are free of material misstatement. We were not engaged to perform an audit of the Trust's internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Trust's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements and financial highlights, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our procedures included confirmation of securities owned as of December 31, 2010, by correspondence with the custodian and brokers or by other appropriate auditing procedures where replies from brokers were not received. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements and financial highlights referred to above present fairly, in all material respects, the financial position of the aforementioned fund of the DWS Variable Series II at December 31, 2010, the results of its operations, the changes in its net assets and the financial highlights for each of the periods indicated therein, in conformity with U.S. generally accepted accounting principles.

Ernst + Young LLP

Boston, Massachusetts
February 14, 2011

# Tax Information

**(Unaudited)**

The Fund designated as capital gain dividends for the year ended December 31, 2010:

| Fund | Capital Gain ($) | % Representing 15% Rate Gains |
|---|---|---|
| DWS Government & Agency Securities VIP | 1,388,000 | 100 |

Please consult a tax advisor if you have questions about federal or state income tax laws, or on how to prepare your tax returns. If you have specific questions about your account, please contact your insurance provider.

# Proxy Voting

The Trust's policies and procedures for voting proxies for portfolio securities and information about how the Trust voted proxies related to its portfolio securities during the 12-month period ended June 30 are available on our Web site — www.dws-investments.com (click on "proxy voting" at the bottom of the page) — or on the SEC's Web site — www.sec.gov. To obtain a written copy of the Trust's policies and procedures without charge, upon request, call us toll free at (800) 728-3337.

# Investment Management Agreement Approval

## DWS Government & Agency Securities VIP

The Board of Trustees, including the Independent Trustees, approved the renewal of your Fund's investment management agreement (the "Agreement") with Deutsche Investment Management Americas Inc. ("DWS") in September 2010.

In terms of the process that the Board followed prior to approving the Agreement, shareholders should know that:

- In September 2010, all but one of the Fund's Trustees were independent of DWS and its affiliates.
- The Trustees meet frequently to discuss fund matters. Each year, the Trustees dedicate substantial time to contract review matters. Over the course of several months, the Board's Contract Committee, in coordination with the Board's Fixed Income and Quant Oversight Committee, reviewed comprehensive materials received from DWS, independent third parties and independent counsel. These materials included an analysis of the Fund's performance, fees and expenses, and profitability compiled by the Fund's independent fee consultant. The Board also received extensive information throughout the year regarding performance of the Fund.
- The Independent Trustees regularly meet privately with their independent counsel to discuss contract review and other matters. In addition, the Independent Trustees were also advised by the Fund's independent fee consultant in the course of their review of the Fund's contractual arrangements and considered a comprehensive report prepared by the independent fee consultant in connection with their deliberations (the "IFC Report").
- In connection with reviewing the Agreement, the Board also reviewed the terms of the Fund's Rule 12b-1 plan, distribution agreement, administrative services agreement, transfer agency agreement and other material service agreements.
- Based on its evaluation of the information provided, the Contract Committee presented its findings and recommendations to the Independent Trustees as a group. The Independent Trustees reviewed the Contract Committee's findings and recommendations and presented their recommendations to the full Board.

In connection with the contract review process, the Contract Committee and the Board considered the factors discussed below, among others. The Board also considered that DWS and its predecessors have managed the Fund since its inception, and the Board believes that a long-term relationship with a capable, conscientious advisor is in the best interests of the Fund. The Board considered, generally, that shareholders chose to invest or remain invested in the Fund knowing that DWS managed the Fund, and that the Agreement was approved by the Fund's shareholders. DWS is part of Deutsche Bank, a major global banking institution that is engaged in a wide range of financial services. The Board believes that there are significant advantages to being part of a global asset management business that offers a wide range of investing expertise and resources, including hundreds of portfolio managers and analysts with research capabilities in many countries throughout the world.

While shareholders may focus primarily on fund performance and fees, the Fund's Board considers these and many other factors, including the quality and integrity of DWS's personnel and such other issues as back-office operations, fund valuations, and compliance policies and procedures.

**Nature, Quality and Extent of Services.** The Board considered the terms of the Agreement, including the scope of advisory services provided under the Agreement. The Board noted that, under the Agreement, DWS provides portfolio management services to the Fund and that, pursuant to a separate administrative services agreement, DWS provides administrative services to the Fund. The Board considered the experience and skills of senior management and investment personnel, the resources made available to such personnel, the ability of DWS to attract and retain high-quality personnel, and the organizational depth and stability of DWS. The Board reviewed the Fund's performance over short-term and long-term periods and compared those returns to various agreed-upon performance measures, including market indices and a peer universe compiled by the independent fee consultant using information supplied by Lipper Inc. ("Lipper"). The Board also noted that it has put into place a process of identifying "Focus Funds" (e.g., funds performing poorly relative to their benchmark or a peer universe compiled by Lipper), and receives more frequent reporting and information from DWS regarding such funds, along with DWS's remedial plans to address underperformance. The Board believes this process is an effective manner of identifying and addressing underperforming funds. Based on the information provided, the Board noted that for the one-, three- and five-year periods ended December 31, 2009, the Fund's performance (Class A shares) was in the 1st quartile of the applicable Lipper universe (the 1st quartile being the best performers and the 4th quartile being the worst performers). The Board also observed that the Fund has outperformed its benchmark in the one-year period and has underperformed its benchmark in the three- and five-year periods ended December 31, 2009.

On the basis of this evaluation and the ongoing review of investment results by the Board, the Board concluded that the nature, quality and extent of services provided by DWS historically have been and continue to be satisfactory.

**Fees and Expenses.** The Board considered the Fund's investment management fee schedule, operating expenses, and total expense ratios, and comparative information provided by Lipper and the independent fee consultant regarding investment management fee rates paid to other investment advisors by similar funds (1st quartile being the most favorable and 4th quartile being the least favorable). With respect to management fees paid to other investment advisors by similar funds, the Board noted that the contractual fee rates paid by the Fund, which include the 0.10% fee paid to DWS under the Fund's administrative services agreement, were at the median (2nd quartile) of the applicable Lipper peer group (based on Lipper data provided as of December 31, 2009). The Board noted that the Fund's Class A shares total (net) operating expenses were expected to be higher than the median (3rd quartile) of the applicable Lipper expense universe (based on Lipper data provided as of December 31, 2009, and analyzing Lipper expense universe Class A expenses less any applicable 12b-1 fees) ("Lipper Universe Expenses"). The Board also reviewed data comparing each share class's total (net) operating expenses to the applicable Lipper Universe Expenses. The Board considered the Fund's management fee rate as compared to fees charged by DWS and certain of its affiliates for comparable mutual funds and considered differences in fund and fee structures between the DWS Funds. The Board also considered how the Fund's total (net) operating expenses compared to the total (net) operating expenses of a more customized peer group selected by Lipper (based on such factors as asset size).

The information considered by the Board as part of its review of management fees included information regarding fees charged by DWS and its affiliates to similar institutional accounts and to similar funds offered primarily to European investors ("DWS Europe funds"), in each case as applicable. The Board observed that advisory fee rates for institutional accounts generally were lower than the management fees charged by similarly managed DWS US mutual funds ("DWS Funds"), but also took note of the differences in services provided to DWS Funds as compared to institutional accounts. In the case of DWS Europe funds, the Board observed that fee rates for DWS Europe funds generally were higher than for similarly managed DWS Funds, but noted that differences in the types of services provided to DWS Funds relative to DWS Europe funds made it difficult to compare such fees.

On the basis of the information provided, the Board concluded that management fees were reasonable and appropriate in light of the nature, quality and extent of services provided by DWS.

**Profitability.** The Board reviewed detailed information regarding revenues received by DWS under the Agreement. The Board considered the estimated costs and pre-tax profits realized by DWS from advising the DWS Funds, as well as estimates of the pre-tax profits attributable to managing the Fund in particular. The Board also received information regarding the estimated enterprise-wide profitability of DWS and its affiliates with respect to all fund services in totality and by fund. The Board reviewed DWS's methodology in allocating its costs to the management of the Fund. Based on the information provided, the Board concluded that the pre-tax profits realized by DWS in connection with the management of the Fund were not unreasonable. The Board also reviewed information regarding the profitability of certain similar investment management firms. The Board noted that while information regarding the profitability of such firms is limited (and in some cases is not necessarily prepared on a comparable basis), DWS and its affiliates' overall profitability with respect to the DWS fund complex (after taking into account distribution and other services provided to the funds by DWS and its affiliates) was lower than the overall profitability levels of many comparable firms for which such data was available.

**Economies of Scale.** The Board considered whether there are economies of scale with respect to the management of the Fund and whether the Fund benefits from any economies of scale. The Board noted that the Fund's management fee schedule includes fee breakpoints. The Board concluded that the Fund's fee schedule represents an appropriate sharing between the Fund and DWS of such economies of scale as may exist in the management of the Fund at current asset levels.

**Other Benefits to DWS and Its Affiliates**. The Board also considered the character and amount of other incidental benefits received by DWS and its affiliates, including any fees received by DWS for administrative services provided to the Fund and any fees received by an affiliate of DWS for distribution services. The Board also considered benefits to DWS related to brokerage and soft-dollar allocations, including allocating brokerage to pay for research generated by parties other than the executing broker dealers, which pertain primarily to funds investing in equity securities, along with the incidental public relations benefits to DWS related to DWS Funds advertising and cross-selling opportunities among DWS products and services. The Board concluded that management fees were reasonable in light of these fallout benefits.

**Compliance.** The Board considered the significant attention and resources dedicated by DWS to documenting and enhancing its compliance processes in recent years. The Board noted in particular (i) the experience and seniority of both DWS's chief compliance officer and the Fund's chief compliance officer; (ii) the large number of

DWS compliance personnel; and (iii) the substantial commitment of resources by DWS and its affiliates to compliance matters.

Based on all of the information considered and the conclusions reached, the Board unanimously (including the Independent Trustees) determined that the continuation of the Agreement is in the best interests of the Fund. In making this determination, the Board did not give particular weight to any single factor identified above. The Board considered these factors over the course of numerous meetings, certain of which were in executive session with only the Independent Trustees and their counsel present. It is possible that individual Trustees may have weighed these factors differently in reaching their individual decisions to approve the continuation of the Agreement.

# Summary of Management Fee Evaluation by Independent Fee Consultant

October 3, 2010

Pursuant to an Order entered into by Deutsche Investment Management Americas and affiliates (collectively, "DeAM") with the Attorney General of New York, I, Thomas H. Mack, have been appointed the Independent Fee Consultant for the DWS Funds (formerly the DWS Scudder Funds). My duties include preparing an annual written evaluation of the management fees DeAM charges the Funds, considering among other factors the management fees charged by other mutual fund companies for like services, management fees DeAM charges other clients for like services, DeAM's costs of supplying services under the management agreements and related profit margins, possible economies of scale if a Fund grows larger, and the nature and quality of DeAM's services, including fund performance. This report summarizes my evaluation for 2010, including my qualifications, the evaluation process for each of the DWS Funds, consideration of certain complex-level factors, and my conclusions. I served in substantially the same capacity in 2007, 2008, and 2009.

## Qualifications

For more than 35 years I have served in various professional capacities within the investment management business. I have held investment analysis and advisory positions, including securities analyst, portfolio strategist and director of investment policy with a large investment firm. I have also performed business management functions, including business development, financial management and marketing research and analysis.

Since 1991, I have been an independent consultant within the asset management industry. I have provided services to over 125 client organizations, including investment managers, mutual fund boards, product distributors and related organizations. Over the past ten years I have completed a number of assignments for mutual fund boards, specifically including assisting boards with management contract renewal.

I hold a Master of Business Administration degree, with highest honors, from Harvard University and Master of Science and Bachelor of Science (highest honors) degrees from the University of California at Berkeley. I am an independent director and audit committee financial expert for two closed-end mutual funds and have served in various leadership and financial oversight capacities with non-profit organizations.

## Evaluation of Fees for each DWS Fund

My work focused primarily on evaluating, fund-by-fund, the fees charged to each of the 118 publicly offered Fund portfolios in the DWS Fund family. For each Fund, I considered each of the key factors mentioned above, as well as any other relevant information. In doing so I worked closely with the Funds' Independent Directors in their annual contract renewal process, as well as in their approval of contracts for several new funds (documented separately).

In evaluating each Fund's fees, I reviewed comprehensive materials provided by or on behalf of DeAM, including expense information prepared by Lipper Analytical, comparative performance information, profitability data, manager histories, and other materials. I also accessed certain additional information from the Lipper and Morningstar databases and drew on my industry knowledge and experience.

To facilitate evaluating this considerable body of information, I prepared for each Fund a document summarizing the key data elements in each area as well as additional analytics discussed below. This made it possible to consider each key data element in the context of the others.

In the course of contract renewal, DeAM agreed to implement a number of fee and expense adjustments requested by the Independent Directors which will favorably impact future fees and expenses, and my evaluation includes the effects of these changes.

### Fees and Expenses Compared with Other Funds

The competitive fee and expense evaluation for each fund focused on two primary comparisons:

- The Fund's contractual management fee (the advisory fee plus the administration fee where applicable) compared with those of a group of typically 12–15 funds in the same Lipper investment category (e.g. Large Capitalization Growth) having similar distribution arrangements and being of similar size.
- The Fund's total expenses compared with a broader universe of funds from the same Lipper investment category and having similar distribution arrangements.

These two comparisons provide a view of not only the level of the fee compared with funds of similar scale but also the total expense the Fund bears for all the services it receives, in comparison with the investment choices available in the Fund's investment category and distribution channel. The principal figure-of-merit used in these comparisons was the subject Fund's percentile ranking against peers.

### DeAM's Fees for Similar Services to Others

DeAM provided management fee schedules for all of its US domiciled fund and non-fund investment management accounts in any of the investment categories where there is a DWS Fund. These similar products included the other DWS Funds, non-fund pooled accounts, institutional accounts and sub-advisory accounts. Using this information, I calculated for each Fund the fee that would be charged to each similar product, at the subject Fund's asset level.

Evaluating information regarding non-fund products is difficult because there are varying levels of services required for different types of accounts, with mutual funds generally requiring considerably more regulatory and administrative types of service as well as having more frequent cash flows than other types of accounts. Also, while mutual fund fees for similar fund products can be expected to be similar, there will be some differences due to different pricing conditions in different distribution channels (e.g. retail funds versus those used in variable insurance products), differences in underlying investment processes and other factors.

### Costs and Profit Margins

DeAM provided a detailed profitability analysis for each Fund. After making some adjustments so that the presentation would be more comparable to the available industry figures, I reviewed profit margins from investment management alone, from investment management plus other fund services (excluding distribution) provided to the Funds by DeAM (principally shareholder services), and DeAM profits from all sources, including distribution. A later section comments on overall profitability.

### Economies of Scale

Economies of scale — an expected decline in management cost per dollar of fund assets as fund assets grow — are very rarely quantified and documented because of inherent difficulties in collecting and analyzing relevant data. However, in virtually every investment category that I reviewed, larger funds tend to have lower fees and lower total expenses than smaller funds. To see how each DWS Fund compares with this industry observation, I reviewed:

The trend in Fund assets over the last five years and the accompanying trend in total expenses. This shows if the Fund has grown and, if so, whether total expense (management fees as well as other expenses) have declined as a percent of assets.

Whether the Fund has break-points in its management fee schedule, the extent of the fee reduction built into the schedule and the asset levels where the breaks take effect, and in the case of a sub-advised Fund how the Fund's break-points compare with those of the sub-advisory fee schedule.

How the Fund's contractual fee schedule compares with trends in the industry data. To accomplish this, I constructed a chart showing how actual latest-fiscal-year contractual fees of the Fund and of other similar funds relate to average fund assets, with the subject Fund's contractual fee schedule superimposed.

### Quality of Service — Performance

The quality-of-service evaluation focused on investment performance, which is the principal result of the investment management service. Each Fund's performance was reviewed over the past 1, 3, 5 and 10 years, as applicable, and compared with that of other funds in the same investment category and with a suitable market index.

In addition, I calculated and reviewed risk-adjusted returns relative to an index of similar mutual funds' returns and a suitable market index. The risk-adjusted returns analysis provides a way of determining the extent to which the Fund's return comparisons are mainly the product of investment value-added (or lack thereof) or alternatively taking considerably more or less risk than is typical in its investment category.

I also received and considered the history of portfolio manager changes for each Fund, as this provided an important context for evaluating the performance results.

## Complex-Level Considerations

While this evaluation was conducted mainly at the individual fund level, there are some issues relating to the reasonableness of fees that can alternatively be considered across the whole fund complex:

I reviewed DeAM's profitability analysis for all DWS Funds, with a view toward determining if the allocation procedures used were reasonable and how profit levels compared with public data for other investment managers.

I considered whether DeAM and affiliates receive any significant ancillary or "fall-out" benefits that should be considered in interpreting the direct profitability results. These would be situations where serving as the investment manager of the Funds is beneficial to another part of the Deutsche Bank organization.

I considered how aggregated DWS Fund expenses had varied over the years, by asset class and in the context of trends in asset levels.

I reviewed the structure of the DeAM organization, trends in staffing levels, and information on compensation of investment management and other professionals compared with industry data.

## Findings

Based on the process and analysis discussed above, which included reviewing a wide range of information from management and external data sources and considering among other factors the fees DeAM charges other clients, the fees charged by other fund managers, DeAM's costs and profits associated with managing the Funds, economies of scale, possible fall-out benefits, and the nature and quality of services provided, in my opinion the management fees charged the DWS Funds are reasonable.

Thomas H. Mack

Thomas H. Mack

# Board Members and Officers

The following table presents certain information regarding the Board Members and Officers of the Trust as of December 31, 2010. Each Board Member's year of birth is set forth in parentheses after his or her name. Unless otherwise noted, (i) each Board Member has engaged in the principal occupation(s) noted in the table for at least the most recent five years, although not necessarily in the same capacity; and (ii) the address of each Independent Board Member is c/o Paul K. Freeman, Independent Chairman, DWS Funds, PO Box 101833, Denver, CO 80250-1833. Except as otherwise noted below, the term of office for each Board Member is until the election and qualification of a successor, or until such Board Member sooner dies, resigns, is removed or as otherwise provided in the governing documents of the fund. Because the fund does not hold an annual meeting of shareholders, each Board Member will hold office for an indeterminate period. The Board Members may also serve in similar capacities with other funds in the fund complex. The Length of Time Served represents the year in which the Board Member joined the board of one or more DWS funds now overseen by the Board.

### Independent Board Members

| Name, Year of Birth, Position with the Fund and Length of Time Served[1] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Paul K. Freeman (1950)<br>Chairperson since 2009<br>Board Member since 1993 | Consultant, World Bank/Inter-American Development Bank; Executive and Governing Council of the Independent Directors Council (education committees); formerly, Project Leader, International Institute for Applied Systems Analysis (1998–2001); Chief Executive Officer, The Eric Group, Inc. (environmental insurance) (1986–1998) | 122 |
| John W. Ballantine (1946)<br>Board Member since 1999 | Retired; formerly, Executive Vice President and Chief Risk Management Officer, First Chicago NBD Corporation/The First National Bank of Chicago (1996–1998); Executive Vice President and Head of International Banking (1995–1996). Directorships: Healthways, Inc. (provider of disease and care management services); Portland General Electric (utility company); Stockwell Capital Investments PLC (private equity). Former Directorships: First Oak Brook Bancshares, Inc. and Oak Brook Bank; Prisma Energy International | 122 |
| Henry P. Becton, Jr. (1943)<br>Board Member since 1990 | Vice Chair and former President, WGBH Educational Foundation. Directorships: Association of Public Television Stations; Lead Director, Becton Dickinson and Company[3] (medical technology company); Lead Director, Belo Corporation[3] (media company); Public Radio International; Public Radio Exchange (PRX); The PBS Foundation. Former Directorships: Boston Museum of Science; American Public Television; Concord Academy; New England Aquarium; Mass. Corporation for Educational Telecommunications; Committee for Economic Development; Public Broadcasting Service | 122 |
| Dawn-Marie Driscoll (1946)<br>Board Member since 1987 | President, Driscoll Associates (consulting firm); Executive Fellow, Center for Business Ethics, Bentley University; formerly, Partner, Palmer & Dodge (1988–1990); Vice President of Corporate Affairs and General Counsel, Filene's (1978–1988). Directorships: Trustee of 22 open-end mutual funds managed by Sun Capital Advisers, Inc. (since 2007); Director of ICI Mutual Insurance Company (since 2007); Advisory Board, Center for Business Ethics, Bentley University; Trustee, Southwest Florida Community Foundation (charitable organization). Former Directorships: Investment Company Institute (audit, executive, nominating committees) and Independent Directors Council (governance, executive committees) | 122 |
| Keith R. Fox (1954)<br>Board Member since 1996 | Managing General Partner, Exeter Capital Partners (a series of private investment funds). Directorships: Progressive International Corporation (kitchen goods importer and distributor); BoxTop Media Inc. (advertising); The Kennel Shop (retailer); former Chairman, National Association of Small Business Investment Companies | 122 |
| Kenneth C. Froewiss (1945)<br>Board Member since 2001 | Adjunct Professor of Finance, NYU Stern School of Business (September 2009–present; Clinical Professor from 1997–September 2009); Member, Finance Committee, Association for Asian Studies (2002–present); Director, Mitsui Sumitomo Insurance Group (US) (2004–present); prior thereto, Managing Director, J.P. Morgan (investment banking firm) (until 1996) | 122 |
| Richard J. Herring (1946)<br>Board Member since 1990 | Jacob Safra Professor of International Banking and Professor, Finance Department, The Wharton School, University of Pennsylvania (since July 1972); Co-Director, Wharton Financial Institutions Center (since July 2000); Co-Chair, U.S. Shadow Financial Regulatory Committee; Executive Director, Financial Economists Roundtable; Director, Japan Equity Fund, Inc. (since September 2007), Thai Capital Fund, Inc. (since September 2007), Singapore Fund, Inc. (since September 2007); Independent Director of Barclays Bank Delaware (since September 2010). Formerly, Vice Dean and Director, Wharton Undergraduate Division (July 1995–June 2000); Director, Lauder Institute of International Management Studies (July 2000–June 2006) | 122 |
| William McClayton (1944)<br>Board Member since 2004+ | Private equity investor (since October 2009); previously, Managing Director, Diamond Management & Technology Consultants, Inc. (global consulting firm) (2001–2009); Directorship: Board of Managers, YMCA of Metropolitan Chicago; formerly: Senior Partner, Arthur Andersen LLP (accounting) (1966–2001); Trustee, Ravinia Festival | 122 |

| Name, Year of Birth, Position with the Fund and Length of Time Served[1] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Rebecca W. Rimel (1951)<br>Board Member since 1995 | President and Chief Executive Officer, The Pew Charitable Trusts (charitable organization) (1994 to present); Trustee, Thomas Jefferson Foundation (charitable organization) (1994 to present); Trustee, Executive Committee, Philadelphia Chamber of Commerce (2001–2007); Director, CardioNet, Inc.[2] (2009–present) (health care). Formerly, Executive Vice President, The Glenmede Trust Company (investment trust and wealth management) (1983–2004); Board Member, Investor Education (charitable organization) (2004–2005); Director, Viasys Health Care[2] (January 2007–June 2007); Trustee, Pro Publica (charitable organization) (2007–2010) | 122 |
| William N. Searcy, Jr. (1946)<br>Board Member since 1993 | Private investor since October 2003; Trustee of 22 open-end mutual funds managed by Sun Capital Advisers, Inc. (since October 1998). Formerly, Pension & Savings Trust Officer, Sprint Corporation[2] (telecommunications) (November 1989–September 2003) | 122 |
| Jean Gleason Stromberg (1943)<br>Board Member since 1997 | Retired. Formerly, Consultant (1997–2001); Director, Financial Markets US Government Accountability Office (1996–1997); Partner, Fulbright & Jaworski, L.L.P. (law firm) (1978–1996). Directorships: The William and Flora Hewlett Foundation. Former Directorships: Service Source, Inc., Mutual Fund Directors Forum (2002–2004), American Bar Retirement Association (funding vehicle for retirement plans) (1987–1990 and 1994–1996) | 122 |
| Robert H. Wadsworth (1940)<br>Board Member since 1999 | President, Robert H. Wadsworth & Associates, Inc. (consulting firm) (1983 to present); Director, The Phoenix Boys Choir Association | 125 |

## Interested Board Member and Officer[4]

| Name, Year of Birth, Position with the Trust/ Corporation and Length of Time Served[1,5] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Ingo Gefeke[7] (1967)<br>Board Member since 2010<br>Executive Vice President since 2010 | Managing Director[3], Deutsche Asset Management; Global Head of Distribution and Product Management, DWS Global Head of Trading and Securities Lending. Member of the Board of Directors of DWS Investment GmbH Frankfurt (since July 2009) and DWS Holding & Service GmbH Frankfurt (since January 2010); formerly, Global Chief Administrative Officer, Deutsche Asset Management (2004–2009); Global Chief Operating Officer, Global Transaction Banking, Deutsche Bank AG, New York (2001–2004); Chief Operating Officer, Global Banking Division Americas, Deutsche Bank AG, New York (1999–2001); Central Management, Global Banking Services, Deutsche Bank AG, Frankfurt (1998–1999); Relationship Management, Deutsche Bank AG, Tokyo, Japan (1997–1998) | 55 |

## Officers[4]

| Name, Year of Birth, Position with the Fund and Length of Time Served[5] | Principal Occupation(s) During Past 5 Years and Other Directorships Held |
|---|---|
| Michael G. Clark[6] (1965)<br>President, 2006–present | Managing Director[3], Deutsche Asset Management (2006–present); President of DWS family of funds; Director, ICI Mutual Insurance Company (since October 2007); formerly, Director of Fund Board Relations (2004–2006) and Director of Product Development (2000–2004), Merrill Lynch Investment Managers; Senior Vice President Operations, Merrill Lynch Asset Management (1999–2000) |
| John Millette[8] (1962)<br>Vice President and Secretary, 1999–present | Director[3], Deutsche Asset Management |
| Paul H. Schubert[6] (1963)<br>Chief Financial Officer, 2004–present<br>Treasurer, 2005–present | Managing Director[3], Deutsche Asset Management (since July 2004); formerly, Executive Director, Head of Mutual Fund Services and Treasurer for UBS Family of Funds (1998–2004); Vice President and Director of Mutual Fund Finance at UBS Global Asset Management (1994–1998) |
| Caroline Pearson[8] (1962)<br>Chief Legal Officer, April 2010–present | Managing Director[3], Deutsche Asset Management; formerly, Assistant Secretary for DWS family of funds (1997–2010) |
| Rita Rubin[9] (1970)<br>Assistant Secretary, 2009–present | Vice President and Counsel, Deutsche Asset Management (since October 2007); formerly, Vice President, Morgan Stanley Investment Management (2004–2007) |
| Paul Antosca[8] (1957)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management (since 2006); Vice President, The Manufacturers Life Insurance Company (U.S.A.) (1990–2006) |
| Jack Clark[8] (1967)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management (since 2007); formerly, Vice President, State Street Corporation (2002–2007) |

| Name, Year of Birth, Position with the Fund and Length of Time Served[5] | Principal Occupation(s) During Past 5 Years and Other Directorships Held |
|---|---|
| Diane Kenneally[8] (1966)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management |
| John Caruso[9] (1965)<br>Anti-Money Laundering Compliance Officer, 2010–present | Managing Director[3], Deutsche Asset Management |
| Robert Kloby[9] (1962)<br>Chief Compliance Officer, 2006–present | Managing Director[3], Deutsche Asset Management |

1 *The length of time served represents the year in which the Board Member joined the board of one or more DWS funds currently overseen by the Board.*

2 *A publicly held company with securities registered pursuant to Section 12 of the Securities Exchange Act of 1934.*

3 *Executive title, not a board directorship.*

4 *As a result of their respective positions held with the Advisor, these individuals are considered "interested persons" of the Advisor within the meaning of the 1940 Act. Interested persons receive no compensation from the fund.*

5 *The length of time served represents the year in which the officer was first elected in such capacity for one or more DWS funds.*

6 *Address: 100 Plaza One, Jersey City, NJ 07311.*

7 *Effective January 11, 2011, Mr. Gefeke, an interested Board Member and Executive Vice President, resigned from the fund's Board and as an officer.*

*The mailing address of Mr. Gefeke is 345 Park Avenue, New York, New York 10154. Mr. Gefeke was an interested Board Member of certain DWS funds by virtue of his positions with Deutsche Asset Management. As an interested person, Mr. Gefeke received no compensation from the fund.*

8 *Address: One Beacon Street, Boston, MA 02108.*

9 *Address: 60 Wall Street, New York, New York 10005.*

*The fund's Statement of Additional Information ("SAI") includes additional information about the Board Members. The SAI is available, without charge, upon request. If you would like to request a copy of the SAI, you may do so by calling the following toll-free number: (800) 728-3337.*

DWS Investments is part of Deutsche Bank's Asset Management division and, within the US, represents the retail asset management activities of Deutsche Bank AG, Deutsche Bank Trust Company Americas, Deutsche Investment Management Americas Inc. and DWS Trust Company.

The views expressed in this report reflect those of the portfolio managers only through the end of the period of the report as stated on the cover. The managers' views are subject to change at any time based on market and other conditions and should not be construed as a recommendation.

This information must be preceded or accompanied by a current prospectus.

Portfolio changes should not be considered recommendations for action by individual investors.

DWS Investments Distributors, Inc.
222 South Riverside Plaza
Chicago, IL 60606
(800) 621-1148

VS2GAS-2 (2/11)

DWS INVESTMENTS
Deutsche Bank Group

DECEMBER 31, 2010

# ANNUAL REPORT

## DWS VARIABLE SERIES II

## DWS High Income VIP

**This report must be preceded or accompanied by a prospectus. To obtain an additional prospectus or summary prospectus, if available, call (800) 728-3337 or your financial representative. We advise you to consider the Fund's objectives, risks, charges and expenses carefully before investing. The summary prospectus and prospectus contain this and other important information about the Fund. Please read the prospectus carefully before you invest.**

*Investments in variable insurance portfolios (VIPs) involve risk. Stocks may decline in value. Bond investments are subject to interest-rate and credit risks. When interest rates rise, bond prices generally fall. Credit risk refers to the ability of an issuer to make timely payments of principal and interest. Investing in derivatives entails special risks relating to liquidity, leverage and credit that may reduce returns and/or increased volatility. Investing in foreign securities, particularly those of emerging markets, presents certain risks, such as currency fluctuations, political and economic changes, and market risks. There are additional risks associated with investing in commodities, high-yield bonds, aggressive growth stocks, non-diversified/ concentrated funds and small- and mid-cap stocks which are more fully explained in the prospectuses. Please read the prospectus for more information.*

*DWS Investments is part of Deutsche Bank's Asset Management division and, within the US, represents the retail asset management activities of Deutsche Bank AG, Deutsche Bank Trust Company Americas, Deutsche Investment Management Americas Inc. and DWS Trust Company.*

*NOT FDIC/NCUA INSURED    NO BANK GUARANTEE    MAY LOSE VALUE    NOT A DEPOSIT*
*NOT INSURED BY ANY FEDERAL GOVERNMENT AGENCY*

DWS INVESTMENTS
Deutsche Bank Group

# Performance Summary

**December 31, 2010**

## DWS High Income VIP

**All performance shown is historical, assumes reinvestment of all dividend and capital gain distributions and does not guarantee future results. Investment return and principal value fluctuate with changing market conditions so that, when redeemed, shares may be worth more or less than their original cost. Current performance may be lower or higher than the performance data quoted. Please contact your participating insurance company for the Fund's most recent month-end performance. Performance doesn't reflect charges and fees ("contract charges") associated with the separate account that invests in the Fund or any variable life insurance policy or variable annuity contract for which the Fund is an investment option. These charges and fees will reduce returns. While all share classes have the same underlying portfolio, their performance will differ.**

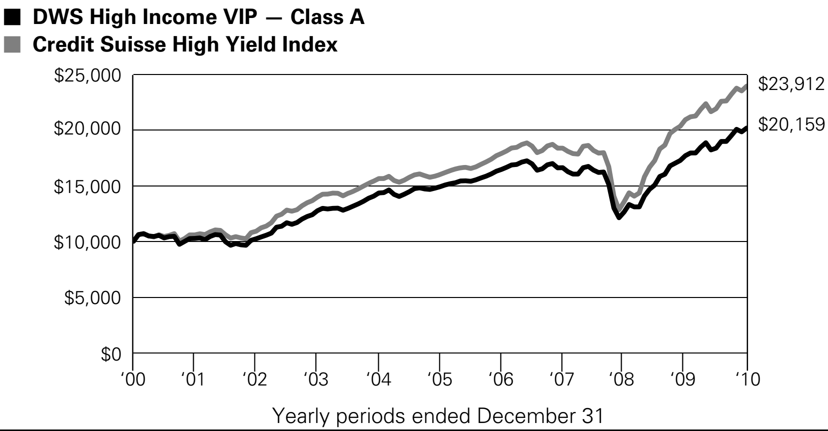
**The gross expense ratios of the Fund, as stated in the fee table of the prospectus dated May 1, 2010 are 0.67% and 0.94% for Class A and Class B shares, respectively, and may differ from the expense ratios disclosed in the Financial Highlights tables in this report.**

### Risk Considerations

Bond investments are subject to interest-rate and credit risks. When interest rates rise, bond prices generally fall. Credit risk refers to the ability of an issuer to make timely payments of principal and interest. Investments in lower-quality and non-rated securities present greater risk of loss than investments in higher-quality securities. See the prospectus for details.

Fund returns shown for the 3-year, 5-year and 10-year/life of class periods reflect a fee waiver and/or expense reimbursement. Without this waiver/reimbursement, returns would have been lower.

### Growth of an Assumed $10,000 Investment in DWS High Income VIP




*The Credit Suisse High Yield Index is an unmanaged, trader-priced portfolio constructed to mirror the global high-yield debt market.*

*Index returns, unlike fund returns, do not reflect any fees or expenses. It is not possible to invest directly into an index.*

### Comparative Results

| DWS High Income VIP | | 1-Year | 3-Year | 5-Year | 10-Year |
|---|---|---|---|---|---|
| **Class A** | Growth of $10,000 | $11,400 | $12,138 | $13,538 | $20,159 |
| | Average annual total return | 14.00% | 6.67% | 6.25% | 7.26% |
| Credit Suisse High Yield Index | Growth of $10,000 | $11,442 | $13,028 | $14,966 | $23,912 |
| | Average annual total return | 14.42% | 9.22% | 8.40% | 9.11% |

| DWS High Income VIP | | 1-Year | 3-Year | 5-Year | Life of Class* |
|---|---|---|---|---|---|
| **Class B** | Growth of $10,000 | $11,364 | $12,040 | $13,329 | $19,657 |
| | Average annual total return | 13.64% | 6.38% | 5.92% | 8.28% |
| Credit Suisse High Yield Index | Growth of $10,000 | $11,442 | $13,028 | $14,966 | $22,564 |
| | Average annual total return | 14.42% | 9.22% | 8.40% | 10.04% |

*The growth of $10,000 is cumulative.*

* *The Fund commenced offering Class B shares on July 1, 2002. Index returns began on June 30, 2002.*

# Information About Your Fund's Expenses

## DWS High Income VIP

As an investor of the Fund, you incur two types of costs: ongoing expenses and transaction costs. Ongoing expenses include management fees, distribution and service (12b-1) fees and other Fund expenses. Examples of transaction costs include contract charges, redemption fees and account maintenance fees, which are not shown in this section. The following tables are intended to help you understand your ongoing expenses (in dollars) of investing in the Fund and to help you compare these expenses with the ongoing expenses of investing in other mutual funds. The example in the table is based on an investment of $1,000 invested at the beginning of the six-month period and held for the entire period (July 1, 2010 to December 31, 2010).

The tables illustrate your Fund's expenses in two ways:

- **Actual Fund Return.** This helps you estimate the actual dollar amount of ongoing expenses (but not transaction costs) paid on a $1,000 investment in the Fund using the Fund's actual return during the period. To estimate the expenses you paid over the period, simply divide your account value by $1,000 (for example, an $8,600 account value divided by $1,000 = 8.6), then multiply the result by the number in the "Expenses Paid per $1,000" line under the share class you hold.
- **Hypothetical 5% Fund Return.** This helps you to compare your Fund's ongoing expenses (but not transaction costs) with those of other mutual funds using the Fund's actual expense ratio and a hypothetical rate of return of 5% per year before expenses. Examples using a 5% hypothetical Fund return may be found in the shareholder reports of other mutual funds. The hypothetical account values and expenses may not be used to estimate the actual ending account balance or expenses you paid for the period.

Please note that the expenses shown in these tables are meant to highlight your ongoing expenses only and do not reflect any transaction costs. The "Expenses Paid per $1,000" line of the tables is useful in comparing ongoing expenses only and will not help you determine the relative total expense of owning different funds. If these transaction costs had been included, your costs would have been higher.

**Expenses and Value of a $1,000 Investment** for the six months ended December 31, 2010

| Actual Fund Return | Class A | Class B |
|---|---|---|
| Beginning Account Value 7/1/10 | $1,000.00 | $1,000.00 |
| Ending Account Value 12/31/10 | $1,098.70 | $1,098.30 |
| Expenses Paid per $1,000* | $ 3.65 | $ 5.02 |
| **Hypothetical 5% Fund Return** | **Class A** | **Class B** |
| Beginning Account Value 7/1/10 | $1,000.00 | $1,000.00 |
| Ending Account Value 12/31/10 | $1,021.73 | $1,020.42 |
| Expenses Paid per $1,000* | $ 3.52 | $ 4.84 |

* *Expenses are equal to the Fund's annualized expense ratio for each share class, multiplied by the average account value over the period, multiplied by the number of days in the most recent six-month period, then divided by 365.*

| Annualized Expense Ratios | Class A | Class B |
|---|---|---|
| DWS Variable Series II — DWS High Income VIP | .69% | .95% |

For more information, please refer to the Fund's prospectus.

These tables do not reflect charges and fees ("contract charges") associated with the separate account that invests in the Fund or any variable life insurance policy or variable annuity contract for which the Fund is an investment option.

# Management Summary

**December 31, 2010**

## DWS High Income VIP

High-yield bonds — as gauged by the Fund's benchmark, the Credit Suisse High Yield Index — returned 14.42% in 2010 and outperformed the broader fixed-income market, as measured by the 6.54% return of the Barclays Capital US Aggregate Bond Index. High-yield bonds were energized by an environment of low government bond yields, improving balance sheets for high-yield companies and a steep decline in the default rate. The Class A shares of the Fund returned 14.00% (unadjusted for contract charges), underperforming the benchmark.

The Fund's underperformance was partially the result of our overweights in certain lower-volatility issuers such as NRG Energy, Inc. and HCA, Inc., as well as our underweights in higher-volatility issuers such as CIT Group, Inc., Realogy Corp.* and Residential Capital.*[1] These detractors demonstrate that our risk management process can sometimes cause us to miss some winners. However, we believe a focus on risk and reward — rather than trying to chase short-term performance in the hottest areas of the market — remains the most prudent strategy.

The largest contributor to the Fund's performance was the Fund's exposure to bonds issued by Ford Motor Co. Ford benefited from rising sales, increased market share and declining debt, all of which set the stage of an upgrade to its credit quality rating.[2] Our security selection in the chemicals sector, were key contributors included Hexion Specialty Chemicals,* Huntsman International LLC and Ashland, Inc., proved helpful to performance.

We maintain an upbeat outlook on high-yield bonds. Many positive factors remain in place, including accommodative monetary policy, new fiscal stimulus, strong corporate balance sheets and the high cash balances of large-cap corporations. The market is also benefiting from increased merger and acquisition activity, a receptive new issue environment, and a lower-than-expected default rate.

Given the supportive factors that characterize the current market backdrop, we believe the combination of attractive yields and a low single-digit default rate indicate a potentially favorable risk/return trade-off for high-yield bonds. However, bottom-up credit research and security selection will be more important than ever, given the substantial impact that individual defaults can have on performance in a low-default environment.

Gary Russell, CFA
*Portfolio Manager*

*The Credit Suisse High Yield Index is an unmanaged, trader-priced portfolio constructed to mirror the global high-yield debt market.*

*The Barclays Capital US Aggregate Bond Index is an unmanaged, market-value-weighted measure of Treasury issues, agency issues, corporate bond issues and mortgage securities.*

*Index returns, unlike fund returns, do not reflect any fees or expenses. It is not possible to invest directly into an index.*

1 *"Overweight" means the Fund holds a higher weighting in a given sector or security than the benchmark. "Underweight" means the Fund holds a lower weighting.*

2 *Credit quality is a measure of a bond issuer's ability to repay interest and principal in a timely manner. Rating agencies assign letter designations such as AAA, AA and so forth. The lower the rating, the higher the probability of default. The fund's credit quality does not remove market risk and is subject to change.*

* *Not held in the portfolio as of December 31, 2010.*

*Portfolio management market commentary is as of December 31, 2010, and may not come to pass. This information is subject to change at any time based on market and other conditions. Past performance does not guarantee future results. Current and future portfolio holdings are subject to risk.*

# Portfolio Summary

## DWS High Income VIP

| **Asset Allocation** (As a % of Investment Portfolio excluding Securities Lending Collateral) | 12/31/10 | 12/31/09 |
|---|---|---|
| Corporate Bonds | 87% | 91% |
| Cash Equivalents | 8% | 0% |
| Loan Participations and Assignments | 4% | 8% |
| Preferred Securities | 1% | 1% |
| | 100% | 100% |

| **Sector Diversification**<br>(As a % of Investment Portfolio excluding Cash Equivalents and Securities Lending Collateral) | 12/31/10 | 12/31/09 |
|---|---|---|
| Consumer Discretionary | 20% | 18% |
| Financials | 19% | 17% |
| Materials | 12% | 14% |
| Energy | 12% | 11% |
| Telecommunication Services | 11% | 11% |
| Industrials | 10% | 8% |
| Health Care | 5% | 7% |
| Information Technology | 4% | 3% |
| Consumer Staples | 4% | 3% |
| Utilities | 3% | 8% |
| | 100% | 100% |

| **Quality** (As a % of Investment Portfolio excluding Cash Equivalents and Securities Lending Collateral) | 12/31/10 | 12/31/09 |
|---|---|---|
| A | — | 1% |
| BBB | — | 7% |
| BB | 15% | 35% |
| B | 54% | 37% |
| CCC | 26% | 14% |
| D | 1% | 3% |
| Not Rated | 4% | 3% |
| | 100% | 100% |

| **Interest Rate Sensitivity** | 12/31/10 | 12/31/09 |
|---|---|---|
| Effective Maturity | 5.5 years | 4.8 years |
| Effective Duration | 3.5 years | 3.7 years |

*Asset allocation, sector diversification and interest rate sensitivity are subject to change.*

*The quality ratings represent the lower of Moody's Investors Service, Inc. ("Moody's") or Standard & Poor's Corporation ("S&P") credit ratings. The ratings of Moody's and S&P represent their opinions as to the quality of the securities they rate. Ratings are relative and subjective and are not absolute standards of quality. The Fund's credit quality does not remove market risk and is subject to change.*

*Effective maturity is the weighted average of the bonds held by the Fund taking into consideration any maturity shortening features.*

*Effective duration is an approximate measure of the Fund's sensitivity to interest rate changes taking into consideration any maturity shortening features.*

*For more complete details about the Fund's investment portfolio, see page 6.*

Following the Fund's fiscal first and third quarter-end, a complete portfolio holdings listing is filed with the SEC on Form N-Q. The form will be available on the SEC's Web site at www.sec.gov, and it also may be reviewed and copied at the SEC's Public Reference Room in Washington, D.C. Information on the operation of the SEC's Public Reference Room may be obtained by calling (800) SEC-0330. The Fund's portfolio holdings are also posted on www.dws-investments.com from time to time. Please see the Fund's current prospectus for more information.

## DWS High Income VIP

| | Principal Amount ($) (a) | Value ($) |
|---|---|---|
| **Corporate Bonds 85.6%** | | |
| **Consumer Discretionary 16.6%** | | |
| AMC Entertainment, Inc.: | | |
| 8.0%, 3/1/2014 | 590,000 | 595,900 |
| 8.75%, 6/1/2019 | 765,000 | 816,638 |
| American Achievement Corp., 144A, 10.875%, 4/15/2016 | 570,000 | 584,250 |
| Ameristar Casinos, Inc., 9.25%, 6/1/2014 | 395,000 | 422,650 |
| Asbury Automotive Group, Inc.: | | |
| 7.625%, 3/15/2017 | 590,000 | 595,900 |
| 144A, 8.375%, 11/15/2020 | 460,000 | 474,950 |
| Ashtead Holdings PLC, 144A, 8.625%, 8/1/2015 | 380,000 | 393,775 |
| Avis Budget Car Rental LLC: | | |
| 144A, 8.25%, 1/15/2019 | 535,000 | 540,350 |
| 9.625%, 3/15/2018 | 260,000 | 280,150 |
| Beazer Homes USA, Inc., 144A, 9.125%, 5/15/2019 | 285,000 | 270,750 |
| Bon-Ton Department Stores, Inc., 10.25%, 3/15/2014 | 155,000 | 158,100 |
| Brunswick Corp., 144A, 11.25%, 11/1/2016 | 295,000 | 351,050 |
| Cablevision Systems Corp.: | | |
| 7.75%, 4/15/2018 | 65,000 | 68,088 |
| 8.0%, 4/15/2020 | 65,000 | 69,550 |
| CanWest MediaWorks LP, 144A, 9.25%, 8/1/2015** | 340,000 | 57,800 |
| Carrols Corp., 9.0%, 1/15/2013 | 225,000 | 225,563 |
| CCO Holdings LLC: | | |
| 7.25%, 10/30/2017 | 520,000 | 527,800 |
| 7.875%, 4/30/2018 | 225,000 | 232,875 |
| 8.125%, 4/30/2020 | 150,000 | 157,875 |
| Cequel Communications Holdings I LLC, 144A, 8.625%, 11/15/2017 | 1,280,000 | 1,337,600 |
| Clear Channel Worldwide Holdings, Inc.: | | |
| Series A, 9.25%, 12/15/2017 | 100,000 | 108,750 |
| Series B, 9.25%, 12/15/2017 | 150,000 | 164,250 |
| CSC Holdings LLC: | | |
| 8.5%, 4/15/2014 | 500,000 | 549,375 |
| 8.5%, 6/15/2015 | 430,000 | 466,550 |
| DineEquity, Inc., 144A, 9.5%, 10/30/2018 | 455,000 | 482,300 |
| DISH DBS Corp., 7.125%, 2/1/2016 | 465,000 | 480,113 |
| Fontainebleau Las Vegas Holdings LLC, 144A, 11.0%, 6/15/2015** | 490,000 | 1,715 |
| Gannett Co., Inc.: | | |
| 8.75%, 11/15/2014 | 145,000 | 162,038 |
| 9.375%, 11/15/2017 | 295,000 | 328,925 |
| Goodyear Tire & Rubber Co., 10.5%, 5/15/2016 | 225,000 | 256,500 |
| Great Canadian Gaming Corp., 144A, 7.25%, 2/15/2015 | 505,000 | 516,362 |
| Group 1 Automotive, Inc., 144A, 3.0%, 3/15/2020 | 375,000 | 466,406 |
| Harrah's Operating Co., Inc.: | | |
| 10.0%, 12/15/2018 | 790,000 | 720,875 |
| 11.25%, 6/1/2017 | 1,415,000 | 1,591,875 |
| 144A, 12.75%, 4/15/2018 | 295,000 | 296,475 |
| Hertz Corp.: | | |
| 144A, 7.5%, 10/15/2018 | 905,000 | 938,937 |
| 8.875%, 1/1/2014 | 645,000 | 659,512 |
| Lear Corp.: | | |
| 7.875%, 3/15/2018 | 235,000 | 251,450 |
| 8.125%, 3/15/2020 | 230,000 | 250,125 |
| Macy's Retail Holdings, Inc., 8.375%, 7/15/2015 | 85,000 | 99,450 |
| Mediacom Broadband LLC, 8.5%, 10/15/2015 | 635,000 | 638,175 |
| Mediacom LLC, 9.125%, 8/15/2019 | 560,000 | 571,200 |
| MGM Resorts International: | | |
| 144A, 9.0%, 3/15/2020 | 145,000 | 159,500 |
| 144A, 10.0%, 11/1/2016 | 105,000 | 107,888 |
| 10.375%, 5/15/2014 | 340,000 | 381,650 |
| 11.125%, 11/15/2017 | 455,000 | 523,250 |
| Michaels Stores, Inc., Step-up Coupon, 0% to 11/1/2011, 13.0% to 11/1/2016 | 150,000 | 148,500 |
| Neiman Marcus Group, Inc., 10.375%, 10/15/2015 | 155,000 | 163,719 |
| Norcraft Companies LP, 10.5%, 12/15/2015 | 1,260,000 | 1,338,750 |
| Norcraft Holdings LP, 9.75%, 9/1/2012 | 630,000 | 633,937 |
| Penske Automotive Group, Inc., 7.75%, 12/15/2016 | 1,085,000 | 1,106,700 |
| PETCO Animal Supplies, Inc., 144A, 9.25%, 12/1/2018 | 315,000 | 331,931 |
| Phillips-Van Heusen Corp., 7.375%, 5/15/2020 | 160,000 | 170,000 |
| Regal Entertainment Group, 9.125%, 8/15/2018 | 140,000 | 149,100 |
| Sabre Holdings Corp., 8.35%, 3/15/2016 | 515,000 | 494,400 |
| Sears Holdings Corp., 144A, 6.625%, 10/15/2018 | 345,000 | 321,713 |
| Seminole Indian Tribe of Florida: | | |
| 144A, 7.75%, 10/1/2017 | 200,000 | 206,500 |
| 144A, 7.804%, 10/1/2020 | 450,000 | 438,525 |
| Simmons Bedding Co., 144A, 11.25%, 7/15/2015 | 315,000 | 340,200 |
| Sirius XM Radio, Inc., 144A, 8.75%, 4/1/2015 | 340,000 | 368,050 |
| Sonic Automotive, Inc.: | | |
| 5.0%, 10/1/2029 | 155,000 | 192,588 |
| Series B, 9.0%, 3/15/2018 | 565,000 | 594,662 |
| Standard Pacific Corp.: | | |
| 8.375%, 5/15/2018 | 100,000 | 100,000 |
| 10.75%, 9/15/2016 | 440,000 | 507,100 |
| Toys "R" Us, Inc., 7.375%, 10/15/2018 | 695,000 | 681,100 |
| Toys "R" Us-Delaware, Inc., 144A, 7.375%, 9/1/2016 | 200,000 | 210,000 |

*The accompanying notes are an integral part of the financial statements.*

| | | Principal Amount ($) (a) | Value ($) |
|---|---|---|---|
| Travelport LLC: | | | |
| 4.921%***, 9/1/2014 | | 390,000 | 345,150 |
| 9.0%, 3/1/2016 | | 390,000 | 377,813 |
| 9.875%, 9/1/2014 | | 275,000 | 267,781 |
| Unitymedia GmbH, 144A, 9.625%, 12/1/2019 | EUR | 550,000 | 808,461 |
| Unitymedia Hessen GmbH & Co., KG, 144A, 8.125%, 12/1/2017 | | 945,000 | 987,525 |
| Univision Communications, Inc., 144A, 7.875%, 11/1/2020 | | 140,000 | 147,000 |
| UPC Holding BV: | | | |
| 144A, 8.0%, 11/1/2016 | EUR | 405,000 | 562,850 |
| 144A, 8.375%, 8/15/2020 | EUR | 210,000 | 290,445 |
| Vertis, Inc., 13.5%, 4/1/2014 (PIK)** | | 258,716 | 7,761 |
| Visant Corp., 144A, 10.0%, 10/1/2017 | | 460,000 | 488,750 |
| Wynn Las Vegas LLC, 7.75%, 8/15/2020 | | 280,000 | 303,100 |
| Young Broadcasting, Inc., 8.75%, 1/15/2014** | | 2,040,000 | 20 |
| | | | **32,419,391** |
| **Consumer Staples 3.6%** | | | |
| B&G Foods, Inc., 7.625%, 1/15/2018 | | 170,000 | 178,925 |
| Dole Food Co., Inc., 144A, 8.0%, 10/1/2016 | | 215,000 | 226,825 |
| FAGE Dairy Industry SA, 144A, 9.875%, 2/1/2020 | | 555,000 | 555,000 |
| General Nutrition Centers, Inc., 5.75%***, 3/15/2014 (PIK) | | 280,000 | 277,200 |
| NBTY, Inc., 144A, 9.0%, 10/1/2018 | | 140,000 | 149,450 |
| North Atlantic Trading Co., 144A, 10.0%, 3/1/2012 | | 2,081,750 | 1,956,845 |
| Rite Aid Corp.: | | | |
| 7.5%, 3/1/2017 | | 295,000 | 283,569 |
| 8.0%, 8/15/2020 | | 580,000 | 603,925 |
| Smithfield Foods, Inc., 7.75%, 7/1/2017 | | 1,880,000 | 1,955,200 |
| Stater Bros. Holdings, Inc., 144A, 7.375%, 11/15/2018 | | 180,000 | 184,500 |
| SUPERVALU, Inc., 8.0%, 5/1/2016 | | 210,000 | 201,075 |
| Tops Holding Corp., 10.125%, 10/15/2015 | | 330,000 | 339,075 |
| | | | **6,911,589** |
| **Energy 10.6%** | | | |
| Allis-Chalmers Energy, Inc., 9.0%, 1/15/2014 | | 300,000 | 304,500 |
| Arch Coal, Inc., 7.25%, 10/1/2020 | | 110,000 | 116,050 |
| Belden & Blake Corp., 8.75%, 7/15/2012 | | 2,050,000 | 1,957,750 |
| Berry Petroleum Co., 6.75%, 11/1/2020 | | 535,000 | 537,675 |
| BreitBurn Energy Partners LP, 144A, 8.625%, 10/15/2020 | | 300,000 | 301,500 |
| Bristow Group, Inc., 7.5%, 9/15/2017 | | 485,000 | 511,675 |
| Chaparral Energy, Inc., 8.5%, 12/1/2015 | | 1,370,000 | 1,393,975 |

| | Principal Amount ($) (a) | Value ($) |
|---|---|---|
| Chesapeake Energy Corp.: | | |
| 6.625%, 8/15/2020 | 365,000 | 359,525 |
| 6.875%, 8/15/2018 | 185,000 | 187,775 |
| 6.875%, 11/15/2020 | 510,000 | 516,375 |
| 7.25%, 12/15/2018 | 620,000 | 641,700 |
| 9.5%, 2/15/2015 | 260,000 | 293,150 |
| Cloud Peak Energy Resources LLC: | | |
| 8.25%, 12/15/2017 | 145,000 | 155,694 |
| 8.5%, 12/15/2019 | 150,000 | 164,250 |
| CONSOL Energy, Inc.: | | |
| 144A, 8.0%, 4/1/2017 | 655,000 | 697,575 |
| 144A, 8.25%, 4/1/2020 | 250,000 | 270,000 |
| Continental Resources, Inc.: | | |
| 144A, 7.125%, 4/1/2021 | 175,000 | 183,750 |
| 7.375%, 10/1/2020 | 195,000 | 206,700 |
| 8.25%, 10/1/2019 | 105,000 | 116,550 |
| Crosstex Energy LP, 8.875%, 2/15/2018 | 365,000 | 391,006 |
| Dynegy Holdings, Inc., 7.75%, 6/1/2019 | 330,000 | 220,275 |
| Energy Transfer Equity LP, 7.5%, 10/15/2020 | 215,000 | 221,450 |
| Frontier Oil Corp., 6.875%, 11/15/2018 | 315,000 | 321,300 |
| Genesis Energy LP, 144A, 7.875%, 12/15/2018 | 365,000 | 363,175 |
| Global Geophysical Services, Inc., 10.5%, 5/1/2017 | 775,000 | 771,125 |
| Harvest Operations Corp., 144A, 6.875%, 10/1/2017 | 140,000 | 144,200 |
| Holly Corp., 9.875%, 6/15/2017 | 545,000 | 594,050 |
| Holly Energy Partners LP, 144A, 8.25%, 3/15/2018 | 330,000 | 344,850 |
| Inergy LP, 144A, 7.0%, 10/1/2018 | 350,000 | 352,625 |
| Linn Energy LLC: | | |
| 144A, 7.75%, 2/1/2021 | 335,000 | 343,375 |
| 144A, 8.625%, 4/15/2020 | 305,000 | 328,638 |
| 11.75%, 5/15/2017 | 650,000 | 744,250 |
| Newfield Exploration Co., 7.125%, 5/15/2018 | 640,000 | 673,600 |
| Offshore Group Investments Ltd., 144A, 11.5%, 8/1/2015 | 275,000 | 298,375 |
| OPTI Canada, Inc., 7.875%, 12/15/2014 | 690,000 | 487,312 |
| Petrohawk Energy Corp.: | | |
| 7.25%, 8/15/2018 | 280,000 | 282,800 |
| 7.875%, 6/1/2015 | 220,000 | 229,075 |
| 10.5%, 8/1/2014 | 380,000 | 433,200 |
| Plains Exploration & Production Co.: | | |
| 7.0%, 3/15/2017 | 220,000 | 226,050 |
| 7.625%, 6/1/2018 | 720,000 | 757,800 |
| 8.625%, 10/15/2019 | 400,000 | 438,000 |
| Range Resources Corp., 6.75%, 8/1/2020 | 105,000 | 108,281 |
| Regency Energy Partners LP, 6.875%, 12/1/2018 | 205,000 | 207,563 |
| Sabine Pass LNG LP: | | |
| 7.25%, 11/30/2013 | 930,000 | 904,425 |
| 7.5%, 11/30/2016 | 100,000 | 93,750 |
| SandRidge Energy, Inc., 8.625%, 4/1/2015 (PIK) | 140,000 | 143,325 |

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| | | Principal Amount ($) (a) | Value ($) |
|---|---|---|---|
| Southwestern Energy Co., 7.5%, 2/1/2018 | | 585,000 | 659,587 |
| Stone Energy Corp.: | | | |
| 6.75%, 12/15/2014 | | 590,000 | 575,250 |
| 8.625%, 2/1/2017 | | 125,000 | 126,875 |
| | | | **20,701,756** |
| **Financials 14.9%** | | | |
| Abengoa Finance SAU, 144A, 8.875%, 11/1/2017 | | 775,000 | 716,875 |
| Algoma Acquisition Corp., 144A, 9.875%, 6/15/2015 | | 830,000 | 747,000 |
| Ally Financial, Inc.: | | | |
| 144A, 6.25%, 12/1/2017 | | 555,000 | 555,000 |
| 7.0%, 2/1/2012 | | 565,000 | 584,775 |
| 144A, 7.5%, 9/15/2020 | | 705,000 | 739,369 |
| 8.0%, 3/15/2020 | | 685,000 | 748,362 |
| 8.0%, 11/1/2031 | | 215,000 | 231,663 |
| Antero Resources Finance Corp., 9.375%, 12/1/2017 | | 70,000 | 73,238 |
| Ardagh Packaging Finance PLC: | | | |
| 144A, 7.375%, 10/15/2017 | | 215,000 | 221,719 |
| 144A, 7.375%, 10/15/2017 | EUR | 140,000 | 188,485 |
| Ashton Woods USA LLC, 144A, Step-up Coupon, 0% to 6/30/2012, 11.0% to 6/30/2015 | | 712,400 | 395,382 |
| AWAS Aviation Capital Ltd., 144A, 7.0%, 10/15/2016 | | 600,000 | 594,750 |
| Blue Acquisition Sub, Inc., 144A, 9.875%, 10/15/2018 (b) | | 165,000 | 175,725 |
| Calpine Construction Finance Co., LP, 144A, 8.0%, 6/1/2016 | | 570,000 | 605,625 |
| Case New Holland, Inc., 7.75%, 9/1/2013 | | 290,000 | 311,750 |
| CIT Group, Inc.: | | | |
| 7.0%, 5/1/2013 | | 430,000 | 438,600 |
| 7.0%, 5/1/2015 | | 623,195 | 624,753 |
| 7.0%, 5/1/2017 | | 2,085,000 | 2,090,212 |
| Dunkin Finance Corp., 144A, 9.625%, 12/1/2018 | | 245,000 | 247,450 |
| DuPont Fabros Technology LP, (REIT), 8.5%, 12/15/2017 | | 435,000 | 465,450 |
| E*TRADE Financial Corp.: | | | |
| 7.375%, 9/15/2013 | | 995,000 | 990,025 |
| 12.5%, 11/30/2017 (PIK) | | 632,000 | 742,600 |
| Express LLC, 8.75%, 3/1/2018 | | 260,000 | 276,250 |
| FCE Bank PLC, 9.375%, 1/17/2014 | EUR | 700,000 | 1,040,644 |
| Fibria Overseas Finance Ltd., 144A, 7.5%, 5/4/2020 | | 257,000 | 269,850 |
| Ford Motor Credit Co., LLC: | | | |
| 6.625%, 8/15/2017 | | 355,000 | 373,102 |
| 8.125%, 1/15/2020 | | 100,000 | 116,341 |
| Fresenius US Finance II, Inc., 144A, 9.0%, 7/15/2015 | | 420,000 | 480,900 |
| GenOn Escrow Corp., 144A, 9.5%, 10/15/2018 | | 140,000 | 139,125 |
| Giraffe Acquisition Corp., 144A, 9.125%, 12/1/2018 | | 330,000 | 344,025 |
| Hellas Telecommunications Finance SCA, 144A, 8.985%, 7/15/2015 (PIK)* | EUR | 322,107 | 258 |
| Hexion US Finance Corp., 8.875%, 2/1/2018 | | 2,000,000 | 2,137,500 |
| Inmarsat Finance PLC, 144A, 7.375%, 12/1/2017 | | 670,000 | 703,500 |
| International Lease Finance Corp.: | | | |
| 144A, 8.625%, 9/15/2015 | | 235,000 | 252,625 |
| 144A, 8.75%, 3/15/2017 | | 465,000 | 498,712 |
| iPayment, Inc., 9.75%, 5/15/2014 | | 475,000 | 446,500 |
| National Money Mart Co., 10.375%, 12/15/2016 | | 790,000 | 853,200 |
| Navios Maritime Acquisition Corp., 144A, 8.625%, 11/1/2017 | | 150,000 | 153,375 |
| Nielsen Finance LLC: | | | |
| Step-up Coupon, 0% to 8/1/2011, 12.5% to 8/1/2016 | | 505,000 | 530,250 |
| 144A, 7.75%, 10/15/2018 | | 150,000 | 155,250 |
| 11.5%, 5/1/2016 | | 150,000 | 173,250 |
| Nuveen Investments, Inc., 10.5%, 11/15/2015 | | 700,000 | 715,750 |
| OMEGA Healthcare Investors, Inc., 144A, (REIT), 6.75%, 10/15/2022 | | 305,000 | 302,331 |
| Pinafore LLC, 144A, 9.0%, 10/1/2018 | | 230,000 | 248,400 |
| Pinnacle Foods Finance LLC: | | | |
| 8.25%, 9/1/2017 | | 425,000 | 434,562 |
| 9.25%, 4/1/2015 | | 695,000 | 723,669 |
| Reynolds Group Issuer, Inc.: | | | |
| 144A, 7.125%, 4/15/2019 | | 415,000 | 422,263 |
| 144A, 7.75%, 10/15/2016 | | 550,000 | 581,625 |
| 144A, 8.5%, 5/15/2018 | | 610,000 | 613,050 |
| 144A, 9.0%, 4/15/2019 | | 590,000 | 611,387 |
| Roadhouse Financing, Inc., 144A, 10.75%, 10/15/2017 | | 230,000 | 248,400 |
| SLM Corp., 8.0%, 3/25/2020 | | 135,000 | 136,877 |
| Susser Holdings LLC, 8.5%, 5/15/2016 | | 175,000 | 187,688 |
| Tropicana Entertainment LLC, 9.625%, 12/15/2014** | | 1,220,000 | 622 |
| UCI Holdco, Inc., 9.25%***, 12/15/2013 (PIK) | | 769,696 | 767,772 |
| Virgin Media Finance PLC, Series 1, 9.5%, 8/15/2016 | | 1,135,000 | 1,282,550 |
| WMG Acquisition Corp., 9.5%, 6/15/2016 | | 375,000 | 402,188 |
| | | | **29,112,599** |
| **Health Care 3.9%** | | | |
| Community Health Systems, Inc., 8.875%, 7/15/2015 | | 435,000 | 456,750 |
| DaVita, Inc.: | | | |
| 6.375%, 11/1/2018 | | 130,000 | 129,350 |
| 6.625%, 11/1/2020 | | 130,000 | 128,700 |
| Hanger Orthopedic Group, Inc., 7.125%, 11/15/2018 | | 140,000 | 139,650 |
| HCA Holdings, Inc., 144A, 7.75%, 5/15/2021 (b) | | 605,000 | 605,000 |
| HCA, Inc.: | | | |
| 9.25%, 11/15/2016 | | 2,040,000 | 2,176,425 |
| 9.625%, 11/15/2016 (PIK) | | 809,000 | 866,641 |
| IASIS Healthcare LLC, 8.75%, 6/15/2014 | | 525,000 | 538,781 |
| Mylan, Inc., 144A, 7.875%, 7/15/2020 | | 95,000 | 102,363 |

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| | | Principal Amount ($) (a) | Value ($) |
|---|---|---|---|
| The Cooper Companies, Inc., 7.125%, 2/15/2015 | | 840,000 | 865,200 |
| Valeant Pharmaceuticals International: | | | |
| 144A, 6.75%, 10/1/2017 | | 245,000 | 243,775 |
| 144A, 7.0%, 10/1/2020 | | 385,000 | 380,187 |
| Vanguard Health Holding Co. II, LLC: | | | |
| 8.0%, 2/1/2018 | | 285,000 | 292,125 |
| 144A, 8.0%, 2/1/2018 | | 305,000 | 311,100 |
| Warner Chilcott Co., LLC, 144A, 7.75%, 9/15/2018 | | 420,000 | 424,200 |
| | | | **7,660,247** |
| **Industrials 8.8%** | | | |
| Accuride Corp., 144A, 9.5%, 8/1/2018 | | 405,000 | 438,413 |
| Actuant Corp., 6.875%, 6/15/2017 | | 300,000 | 306,750 |
| AMGH Merger Sub, Inc., 144A, 9.25%, 11/1/2018 | | 190,000 | 199,500 |
| ARAMARK Corp., 8.5%, 2/1/2015 | | 560,000 | 585,200 |
| Armored Autogroup, Inc., 144A, 9.25%, 11/1/2018 | | 610,000 | 605,425 |
| ArvinMeritor, Inc., 8.125%, 9/15/2015 | | 280,000 | 292,950 |
| BE Aerospace, Inc.: | | | |
| 6.875%, 10/1/2020 | | 210,000 | 216,825 |
| 8.5%, 7/1/2018 | | 300,000 | 328,500 |
| Belden, Inc., 7.0%, 3/15/2017 | | 420,000 | 425,250 |
| Briggs & Stratton Corp., 6.875%, 12/15/2020 | | 195,000 | 198,900 |
| Cenveo Corp., 8.875%, 2/1/2018 | | 1,055,000 | 1,020,712 |
| CHC Helicopter SA, 144A, 9.25%, 10/15/2020 | | 390,000 | 403,650 |
| Congoleum Corp., 9.0%, 12/31/2017 (PIK) | | 396,000 | 272,998 |
| Corrections Corp. of America, 7.75%, 6/1/2017 | | 35,000 | 37,144 |
| Delta Air Lines, Inc., 144A, 9.5%, 9/15/2014 | | 99,000 | 107,786 |
| DynCorp International, Inc., 144A, 10.375%, 7/1/2017 | | 490,000 | 502,250 |
| FTI Consulting, Inc., 144A, 6.75%, 10/1/2020 | | 195,000 | 193,538 |
| Garda World Security Corp., 144A, 9.75%, 3/15/2017 | | 375,000 | 402,188 |
| Great Lakes Dredge & Dock Co., 7.75%, 12/15/2013 | | 300,000 | 302,625 |
| Interline Brands, Inc., 144A, 7.0%, 11/15/2018 | | 295,000 | 299,425 |
| K. Hovnanian Enterprises, Inc.: | | | |
| 8.875%, 4/1/2012 | | 435,000 | 426,300 |
| 10.625%, 10/15/2016 | | 365,000 | 374,125 |
| Kansas City Southern de Mexico SA de CV: | | | |
| 7.375%, 6/1/2014 | | 1,045,000 | 1,092,025 |
| 8.0%, 2/1/2018 | | 715,000 | 773,987 |
| Kansas City Southern Railway Co., 8.0%, 6/1/2015 | | 655,000 | 704,125 |
| Navios Maritime Holdings, Inc., 9.5%, 12/15/2014 | | 680,000 | 707,200 |
| Ply Gem Industries, Inc., 13.125%, 7/15/2014 | | 515,000 | 547,187 |
| RailAmerica, Inc., 9.25%, 7/1/2017 | | 304,000 | 334,020 |
| RBS Global, Inc. & Rexnord Corp.: | | | |
| 8.5%, 5/1/2018 | | 715,000 | 759,687 |
| 11.75%, 8/1/2016 | | 120,000 | 128,700 |
| Rearden G Holdings EINS GmbH, 144A, 7.875%, 3/30/2020 | | 135,000 | 142,425 |
| Sitel LLC, 144A, 11.5%, 4/1/2018 | | 565,000 | 466,125 |
| Spirit AeroSystems, Inc.: | | | |
| 144A, 6.75%, 12/15/2020 | | 205,000 | 205,513 |
| 7.5%, 10/1/2017 | | 215,000 | 223,600 |
| SPX Corp., 144A, 6.875%, 9/1/2017 | | 130,000 | 138,125 |
| Titan International, Inc., 144A, 7.875%, 10/1/2017 | | 945,000 | 996,975 |
| Triumph Group, Inc., 8.0%, 11/15/2017 | | 75,000 | 78,000 |
| Tutor Perini Corp., 144A, 7.625%, 11/1/2018 | | 325,000 | 326,625 |
| United Rentals North America, Inc.: | | | |
| 9.25%, 12/15/2019 | | 830,000 | 923,375 |
| 10.875%, 6/15/2016 | | 390,000 | 445,575 |
| USG Corp., 144A, 9.75%, 8/1/2014 | | 220,000 | 232,100 |
| | | | **17,165,823** |
| **Information Technology 4.1%** | | | |
| Alcatel-Lucent USA, Inc., 6.45%, 3/15/2029 | | 570,000 | 450,300 |
| Allen Systems Group, Inc., 144A, 10.5%, 11/15/2016 | | 210,000 | 211,575 |
| Amkor Technology, Inc., 7.375%, 5/1/2018 | | 250,000 | 260,000 |
| Aspect Software, Inc., 144A, 10.625%, 5/15/2017 | | 350,000 | 359,188 |
| CDW LLC, 11.0%, 10/12/2015 | | 440,000 | 456,500 |
| Fidelity National Information Services, Inc.: | | | |
| 144A, 7.625%, 7/15/2017 | | 95,000 | 99,988 |
| 144A, 7.875%, 7/15/2020 | | 130,000 | 137,475 |
| First Data Corp., 144A, 8.875%, 8/15/2020 (b) | | 495,000 | 522,225 |
| Freescale Semiconductor, Inc., 144A, 9.25%, 4/15/2018 | | 1,520,000 | 1,672,000 |
| InterXion Holding NV, 144A, 9.5%, 2/12/2017 | EUR | 210,000 | 294,654 |
| Jabil Circuit, Inc., 7.75%, 7/15/2016 | | 145,000 | 162,763 |
| MasTec, Inc., 7.625%, 2/1/2017 | | 610,000 | 606,950 |
| SunGard Data Systems, Inc.: | | | |
| 144A, 7.375%, 11/15/2018 | | 140,000 | 140,700 |
| 10.25%, 8/15/2015 | | 1,790,000 | 1,881,737 |
| 10.625%, 5/15/2015 | | 365,000 | 402,412 |
| Vangent, Inc., 9.625%, 2/15/2015 | | 350,000 | 316,750 |
| | | | **7,975,217** |
| **Materials 10.9%** | | | |
| Appleton Papers, Inc., 144A, 11.25%, 12/15/2015 | | 237,000 | 189,600 |
| Ashland, Inc., 9.125%, 6/1/2017 | | 260,000 | 299,650 |

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| | | Principal Amount ($) (a) | Value ($) |
|---|---|---|---|
| Berry Plastics Corp.: | | | |
| 8.25%, 11/15/2015 | | 660,000 | 699,600 |
| 9.5%, 5/15/2018 | | 390,000 | 390,975 |
| 144A, 9.75%, 1/15/2021 | | 460,000 | 455,400 |
| Boise Paper Holdings LLC, 8.0%, 4/1/2020 | | 170,000 | 181,900 |
| BWAY Parent Co., Inc., 144A, 10.125%, 11/1/2015 (PIK) | | 230,000 | 232,300 |
| Celanese US Holdings LLC, 144A, 6.625%, 10/15/2018 | | 200,000 | 206,500 |
| Clearwater Paper Corp., 144A, 7.125%, 11/1/2018 | | 390,000 | 402,675 |
| Clondalkin Acquisition BV, 144A, 2.302%***, 12/15/2013 | | 265,000 | 253,738 |
| CPG International I, Inc., 10.5%, 7/1/2013 | | 880,000 | 897,600 |
| Crown Americas LLC, 7.625%, 5/15/2017 | | 40,000 | 43,000 |
| Crown European Holdings SA, 144A, 7.125%, 8/15/2018 | EUR | 125,000 | 174,137 |
| Domtar Corp., 10.75%, 6/1/2017 | | 380,000 | 478,800 |
| Essar Steel Algoma, Inc., 144A, 9.375%, 3/15/2015 | | 1,410,000 | 1,418,812 |
| Exopack Holding Corp., 11.25%, 2/1/2014 | | 1,415,000 | 1,468,062 |
| FMG Resources August 2006 Pty Ltd., 144A, 7.0%, 11/1/2015 | | 140,000 | 143,500 |
| GEO Specialty Chemicals, Inc.: | | | |
| 144A, 7.5%, 3/31/2015 (PIK) | | 1,297,793 | 1,116,102 |
| 10.0%, 3/31/2015 | | 1,277,440 | 1,162,470 |
| Graphic Packaging International, Inc.: | | | |
| 7.875%, 10/1/2018 | | 70,000 | 73,325 |
| 9.5%, 6/15/2017 | | 810,000 | 883,912 |
| Hexcel Corp., 6.75%, 2/1/2015 | | 1,425,000 | 1,453,500 |
| Huntsman International LLC: | | | |
| 8.625%, 3/15/2020 | | 330,000 | 358,875 |
| 144A, 8.625%, 3/15/2021 | | 140,000 | 151,200 |
| Ineos Finance PLC: | | | |
| 144A, 9.0%, 5/15/2015 | | 325,000 | 345,719 |
| 144A, 9.25%, 5/15/2015 | EUR | 120,000 | 169,977 |
| Koppers, Inc., 7.875%, 12/1/2019 | | 440,000 | 471,900 |
| Lumena Resources Corp., 144A, 12.0%, 10/27/2014 | | 1,120,000 | 1,041,600 |
| Lyondell Chemical Co., 144A, 8.0%, 11/1/2017 | | 323,000 | 357,319 |
| Millar Western Forest Products Ltd., 7.75%, 11/15/2013 | | 200,000 | 189,500 |
| Momentive Performance Materials, Inc.: | | | |
| 144A, 9.0%, 1/15/2021 | | 385,000 | 406,175 |
| 144A, 9.5%, 1/15/2021 | EUR | 385,000 | 535,054 |
| NewMarket Corp., 7.125%, 12/15/2016 | | 1,005,000 | 1,027,612 |
| OI European Group BV, 144A, 6.75%, 9/15/2020 | EUR | 130,000 | 175,022 |
| Radnor Holdings Corp., 11.0%, 3/15/2010** | | 265,000 | 27 |

| | | Principal Amount ($) (a) | Value ($) |
|---|---|---|---|
| Rain CII Carbon LLC, 144A, 8.0%, 12/1/2018 | | 270,000 | 276,750 |
| Silgan Holdings, Inc., 7.25%, 8/15/2016 | | 415,000 | 441,975 |
| Solo Cup Co., 10.5%, 11/1/2013 | | 210,000 | 219,450 |
| Texas Industries, Inc., 144A, 9.25%, 8/15/2020 | | 465,000 | 494,063 |
| United States Steel Corp., 7.375%, 4/1/2020 | | 480,000 | 492,000 |
| Viskase Companies, Inc., 144A, 9.875%, 1/15/2018 | | 940,000 | 979,950 |
| Wolverine Tube, Inc., 15.0%, 3/31/2012 (PIK)** | | 830,088 | 448,248 |
| | | | **21,207,974** |
| **Telecommunication Services 9.7%** | | | |
| Buccaneer Merger Sub, Inc., 144A, 9.125%, 1/15/2019 | | 130,000 | 134,225 |
| Cincinnati Bell, Inc.: | | | |
| 8.25%, 10/15/2017 | | 720,000 | 712,800 |
| 8.375%, 10/15/2020 | | 1,030,000 | 988,800 |
| 8.75%, 3/15/2018 | | 350,000 | 328,125 |
| Clearwire Communications LLC, 144A, 12.0%, 12/1/2015 | | 240,000 | 259,200 |
| Cricket Communications, Inc.: | | | |
| 144A, 7.75%, 10/15/2020 | | 1,455,000 | 1,385,887 |
| 10.0%, 7/15/2015 (b) | | 380,000 | 407,075 |
| Crown Castle International Corp., 9.0%, 1/15/2015 | | 775,000 | 854,437 |
| Digicel Group Ltd., 144A, 10.5%, 4/15/2018 | | 495,000 | 544,500 |
| Digicel Ltd., 144A, 8.25%, 9/1/2017 | | 1,090,000 | 1,117,250 |
| ERC Ireland Preferred Equity Ltd., 144A, 8.05%***, 2/15/2017 (PIK) | EUR | 638,816 | 76,584 |
| Frontier Communications Corp.: | | | |
| 7.875%, 4/15/2015 | | 65,000 | 71,013 |
| 8.25%, 4/15/2017 | | 395,000 | 433,512 |
| 8.5%, 4/15/2020 | | 525,000 | 573,562 |
| 8.75%, 4/15/2022 | | 70,000 | 76,300 |
| Grupo Iusacell Celular SA de CV, 10.0%, 3/31/2012** | | 278,182 | 102,927 |
| Hughes Network Systems LLC, 9.5%, 4/15/2014 | | 1,105,000 | 1,139,531 |
| Intelsat Corp., 9.25%, 6/15/2016 | | 1,735,000 | 1,873,800 |
| Intelsat Jackson Holdings SA: | | | |
| 144A, 7.25%, 10/15/2020 | | 695,000 | 701,950 |
| 11.25%, 6/15/2016 | | 65,000 | 70,038 |
| Intelsat Luxembourg SA, 11.5%, 2/4/2017 (PIK) | | 765,000 | 845,325 |
| Intelsat Subsidiary Holding Co. SA: | | | |
| Series B, 144A, 8.875%, 1/15/2015 | | 165,000 | 168,713 |
| 8.875%, 1/15/2015 | | 960,000 | 986,400 |
| MetroPCS Wireless, Inc.: | | | |
| 6.625%, 11/15/2020 | | 480,000 | 457,200 |
| 7.875%, 9/1/2018 | | 135,000 | 140,063 |
| Pacnet Ltd., 144A, 9.25%, 11/9/2015 | | 225,000 | 231,190 |
| Sprint Nextel Corp., 8.375%, 8/15/2017 | | 590,000 | 632,775 |

*The accompanying notes are an integral part of the financial statements.*

| | | Principal Amount ($) (a) | Value ($) |
|---|---|---|---|
| Telesat Canada, 11.0%, 11/1/2015 | | 1,545,000 | 1,734,261 |
| West Corp.: | | | |
| 144A, 7.875%, 1/15/2019 | | 285,000 | 289,988 |
| 144A, 8.625%, 10/1/2018 | | 75,000 | 79,500 |
| Windstream Corp.: | | | |
| 7.0%, 3/15/2019 | | 430,000 | 423,550 |
| 7.875%, 11/1/2017 | | 845,000 | 888,306 |
| 8.125%, 9/1/2018 | | 180,000 | 189,000 |
| 8.625%, 8/1/2016 | | 70,000 | 73,675 |
| | | | **18,991,462** |
| **Utilities 2.5%** | | | |
| AES Corp.: | | | |
| 8.0%, 10/15/2017 | | 415,000 | 438,863 |
| 8.0%, 6/1/2020 | | 525,000 | 556,500 |
| Calpine Corp.: | | | |
| 144A, 7.5%, 2/15/2021 | | 485,000 | 477,725 |
| 144A, 7.875%, 7/31/2020 | | 560,000 | 567,000 |
| Edison Mission Energy, 7.0%, 5/15/2017 | | 1,220,000 | 966,850 |
| Ferrellgas LP, 144A, 6.5%, 5/1/2021 | | 120,000 | 117,000 |
| GenOn Energy, Inc., 7.875%, 6/15/2017 | | 150,000 | 145,500 |
| NRG Energy, Inc.: | | | |
| 7.375%, 1/15/2017 | | 990,000 | 1,019,700 |
| 144A, 8.25%, 9/1/2020 | | 490,000 | 502,250 |
| | | | **4,791,388** |
| **Total Corporate Bonds** (Cost $166,048,582) | | | **166,937,446** |

## Loan Participations and Assignments 4.3%

### Senior Loans***

| | | Principal Amount ($) (a) | Value ($) |
|---|---|---|---|
| Alliance Mortgage Cycle Loan, Term Loan A, 9.5%, 6/1/2010** | | 700,000 | 0 |
| Buffets, Inc.: | | | |
| Letter of Credit, First Lien, 7.539%, 4/22/2015 (PIK) | | 94,092 | 71,980 |
| Term Loan B, 12.0%, 4/21/2015 (PIK) | | 379,251 | 356,307 |
| Burger King Corp., New Term Loan B, 6.25%, 10/19/2016 | | 475,000 | 482,880 |
| Clear Channel Communication, Term Loan B, 3.911%, 1/28/2016 | | 580,000 | 505,760 |
| Dunkin' Brands, Inc., Term Loan B, 5.75%, 11/23/2017 | | 360,000 | 364,851 |
| Hawker Beechcraft Acquisition Co., LLC: | | | |
| Term Loan, 2.261%, 3/26/2014 | | 1,014,352 | 892,112 |
| Letter of Credit, 2.289%, 3/26/2014 | | 60,643 | 53,335 |
| IASIS Healthcare LLC, Term Loan, 5.538%, 6/13/2014 (PIK) | | 681,580 | 657,554 |
| Kabel Deutschland GmbH, Term Loan, 8.272%, 11/19/2014 (PIK) | EUR | 1,699,736 | 2,265,246 |
| Nuveen Investments, Inc., First Lien, Term Loan, 3.303%, 11/13/2014 | | 590,000 | 565,049 |
| Pinafore LLC, Term Loan B, 6.25%, 9/29/2016 | | 606,772 | 616,065 |
| Roundy's Supermarkets, Inc., Second Lien, Term Loan, 10.0%, 4/18/2016 | | 325,000 | 330,486 |
| Tribune Co., Term Loan B, LIBOR plus 3.0%, 6/4/2014** | | 1,009,426 | 705,589 |
| US Foodservice, Inc., Term Loan B, 2.76%, 7/3/2014 | | 465,179 | 427,732 |
| **Total Loan Participations and Assignments** (Cost $9,217,474) | | | **8,294,946** |

## Preferred Security 0.5%

### Materials

| | Principal Amount ($) (a) | Value ($) |
|---|---|---|
| Hercules, Inc., 6.5%, 6/30/2029 (Cost $733,742) | 1,135,000 | **879,625** |

| | Units | Value ($) |
|---|---|---|
| **Other Investments 0.0%** | | |
| **Consumer Discretionary** | | |
| AOT Bedding Super Holdings LLC* (Cost $31,000) | 31 | **31,000** |

| | Shares | Value ($) |
|---|---|---|
| **Common Stocks 0.1%** | | |
| **Consumer Discretionary 0.1%** | | |
| Buffets Restaurants Holdings, Inc.* | 18,256 | 63,896 |
| Dex One Corp.* | 3,884 | 28,975 |
| SuperMedia, Inc.* | 726 | 6,323 |
| Trump Entertainment Resorts, Inc.* | 45 | 821 |
| Vertis Holdings, Inc.* | 9,993 | 0 |
| | | **100,015** |
| **Industrials 0.0%** | | |
| Congoleum Corp.* | 1,200,000 | 1 |
| Quad Graphics, Inc.* | 649 | 26,778 |
| | | **26,779** |
| **Materials 0.0%** | | |
| GEO Specialty Chemicals, Inc.* | 24,225 | 20,591 |
| GEO Specialty Chemicals, Inc. 144A* | 2,206 | 1,875 |
| | | **22,466** |
| **Total Common Stocks** (Cost $2,406,514) | | **149,260** |
| **Warrants 0.0%** | | |
| **Consumer Discretionary 0.0%** | | |
| Reader's Digest Association, Inc., Expiration Date 2/19/2014* | 1,115 | **33** |
| **Materials 0.0%** | | |
| Hercules Trust II, Expiration Date 3/31/2029* | 1,100 | **12,514** |
| **Total Warrants** (Cost $244,286) | | **12,547** |

*The accompanying notes are an integral part of the financial statements.*

| | Shares | Value ($) |
|---|---|---|
| **Preferred Stock 0.2%** | | |
| **Financials** | | |
| Ally Financial, Inc. Series G, 144A, 7.0% (Cost $402,862) | 440 | **415,869** |
| **Securities Lending Collateral 0.7%** | | |
| Daily Assets Fund Institutional, 0.27% (c) (d) (Cost $1,419,848) | 1,419,848 | **1,419,848** |

| | Shares | Value ($) |
|---|---|---|
| **Cash Equivalents 7.9%** | | |
| Central Cash Management Fund, 0.19% (c) (Cost $15,421,844) | 15,421,844 | **15,421,844** |

| | % of Net Assets | Value ($) |
|---|---|---|
| **Total Investment Portfolio** (Cost $195,926,152)† | 99.3 | **193,562,385** |
| **Other Assets and Liabilities, Net** | 0.7 | **1,455,541** |
| **Net Assets** | 100.0 | **195,017,926** |

* *Non-income producing security.*

** *Non-income producing security. Issuer has defaulted on the payment of principal or interest or has filed for bankruptcy. The following table represents bonds and senior loans that are in default:*

| Securities | Coupon | Maturity Date | Principal Amount ($) | | Acquisition Cost ($) | Value ($) |
|---|---|---|---|---|---|---|
| Alliance Mortgage Cycle Loan | 9.5% | 6/1/2010 | 700,000 | USD | 700,000 | 0 |
| CanWest MediaWorks LP | 9.25% | 8/1/2015 | 340,000 | USD | 340,000 | 57,800 |
| Fontainebleau Las Vegas Holdings LLC | 11.0% | 6/15/2015 | 490,000 | USD | 495,963 | 1,715 |
| Grupo Iusacell Celular SA de CV | 10.0% | 3/31/2012 | 278,182 | USD | 264,717 | 102,927 |
| Radnor Holdings Corp. | 11.0% | 3/15/2010 | 265,000 | USD | 234,313 | 27 |
| Tribune Co. | LIBOR plus 3.0% | 6/4/2014 | 1,009,426 | USD | 905,407 | 705,589 |
| Tropicana Entertainment LLC | 9.625% | 12/15/2014 | 1,220,000 | USD | 959,601 | 622 |
| Vertis, Inc. | 13.5% | 4/1/2014 | 258,716 | USD | 105,102 | 7,761 |
| Wolverine Tube, Inc. | 15.0% | 3/31/2012 | 830,088 | USD | 830,088 | 448,248 |
| Young Broadcasting, Inc. | 8.75% | 1/15/2014 | 2,040,000 | USD | 1,981,498 | 20 |
| | | | | | **6,816,689** | **1,324,709** |

*** *These securities are shown at their current rate as of December 31, 2010. Floating rate securities' yields vary with a designated market index or market rate, such as the coupon-equivalent of the US Treasury bill rate.*

† *The cost for federal income tax purposes was $195,945,391. At December 31, 2010, net unrealized depreciation for all securities based on tax cost was $2,383,006. This consisted of aggregate gross unrealized appreciation for all securities in which there was an excess of value over tax cost of $9,065,576 and aggregate gross unrealized depreciation for all securities in which there was an excess of tax cost over value of $11,448,582.*

(a) *Principal amount stated in US dollars unless otherwise noted.*

(b) *All or a portion of these securities were on loan (see Notes to Financial Statements). The value of all securities loaned at December 31, 2010 amounted to $1,366,721, which is 0.7% of net assets.*

(c) *Affiliated fund managed by Deutsche Investment Management Americas Inc. The rate shown is the annualized seven-day yield at period end.*

(d) *Represents collateral held in connection with securities lending. Income earned by the Fund is net of borrower rebates.*

*144A: Security exempt from registration under Rule 144A of the Securities Act of 1933. These securities may be resold in transactions exempt from registration, normally to qualified institutional buyers.*

*LIBOR: London InterBank Offered Rate*

*PIK: Denotes that all or a portion of the income is paid in kind.*

*REIT: Real Estate Investment Trust*

*The accompanying notes are an integral part of the financial statements.*

*At December 31, 2010, open credit default swap contracts sold were as follows:*

| Effective/ Expiration Date | Notional Amount ($) (e) | Fixed Cash Flows Received | Underlying Debt Obligation/Quality Rating (f) | Value ($) | Upfront Payments Paid/ (Received) ($) | Unrealized Appreciation ($) |
|---|---|---|---|---|---|---|
| 6/21/2010<br>9/20/2013 | 380,000[1] | 5.0% | Ford Motor Co.,<br>6.5%, 8/1/2018, B | 38,123 | 4,658 | 33,465 |
| 6/21/2010<br>9/20/2013 | 1,230,000[2] | 5.0% | Ford Motor Co.,<br>6.5%, 8/1/2018, B | 127,393 | (56,319) | 183,712 |
| 6/21/2010<br>9/20/2015 | 560,000[3] | 5.0% | Ford Motor Co.,<br>6.5%, 8/1/2018, B | 63,225 | (9,982) | 73,207 |
| 6/21/2010<br>9/20/2015 | 175,000[4] | 5.0% | Ford Motor Co.,<br>6.5%, 8/1/2018, B | 19,758 | (16,625) | 36,383 |
| 6/21/2010<br>9/20/2015 | 320,000[5] | 5.0% | Ford Motor Co.,<br>6.5%, 8/1/2018, B | 32,103 | (9,200) | 41,303 |
| 6/21/2010<br>9/20/2015 | 100,000[2] | 5.0% | Ford Motor Co.,<br>6.5%, 8/1/2018, B | 11,290 | (6,896) | 18,186 |
| **Total unrealized appreciation** | | | | | | **386,256** |

(e) *The maximum potential amount of future undiscounted payments that the Fund could be required to make under a credit default swap contract would be the notional amount of the contract. These potential amounts would be partially offset by any recovery values of the referenced debt obligation or net amounts received from the settlement of buy protection credit default swap contracts entered into by the Fund for the same referenced debt obligation.*

(f) *The quality ratings represent the lower of Moody's Investors Service, Inc. ("Moody's") or Standard & Poor's Corporation ("S&P") credit ratings.*

*Counterparties:*

1 *Citigroup, Inc.*

2 *The Goldman Sachs & Co.*

3 *Bank of America*

4 *JPMorgan Chase Securities, Inc.*

5 *Credit Suisse*

*At December 31, 2010, the Fund had the following open forward foreign currency exchange contracts:*

| Contracts to Deliver | | In Exchange For | | Settlement Date | Unrealized Appreciation ($) | Counterparty |
|---|---|---|---|---|---|---|
| USD | 120,274 | EUR | 91,900 | 1/20/2011 | **2,528** | JP Morgan Chase Securities, Inc. |

| Contracts to Deliver | | In Exchange For | | Settlement Date | Unrealized Depreciation ($) | Counterparty |
|---|---|---|---|---|---|---|
| EUR | 4,957,900 | USD | 6,564,051 | 1/20/2011 | **(60,959)** | JPMorgan Chase Securities, Inc. |

| **Currency Abbreviations** | | | |
|---|---|---|---|
| EUR | Euro | USD | United States Dollar |

*For information on the Fund's policy and additional disclosures regarding credit default swap contracts and forward foreign currency exchange contracts, please refer to Note A in the accompanying Notes to Financial Statements.*

*The accompanying notes are an integral part of the financial statements.*

## Fair Value Measurements

*Various inputs are used in determining the value of the Fund's investments. These inputs are summarized in three broad levels. Level 1 includes quoted prices in active markets for identical securities. Level 2 includes other significant observable inputs (including quoted prices for similar securities, interest rates, prepayment speeds, and credit risk). Level 3 includes significant unobservable inputs (including the Fund's own assumptions in determining the fair value of investments). The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities.*

*The following is a summary of the inputs used as of December 31, 2010 in valuing the Fund's investments. For information on the Fund's policy regarding the valuation of investments, please refer to the Security Valuation section of Note A in the accompanying Notes to Financial Statements.*

| **Assets** | **Level 1** | **Level 2** | **Level 3** | **Total** |
|---|---|---|---|---|
| Fixed Income Investments (g) | | | | |
| Corporate Bonds | $ — | $ 164,153,007 | $ 2,784,439 | $ 166,937,446 |
| Loan Participations and Assignments | — | 8,294,946 | 0 | 8,294,946 |
| Preferred Security | — | 879,625 | — | 879,625 |
| Other Investments | — | — | 31,000 | 31,000 |
| Common Stocks (g) | 125,972 | — | 23,288 | 149,260 |
| Warrants (g) | — | — | 12,547 | 12,547 |
| Preferred Stock | — | 415,869 | — | 415,869 |
| Short-Term Investments (g) | 16,841,692 | — | — | 16,841,692 |
| Derivatives (h) | — | 388,784 | — | 388,784 |
| **Total** | **$ 16,967,664** | **$ 174,132,231** | **$ 2,851,274** | **$ 193,951,169** |
| **Liabilities** | | | | |
| Derivatives (h) | $ — | $ (60,959) | $ — | $ (60,959) |
| **Total** | **$ —** | **$ (60,959)** | **$ —** | **$ (60,959)** |

*There have been no significant transfers between Level 1 and Level 2 fair value measurements during the year ended December 31, 2010.*

(g) *See Investment Portfolio for additional detailed categorizations.*

(h) *Derivatives include unrealized appreciation (depreciation) on open credit default swap contracts and forward foreign currency exchange contracts.*

## Level 3 Reconciliation

*The following is a reconciliation of the Fund's Level 3 investments for which significant unobservable inputs were used in determining value:*

| | **Corporate Bonds** | **Loan Participations and Assignments** | **Other Investments** | **Common Stocks** | **Convertible Preferred Stocks** | **Warrants** | **Total** |
|---|---|---|---|---|---|---|---|
| **Balance as of December 31, 2009** | $ 2,525,906 | $ 1,393,416 | $ — | $ 22,466 | $ 0 | $ 5,989 | **$ 3,947,777** |
| Realized gains (loss) | — | 98,158 | — | — | (46,019) | — | **52,139** |
| Change in unrealized appreciation (depreciation) | 233,232 | 38,370 | 0 | (89) | 46,019 | 6,558 | **324,090** |
| Amortization premium/discount | 16,050 | 11,724 | — | — | — | — | **27,774** |
| Net purchases (sales) | 165,230 | (1,541,668) | 31,000 | 911 | 0 | 0 | **(1,344,527)** |
| Transfers into Level 3 | 57,741 (i) | — | — | — | — | — | **57,741** |
| Transfers (out) of Level 3 | (213,720) (j) | — | — | — | — | — | **(213,720)** |
| **Balance as of December 31, 2010** | **$ 2,784,439** | **$ 0** | **$ 31,000** | **$ 23,288** | **$ —** | **$ 12,547** | **$ 2,851,274** |
| **Net change in unrealized appreciation (depreciation) from investments still held as of December 31, 2010** | **$ (710,006)** | **$ 0** | **$ 0** | **$ (89)** | **$ —** | **$ 6,558** | **$ (690,530)** |

*Transfers between price levels are recognized at the beginning of the reporting period.*

(i) *The investment was transferred from Level 2 to Level 3 because of the lack of observable market data due to a decrease in market activity.*

(j) *The investment was transferred from Level 3 to Level 2 as a result of the availability of a pricing source supported by observable inputs.*

*The accompanying notes are an integral part of the financial statements.*

# Statement of Assets and Liabilities

as of December 31, 2010

| Assets | |
|---|---|
| Investments: | |
| Investments in unaffiliated securities, at value (cost $179,084,460) — including $1,366,721 of securities loaned | $ 176,720,693 |
| Investment in Daily Assets Fund Institutional (cost $1,419,848)* | 1,419,848 |
| Investment in Central Cash Management Fund (cost $15,421,844) | 15,421,844 |
| Total investments, at value (cost $195,926,152) | 193,562,385 |
| Cash | 75,291 |
| Deposits from broker for open swap contracts | 110,000 |
| Foreign currency, at value (cost $132) | 134 |
| Receivable for investments sold | 368,304 |
| Receivable for Fund shares sold | 43,905 |
| Unrealized appreciation on open swap contracts | 386,256 |
| Upfront payments paid on swaps | 4,658 |
| Unrealized appreciation on open forward foreign currency exchange contracts | 2,528 |
| Interest receivable | 3,600,397 |
| Foreign taxes recoverable | 3,198 |
| Other assets | 1,102 |
| Total assets | 198,158,158 |

| Liabilities | |
|---|---|
| Payable for investments purchased | 1,180,462 |
| Payable upon return of deposit | 110,000 |
| Payable for Fund shares redeemed | 46,874 |
| Payable upon return of securities loaned | 1,419,848 |
| Upfront payments received on open swap contracts | 99,022 |
| Unrealized depreciation on open forward foreign currency exchange contracts | 60,959 |
| Accrued management fee | 79,351 |
| Other accrued expenses and payables | 143,716 |
| Total liabilities | 3,140,232 |
| **Net assets, at value** | **$ 195,017,926** |

| Net Assets Consist of | |
|---|---|
| Undistributed net investment income | 15,993,708 |
| Net unrealized appreciation (depreciation) on: Investments | (2,363,767) |
| Swap contracts | 386,256 |
| Foreign currency | (58,348) |
| Accumulated net realized gain (loss) | (53,315,448) |
| Paid-in capital | 234,375,525 |
| **Net assets, at value** | **$ 195,017,926** |
| **Class A** **Net Asset Value,** offering and redemption price per share ($194,873,758 ÷ 28,235,548 outstanding shares of beneficial interest, no par value, unlimited number of shares authorized) | **$ 6.90** |
| **Class B** **Net Asset Value,** offering and redemption price per share ($144,168 ÷ 20,802 outstanding shares of beneficial interest, no par value, unlimited number of shares authorized) | **$ 6.93** |

* *Represents collateral on securities loaned.*

# Statement of Operations

for the year ended December 31, 2010

| Investment Income | |
|---|---|
| Interest (net of foreign taxes withheld of $1,461) | $ 16,276,745 |
| Income distributions — Central Cash Management Fund | 20,610 |
| Securities lending income, including income from Daily Assets Fund Institutional, net of borrower rebates | 12,213 |
| Total income | 16,309,568 |
| Expenses: | |
| Management fee | 946,284 |
| Administration fee | 189,257 |
| Services to shareholders | 7,017 |
| Distribution service fee (Class B) | 367 |
| Custodian fee | 48,519 |
| Legal fees | 54,464 |
| Audit and tax fees | 74,597 |
| Trustees' fees and expenses | 9,300 |
| Reports to shareholders | 11,655 |
| Other | 25,049 |
| Total expenses | 1,366,509 |
| **Net investment income (loss)** | **14,943,059** |

| Realized and Unrealized Gain (Loss) | |
|---|---|
| Net realized gain (loss) from: | |
| Investments | 797,934 |
| Swap contracts | 1,020,868 |
| Foreign currency | 1,101,998 |
| | 2,920,800 |
| Change in net unrealized appreciation (depreciation) on: | |
| Investments | 6,596,217 |
| Swap contracts | 386,256 |
| Foreign currency | (30,720) |
| | 6,951,753 |
| **Net gain (loss)** | **9,872,553** |
| **Net increase (decrease) in net assets resulting from operations** | **$ 24,815,612** |

*The accompanying notes are an integral part of the financial statements.*

# Statement of Changes in Net Assets

| Increase (Decrease) in Net Assets | Years Ended December 31, 2010 | 2009 |
|---|---|---|
| Operations: | | |
| Net investment income | $ 14,943,059 | $ 15,506,352 |
| Net realized gain (loss) | 2,920,800 | (10,439,947) |
| Change in net unrealized appreciation (depreciation) | 6,951,753 | 54,537,371 |
| Net increase (decrease) in net assets resulting from operations | 24,815,612 | 59,603,776 |
| Distributions to shareholders from: | | |
| Net investment income: | | |
| Class A | (15,325,538) | (18,645,480) |
| Class B | (11,524) | (15,950) |
| Total distributions | (15,337,062) | (18,661,430) |
| Fund share transactions: | | |
| **Class A** | | |
| Proceeds from shares sold | 73,550,670 | 36,369,714 |
| Reinvestment of distributions | 15,325,538 | 18,645,480 |
| Payments for shares redeemed | (100,347,223) | (52,798,244) |
| Net increase (decrease) in net assets from Class A share transactions | (11,471,015) | 2,216,950 |
| **Class B** | | |
| Proceeds from shares sold | 2,173 | 2,036 |
| Reinvestment of distributions | 11,524 | 15,950 |
| Payments for shares redeemed | (27,277) | (32,524) |
| Net increase (decrease) in net assets from Class B share transactions | (13,580) | (14,538) |
| **Increase (decrease) in net assets** | (2,006,045) | 43,144,758 |
| Net assets at beginning of period | 197,023,971 | 153,879,213 |
| Net assets at end of period (including undistributed net investment income of $15,993,708 and $15,102,955, respectively) | **$ 195,017,926** | **$ 197,023,971** |

| Other Information | | |
|---|---|---|
| **Class A** | | |
| Shares outstanding at beginning of period | 30,057,940 | 29,000,230 |
| Shares sold | 11,151,687 | 6,555,256 |
| Shares issued to shareholders in reinvestment of distributions | 2,379,742 | 3,844,429 |
| Shares redeemed | (15,353,821) | (9,341,975) |
| Net increase (decrease) in Class A shares | (1,822,392) | 1,057,710 |
| Shares outstanding at end of period | **28,235,548** | **30,057,940** |
| **Class B** | | |
| Shares outstanding at beginning of period | 22,888 | 25,274 |
| Shares sold | 319 | 379 |
| Shares issued to shareholders in reinvestment of distributions | 1,778 | 3,268 |
| Shares redeemed | (4,183) | (6,033) |
| Net increase (decrease) in Class B shares | (2,086) | (2,386) |
| Shares outstanding at end of period | **20,802** | **22,888** |

*The accompanying notes are an integral part of the financial statements.*

# Financial Highlights

## Class A

| Years Ended December 31, | 2010 | 2009 | 2008 | 2007 | 2006 |
|---|---|---|---|---|---|
| **Selected Per Share Data** | | | | | |
| **Net asset value, beginning of period** | **$ 6.55** | **$ 5.30** | **$ 7.81** | **$ 8.38** | **$ 8.23** |
| *Income (loss) from investment operations:* | | | | | |
| Net investment income[a] | .52 | .51 | .57 | .63 | .62 |
| Net realized and unrealized gain (loss) | .36 | 1.40 | (2.29) | (.54) | .19 |
| **Total from investment operations** | .88 | 1.91 | (1.72) | .09 | .81 |
| *Less distributions from:* | | | | | |
| Net investment income | (.53) | (.66) | (.79) | (.66) | (.66) |
| **Net asset value, end of period** | **$ 6.90** | **$ 6.55** | **$ 5.30** | **$ 7.81** | **$ 8.38** |
| Total Return (%) | 14.00 | 39.99 | (23.94)[b] | .96 | 10.47 |
| **Ratios to Average Net Assets and Supplemental Data** | | | | | |
| Net assets, end of period ($ millions) | 195 | 197 | 154 | 248 | 322 |
| Ratio of expenses before expense reductions (%) | .72 | .67 | .80 | .69 | .71 |
| Ratio of expenses after expense reductions (%) | .72 | .67 | .79 | .69 | .71 |
| Ratio of net investment income (%) | 7.90 | 8.81 | 8.42 | 7.84 | 7.73 |
| Portfolio turnover rate (%) | 93 | 66 | 38 | 61 | 93 |

[a] *Based on average shares outstanding during the period.*

[b] *Total return would have been lower had certain expenses not been reduced.*

## Class B

| Years Ended December 31, | 2010 | 2009 | 2008 | 2007 | 2006 |
|---|---|---|---|---|---|
| **Selected Per Share Data** | | | | | |
| **Net asset value, beginning of period** | **$ 6.58** | **$ 5.31** | **$ 7.81** | **$ 8.38** | **$ 8.22** |
| *Income (loss) from investment operations:* | | | | | |
| Net investment income[a] | .50 | .49 | .53 | .60 | .59 |
| Net realized and unrealized gain (loss) | .36 | 1.42 | (2.27) | (.54) | .20 |
| **Total from investment operations** | .86 | 1.91 | (1.74) | .06 | .79 |
| *Less distributions from:* | | | | | |
| Net investment income | (.51) | (.64) | (.76) | (.63) | (.63) |
| **Net asset value, end of period** | **$ 6.93** | **$ 6.58** | **$ 5.31** | **$ 7.81** | **$ 8.38** |
| Total Return (%) | 13.64 | 39.64 | (24.13)[b] | .54 | 10.11 |
| **Ratios to Average Net Assets and Supplemental Data** | | | | | |
| Net assets, end of period ($ millions) | .1 | .2 | .1 | 10 | 53 |
| Ratio of expenses before expense reductions (%) | .99 | .94 | 1.25 | 1.08 | 1.10 |
| Ratio of expenses after expense reductions (%) | .99 | .94 | 1.23 | 1.08 | 1.10 |
| Ratio of net investment income (%) | 7.63 | 8.54 | 7.98 | 7.45 | 7.34 |
| Portfolio turnover rate (%) | 93 | 66 | 38 | 61 | 93 |

[a] *Based on average shares outstanding during the period.*

[b] *Total return would have been lower had certain expenses not been reduced.*

# Notes to Financial Statements

## A. Organization and Significant Accounting Policies

DWS Variable Series II (the "Trust") is registered under the Investment Company Act of 1940, as amended (the "1940 Act"), as an open-end management investment company organized as a Massachusetts business trust. The Trust offers seventeen funds (hereinafter referred to individually as "Fund" or collectively as "Funds"). The Fund is classified as a non-diversified, open-end management investment company.

**Multiple Classes of Shares of Beneficial Interest.** Certain Funds of the Trust offer two classes of shares (Class A shares and Class B shares). Sales of Class B shares are subject to record keeping fees up to 0.15% and Rule 12b-1 fees under the 1940 Act equal to an annual rate of 0.25%, of the average daily net assets of the Class B shares of the applicable Fund. Class A shares are not subject to such fees.

Investment income, realized and unrealized gains and losses, and certain fund-level expenses and expense reductions, if any, are borne pro rata on the basis of relative net assets by the holders of all classes of shares except that each class bears certain expenses unique to that class (including the applicable Rule 12b-1 fee and record keeping fees). Differences in class-level expenses may result in payment of different per share dividends by class. All shares have equal rights with respect to voting subject to class-specific arrangements.

The Trust's financial statements are prepared in accordance with accounting principles generally accepted in the United States of America which require the use of management estimates. Actual results could differ from those estimates. The policies described below are followed consistently by the Trust in the preparation of its financial statements.

**Security Valuation.** Investments are stated at value determined as of the close of regular trading on the New York Stock Exchange on each day the exchange is open for trading.

Various inputs are used in determining the value of the Fund's investments. These inputs are summarized in three broad levels. Level 1 includes quoted prices in active markets for identical securities. Level 2 includes other significant observable inputs (including quoted prices for similar securities, interest rates, prepayment speeds, and credit risk). Level 3 includes significant unobservable inputs (including the Fund's own assumptions in determining the fair value of investments). The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities.

Equity securities are valued at the most recent sale price or official closing price reported on the exchange (US or foreign) or over-the-counter market on which they trade and are categorized as Level 1 securities. Securities for which no sales are reported are valued at the calculated mean between the most recent bid and asked quotations on the relevant market or, if a mean cannot be determined, at the most recent bid quotation.

Debt securities are valued by independent pricing services approved by the Fund's Board. If the pricing services are unable to provide valuations, securities are valued at the most recent bid quotation or evaluated price, as applicable, obtained from one or more broker-dealers. Such services may use various pricing techniques which take into account appropriate factors such as yield, quality, coupon rate, maturity, type of issue, trading characteristics and other data, as well as broker quotes. These securities are generally categorized as Level 2.

Forward currency contracts are valued at the prevailing forward exchange rate of the underlying currencies and are categorized as Level 2.

Swap contracts are valued daily based upon prices supplied by a Board approved pricing vendor, if available, and otherwise are valued at the price provided by the broker-dealer. Swap contracts are generally categorized as Level 2.

Money market instruments purchased with an original or remaining maturity of sixty days or less, maturing at par, are valued at amortized cost, which approximates value, and are categorized as Level 2. Investments in open-end investment companies are valued at their net asset value each business day and are categorized as Level 1.

Securities and other assets for which market quotations are not readily available or for which the above valuation procedures are deemed not to reflect fair value are valued in a manner that is intended to reflect their fair value as determined in accordance with procedures approved by the Board and are generally categorized as Level 3. In accordance with the Fund's valuation procedures, factors used in determining value may include, but are not limited to, the type of the security; the size of the holding; the initial cost of the security; the existence of any contractual restrictions on the security's disposition; the price and extent of public trading in similar securities of the issuer or of comparable companies; quotations or evaluated prices from broker-dealers and/or pricing services; information obtained from the issuer, analysts, and/or the appropriate stock exchange (for exchange-traded securities); an analysis of the company's or issuer's financial statements; an evaluation of the forces that influence the issuer and the market(s) in which the security is purchased and sold and with respect to debt securities; the maturity, coupon, creditworthiness, currency denomination and the movement of the market

in which the security is normally traded. The value determined under these procedures may differ from published values for the same securities.

Disclosure about the classification of fair value measurements is included in a table following the Fund's Investment Portfolio.

**Foreign Currency Translations.** The books and records of the Trust are maintained in US dollars. Investment securities and other assets and liabilities denominated in a foreign currency are translated into US dollars at the prevailing exchange rates at period end. Purchases and sales of investment securities, income and expenses are translated into US dollars at the prevailing exchange rates on the respective dates of the transactions.

Net realized and unrealized gains and losses on foreign currency transactions represent net gains and losses between trade and settlement dates on securities transactions, the disposition of forward foreign currency exchange contracts and foreign currencies, and the difference between the amount of net investment income accrued and the US dollar amount actually received. That portion of both realized and unrealized gains and losses on investments that results from fluctuations in foreign currency exchange rates is not separately disclosed but is included with net realized and unrealized gain/appreciation and loss/depreciation on investments.

**Securities Lending.** The Fund lends securities to certain financial institutions. The Fund retains beneficial ownership of the securities it has loaned and continues to receive interest and dividends paid by the issuer of securities and to participate in any changes in their market value. The Fund requires the borrowers of the securities to maintain collateral with the Fund consisting of either cash or liquid, unencumbered assets having a value at least equal to the value of the securities loaned. When the collateral falls below specified amounts, the lending agent will use its best effort to obtain additional collateral on the next business day to meet required amounts under the security lending agreement. The Fund may invest the cash collateral into a joint trading account in an affiliated money market fund pursuant to Exemptive Orders issued by the SEC. The Fund receives compensation for lending its securities either in the form of fees or by earning interest on invested cash collateral net of borrower rebates and fees paid to a lending agent. Either the Fund or the borrower may terminate the loan. There may be risks of delay and costs in recovery of securities or even loss of rights in the collateral should the borrower of the securities fail financially. The Fund is also subject to all investment risks associated with the reinvestment of any cash collateral received, including, but not limited to, interest rate, credit and liquidity risk associated with such investments.

**Loan Participations and Assignments.** The Fund invests in Loan Participations and Assignments. Loan Participations and Assignments are portions of loans originated by banks and sold in pieces to investors. These US dollar-denominated fixed and floating rate loans ("Loans") in which the Fund invests, are arranged between the borrower and one or more financial institutions ("Lenders"). These Loans may take the form of Senior Loans, which are corporate obligations often issued in connection with recapitalizations, acquisitions, leveraged buy-outs and refinancings, and Sovereign Loans, which are debt instruments between a foreign sovereign entity and one or more financial institutions. The Fund invests in such Loans in the form of participations in Loans ("Participations") or assignments of all or a portion of Loans from third parties ("Assignments"). Participations typically result in the Fund having a contractual relationship only with the Lender, not with the borrower. The Fund has the right to receive payments of principal, interest and any fees to which it is entitled from the Lender selling the Participation and only upon receipt by the Lender of the payments from the borrower. In connection with purchasing Participations, the Fund generally has no right to enforce compliance by the borrower with the terms of the loan agreement relating to the Loan, or any rights of set-off against the borrower, and the Fund will not benefit directly from any collateral supporting the Loan in which it has purchased the Participation. As a result, the Fund assumes the credit risk of both the borrower and the Lender that is selling the Participation. Assignments typically result in the Fund having a direct contractual relationship with the borrower, and the Fund may enforce compliance by the borrower with the terms of the loan agreement. All Loan Participations and Assignments involve interest rate risk, liquidity risk and credit risk, including the potential default or insolvency of the borrower.

**When-Issued/Delayed Delivery Securities.** The Fund may purchase securities with delivery or payment to occur at a later date beyond the normal settlement period. At the time the Fund enters into a commitment to purchase a security, the transaction is recorded and the value of the security is reflected in the net asset value. The price of such security and the date when the security will be delivered and paid for are fixed at the time the transaction is negotiated. The value of the security may vary with market fluctuations. No interest accrues to the Fund until payment takes place. At the time the Fund enters into this type of transaction it is required to segregate cash or other liquid assets at least equal to the amount of the commitment.

Certain risks may arise upon entering into when-issued or delayed delivery securities from the potential inability of counterparties to meet the terms of their contracts or if the issuer does not issue the securities due to political, economic, or other factors. Additionally, losses may arise due to changes in the value of the underlying securities.

**Taxes.** The Fund's policy is to comply with the requirements of the Internal Revenue Code, as amended, which are applicable to regulated investment companies and to distribute all of its taxable income to its shareholders.

At December 31, 2010, the Fund had an approximate net tax basis capital loss carryforward which may be applied against any realized net taxable capital gains of each succeeding year until fully utilized or until the following expiration dates, whichever occurs first:

| Fund | Capital Loss Carryforward ($) | Expiration Date | Capital Loss Carryforward Utilized ($) | Capital Loss Carryforward Expired ($) |
|---|---|---|---|---|
| DWS High Income VIP | 13,877,000 | 12/31/2011 | 1,517,000 | 53,591,000 |
| | 3,844,000 | 12/31/2014 | | |
| | 858,000 | 12/31/2015 | | |
| | 17,300,000 | 12/31/2016 | | |
| | 17,232,000 | 12/31/2017 | | |

In addition, from November 1, 2010 through December 31, 2010, the Fund incurred net realized capital losses. As permitted by tax regulations, the Fund intends to elect to defer these losses and treat them as arising in the fiscal year ended December 31, 2011.

| Fund | |
|---|---|
| DWS High Income VIP | $ 185,000 |

The Fund has reviewed the tax positions for the open tax years as of December 31, 2010 and has determined that no provision for income tax is required in the Fund's financial statements. The Fund's federal tax returns for the prior three fiscal years remain open subject to examination by the Internal Revenue Service.

**Distribution of Income and Gains.** Distributions of net investment income of the Fund, if any, are made annually. Net realized gains from investment transactions, in excess of available capital loss carryforwards, would be taxable to the Fund if not distributed and, therefore, will be distributed to shareholders at least annually. The Fund may also make additional distributions for tax purposes if necessary.

The timing and characterization of certain income and capital gains distributions are determined annually in accordance with federal tax regulations which may differ from accounting principles generally accepted in the United States of America. These differences primarily relate to investments in foreign denominated investments, investments in forward currency contracts, investments in swap contracts and certain securities sold at a loss. As a result, net investment income (loss) and net realized gain (loss) on investment transactions for a reporting period may differ significantly from distributions during such period. Accordingly, the Fund may periodically make reclassifications among certain of its capital accounts without impacting the net asset value of the Fund.

At December 31, 2010, the Fund's components of distributable earnings on a tax basis were as follows:

| Fund | Undistributed Ordinary Income ($)* | Capital Loss Carryforwards ($) | Unrealized Appreciation (Depreciation) on Investments ($) |
|---|---|---|---|
| DWS High Income VIP | 16,310,534 | (53,111,000) | (2,383,006) |

In addition, the tax character of distributions paid by the Fund is summarized as follows:

| | Distributions from Ordinary Income ($)* | |
|---|---|---|
| | Years Ended December 31, | |
| Fund | 2010 | 2009 |
| DWS High Income VIP | 15,337,062 | 18,661,430 |

* *For tax purposes, short-term capital gain distributions are considered ordinary income distributions.*

**Expenses.** Expenses of the Trust arising in connection with a specific fund are allocated to that fund. Other Trust expenses which cannot be directly attributed to a fund are apportioned among the funds in the Trust.

**Contingencies.** In the normal course of business, the Fund may enter into contracts with service providers that contain general indemnification clauses. The Fund's maximum exposure under these arrangements is unknown as this would involve future claims that may be made against the Fund that have not yet been made. However, based on experience, the Fund expects the risk of loss to be remote.

**Other.** Investment transactions are accounted for on a trade date plus one basis for daily net asset value calculations. However, for financial reporting purposes, investment transactions are reported on trade date. Interest income is recorded on the accrual basis. Realized gains and losses from investment transactions are recorded on an identified cost basis. All discounts and premiums are accreted/amortized for both tax and financial reporting purposes for the Fund, with the exception of securities in default of principal.

### B. Derivative Instruments

**Credit Default Swap Contracts.** A credit default swap is a contract between a buyer and a seller of protection against pre-defined credit events for the reference entity. For the year ended December 31, 2010, the Fund bought or sold credit default swap contracts to gain exposure to an underlying issuer's credit quality characteristics without directly investing in that issuer, or to hedge the risk of default on Fund securities. As a seller in the credit default swap contract, the Fund is required to pay the par (or other agreed-upon) value of the referenced entity to the counterparty with the occurrence of a credit event by a third party, such as a US or foreign corporate issuer, on the reference entity, which would likely result in a loss to the Fund. In return, the Fund receives from the counterparty a periodic stream of payments over the term of the contract provided that no credit event has occurred. If no credit event occurs, the Fund keeps the stream of payments with no payment obligations. The Fund may also buy credit default swap contracts in order to hedge against the risk of a credit event on debt securities, in which case the Fund functions as the counterparty referenced above. This involves the risk that the contract may expire worthless. It also involves counterparty risk that the seller may fail to satisfy its payment obligations to the Fund with the occurrence of a credit event. When the Fund sells a credit default swap contract it will cover its commitment. This may be achieved by, among other methods, maintaining cash or liquid assets equal to the aggregate notional value of the reference entities for all outstanding credit default swap contracts sold by the Fund.

The value of the credit default swap is adjusted daily and the change in value, if any, is recorded daily as unrealized appreciation or depreciation in the Statement of Assets and Liabilities. An upfront payment made by the Fund is recorded as an asset in the Statement of Assets and Liabilities. An upfront payment received by the Fund is recorded as a liability in the Statement of Assets and Liabilities. Under the terms of the credit default swap contracts, the Fund receives or makes quarterly payments based on a specified interest rate on a fixed notional amount. These payments are recorded as a realized gain or loss in the Statement of Operations. Payments received or made as a result of a credit event or termination of the contract are recognized, net of a proportional amount of the upfront payment, as realized gains or losses in the Statement of Operations.

A summary of the open credit default swap contracts as of December 31, 2010 is included in a table following the Fund's Investment Portfolio. For the year ended December 31, 2010, the Fund's investment in credit default swap contracts sold had a total notional value generally indicative of a range from $0 to approximately $17,275,000.

**Forward Foreign Currency Exchange Contracts.** A forward foreign currency exchange contract ("forward currency contract") is a commitment to purchase or sell a foreign currency at the settlement date at a negotiated rate. For the year ended December 31, 2010, the Fund entered into forward currency contracts in order to hedge its exposure to changes in foreign currency exchange rates on its foreign currency denominated portfolio holdings and to facilitate transactions in foreign currency denominated securities.

Forward currency contracts are valued at the prevailing forward exchange rate of the underlying currencies and unrealized gain (loss) is recorded daily. On the settlement date of the forward currency contract, the Fund records a realized gain or loss equal to the difference between the value of the contract at the time it was opened and the value of the contract at the time it was closed. Certain risks may arise upon entering into forward currency contracts from the potential inability of counterparties to meet the terms of their contracts. The maximum counterparty credit risk to the Fund is measured by the unrealized gain on appreciated contracts. Additionally, when utilizing forward currency contracts to hedge, the Fund gives up the opportunity to profit from favorable exchange rate movements during the term of the contract.

A summary of the open forward currency contracts as of December 31, 2010 is included in a table following the Fund's Investment Portfolio. For the year ended December 31, 2010, the Fund's investment in forward currency contracts US dollars purchased had a total contract value generally indicative of a range from approximately $6,564,000 to $13,966,000. The Fund's investment in forward currency contracts US dollars sold had a total contract value generally indicative of a range from $0 to approximately $210,000.

The following table summarizes the value of the Fund's derivative instruments held as of December 31, 2010 and the related location in the accompanying Statement of Assets and Liabilities, presented by primary underlying risk exposure:

| Asset Derivatives | Forward Contracts | Swap Contracts | Total |
|---|---|---|---|
| Credit Contracts (a) | $ — | $ 386,256 | $ 386,256 |
| Foreign Exchange Contracts (b) | 2,528 | — | 2,528 |
| | **$ 2,528** | **$ 386,256** | **$ 388,784** |

*Each of the above derivatives is located in the following Statement of Assets and Liabilities accounts:*

(a) *Unrealized appreciation on open swap contracts*

(b) *Unrealized appreciation on open forward foreign currency exchange contracts*

| Liability Derivative | Forward Contracts |
|---|---|
| Foreign Exchange Contracts (a) | $ (60,959) |

*The above derivative is located in the following Statement of Assets and Liabilities account:*

(a) *Unrealized depreciation on open forward foreign currency exchange contracts*

Additionally, the amount of unrealized and realized gains and losses on derivative instruments recognized in Fund earnings during the year ended December 31, 2010 and the related location in the accompanying Statement of Operations is summarized in the following tables by primary underlying risk exposure:

| Realized Gain (Loss) | Forward Contracts | Swap Contracts | Total |
|---|---|---|---|
| Credit Contracts (a) | $ — | $ 1,020,868 | $ 1,020,868 |
| Foreign Exchange Contracts (b) | 1,453,531 | — | 1,453,531 |
| | **$ 1,453,531** | **$ 1,020,868** | **$ 2,474,399** |

*Each of the above derivatives is located in the following Statement of Operations accounts:*

(a) *Net realized gain (loss) from swap contracts*

(b) *Net realized gain (loss) from foreign currency (Statement of Operations includes both forward currency contracts and foreign currency transactions)*

| Change in Net Unrealized Appreciation (Depreciation) | Forward Contracts | Swap Contracts | Total |
|---|---|---|---|
| Credit Contracts (a) | $ — | $ 386,256 | $ 386,256 |
| Foreign Exchange Contracts (b) | (34,981) | — | (34,981) |
| | **$ (34,981)** | **$ 386,256** | **$ 351,275** |

*Each of the above derivatives is located in the following Statement of Operations accounts:*

(a) *Change in net unrealized appreciation (depreciation) on swap contracts*

(b) *Change in net unrealized appreciation (depreciation) on foreign currency (Statement of Operations includes both forward currency contracts and foreign currency transactions)*

## C. Purchases and Sales of Securities

During the year ended December 31, 2010, purchases and sales of investment transactions (excluding short-term investments) were as follows:

| Fund | Purchases ($) | Sales ($) |
|---|---|---|
| DWS High Income VIP | 165,760,238 | 191,044,642 |

## D. Related Parties

**Management Agreement.** Under the Investment Management Agreement with Deutsche Investment Management Americas Inc. ("DIMA" or the "Advisor"), an indirect, wholly owned subsidiary of Deutsche Bank AG, the Advisor directs the investments of the Fund in accordance with its investment objectives, policies and restrictions. The Advisor determines the securities, instruments and other contracts relating to investments to be purchased, sold or entered into by the Fund.

Under the Investment Management Agreement with the Advisor, the fee is equivalent to the annual rates shown below of the Fund's average daily net assets, computed and accrued daily and payable monthly:

| Fund | Annual Management Fee Rate |
|---|---|
| DWS High Income VIP<br>$0–$250 million | .500% |
| next $750 million | .470% |
| next $1.5 billion | .450% |
| next $2.5 billion | .430% |
| next $2.5 billion | .400% |
| next $2.5 billion | .380% |
| next $2.5 billion | .360% |
| over $12.5 billion | .340% |

For the period from January 1, 2010 through September 30, 2010, the Advisor had contractually agreed to waive its fee and/or reimburse certain operating expenses to the extent necessary to maintain the operating expenses (excluding certain expenses such as extraordinary expenses, taxes, brokerage and interest expense) of the class as follows:

| Fund | Annual Rate |
|---|---|
| DWS High Income VIP<br>Class B | 1.25% |

Accordingly, for the year ended December 31, 2010, the total management fee and effective management fee rate were as follows:

| Fund | Total Aggregated ($) | Annual Effective Rate |
|---|---|---|
| DWS High Income VIP | 946,284 | .50% |

**Administration Fee.** Pursuant to an Administrative Services Agreement, DIMA provides most administrative services to the Fund. For all services provided under the Administrative Services Agreement, the Fund pays DIMA an annual fee ("Administration Fee") of 0.10% of the Fund's average daily net assets, computed and accrued daily and payable monthly. For the year ended December 31, 2010, the Administration Fee was as follows:

| Fund | Total Aggregated ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS High Income VIP | 189,257 | 15,979 |

**Service Provider Fees.** DWS Investments Service Company ("DISC"), an affiliate of the Advisor, is the transfer agent, dividend-paying agent and shareholder service agent for the Fund. Pursuant to a sub-transfer agency agreement between DISC and DST Systems, Inc. ("DST"), DISC has delegated certain transfer agent, dividend-paying agent and shareholder service agent functions to DST. DISC compensates DST out of the shareholder servicing fee it receives from the Fund. For the year ended December 31, 2010, the amounts charged to the Fund by DISC were as follows:

| Fund | Total Aggregated ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS High Income VIP Class A | 307 | 71 |
| DWS High Income VIP Class B | 24 | 6 |

**Distribution Service Agreement**. Under the Fund's Class B 12b-1 plans, DWS Investments Distributors, Inc. ("DIDI") received a fee ("Distribution Service Fee") of 0.25% of average daily net assets of Class B shares. For the year ended December 31, 2010, the Distribution Service Fee was as follows:

| Fund | Total Aggregated ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS High Income VIP | 367 | 31 |

**Typesetting and Filing Service Fees.** Under an agreement with DIMA, DIMA is compensated for providing typesetting and certain regulatory filing services to the Fund. For the year ended December 31, 2010, the amount charged to the Fund by DIMA included in the Statement of Operations under "reports to shareholders" was as follows:

| Fund | Amount ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS High Income VIP | 11,655 | 2,493 |

**Trustees' Fees and Expenses.** The Fund paid each Trustee not affiliated with the Advisor retainer fees plus specified amounts for various committee services and for the Board Chairperson.

**Affiliated Cash Management Vehicles.** The Fund may invest uninvested cash balances in Central Cash Management Fund, which is managed by the Advisor. The Fund indirectly bears their proportionate share of the expenses of the underlying money market funds. Central Cash Management Fund does not pay the Advisor an investment management fee. Central Cash Management Fund seeks a high level of current income consistent with liquidity and the preservation of capital.

## E. Investing in High Yield Securities

The Fund's performance could be hurt if a security declines in credit quality or goes into default, or if an issuer does not make timely payments of interest or principal. Because the issuers of high-yield debt securities or junk bonds (debt securities rated below the fourth-highest category) may be in uncertain financial health, the prices of their debt securities can be more vulnerable to bad economic news, or even the expectation of bad news, than investment-grade debt securities. Because the Fund may invest in securities not paying current interest or in securities already in default, these risks may be more pronounced.

## F. Ownership of the Fund

At December 31, 2010, the beneficial ownership in the Fund was as follows:

**DWS High Income VIP:** Three Participating Insurance Companies were owners of record of 10% or more of the total outstanding Class A shares of the Fund, each owning 34%, 32% and 28%. One Participating Insurance Company was the owner of record of 10% or more of the total outstanding Class B shares of the Fund, owning 100%.

## G. Line of Credit

The Trust and other affiliated fund (the "Participants") share in a $450 million revolving credit facility provided by a syndication of banks. The Fund may borrow for temporary or emergency purposes, including the meeting of redemption requests that otherwise might require the untimely disposition of securities. The Participants are charged an annual commitment fee which is allocated based on net assets, among each of the Participants. Interest is calculated at a rate per annum equal to the sum of the Federal Funds Rate plus 1.25 percent plus if LIBOR exceeds the Federal Funds Rate the amount of such excess. The Fund may borrow up to a maximum of 33 percent of its net assets under the agreement.

# Report of Independent Registered Public Accounting Firm

**To the Board of Trustees and Shareholders of DWS Variable Series II:**

We have audited the accompanying statement of assets and liabilities of DWS High Income VIP, one of the funds constituting the DWS Variable Series II (the "Trust"), including the investment portfolio, as of December 31, 2010, and the related statement of operations, the statement of changes in net assets and the financial highlights for each of the periods indicated therein. These financial statements and financial highlights are the responsibility of the Trust's management. Our responsibility is to express an opinion on these financial statements and financial highlights based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements and financial highlights are free of material misstatement. We were not engaged to perform an audit of the Trust's internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Trust's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements and financial highlights, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our procedures included confirmation of securities owned as of December 31, 2010, by correspondence with the custodian and brokers or by other appropriate auditing procedures where replies from brokers were not received. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements and financial highlights referred to above present fairly, in all material respects, the financial position of the aforementioned fund of the DWS Variable Series II at December 31, 2010, the results of its operations, the changes in its net assets and the financial highlights for each of the periods indicated therein, in conformity with U.S. generally accepted accounting principles.

Ernst + Young LLP

Boston, Massachusetts
February 14, 2011

## Tax Information

**(Unaudited)**

Please consult a tax advisor if you have questions about federal or state income tax laws, or on how to prepare your tax returns. If you have specific questions about your account, please contact your insurance provider.

## Proxy Voting

The Trust's policies and procedures for voting proxies for portfolio securities and information about how the Trust voted proxies related to its portfolio securities during the 12-month period ended June 30 are available on our Web site — www.dws-investments.com (click on "proxy voting" at the bottom of the page) — or on the SEC's Web site — www.sec.gov. To obtain a written copy of the Trust's policies and procedures without charge, upon request, call us toll free at (800) 728-3337.

# Investment Management Agreement Approval

## DWS High Income VIP

The Board of Trustees, including the Independent Trustees, approved the renewal of your Fund's investment management agreement (the "Agreement") with Deutsche Investment Management Americas Inc. ("DWS") in September 2010.

In terms of the process that the Board followed prior to approving the Agreement, shareholders should know that:

- In September 2010, all but one of the Fund's Trustees were independent of DWS and its affiliates.
- The Trustees meet frequently to discuss fund matters. Each year, the Trustees dedicate substantial time to contract review matters. Over the course of several months, the Board's Contract Committee, in coordination with the Board's Fixed Income and Quant Oversight Committee, reviewed comprehensive materials received from DWS, independent third parties and independent counsel. These materials included an analysis of the Fund's performance, fees and expenses, and profitability compiled by the Fund's independent fee consultant. The Board also received extensive information throughout the year regarding performance of the Fund.
- The Independent Trustees regularly meet privately with their independent counsel to discuss contract review and other matters. In addition, the Independent Trustees were also advised by the Fund's independent fee consultant in the course of their review of the Fund's contractual arrangements and considered a comprehensive report prepared by the independent fee consultant in connection with their deliberations (the "IFC Report").
- In connection with reviewing the Agreement, the Board also reviewed the terms of the Fund's Rule 12b-1 plan, distribution agreement, administrative services agreement, transfer agency agreement and other material service agreements.
- Based on its evaluation of the information provided, the Contract Committee presented its findings and recommendations to the Independent Trustees as a group. The Independent Trustees reviewed the Contract Committee's findings and recommendations and presented their recommendations to the full Board.

In connection with the contract review process, the Contract Committee and the Board considered the factors discussed below, among others. The Board also considered that DWS and its predecessors have managed the Fund since its inception, and the Board believes that a long-term relationship with a capable, conscientious advisor is in the best interests of the Fund. The Board considered, generally, that shareholders chose to invest or remain invested in the Fund knowing that DWS managed the Fund, and that the Agreement was approved by the Fund's shareholders. DWS is part of Deutsche Bank, a major global banking institution that is engaged in a wide range of financial services. The Board believes that there are significant advantages to being part of a global asset management business that offers a wide range of investing expertise and resources, including hundreds of portfolio managers and analysts with research capabilities in many countries throughout the world.

While shareholders may focus primarily on fund performance and fees, the Fund's Board considers these and many other factors, including the quality and integrity of DWS's personnel and such other issues as back-office operations, fund valuations, and compliance policies and procedures.

**Nature, Quality and Extent of Services.** The Board considered the terms of the Agreement, including the scope of advisory services provided under the Agreement. The Board noted that, under the Agreement, DWS provides portfolio management services to the Fund and that, pursuant to a separate administrative services agreement, DWS provides administrative services to the Fund. The Board considered the experience and skills of senior management and investment personnel, the resources made available to such personnel, the ability of DWS to attract and retain high-quality personnel, and the organizational depth and stability of DWS. The Board reviewed the Fund's performance over short-term and long-term periods and compared those returns to various agreed-upon performance measures, including market indices and a peer universe compiled by the independent fee consultant using information supplied by Lipper Inc. ("Lipper"). The Board also noted that it has put into place a process of identifying "Focus Funds" (e.g., funds performing poorly relative to their benchmark or a peer universe compiled by Lipper), and receives more frequent reporting and information from DWS regarding such funds, along with DWS's remedial plans to address underperformance. The Board believes this process is an effective manner of identifying and addressing underperforming funds. Based on the information provided, the Board noted that for the one-, three- and five-year periods ended December 31, 2009, the Fund's performance (Class A shares) was in the 3rd quartile, 4th quartile and 3rd quartile, respectively, of the applicable Lipper universe (the 1st quartile being the best performers and the 4th quartile being the worst performers). The Board also observed that the Fund has underperformed its benchmark in the one-, three- and five-year periods ended December 31, 2009.

On the basis of this evaluation and the ongoing review of investment results by the Board, the Board concluded that the nature, quality and extent of services provided by DWS historically have been and continue to be satisfactory.

**Fees and Expenses.** The Board considered the Fund's investment management fee schedule, operating expenses, and total expense ratios, and comparative information provided by Lipper and the independent fee consultant regarding investment management fee rates paid to other investment advisors by similar funds (1st quartile being the most favorable and 4th quartile being the least favorable). With respect to management fees paid to other investment advisors by similar funds, the Board noted that the contractual fee rates paid by the Fund, which include the 0.10% fee paid to DWS under the Fund's administrative services agreement, were lower than the median (1st quartile) of the applicable Lipper peer group (based on Lipper data provided as of December 31, 2009). The Board noted that the Fund's Class A shares total (net) operating expenses were expected to be lower than the median (2nd quartile) of the applicable Lipper expense universe (based on Lipper data provided as of December 31, 2009, and analyzing Lipper expense universe Class A expenses less any applicable 12b-1 fees) ("Lipper Universe Expenses"). The Board also reviewed data comparing each share class's total (net) operating expenses to the applicable Lipper Universe Expenses. The Board considered the Fund's management fee rate as compared to fees charged by DWS and certain of its affiliates for comparable mutual funds and considered differences in fund and fee structures between the DWS Funds. The Board also considered how the Fund's total (net) operating expenses compared to the total (net) operating expenses of a more customized peer group selected by Lipper (based on such factors as asset size).

The information considered by the Board as part of its review of management fees included information regarding fees charged by DWS and its affiliates to similar institutional accounts and to similar funds offered primarily to European investors ("DWS Europe funds"), in each case as applicable. The Board observed that advisory fee rates for institutional accounts generally were lower than the management fees charged by similarly managed DWS US mutual funds ("DWS Funds"), but also took note of the differences in services provided to DWS Funds as compared to institutional accounts. In the case of DWS Europe funds, the Board observed that fee rates for DWS Europe funds generally were higher than for similarly managed DWS Funds, but noted that differences in the types of services provided to DWS Funds relative to DWS Europe funds made it difficult to compare such fees.

On the basis of the information provided, the Board concluded that management fees were reasonable and appropriate in light of the nature, quality and extent of services provided by DWS.

**Profitability.** The Board reviewed detailed information regarding revenues received by DWS under the Agreement. The Board considered the estimated costs and pre-tax profits realized by DWS from advising the DWS Funds, as well as estimates of the pre-tax profits attributable to managing the Fund in particular. The Board also received information regarding the estimated enterprise-wide profitability of DWS and its affiliates with respect to all fund services in totality and by fund. The Board reviewed DWS's methodology in allocating its costs to the management of the Fund. Based on the information provided, the Board concluded that the pre-tax profits realized by DWS in connection with the management of the Fund were not unreasonable. The Board also reviewed information regarding the profitability of certain similar investment management firms. The Board noted that while information regarding the profitability of such firms is limited (and in some cases is not necessarily prepared on a comparable basis), DWS and its affiliates' overall profitability with respect to the DWS fund complex (after taking into account distribution and other services provided to the funds by DWS and its affiliates) was lower than the overall profitability levels of many comparable firms for which such data was available.

**Economies of Scale.** The Board considered whether there are economies of scale with respect to the management of the Fund and whether the Fund benefits from any economies of scale. The Board noted that the Fund's management fee schedule includes fee breakpoints. The Board concluded that the Fund's fee schedule represents an appropriate sharing between the Fund and DWS of such economies of scale as may exist in the management of the Fund at current asset levels.

**Other Benefits to DWS and Its Affiliates.** The Board also considered the character and amount of other incidental benefits received by DWS and its affiliates, including any fees received by DWS for administrative services provided to the Fund and any fees received by an affiliate of DWS for distribution services. The Board also considered benefits to DWS related to brokerage and soft-dollar allocations, including allocating brokerage to pay for research generated by parties other than the executing broker dealers, which pertain primarily to funds investing in equity securities, along with the incidental public relations benefits to DWS related to DWS Funds advertising and cross-selling opportunities among DWS products and services. The Board concluded that management fees were reasonable in light of these fallout benefits.

**Compliance.** The Board considered the significant attention and resources dedicated by DWS to documenting and enhancing its compliance processes in recent years. The Board noted in particular (i) the experience and seniority of both DWS's chief compliance officer and the Fund's chief compliance officer; (ii) the large number of

DWS compliance personnel; and (iii) the substantial commitment of resources by DWS and its affiliates to compliance matters.

Based on all of the information considered and the conclusions reached, the Board unanimously (including the Independent Trustees) determined that the continuation of the Agreement is in the best interests of the Fund. In making this determination, the Board did not give particular weight to any single factor identified above. The Board considered these factors over the course of numerous meetings, certain of which were in executive session with only the Independent Trustees and their counsel present. It is possible that individual Trustees may have weighed these factors differently in reaching their individual decisions to approve the continuation of the Agreement.

# Summary of Management Fee Evaluation by Independent Fee Consultant

October 3, 2010

Pursuant to an Order entered into by Deutsche Investment Management Americas and affiliates (collectively, "DeAM") with the Attorney General of New York, I, Thomas H. Mack, have been appointed the Independent Fee Consultant for the DWS Funds (formerly the DWS Scudder Funds). My duties include preparing an annual written evaluation of the management fees DeAM charges the Funds, considering among other factors the management fees charged by other mutual fund companies for like services, management fees DeAM charges other clients for like services, DeAM's costs of supplying services under the management agreements and related profit margins, possible economies of scale if a Fund grows larger, and the nature and quality of DeAM's services, including fund performance. This report summarizes my evaluation for 2010, including my qualifications, the evaluation process for each of the DWS Funds, consideration of certain complex-level factors, and my conclusions. I served in substantially the same capacity in 2007, 2008, and 2009.

## Qualifications

For more than 35 years I have served in various professional capacities within the investment management business. I have held investment analysis and advisory positions, including securities analyst, portfolio strategist and director of investment policy with a large investment firm. I have also performed business management functions, including business development, financial management and marketing research and analysis.

Since 1991, I have been an independent consultant within the asset management industry. I have provided services to over 125 client organizations, including investment managers, mutual fund boards, product distributors and related organizations. Over the past ten years I have completed a number of assignments for mutual fund boards, specifically including assisting boards with management contract renewal.

I hold a Master of Business Administration degree, with highest honors, from Harvard University and Master of Science and Bachelor of Science (highest honors) degrees from the University of California at Berkeley. I am an independent director and audit committee financial expert for two closed-end mutual funds and have served in various leadership and financial oversight capacities with non-profit organizations.

## Evaluation of Fees for each DWS Fund

My work focused primarily on evaluating, fund-by-fund, the fees charged to each of the 118 publicly offered Fund portfolios in the DWS Fund family. For each Fund, I considered each of the key factors mentioned above, as well as any other relevant information. In doing so I worked closely with the Funds' Independent Directors in their annual contract renewal process, as well as in their approval of contracts for several new funds (documented separately).

In evaluating each Fund's fees, I reviewed comprehensive materials provided by or on behalf of DeAM, including expense information prepared by Lipper Analytical, comparative performance information, profitability data, manager histories, and other materials. I also accessed certain additional information from the Lipper and Morningstar databases and drew on my industry knowledge and experience.

To facilitate evaluating this considerable body of information, I prepared for each Fund a document summarizing the key data elements in each area as well as additional analytics discussed below. This made it possible to consider each key data element in the context of the others.

In the course of contract renewal, DeAM agreed to implement a number of fee and expense adjustments requested by the Independent Directors which will favorably impact future fees and expenses, and my evaluation includes the effects of these changes.

### Fees and Expenses Compared with Other Funds

The competitive fee and expense evaluation for each fund focused on two primary comparisons:

- The Fund's contractual management fee (the advisory fee plus the administration fee where applicable) compared with those of a group of typically 12–15 funds in the same Lipper investment category (e.g. Large Capitalization Growth) having similar distribution arrangements and being of similar size.
- The Fund's total expenses compared with a broader universe of funds from the same Lipper investment category and having similar distribution arrangements.

These two comparisons provide a view of not only the level of the fee compared with funds of similar scale but also the total expense the Fund bears for all the services it receives, in comparison with the investment choices available in the Fund's investment category and distribution channel. The principal figure-of-merit used in these comparisons was the subject Fund's percentile ranking against peers.

### DeAM's Fees for Similar Services to Others

DeAM provided management fee schedules for all of its US domiciled fund and non-fund investment management accounts in any of the investment categories where there is a DWS Fund. These similar products included the other DWS Funds, non-fund pooled accounts, institutional accounts and sub-advisory accounts. Using this information, I calculated for each Fund the fee that would be charged to each similar product, at the subject Fund's asset level.

Evaluating information regarding non-fund products is difficult because there are varying levels of services required for different types of accounts, with mutual funds generally requiring considerably more regulatory and administrative types of service as well as having more frequent cash flows than other types of accounts. Also, while mutual fund fees for similar fund products can be expected to be similar, there will be some differences due to different pricing conditions in different distribution channels (e.g. retail funds versus those used in variable insurance products), differences in underlying investment processes and other factors.

**Costs and Profit Margins**

DeAM provided a detailed profitability analysis for each Fund. After making some adjustments so that the presentation would be more comparable to the available industry figures, I reviewed profit margins from investment management alone, from investment management plus other fund services (excluding distribution) provided to the Funds by DeAM (principally shareholder services), and DeAM profits from all sources, including distribution. A later section comments on overall profitability.

**Economies of Scale**

Economies of scale — an expected decline in management cost per dollar of fund assets as fund assets grow — are very rarely quantified and documented because of inherent difficulties in collecting and analyzing relevant data. However, in virtually every investment category that I reviewed, larger funds tend to have lower fees and lower total expenses than smaller funds. To see how each DWS Fund compares with this industry observation, I reviewed:

- The trend in Fund assets over the last five years and the accompanying trend in total expenses. This shows if the Fund has grown and, if so, whether total expense (management fees as well as other expenses) have declined as a percent of assets.
- Whether the Fund has break-points in its management fee schedule, the extent of the fee reduction built into the schedule and the asset levels where the breaks take effect, and in the case of a sub-advised Fund how the Fund's break-points compare with those of the sub-advisory fee schedule.
- How the Fund's contractual fee schedule compares with trends in the industry data. To accomplish this, I constructed a chart showing how actual latest-fiscal-year contractual fees of the Fund and of other similar funds relate to average fund assets, with the subject Fund's contractual fee schedule superimposed.

**Quality of Service — Performance**

The quality-of-service evaluation focused on investment performance, which is the principal result of the investment management service. Each Fund's performance was reviewed over the past 1, 3, 5 and 10 years, as applicable, and compared with that of other funds in the same investment category and with a suitable market index.

In addition, I calculated and reviewed risk-adjusted returns relative to an index of similar mutual funds' returns and a suitable market index. The risk-adjusted returns analysis provides a way of determining the extent to which the Fund's return comparisons are mainly the product of investment value-added (or lack thereof) or alternatively taking considerably more or less risk than is typical in its investment category.

I also received and considered the history of portfolio manager changes for each Fund, as this provided an important context for evaluating the performance results.

## Complex-Level Considerations

While this evaluation was conducted mainly at the individual fund level, there are some issues relating to the reasonableness of fees that can alternatively be considered across the whole fund complex:

- I reviewed DeAM's profitability analysis for all DWS Funds, with a view toward determining if the allocation procedures used were reasonable and how profit levels compared with public data for other investment managers.
- I considered whether DeAM and affiliates receive any significant ancillary or "fall-out" benefits that should be considered in interpreting the direct profitability results. These would be situations where serving as the investment manager of the Funds is beneficial to another part of the Deutsche Bank organization.
- I considered how aggregated DWS Fund expenses had varied over the years, by asset class and in the context of trends in asset levels.
- I reviewed the structure of the DeAM organization, trends in staffing levels, and information on compensation of investment management and other professionals compared with industry data.

## Findings

Based on the process and analysis discussed above, which included reviewing a wide range of information from management and external data sources and considering among other factors the fees DeAM charges other clients, the fees charged by other fund managers, DeAM's costs and profits associated with managing the Funds, economies of scale, possible fall-out benefits, and the nature and quality of services provided, in my opinion the management fees charged the DWS Funds are reasonable.

Thomas H. Mack

Thomas H. Mack

# Board Members and Officers

The following table presents certain information regarding the Board Members and Officers of the Trust as of December 31, 2010. Each Board Member's year of birth is set forth in parentheses after his or her name. Unless otherwise noted, (i) each Board Member has engaged in the principal occupation(s) noted in the table for at least the most recent five years, although not necessarily in the same capacity; and (ii) the address of each Independent Board Member is c/o Paul K. Freeman, Independent Chairman, DWS Funds, PO Box 101833, Denver, CO 80250-1833. Except as otherwise noted below, the term of office for each Board Member is until the election and qualification of a successor, or until such Board Member sooner dies, resigns, is removed or as otherwise provided in the governing documents of the fund. Because the fund does not hold an annual meeting of shareholders, each Board Member will hold office for an indeterminate period. The Board Members may also serve in similar capacities with other funds in the fund complex. The Length of Time Served represents the year in which the Board Member joined the board of one or more DWS funds now overseen by the Board.

### Independent Board Members

| Name, Year of Birth, Position with the Fund and Length of Time Served[1] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Paul K. Freeman (1950)<br>Chairperson since 2009<br>Board Member since 1993 | Consultant, World Bank/Inter-American Development Bank; Executive and Governing Council of the Independent Directors Council (education committees); formerly, Project Leader, International Institute for Applied Systems Analysis (1998–2001); Chief Executive Officer, The Eric Group, Inc. (environmental insurance) (1986–1998) | 122 |
| John W. Ballantine (1946)<br>Board Member since 1999 | Retired; formerly, Executive Vice President and Chief Risk Management Officer, First Chicago NBD Corporation/The First National Bank of Chicago (1996–1998); Executive Vice President and Head of International Banking (1995–1996). Directorships: Healthways, Inc. (provider of disease and care management services); Portland General Electric (utility company); Stockwell Capital Investments PLC (private equity). Former Directorships: First Oak Brook Bancshares, Inc. and Oak Brook Bank; Prisma Energy International | 122 |
| Henry P. Becton, Jr. (1943)<br>Board Member since 1990 | Vice Chair and former President, WGBH Educational Foundation. Directorships: Association of Public Television Stations; Lead Director, Becton Dickinson and Company[3] (medical technology company); Lead Director, Belo Corporation[3] (media company); Public Radio International; Public Radio Exchange (PRX); The PBS Foundation. Former Directorships: Boston Museum of Science; American Public Television; Concord Academy; New England Aquarium; Mass. Corporation for Educational Telecommunications; Committee for Economic Development; Public Broadcasting Service | 122 |
| Dawn-Marie Driscoll (1946)<br>Board Member since 1987 | President, Driscoll Associates (consulting firm); Executive Fellow, Center for Business Ethics, Bentley University; formerly, Partner, Palmer & Dodge (1988–1990); Vice President of Corporate Affairs and General Counsel, Filene's (1978–1988). Directorships: Trustee of 22 open-end mutual funds managed by Sun Capital Advisers, Inc. (since 2007); Director of ICI Mutual Insurance Company (since 2007); Advisory Board, Center for Business Ethics, Bentley University; Trustee, Southwest Florida Community Foundation (charitable organization). Former Directorships: Investment Company Institute (audit, executive, nominating committees) and Independent Directors Council (governance, executive committees) | 122 |
| Keith R. Fox (1954)<br>Board Member since 1996 | Managing General Partner, Exeter Capital Partners (a series of private investment funds). Directorships: Progressive International Corporation (kitchen goods importer and distributor); BoxTop Media Inc. (advertising); The Kennel Shop (retailer); former Chairman, National Association of Small Business Investment Companies | 122 |
| Kenneth C. Froewiss (1945)<br>Board Member since 2001 | Adjunct Professor of Finance, NYU Stern School of Business (September 2009–present; Clinical Professor from 1997–September 2009); Member, Finance Committee, Association for Asian Studies (2002–present); Director, Mitsui Sumitomo Insurance Group (US) (2004–present); prior thereto, Managing Director, J.P. Morgan (investment banking firm) (until 1996) | 122 |
| Richard J. Herring (1946)<br>Board Member since 1990 | Jacob Safra Professor of International Banking and Professor, Finance Department, The Wharton School, University of Pennsylvania (since July 1972); Co-Director, Wharton Financial Institutions Center (since July 2000); Co-Chair, U.S. Shadow Financial Regulatory Committee; Executive Director, Financial Economists Roundtable; Director, Japan Equity Fund, Inc. (since September 2007), Thai Capital Fund, Inc. (since September 2007), Singapore Fund, Inc. (since September 2007); Independent Director of Barclays Bank Delaware (since September 2010). Formerly, Vice Dean and Director, Wharton Undergraduate Division (July 1995–June 2000); Director, Lauder Institute of International Management Studies (July 2000–June 2006) | 122 |
| William McClayton (1944)<br>Board Member since 2004+ | Private equity investor (since October 2009); previously, Managing Director, Diamond Management & Technology Consultants, Inc. (global consulting firm) (2001–2009); Directorship: Board of Managers, YMCA of Metropolitan Chicago; formerly: Senior Partner, Arthur Andersen LLP (accounting) (1966–2001); Trustee, Ravinia Festival | 122 |

| Name, Year of Birth, Position with the Fund and Length of Time Served[1] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Rebecca W. Rimel (1951)<br>Board Member since 1995 | President and Chief Executive Officer, The Pew Charitable Trusts (charitable organization) (1994 to present); Trustee, Thomas Jefferson Foundation (charitable organization) (1994 to present); Trustee, Executive Committee, Philadelphia Chamber of Commerce (2001–2007); Director, CardioNet, Inc.[2] (2009–present) (health care). Formerly, Executive Vice President, The Glenmede Trust Company (investment trust and wealth management) (1983–2004); Board Member, Investor Education (charitable organization) (2004–2005); Director, Viasys Health Care[2] (January 2007–June 2007); Trustee, Pro Publica (charitable organization) (2007–2010) | 122 |
| William N. Searcy, Jr. (1946)<br>Board Member since 1993 | Private investor since October 2003; Trustee of 22 open-end mutual funds managed by Sun Capital Advisers, Inc. (since October 1998). Formerly, Pension & Savings Trust Officer, Sprint Corporation[2] (telecommunications) (November 1989–September 2003) | 122 |
| Jean Gleason Stromberg (1943)<br>Board Member since 1997 | Retired. Formerly, Consultant (1997–2001); Director, Financial Markets US Government Accountability Office (1996–1997); Partner, Fulbright & Jaworski, L.L.P. (law firm) (1978–1996). Directorships: The William and Flora Hewlett Foundation. Former Directorships: Service Source, Inc., Mutual Fund Directors Forum (2002–2004), American Bar Retirement Association (funding vehicle for retirement plans) (1987–1990 and 1994–1996) | 122 |
| Robert H. Wadsworth (1940)<br>Board Member since 1999 | President, Robert H. Wadsworth & Associates, Inc. (consulting firm) (1983 to present); Director, The Phoenix Boys Choir Association | 125 |

## Interested Board Member and Officer[4]

| Name, Year of Birth, Position with the Trust/ Corporation and Length of Time Served[1,5] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Ingo Gefeke[7] (1967)<br>Board Member since 2010<br>Executive Vice President since 2010 | Managing Director[3], Deutsche Asset Management; Global Head of Distribution and Product Management, DWS Global Head of Trading and Securities Lending. Member of the Board of Directors of DWS Investment GmbH Frankfurt (since July 2009) and DWS Holding & Service GmbH Frankfurt (since January 2010); formerly, Global Chief Administrative Officer, Deutsche Asset Management (2004–2009); Global Chief Operating Officer, Global Transaction Banking, Deutsche Bank AG, New York (2001–2004); Chief Operating Officer, Global Banking Division Americas, Deutsche Bank AG, New York (1999–2001); Central Management, Global Banking Services, Deutsche Bank AG, Frankfurt (1998–1999); Relationship Management, Deutsche Bank AG, Tokyo, Japan (1997–1998) | 55 |

## Officers[4]

| Name, Year of Birth, Position with the Fund and Length of Time Served[5] | Principal Occupation(s) During Past 5 Years and Other Directorships Held |
|---|---|
| Michael G. Clark[6] (1965)<br>President, 2006–present | Managing Director[3], Deutsche Asset Management (2006–present); President of DWS family of funds; Director, ICI Mutual Insurance Company (since October 2007); formerly, Director of Fund Board Relations (2004–2006) and Director of Product Development (2000–2004), Merrill Lynch Investment Managers; Senior Vice President Operations, Merrill Lynch Asset Management (1999–2000) |
| John Millette[8] (1962)<br>Vice President and Secretary, 1999–present | Director[3], Deutsche Asset Management |
| Paul H. Schubert[6] (1963)<br>Chief Financial Officer, 2004–present<br>Treasurer, 2005–present | Managing Director[3], Deutsche Asset Management (since July 2004); formerly, Executive Director, Head of Mutual Fund Services and Treasurer for UBS Family of Funds (1998–2004); Vice President and Director of Mutual Fund Finance at UBS Global Asset Management (1994–1998) |
| Caroline Pearson[8] (1962)<br>Chief Legal Officer, April 2010–present | Managing Director[3], Deutsche Asset Management; formerly, Assistant Secretary for DWS family of funds (1997–2010) |
| Rita Rubin[9] (1970)<br>Assistant Secretary, 2009–present | Vice President and Counsel, Deutsche Asset Management (since October 2007); formerly, Vice President, Morgan Stanley Investment Management (2004–2007) |
| Paul Antosca[8] (1957)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management (since 2006); Vice President, The Manufacturers Life Insurance Company (U.S.A.) (1990–2006) |
| Jack Clark[8] (1967)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management (since 2007); formerly, Vice President, State Street Corporation (2002–2007) |

| Name, Year of Birth, Position with the Fund and Length of Time Served[5] | Principal Occupation(s) During Past 5 Years and Other Directorships Held |
|---|---|
| Diane Kenneally[8] (1966)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management |
| John Caruso[9] (1965)<br>Anti-Money Laundering Compliance Officer, 2010–present | Managing Director[3], Deutsche Asset Management |
| Robert Kloby[9] (1962)<br>Chief Compliance Officer, 2006–present | Managing Director[3], Deutsche Asset Management |

1 *The length of time served represents the year in which the Board Member joined the board of one or more DWS funds currently overseen by the Board.*

2 *A publicly held company with securities registered pursuant to Section 12 of the Securities Exchange Act of 1934.*

3 *Executive title, not a board directorship.*

4 *As a result of their respective positions held with the Advisor, these individuals are considered "interested persons" of the Advisor within the meaning of the 1940 Act. Interested persons receive no compensation from the fund.*

5 *The length of time served represents the year in which the officer was first elected in such capacity for one or more DWS funds.*

6 *Address: 100 Plaza One, Jersey City, NJ 07311.*

7 *Effective January 11, 2011, Mr. Gefeke, an interested Board Member and Executive Vice President, resigned from the fund's Board and as an officer.*

*The mailing address of Mr. Gefeke is 345 Park Avenue, New York, New York 10154. Mr. Gefeke was an interested Board Member of certain DWS funds by virtue of his positions with Deutsche Asset Management. As an interested person, Mr. Gefeke received no compensation from the fund.*

8 *Address: One Beacon Street, Boston, MA 02108.*

9 *Address: 60 Wall Street, New York, New York 10005.*

*The fund's Statement of Additional Information ("SAI") includes additional information about the Board Members. The SAI is available, without charge, upon request. If you would like to request a copy of the SAI, you may do so by calling the following toll-free number: (800) 728-3337.*

## Notes

DWS Investments is part of Deutsche Bank's Asset Management division and, within the US, represents the retail asset management activities of Deutsche Bank AG, Deutsche Bank Trust Company Americas, Deutsche Investment Management Americas Inc. and DWS Trust Company.

The views expressed in this report reflect those of the portfolio managers only through the end of the period of the report as stated on the cover. The managers' views are subject to change at any time based on market and other conditions and should not be construed as a recommendation.

This information must be preceded or accompanied by a current prospectus.

Portfolio changes should not be considered recommendations for action by individual investors.

DWS Investments Distributors, Inc.
222 South Riverside Plaza
Chicago, IL 60606
(800) 621-1148

VS2HI-2 (2/11)

DWS INVESTMENTS
Deutsche Bank Group

DECEMBER 31, 2010

# ANNUAL REPORT

## DWS VARIABLE SERIES II

## DWS Large Cap Value VIP

**This report must be preceded or accompanied by a prospectus. To obtain an additional prospectus or summary prospectus, if available, call (800) 728-3337 or your financial representative. We advise you to consider the Fund's objectives, risks, charges and expenses carefully before investing. The summary prospectus and prospectus contain this and other important information about the Fund. Please read the prospectus carefully before you invest.**

*Investments in variable insurance portfolios (VIPs) involve risk. Stocks may decline in value. Bond investments are subject to interest-rate and credit risks. When interest rates rise, bond prices generally fall. Credit risk refers to the ability of an issuer to make timely payments of principal and interest. Investing in derivatives entails special risks relating to liquidity, leverage and credit that may reduce returns and/or increased volatility. Investing in foreign securities, particularly those of emerging markets, presents certain risks, such as currency fluctuations, political and economic changes, and market risks. There are additional risks associated with investing in commodities, high-yield bonds, aggressive growth stocks, non-diversified/ concentrated funds and small- and mid-cap stocks which are more fully explained in the prospectuses. Please read the prospectus for more information.*

*DWS Investments is part of Deutsche Bank's Asset Management division and, within the US, represents the retail asset management activities of Deutsche Bank AG, Deutsche Bank Trust Company Americas, Deutsche Investment Management Americas Inc. and DWS Trust Company.*



DWS INVESTMENTS
Deutsche Bank Group

## DWS Large Cap Value VIP

**All performance shown is historical, assumes reinvestment of all dividend and capital gain distributions and does not guarantee future results. Investment return and principal value fluctuate with changing market conditions so that, when redeemed, shares may be worth more or less than their original cost. Current performance may be lower or higher than the performance data quoted. Please contact your participating insurance company for the Fund's most recent month-end performance. Performance doesn't reflect charges and fees ("contract charges") associated with the separate account that invests in the Fund or any variable life insurance policy or variable annuity contract for which the Fund is an investment option. These charges and fees will reduce returns. While all share classes have the same underlying portfolio, their performance will differ.**

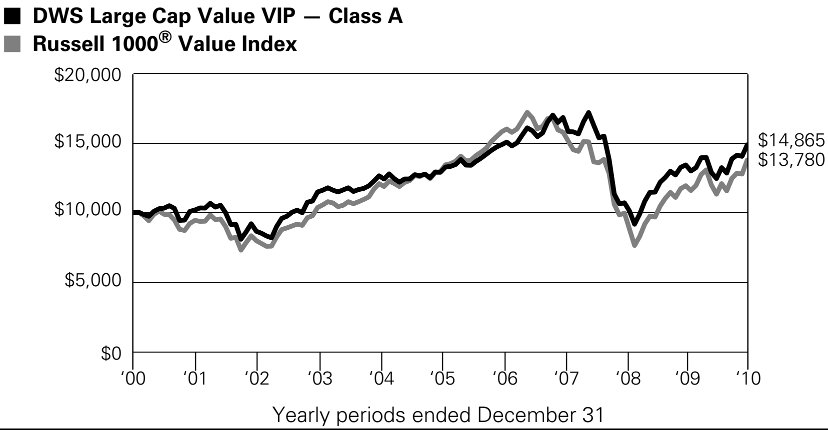
**The gross expense ratios of the Fund, as stated in the fee table of the prospectus dated May 1, 2010 are 0.76% and 1.06% for Class A and Class B shares, respectively, and may differ from the expense ratios disclosed in the Financial Highlights tables in this report.**

### Risk Considerations

Stocks may decline in value. See the prospectus for details.

Fund returns shown for the 3-year, 5-year and 10-year/Life of Class periods reflect a fee waiver and/or expense reimbursement. Without this waiver/reimbursement, returns would have been lower.

### Growth of an Assumed $10,000 Investment in DWS Large Cap Value VIP




*The Russell 1000® Value Index is an unmanaged index that consists of those stocks in the Russell 1000 Index with less-than-average growth orientation. Russell 1000® Index is an unmanaged price-only index of the 1,000 largest capitalized companies that are domiciled in the US and whose common stocks are traded.*

*Index returns assume reinvestment of dividends and, unlike fund returns, do not reflect any fees or expenses. It is not possible to invest directly into an index.*

### Comparative Results

| DWS Large Cap Value VIP | | 1-Year | 3-Year | 5-Year | 10-Year |
|---|---|---|---|---|---|
| **Class A** | Growth of $10,000 | $11,077 | $8,833 | $11,534 | $14,865 |
| | Average annual total return | 10.77% | –4.05% | 2.90% | 4.04% |
| Russell 1000 Value Index | Growth of $10,000 | $11,551 | $8,731 | $10,654 | $13,780 |
| | Average annual total return | 15.51% | –4.42% | 1.28% | 3.26% |

| DWS Large Cap Value VIP | | 1-Year | 3-Year | 5-Year | Life of Class* |
|---|---|---|---|---|---|
| **Class B** | Growth of $10,000 | $11,053 | $8,744 | $11,335 | $14,675 |
| | Average annual total return | 10.53% | –4.38% | 2.54% | 4.62% |
| Russell 1000 Value Index | Growth of $10,000 | $11,551 | $8,731 | $10,654 | $15,327 |
| | Average annual total return | 15.51% | –4.42% | 1.28% | 5.15% |

*The growth of $10,000 is cumulative.*

* *The Fund commenced offering Class B shares on July 1, 2002. Index returns began on June 30, 2002.*

# Information About Your Fund's Expenses

## DWS Large Cap Value VIP

As an investor of the Fund, you incur two types of costs: ongoing expenses and transaction costs. Ongoing expenses include management fees, distribution and service (12b-1) fees and other Fund expenses. Examples of transaction costs include contract charges, redemption fees and account maintenance fees, which are not shown in this section. The following tables are intended to help you understand your ongoing expenses (in dollars) of investing in the Fund and to help you compare these expenses with the ongoing expenses of investing in other mutual funds. The example in the table is based on an investment of $1,000 invested at the beginning of the six-month period and held for the entire period (July 1, 2010 to December 31, 2010).

The tables illustrate your Fund's expenses in two ways:

- **Actual Fund Return.** This helps you estimate the actual dollar amount of ongoing expenses (but not transaction costs) paid on a $1,000 investment in the Fund using the Fund's actual return during the period. To estimate the expenses you paid over the period, simply divide your account value by $1,000 (for example, an $8,600 account value divided by $1,000 = 8.6), then multiply the result by the number in the "Expenses Paid per $1,000" line under the share class you hold.
- **Hypothetical 5% Fund Return.** This helps you to compare your Fund's ongoing expenses (but not transaction costs) with those of other mutual funds using the Fund's actual expense ratio and a hypothetical rate of return of 5% per year before expenses. Examples using a 5% hypothetical Fund return may be found in the shareholder reports of other mutual funds. The hypothetical account values and expenses may not be used to estimate the actual ending account balance or expenses you paid for the period.

Please note that the expenses shown in these tables are meant to highlight your ongoing expenses only and do not reflect any transaction costs. The "Expenses Paid per $1,000" line of the tables is useful in comparing ongoing expenses only and will not help you determine the relative total expense of owning different funds. If these transaction costs had been included, your costs would have been higher.

**Expenses and Value of a $1,000 Investment** for the six months ended December 31, 2010

| Actual Fund Return | Class A | Class B |
|---|---|---|
| Beginning Account Value 7/1/10 | $1,000.00 | $1,000.00 |
| Ending Account Value 12/31/10 | $1,194.30 | $1,192.90 |
| Expenses Paid per $1,000* | $ 4.48 | $ 6.08 |
| **Hypothetical 5% Fund Return** | **Class A** | **Class B** |
| Beginning Account Value 7/1/10 | $1,000.00 | $1,000.00 |
| Ending Account Value 12/31/10 | $1,021.12 | $1,019.66 |
| Expenses Paid per $1,000* | $ 4.13 | $ 5.60 |

* *Expenses are equal to the Fund's annualized expense ratio for each share class, multiplied by the average account value over the period, multiplied by the number of days in the most recent six-month period, then divided by 365.*

| Annualized Expense Ratios | Class A | Class B |
|---|---|---|
| DWS Variable Series II — DWS Large Cap Value VIP | .81% | 1.10% |

For more information, please refer to the Fund's prospectus.

These tables do not reflect charges and fees ("contract charges") associated with the separate account that invests in the Fund or any variable life insurance policy or variable annuity contract for which the Fund is an investment option.

## DWS Large Cap Value VIP

The DWS Large Cap Value VIP delivered a total return of 10.77% in 2010 (Class A shares, unadjusted for contract charges) but underperformed the 15.51% return of the benchmark, the Russell 1000® Value Index. While we added quite a bit of value through our sector allocations — specifically, our underweight in financials and overweight in energy — this was more than offset by the underperformance of our individual stock picks.[1]

Although the Fund (Class A shares) lagged the Russell 1000 Value Index during the past year, it has outpaced the benchmark by a comfortable margin over the 3-, 5- and 10-year periods ended December 31, 2010.

An important reason for the Fund's underperformance was our preference for high-dividend-paying stocks with stable cash flows and our corresponding underweight in the higher-risk cyclical areas of the market. This positioning was based on our view that the economic recovery was largely the result of short-term, unsustainable fiscal and monetary stimuli rather than a sustainable, longer-term improvement in final demand. Expecting that this would ultimately result in a lower-growth, lower-return market environment, we shifted assets out of cyclical deep-value stocks into less cyclical stable-value stocks during the early part of the year. Unfortunately, cyclical higher-beta stocks, in fact, strongly outperformed the market by a substantial margin during the past 12 months.[2]

Although our defensive approach hurt performance in 2010, we believe it remains appropriate given our ongoing caution regarding the broader market. Additionally, it positions the Fund in the areas of the market with the most attractive valuations.[3] Many cyclical stocks staged substantial rallies in the fourth quarter, leaving them vulnerable to potential disappointments. Conversely, many stocks that lagged during the recent run-up offer much more reasonable valuations. These types of out-of-favor, undervalued stocks are typically characterized by more muted investor expectations, meaning that they are both less vulnerable to disappointments and more likely to have upside potential. We therefore remain consistent in our strategy as we await the potential return to compelling performance for the market's most attractively valued companies.

Thomas Schuessler, PhD.
*Lead Portfolio Manager*

Volker Dosch
Oliver Pfeil, PhD.
*Portfolio Managers*

*The Russell 1000® Value Index is an unmanaged index that consists of those stocks in the Russell 1000 Index with less-than-average growth orientation. Russell 1000® Index is an unmanaged price-only index of the 1,000 largest capitalized companies that are domiciled in the US and whose common stocks are traded.*

*Index returns assume reinvestment of dividends and, unlike fund returns, do not reflect any fees or expenses. It is not possible to invest directly into an index.*

1 *"Overweight" means the Fund holds a higher weighting in a given sector or security than the benchmark. "Underweight" means the Fund holds a lower weighting.*

2 *Beta is a measure of volatility, or systematic risk, of a security or a portfolio in comparison to the market as a whole.*

3 *"Valuation" refers to the price investors pay for a given security. An asset can be undervalued, meaning that it trades for less than its intrinsic value, or overvalued, which means that it trades at a more expensive price than its underlying worth.*

*Portfolio management market commentary is as of December 31, 2010, and may not come to pass. This information is subject to change at any time based on market and other conditions. Past performance does not guarantee future results. Current and future portfolio holdings are subject to risk.*

# Portfolio Summary

## DWS Large Cap Value VIP

| **Asset Allocation** (As a % of Investment Portfolio excluding Securities Lending Collateral) | **12/31/10** | **12/31/09** |
|---|---|---|
| Common Stocks | 98% | 99% |
| Cash Equivalents | 2% | 1% |
| | 100% | 100% |

| **Sector Diversification** (As a % of Common Stocks) | **12/31/10** | **12/31/09** |
|---|---|---|
| Energy | 18% | 15% |
| Financials | 13% | 15% |
| Health Care | 12% | 13% |
| Consumer Staples | 12% | 12% |
| Utilities | 10% | 11% |
| Telecommunication Services | 9% | 11% |
| Information Technology | 8% | 2% |
| Consumer Discretionary | 7% | 5% |
| Industrials | 6% | 10% |
| Materials | 5% | 6% |
| | 100% | 100% |

*Asset allocation and sector diversification are subject to change.*

*For more complete details about the Fund's investment portfolio, see page 6.*

Following the Fund's fiscal first and third quarter-end, a complete portfolio holdings listing is filed with the SEC on Form N-Q. The form will be available on the SEC's Web site at www.sec.gov, and it also may be reviewed and copied at the SEC's Public Reference Room in Washington, D.C. Information on the operation of the SEC's Public Reference Room may be obtained by calling (800) SEC-0330. The Fund's portfolio holdings are also posted on www.dws-investments.com from time to time. Please see the Fund's current prospectus for more information.

# Investment Portfolio

December 31, 2010

## DWS Large Cap Value VIP

| | Shares | Value ($) |
|---|---|---|
| **Common Stocks 97.8%** | | |
| **Consumer Discretionary 7.2%** | | |
| **Distributors 2.1%** | | |
| Genuine Parts Co. | 84,678 | **4,347,369** |
| **Diversified Consumer Services 1.3%** | | |
| H&R Block, Inc. (a) | 217,813 | **2,594,153** |
| **Hotels Restaurants & Leisure 1.3%** | | |
| Carnival Corp. (Units) | 59,867 | **2,760,467** |
| **Media 1.4%** | | |
| News Corp. "A" | 197,872 | **2,881,016** |
| **Textiles, Apparel & Luxury Goods 1.1%** | | |
| VF Corp. (a) | 26,538 | **2,287,045** |
| **Consumer Staples 11.5%** | | |
| **Beverages 1.4%** | | |
| PepsiCo, Inc. | 42,128 | **2,752,222** |
| **Food & Staples Retailing 3.1%** | | |
| CVS Caremark Corp. | 103,849 | 3,610,830 |
| Kroger Co. | 123,703 | 2,765,999 |
| | | **6,376,829** |
| **Food Products 2.9%** | | |
| General Mills, Inc. | 50,103 | 1,783,166 |
| Kellogg Co. | 43,279 | 2,210,692 |
| Mead Johnson Nutrition Co. | 32,885 | 2,047,091 |
| | | **6,040,949** |
| **Tobacco 4.1%** | | |
| Altria Group, Inc. | 172,422 | 4,245,030 |
| Philip Morris International, Inc. | 73,171 | 4,282,698 |
| | | **8,527,728** |
| **Energy 17.6%** | | |
| **Energy Equipment & Services 4.7%** | | |
| Ensco PLC (ADR) | 64,045 | 3,418,722 |
| Noble Corp. | 90,557 | 3,239,224 |
| Transocean Ltd.* (a) | 44,883 | 3,119,817 |
| | | **9,777,763** |
| **Oil, Gas & Consumable Fuels 12.9%** | | |
| Canadian Natural Resources Ltd. | 69,548 | 3,089,322 |
| Chevron Corp. | 49,457 | 4,512,951 |
| ConocoPhillips | 51,156 | 3,483,723 |
| Exxon Mobil Corp. | 50,290 | 3,677,205 |
| Marathon Oil Corp. (a) | 119,795 | 4,436,009 |
| Nexen, Inc. | 104,342 | 2,389,432 |
| Suncor Energy, Inc. | 131,220 | 5,024,414 |
| | | **26,613,056** |
| **Financials 12.6%** | | |
| **Diversified Financial Services 1.8%** | | |
| JPMorgan Chase & Co. | 85,723 | **3,636,370** |
| **Insurance 10.8%** | | |
| Assurant, Inc. | 74,334 | 2,863,346 |
| Fidelity National Financial, Inc. "A" (a) | 148,069 | 2,025,584 |
| HCC Insurance Holdings, Inc. | 73,331 | 2,122,199 |
| Lincoln National Corp. (a) | 133,833 | 3,721,896 |
| MetLife, Inc. | 95,678 | 4,251,930 |
| PartnerRe Ltd. (a) | 50,697 | 4,073,504 |
| Prudential Financial, Inc. | 57,640 | 3,384,044 |
| | | **22,442,503** |
| **Health Care 12.0%** | | |
| **Health Care Equipment & Supplies 3.1%** | | |
| Baxter International, Inc. | 72,472 | 3,668,533 |
| Becton, Dickinson & Co. (a) | 32,656 | 2,760,085 |
| | | **6,428,618** |
| **Health Care Providers & Services 3.0%** | | |
| McKesson Corp. | 56,640 | 3,986,323 |
| WellPoint, Inc.* | 38,719 | 2,201,562 |
| | | **6,187,885** |
| **Life Sciences Tools & Services 1.1%** | | |
| Thermo Fisher Scientific, Inc.* | 40,838 | **2,260,792** |
| **Pharmaceuticals 4.8%** | | |
| Johnson & Johnson | 32,793 | 2,028,247 |
| Merck & Co., Inc. | 106,108 | 3,824,132 |
| Teva Pharmaceutical Industries Ltd. (ADR) | 77,764 | 4,053,838 |
| | | **9,906,217** |
| **Industrials 5.6%** | | |
| **Aerospace & Defense 3.8%** | | |
| Northrop Grumman Corp. | 42,452 | 2,750,041 |
| Raytheon Co. | 56,220 | 2,605,235 |
| United Technologies Corp. | 31,674 | 2,493,377 |
| | | **7,848,653** |
| **Machinery 1.8%** | | |
| Dover Corp. (a) | 63,567 | **3,715,491** |
| **Information Technology 8.0%** | | |
| **Communications Equipment 1.7%** | | |
| Brocade Communications Systems, Inc.* | 254,336 | 1,345,438 |
| Cisco Systems, Inc.* | 104,962 | 2,123,381 |
| | | **3,468,819** |
| **Computers & Peripherals 1.6%** | | |
| Hewlett-Packard Co. | 81,776 | **3,442,769** |
| **IT Services 1.1%** | | |
| Automatic Data Processing, Inc. | 49,734 | **2,301,689** |
| **Semiconductors & Semiconductor Equipment 1.7%** | | |
| Intel Corp. | 168,322 | **3,539,812** |
| **Software 1.9%** | | |
| Microsoft Corp. | 138,377 | **3,863,486** |
| **Materials 5.1%** | | |
| **Chemicals 3.4%** | | |
| Air Products & Chemicals, Inc. | 45,671 | 4,153,778 |
| Praxair, Inc. (a) | 30,296 | 2,892,359 |
| | | **7,046,137** |
| **Containers & Packaging 1.7%** | | |
| Sonoco Products Co. (a) | 101,372 | **3,413,195** |
| **Telecommunication Services 8.5%** | | |
| **Diversified Telecommunication Services 7.1%** | | |
| AT&T, Inc. | 163,617 | 4,807,068 |
| BCE, Inc. | 28,303 | 1,003,624 |

*The accompanying notes are an integral part of the financial statements.*

| | Shares | Value ($) |
|---|---|---|
| CenturyLink, Inc. (a) | 126,161 | 5,824,853 |
| Verizon Communications, Inc. | 82,706 | 2,959,221 |
| | | **14,594,766** |
| **Wireless Telecommunication Services 1.4%** | | |
| Vodafone Group PLC (ADR) (a) | 113,690 | **3,004,827** |
| **Utilities 9.7%** | | |
| **Electric Utilities 7.7%** | | |
| Allegheny Energy, Inc. | 97,123 | 2,354,262 |
| American Electric Power Co., Inc. | 74,383 | 2,676,300 |
| Duke Energy Corp. (a) | 130,206 | 2,318,969 |
| Entergy Corp. | 34,093 | 2,414,807 |
| Exelon Corp. (a) | 30,886 | 1,286,093 |
| FirstEnergy Corp. (a) | 65,378 | 2,420,294 |
| Southern Co. (a) | 64,406 | 2,462,241 |
| | | **15,932,966** |
| **Multi-Utilities 2.0%** | | |
| PG&E Corp. | 87,684 | **4,194,801** |
| **Total Common Stocks** (Cost $163,225,850) | | **202,188,393** |

## Securities Lending Collateral 18.8%

| | Shares | Value ($) |
|---|---|---|
| Daily Assets Fund Institutional, 0.27% (b) (c) (Cost $38,843,948) | 38,843,948 | **38,843,948** |

## Cash Equivalents 2.3%

| | Shares | Value ($) |
|---|---|---|
| Central Cash Management Fund, 0.19% (b) (Cost $4,846,822) | 4,846,822 | **4,846,822** |

| | % of Net Assets | Value ($) |
|---|---|---|
| **Total Investment Portfolio** (Cost $206,916,620)† | 118.9 | **245,879,163** |
| **Other Assets and Liabilities, Net** | (18.9) | **(39,120,423)** |
| **Net Assets** | 100.0 | **206,758,740** |

* *Non-income producing security.*

† *The cost for federal income tax purposes was $209,013,049. At December 31, 2010, net unrealized appreciation for all securities based on tax cost was $36,866,114. This consisted of aggregate gross unrealized appreciation for all securities in which there was an excess of value over tax cost of $42,154,718 and aggregate gross unrealized depreciation for all securities in which there was an excess of tax cost over value of $5,288,604.*

(a) *All or a portion of these securities were on loan (see Notes to Financial Statements). The value of all securities loaned at December 31, 2010 amounted to $37,916,422, which is 18.3% of net assets.*

(b) *Affiliated fund managed by Deutsche Investment Management Americas Inc. The rate shown is the annualized seven-day yield at period end.*

(c) *Represents collateral held in connection with securities lending. Income earned by the Fund is net of borrower rebates.*

*ADR: American Depositary Receipt*

### Fair Value Measurements

*Various inputs are used in determining the value of the Fund's investments. These inputs are summarized in three broad levels. Level 1 includes quoted prices in active markets for identical securities. Level 2 includes other significant observable inputs (including quoted prices for similar securities, interest rates, prepayment speeds, and credit risk). Level 3 includes significant unobservable inputs (including the Fund's own assumptions in determining the fair value of investments). The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities.*

*The following is a summary of the inputs used as of December 31, 2010 in valuing the Fund's investments. For information on the Fund's policy regarding the valuation of investments, please refer to the Security Valuation section of Note A in the accompanying Notes to Financial Statements.*

| Assets | Level 1 | Level 2 | Level 3 | Total |
|---|---|---|---|---|
| Common Stocks (d) | $ 202,188,393 | $ — | $ — | $ 202,188,393 |
| Short-Term Investments (d) | 43,690,770 | — | — | 43,690,770 |
| **Total** | **$ 245,879,163** | **$ —** | **$ —** | **$ 245,879,163** |

*There have been no significant transfers between Level 1 and Level 2 fair value measurements during the year ended December 31, 2010.*

(d) *See Investment Portfolio for additional detailed categorizations.*

*The accompanying notes are an integral part of the financial statements.*

# Statement of Assets and Liabilities

as of December 31, 2010

| **Assets** | | |
|---|---|---|
| Investments: | | |
| Investments in unaffiliated securities, at value (cost $163,225,850) — including $37,916,422 of securities loaned | $ | 202,188,393 |
| Investment in Daily Assets Fund Institutional (cost $38,843,948)* | | 38,843,948 |
| Investment in Central Cash Management Fund (cost $4,846,822) | | 4,846,822 |
| Total investments, at value (cost $206,916,620) | | 245,879,163 |
| Cash | | 21,120 |
| Foreign currency, at value (cost $10,034) | | 11,513 |
| Receivable for Fund shares sold | | 150,489 |
| Dividends receivable | | 450,987 |
| Interest receivable | | 7,301 |
| Foreign taxes recoverable | | 22,127 |
| Other assets | | 1,106 |
| Total assets | | 246,543,806 |
| **Liabilities** | | |
| Payable upon return of securities loaned | | 38,843,948 |
| Payable for investments purchased | | 628,063 |
| Payable for Fund shares redeemed | | 114,217 |
| Accrued management fee | | 106,533 |
| Other accrued expenses and payables | | 92,305 |
| Total liabilities | | 39,785,066 |
| **Net assets, at value** | **$** | **206,758,740** |
| **Net Assets Consist of** | | |
| Undistributed net investment income | | 4,084,211 |
| Net unrealized appreciation (depreciation) on: | | |
| Investments | | 38,962,543 |
| Foreign currency | | 6,252 |
| Accumulated net realized gain (loss) | | (43,182,951) |
| Paid-in capital | | 206,888,685 |
| **Net assets, at value** | **$** | **206,758,740** |
| **Class A** | | |
| **Net Asset Value,** offering and redemption price per share ($205,517,002 ÷ 17,416,427 outstanding shares of beneficial interest, no par value, unlimited number of shares authorized) | **$** | **11.80** |
| **Class B** | | |
| **Net Asset Value,** offering and redemption price per share ($1,241,738 ÷ 105,172 outstanding shares of beneficial interest, no par value, unlimited number of shares authorized) | **$** | **11.81** |

* *Represents collateral on securities loaned.*

# Statement of Operations

for the year ended December 31, 2010

| **Investment Income** | | |
|---|---|---|
| Income: | | |
| Dividends (net of foreign taxes withheld of $40,452) | $ | 5,902,166 |
| Income distributions — Central Cash Management Fund | | 15,586 |
| Securities lending income, including income from Daily Assets Fund Institutional, net of borrower rebates | | 32,223 |
| Total income | | 5,949,975 |
| Expenses: | | |
| Management fee | | 1,313,548 |
| Administration fee | | 202,084 |
| Services to shareholders | | 5,403 |
| Distribution service fee (Class B) | | 2,177 |
| Record keeping fees (Class B) | | 316 |
| Custodian fee | | 11,677 |
| Professional fees | | 62,232 |
| Trustees' fees and expenses | | 8,477 |
| Reports to shareholders | | 39,446 |
| Other | | 5,790 |
| Total expenses | | 1,651,150 |
| **Net investment income (loss)** | | **4,298,825** |
| **Realized and Unrealized Gain (Loss)** | | |
| Net realized gain (loss) from: | | |
| Investments | | 7,964,499 |
| Foreign currency | | 1,697 |
| Payment by affiliate (see Note F) | | 62,550 |
| | | 8,028,746 |
| Change in net unrealized appreciation (depreciation) on: | | |
| Investments | | 7,886,334 |
| Foreign currency | | 3,358 |
| | | 7,889,692 |
| **Net gain (loss)** | | **15,918,438** |
| **Net increase (decrease) in net assets resulting from operations** | **$** | **20,217,263** |

*The accompanying notes are an integral part of the financial statements.*

# Statement of Changes in Net Assets

| Increase (Decrease) in Net Assets | Years Ended December 31, 2010 | 2009 |
|---|---|---|
| Operations: | | |
| Net investment income (loss) | $ 4,298,825 | $ 3,970,664 |
| Net realized gain (loss) | 8,028,746 | (2,868,405) |
| Change in net unrealized appreciation (depreciation) | 7,889,692 | 44,336,276 |
| Net increase (decrease) in net assets resulting from operations | 20,217,263 | 45,438,535 |
| Distributions to shareholders from: | | |
| Net investment income: | | |
| Class A | (4,108,146) | (2,847,989) |
| Class B | (14,019) | (9,025) |
| Total distributions | $ (4,122,165) | $ (2,857,014) |
| Fund share transactions: | | |
| **Class A** | | |
| Proceeds from shares sold | 8,671,405 | 5,193,145 |
| Net assets acquired in tax-free reorganization | — | 107,453,089 |
| Reinvestment of distributions | 4,108,146 | 2,847,989 |
| Payments for shares redeemed | (36,788,065) | (62,359,106) |
| Net increase (decrease) in net assets from Class A share transactions | (24,008,514) | 53,135,117 |
| **Class B** | | |
| Proceeds from shares sold | 506,629 | 313,837 |
| Net assets acquired in tax-free reorganization | — | 202,242 |
| Reinvestment of distributions | 14,019 | 9,025 |
| Payments for shares redeemed | (88,091) | (238,487) |
| Net increase (decrease) in net assets from Class B share transactions | 432,557 | 286,617 |
| **Increase (decrease) in net assets** | (7,480,859) | 96,003,255 |
| Net assets at beginning of period | 214,239,599 | 118,236,344 |
| Net assets at end of period (including undistributed net investment income of $4,084,211 and $3,905,854, respectively) | **$ 206,758,740** | **$ 214,239,599** |

| Other Information | | |
|---|---|---|
| **Class A** | | |
| Shares outstanding at beginning of period | 19,667,770 | 13,220,277 |
| Shares sold | 778,508 | 540,244 |
| Shares issued in tax-free reorganization | — | 12,224,432 |
| Shares issued to shareholders in reinvestment of distributions | 366,145 | 355,554 |
| Shares redeemed | (3,395,996) | (6,672,737) |
| Net increase (decrease) in Class A shares | (2,251,343) | 6,447,493 |
| Shares outstanding at end of period | **17,416,427** | **19,667,770** |
| **Class B** | | |
| Shares outstanding at beginning of period | 66,594 | 32,776 |
| Shares sold | 45,434 | 32,526 |
| Shares issued in tax-free reorganization | — | 22,957 |
| Shares issued to shareholders in reinvestment of distributions | 1,246 | 1,124 |
| Shares redeemed | (8,102) | (22,789) |
| Net increase (decrease) in Class B shares | 38,578 | 33,818 |
| Shares outstanding at end of period | **105,172** | **66,594** |

*The accompanying notes are an integral part of the financial statements.*

# Financial Highlights

## Class A

| Years Ended December 31, | 2010 | 2009 | 2008 | 2007 | 2006 |
|---|---|---|---|---|---|
| **Selected Per Share Data** | | | | | |
| **Net asset value, beginning of period** | **$10.86** | **$ 8.92** | **$19.21** | **$17.96** | **$15.81** |
| *Income (loss) from investment operations:* | | | | | |
| Net investment income (loss)[a] | .23 | .21 | .21 | .26 | .29[c] |
| Net realized and unrealized gain (loss) | .93 | 1.97 | (5.68) | 1.98 | 2.12 |
| **Total from investment operations** | 1.16 | 2.18 | (5.47) | 2.24 | 2.41 |
| *Less distributions from:* | | | | | |
| Net investment income | (.22) | (.24) | (.34) | (.32) | (.26) |
| Net realized gains | — | — | (4.48) | (.67) | — |
| **Total distributions** | (.22) | (.24) | (4.82) | (.99) | (.26) |
| **Net asset value, end of period** | **$11.80** | **$10.86** | **$ 8.92** | **$19.21** | **$17.96** |
| Total Return (%) | 10.77 | 25.37 | (36.40)[b] | 13.15[b,d] | 15.41[c] |
| **Ratios to Average Net Assets and Supplemental Data** | | | | | |
| Net assets, end of period ($ millions) | 206 | 214 | 118 | 229 | 275 |
| Ratio of expenses before expense reductions (%) | .82 | .76 | .87 | .83 | .83 |
| Ratio of expenses after expense reductions (%) | .82 | .76 | .86 | .82 | .83 |
| Ratio of net investment income (loss) (%) | 2.13 | 2.22 | 1.59 | 1.43 | 1.73[c] |
| Portfolio turnover rate (%) | 32 | 76 | 97 | 103 | 76 |

[a] *Based on average shares outstanding during the period.*

[b] *Total return would have been lower had certain expenses not been reduced.*

[c] *Includes non-recurring income from the Advisor recorded as a result of an administrative proceeding regarding disclosure of brokerage allocation practices in connection with sales of DWS Funds. The non-recurring income resulted in an increase in net investment income of $0.008 per share and an increase in the ratio of net investment income of 0.04%. Excluding this non-recurring income, total return would have been 0.04% lower.*

[d] *Includes a reimbursement from the Advisor to reimburse the effect of losses incurred as the result of certain operation errors during the period. Excluding this reimbursement, total return would have been 0.04% lower.*

## Class B

| Years Ended December 31, | 2010 | 2009 | 2008 | 2007 | 2006 |
|---|---|---|---|---|---|
| **Selected Per Share Data** | | | | | |
| **Net asset value, beginning of period** | **$10.86** | **$ 8.92** | **$19.20** | **$17.94** | **$15.79** |
| *Income (loss) from investment operations:* | | | | | |
| Net investment income (loss)[a] | .20 | .19 | .12 | .19 | .23[c] |
| Net realized and unrealized gain (loss) | .93 | 1.96 | (5.64) | 1.99 | 2.11 |
| **Total from investment operations** | 1.13 | 2.15 | (5.52) | 2.18 | 2.34 |
| *Less distributions from:* | | | | | |
| Net investment income | (.18) | (.21) | (.28) | (.25) | (.19) |
| Net realized gains | — | — | (4.48) | (.67) | — |
| **Total distributions** | (.18) | (.21) | (4.76) | (.92) | (.19) |
| **Net asset value, end of period** | **$11.81** | **$10.86** | **$ 8.92** | **$19.20** | **$17.94** |
| Total Return (%) | 10.53 | 24.86 | (36.64)[b] | 12.77[b,d] | 14.96[c] |
| **Ratios to Average Net Assets and Supplemental Data** | | | | | |
| Net assets, end of period ($ millions) | 1 | 1 | .29 | 8 | 40 |
| Ratio of expenses before expense reductions (%) | 1.11 | 1.06 | 1.28 | 1.21 | 1.21 |
| Ratio of expenses after expense reductions (%) | 1.11 | 1.06 | 1.26 | 1.20 | 1.21 |
| Ratio of net investment income (loss) (%) | 1.84 | 1.92 | 1.20 | 1.06 | 1.35[c] |
| Portfolio turnover rate (%) | 32 | 76 | 97 | 103 | 76 |

[a] *Based on average shares outstanding during the period.*

[b] *Total return would have been lower had certain expenses not been reduced.*

[c] *Includes non-recurring income from the Advisor recorded as a result of an administrative proceeding regarding disclosure of brokerage allocation practices in connection with sales of DWS Funds. The non-recurring income resulted in an increase in net investment income of $0.008 per share and an increase in the ratio of net investment income of 0.04%. Excluding this non-recurring income, total return would have been 0.04% lower.*

[d] *Includes a reimbursement from the Advisor to reimburse the effect of losses incurred as the result of certain operation errors during the period. Excluding this reimbursement, total return would have been 0.04% lower.*

# Notes to Financial Statements

## A. Organization and Significant Accounting Policies

DWS Variable Series II (the "Trust") is registered under the Investment Company Act of 1940, as amended (the "1940 Act"), as an open-end management investment company organized as a Massachusetts business trust. The Trust offers seventeen funds (hereinafter referred to individually as "Fund" or collectively as "Funds"). The Fund is classified as a diversified open-end management investment company.

**Multiple Classes of Shares of Beneficial Interest.** Certain Funds of the Trust offer two classes of shares (Class A shares and Class B shares). Sales of Class B shares are subject to record keeping fees up to 0.15% and Rule 12b-1 fees under the 1940 Act equal to an annual rate of 0.25%, of the average daily net assets of the Class B shares of the applicable Fund. Class A shares are not subject to such fees.

Investment income, realized and unrealized gains and losses, and certain fund-level expenses and expense reductions, if any, are borne pro rata on the basis of relative net assets by the holders of all classes of shares except that each class bears certain expenses unique to that class (including the applicable Rule 12b-1 fee and record keeping fees). Differences in class-level expenses may result in payment of different per share dividends by class. All shares have equal rights with respect to voting subject to class-specific arrangements.

The Trust's financial statements are prepared in accordance with accounting principles generally accepted in the United States of America which require the use of management estimates. Actual results could differ from those estimates. The policies described below are followed consistently by the Trust in the preparation of its financial statements.

**Security Valuation.** Investments are stated at value determined as of the close of regular trading on the New York Stock Exchange on each day the exchange is open for trading.

Various inputs are used in determining the value of the Fund's investments. These inputs are summarized in three broad levels. Level 1 includes quoted prices in active markets for identical securities. Level 2 includes other significant observable inputs (including quoted prices for similar securities, interest rates, prepayment speeds, and credit risk). Level 3 includes significant unobservable inputs (including the Fund's own assumptions in determining the fair value of investments). The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities.

Equity securities are valued at the most recent sale price or official closing price reported on the exchange (US or foreign) or over-the-counter market on which they trade and are categorized as Level 1 securities. Securities for which no sales are reported are valued at the calculated mean between the most recent bid and asked quotations on the relevant market or, if a mean cannot be determined, at the most recent bid quotation.

Money market instruments purchased with an original or remaining maturity of sixty days or less, maturing at par, are valued at amortized cost, which approximates value, and are categorized as Level 2. Investments in open-end investment companies are valued at their net asset value each business day and are categorized as Level 1.

Securities and other assets for which market quotations are not readily available or for which the above valuation procedures are deemed not to reflect fair value are valued in a manner that is intended to reflect their fair value as determined in accordance with procedures approved by the Board and are generally categorized as Level 3. In accordance with the Fund's valuation procedures, factors used in determining value may include, but are not limited to, the type of the security; the size of the holding; the initial cost of the security; the existence of any contractual restrictions on the security's disposition; the price and extent of public trading in similar securities of the issuer or of comparable companies; quotations or evaluated prices from broker-dealers and/or pricing services; information obtained from the issuer, analysts, and/or the appropriate stock exchange (for exchange-traded securities); an analysis of the company's or issuer's financial statements; an evaluation of the forces that influence the issuer and the market(s) in which the security is purchased and sold and with respect to debt securities; the maturity, coupon, creditworthiness, currency denomination and the movement of the market in which the security is normally traded. The value determined under these procedures may differ from published values for the same securities.

Disclosure about the classification of fair value measurements is included in a table following the Fund's Investment Portfolio.

**Foreign Currency Translations.** The books and records of the Trust are maintained in US dollars. Investment securities and other assets and liabilities denominated in a foreign currency are translated into US dollars at the prevailing exchange rates at period end. Purchases and sales of investment securities, income and expenses are translated into US dollars at the prevailing exchange rates on the respective dates of the transactions.

Net realized and unrealized gains and losses on foreign currency transactions represent net gains and losses between trade and settlement dates on securities transactions, the disposition of forward foreign currency exchange contracts and foreign currencies, and the difference between the amount of net investment income accrued and the US dollar amount actually received. That portion of both realized and unrealized gains and losses on investments that results from fluctuations in foreign currency exchange rates is not separately disclosed but is included with net realized and unrealized gain/appreciation and loss/depreciation on investments.

**Securities Lending.** The Fund lends securities to certain financial institutions. The Fund retains beneficial ownership of the securities it has loaned and continues to receive interest and dividends paid by the issuer of securities and to participate in any changes in their market value. The Fund requires the borrowers of the securities to maintain collateral with the Fund consisting of either cash or liquid, unencumbered assets having a value at least equal to the value of the securities loaned. When the collateral falls below specified amounts, the lending agent will use its best effort to obtain additional collateral on the next business day to meet required amounts under the security lending agreement. The Fund may invest the cash collateral into a joint trading account in an affiliated money market fund pursuant to Exemptive Orders issued by the SEC. The Fund receives compensation for lending its securities either in the form of fees or by earning interest on invested cash collateral net of borrower rebates and fees paid to a lending agent. Either the Fund or the borrower may terminate the loan. There may be risks of delay and costs in recovery of securities or even loss of rights in the collateral should the borrower of the securities fail financially. The Fund is also subject to all investment risks associated with the reinvestment of any cash collateral received, including, but not limited to, interest rate, credit and liquidity risk associated with such investments.

**Taxes.** The Fund's policy is to comply with the requirements of the Internal Revenue Code, as amended, which are applicable to regulated investment companies and to distribute all of its taxable income to its shareholders.

At December 31, 2010, the Fund had an approximate net tax basis capital loss carryforward which may be applied against any realized net taxable capital gains of each succeeding year until fully utilized or until the following expiration dates, whichever occurs first:

| Fund | Capital Loss Carryforward ($) | Expiration Date | Capital Loss Carryforward Utilized ($) |
|---|---|---|---|
| DWS Large Cap Value VIP | 29,003,000 | 12/31/2016 | 7,651,000 |
| | 12,084,000 | 12/31/2017 | |

In addition, included in the Fund's net tax basis capital loss carryforward of approximately $41,087,000 is $19,469,000 inherited from its merger with DWS Davis Venture Value VIP in fiscal year 2009, which may be applied against any realized net taxable capital gains of each succeeding year until fully utilized or until the above expiration dates, whichever occurs first, subject to certain limitations under Sections 381–384 of the Internal Revenue Code.

The Fund has reviewed the tax positions for the open tax years as of December 31, 2010 and has determined that no provision for income tax is required in the Fund's financial statements. The Fund's federal tax returns for the prior three fiscal years remain open subject to examination by the Internal Revenue Service.

**Distribution of Income and Gains.** Distributions of net investment income of the Fund, if any, are made annually. Net realized gains from investment transactions, in excess of available capital loss carryforwards, would be taxable to the Fund if not distributed and, therefore, will be distributed to shareholders at least annually. The Fund may also make additional distributions for tax purposes if necessary.

The timing and characterization of certain income and capital gains distributions are determined annually in accordance with federal tax regulations which may differ from accounting principles generally accepted in the United States of America. These differences primarily relate to certain securities sold at a loss. As a result, net investment income (loss) and net realized gain (loss) on investment transactions for a reporting period may differ significantly from distributions during such period. Accordingly, the Fund may periodically make reclassifications among certain of its capital accounts without impacting the net asset value of the Fund.

At December 31, 2010, the Fund's components of distributable earnings on a tax basis were as follows:

| Fund | Undistributed Ordinary Income ($)* | Capital Loss Carryforwards ($) | Unrealized Appreciation (Depreciation) on Investments ($) |
|---|---|---|---|
| DWS Large Cap Value VIP | 4,084,211 | (41,087,000) | 36,866,114 |

In addition, the tax character of distributions paid by the Fund is summarized as follows:

| Fund | Distributions from Ordinary Income ($)* Years Ended December 31, 2010 | 2009 |
|---|---|---|
| DWS Large Cap Value VIP | 4,122,165 | 2,857,014 |

* *For tax purposes, short-term capital gain distributions are considered ordinary income distributions.*

**Expenses.** Expenses of the Trust arising in connection with a specific fund are allocated to that fund. Other Trust expenses which cannot be directly attributed to a fund are apportioned among the funds in the Trust.

**Contingencies.** In the normal course of business, the Fund may enter into contracts with service providers that contain general indemnification clauses. The Fund's maximum exposure under these arrangements is unknown as this would involve future claims that may be made against the Fund that have not yet been made. However, based on experience, the Fund expects the risk of loss to be remote.

**Other.** Investment transactions are accounted for on a trade date plus one basis for daily net asset value calculations. However, for financial reporting purposes, investment transactions are reported on trade date. Interest income is recorded on the accrual basis. Dividend income is recorded on the ex-dividend date net of foreign withholding taxes. Realized gains and losses from investment transactions are recorded on an identified cost basis.

## B. Purchases and Sales of Securities

During the year ended December 31, 2010, purchases and sales of investment transactions (excluding short-term investments) were as follows:

| Fund | Purchases ($) | Sales ($) |
|---|---|---|
| DWS Large Cap Value VIP | 61,553,310 | 87,416,345 |

## C. Related Parties

**Management Agreement.** Under the Investment Management Agreement with Deutsche Investment Management Americas Inc. ("DIMA" or the "Advisor"), an indirect, wholly owned subsidiary of Deutsche Bank AG, the Advisor directs the investments of the Fund in accordance with its investment objectives, policies and restrictions. The Advisor determines the securities, instruments and other contracts relating to investments to be purchased, sold or entered into by the Fund or delegates such responsibility to the Fund's subadvisor.

Deutsche Asset Management International GmbH ("DeAMi") serves as subadvisor to the Fund. DeAMi is paid by the Advisor for its services.

Under the Investment Management Agreement with the Advisor, the fee is equivalent to the annual rates shown below of the Fund's average daily net assets, computed and accrued daily and payable monthly:

| Fund | Annual Management Fee Rate |
|---|---|
| DWS Large Cap Value VIP | |
| $0–$250 million | .650% |
| next $750 million | .625% |
| next $1.5 billion | .600% |
| next $2.5 billion | .575% |
| next $2.5 billion | .550% |
| next $2.5 billion | .525% |
| next $2.5 billion | .500% |
| over $12.5 billion | .475% |

For the period from January 1, 2010 through September 30, 2010, the Advisor had contractually agreed to waive its fee and/or reimburse certain operating expenses to the extent necessary to maintain the operating expenses (excluding certain expenses such as extraordinary expenses, taxes, brokerage and interest expense) of each class as follows:

| Fund | Annual Rate |
|---|---|
| DWS Large Cap Value VIP | |
| Class A | .88% |
| Class B | 1.28% |

Accordingly, for the year ended December 31, 2010, the total management fee and effective management fee rate were as follows:

| Fund | Total Aggregated ($) | Annual Effective Rate |
|---|---|---|
| DWS Large Cap Value VIP | 1,313,548 | .65% |

**Administration Fee.** Pursuant to an Administrative Services Agreement, DIMA provides most administrative services to the Fund. For all services provided under the Administrative Services Agreement, the Fund pays DIMA an annual fee ("Administration Fee") of 0.10% of the Fund's average daily net assets, computed and accrued daily and payable monthly. For the year ended December 31, 2010, the Administration Fee was as follows:

| Fund | Total Aggregated ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS Large Cap Value VIP | 202,084 | 17,334 |

**Service Provider Fees.** DWS Investments Service Company ("DISC"), an affiliate of the Advisor, is the transfer agent, dividend-paying agent and shareholder service agent for the Fund. Pursuant to a sub-transfer agency agreement between DISC and DST Systems, Inc. ("DST"), DISC has delegated certain transfer agent, dividend-paying agent and shareholder service agent functions to DST. DISC compensates DST out of the shareholder servicing fee it receives from the Fund. For the year ended December 31, 2010, the amounts charged to the Fund by DISC were as follows:

| Fund | Total Aggregated ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS Large Cap Value VIP Class A | 279 | 71 |
| DWS Large Cap Value VIP Class B | 47 | 12 |

**Distribution Service Agreement**. Under the Fund's Class B 12b-1 plans, DWS Investments Distributors, Inc. ("DIDI") received a fee ("Distribution Service Fee") of 0.25% of average daily net assets of Class B shares. For the year ended December 31, 2010, the Distribution Service Fee was as follows:

| Fund | Total Aggregated ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS Large Cap Value VIP | 2,177 | 235 |

**Typesetting and Filing Service Fees.** Under an agreement with DIMA, DIMA is compensated for providing typesetting and certain regulatory filing services to the Fund. For the year ended December 31, 2010, the amount charged to the Fund by DIMA included in the Statement of Operations under "reports to shareholders" was as follows:

| Fund | Amount ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS Large Cap Value VIP | 11,866 | 2,924 |

**Trustees' Fees and Expenses.** The Fund paid each Trustee not affiliated with the Advisor retainer fees plus specified amounts for various committee services and for the Board Chairperson.

**Affiliated Cash Management Vehicles.** The Fund may invest uninvested cash balances in Central Cash Management Fund, which is managed by the Advisor. The Fund indirectly bears their proportionate share of the expenses of the underlying money market funds. Central Cash Management Fund does not pay the Advisor an investment management fee. Central Cash Management Fund seeks a high level of current income consistent with liquidity and the preservation of capital.

## D. Ownership of the Fund

At December 31, 2010, the beneficial ownership in the Fund was as follows:

**DWS Large Cap Value VIP:** Three Participating Insurance Companies were owners of record of 10% or more of the total outstanding Class A shares of the Fund, each owning 53%, 30% and 10%. Two Participating Insurance Companies were owners of record of 10% or more of the total outstanding Class B shares of the Fund, each owning 86% and 14%.

## E. Line of Credit

The Trust and other affiliated fund (the "Participants") share in a $450 million revolving credit facility provided by a syndication of banks. The Fund may borrow for temporary or emergency purposes, including the meeting of redemption requests that otherwise might require the untimely disposition of securities. The Participants are charged an annual commitment fee which is allocated based on net assets, among each of the Participants. Interest is calculated at a rate per annum equal to the sum of the Federal Funds Rate plus 1.25 percent plus if LIBOR exceeds the Federal Funds Rate the amount of such excess. The Fund may borrow up to a maximum of 33 percent of its net assets under the agreement.

## F. Payment by Affiliates

During the year ended December 31, 2010, the Advisor agreed to reimburse the Fund $62,550 for losses incurred on trades executed incorrectly. The amount of the reimbursement is 0.03% of the Fund's average net assets.

## G. Acquisition of Assets

On April 24, 2009, the Fund acquired all of the net assets of DWS Davis Venture Value VIP pursuant to a plan of reorganization approved by shareholders on November 21, 2008. The primary reason for the acquisition was to consolidate Funds managed by the Advisor with comparable investment objectives. The acquisition was accomplished by a tax-free exchange of 17,064,120 Class A shares and 32,154 Class B shares of DWS Davis Venture Value VIP for 12,224,432 Class A shares and 22,957 Class B shares of the Fund, respectively, outstanding on April 24, 2009. DWS Davis Venture Value VIP's net assets at that date, $107,655,331, including $5,676,099 of net unrealized appreciation, were combined with those of the Fund. The aggregate net assets of the Fund immediately before the acquisition were $106,678,067. The combined net assets of the Fund immediately following the acquisition were $214,333,398.

## H. Subsequent Event

On January 12, 2011, the Board of the following Acquired Fund approved, in principle, the merger of the Acquired Fund into the Acquiring Fund. Completion of the merger is subject to a number of conditions. The merger is expected to be completed on or about May 1, 2011.

| Acquired Fund | Acquiring Fund |
|---|---|
| DWS Variable Series II — DWS Strategic Value VIP | DWS Variable Series II — DWS Large Cap Value VIP |

# Report of Independent Registered Public Accounting Firm

**To the Board of Trustees and Shareholders of DWS Variable Series II:**

We have audited the accompanying statement of assets and liabilities of DWS Large Cap Value VIP, one of the funds constituting the DWS Variable Series II (the "Trust"), including the investment portfolio, as of December 31, 2010, and the related statement of operations, the statement of changes in net assets and the financial highlights for each of the periods indicated therein. These financial statements and financial highlights are the responsibility of the Trust's management. Our responsibility is to express an opinion on these financial statements and financial highlights based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements and financial highlights are free of material misstatement. We were not engaged to perform an audit of the Trust's internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Trust's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements and financial highlights, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our procedures included confirmation of securities owned as of December 31, 2010, by correspondence with the custodian and brokers or by other appropriate auditing procedures where replies from brokers were not received. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements and financial highlights referred to above present fairly, in all material respects, the financial position of the aforementioned fund of the DWS Variable Series II at December 31, 2010, the results of its operations, the changes in its net assets and the financial highlights for each of the periods indicated therein, in conformity with U.S. generally accepted accounting principles.

Ernst & Young LLP

Boston, Massachusetts
February 14, 2011

# Tax Information

**(Unaudited)**

For corporate shareholders, the following percentage of income dividends paid during the Fund's fiscal year ended December 31, 2010 qualified for the dividends received deduction:

| Fund | Dividends Received % |
|---|---|
| DWS Large Cap Value VIP | 100 |

Please consult a tax advisor if you have questions about federal or state income tax laws, or on how to prepare your tax returns. If you have specific questions about your account, please contact your insurance provider.

# Proxy Voting

The Trust's policies and procedures for voting proxies for portfolio securities and information about how the Trust voted proxies related to its portfolio securities during the 12-month period ended June 30 are available on our Web site — www.dws-investments.com (click on "proxy voting" at the bottom of the page) — or on the SEC's Web site — www.sec.gov. To obtain a written copy of the Trust's policies and procedures without charge, upon request, call us toll free at (800) 728-3337.

# Investment Management Agreement Approval

## DWS Large Cap Value VIP

The Board of Trustees, including the Independent Trustees, approved the renewal of your Fund's investment management agreement (the "Agreement") with Deutsche Investment Management Americas Inc. ("DWS") and sub-advisory agreement (the "Sub-Advisory Agreement" and together with the Agreement, the "Agreements") between DWS and Deutsche Asset Management International GmbH ("DeAMi"), an affiliate of DWS, in September 2010.

In terms of the process that the Board followed prior to approving the Agreements, shareholders should know that:

- In September 2010, all but one of the Fund's Trustees were independent of DWS and its affiliates.
- The Trustees meet frequently to discuss fund matters. Each year, the Trustees dedicate substantial time to contract review matters. Over the course of several months, the Board's Contract Committee, in coordination with the Board's Equity Oversight Committee, reviewed comprehensive materials received from DWS, independent third parties and independent counsel. These materials included an analysis of the Fund's performance, fees and expenses, and profitability compiled by the Fund's independent fee consultant. The Board also received extensive information throughout the year regarding performance of the Fund.
- The Independent Trustees regularly meet privately with their independent counsel to discuss contract review and other matters. In addition, the Independent Trustees were also advised by the Fund's independent fee consultant in the course of their review of the Fund's contractual arrangements and considered a comprehensive report prepared by the independent fee consultant in connection with their deliberations (the "IFC Report").
- In connection with reviewing the Agreements, the Board also reviewed the terms of the Fund's Rule 12b-1 plan, distribution agreement, administrative services agreement, transfer agency agreement and other material service agreements.
- Based on its evaluation of the information provided, the Contract Committee presented its findings and recommendations to the Independent Trustees as a group. The Independent Trustees reviewed the Contract Committee's findings and recommendations and presented their recommendations to the full Board.

In connection with the contract review process, the Contract Committee and the Board considered the factors discussed below, among others. The Board also considered that DWS and its predecessors have managed the Fund since its inception, and the Board believes that a long-term relationship with a capable, conscientious advisor is in the best interests of the Fund. The Board considered, generally, that shareholders chose to invest or remain invested in the Fund knowing that DWS managed the Fund, and that the Agreement was approved by the Fund's shareholders. DWS and DeAMi are part of Deutsche Bank, a major global banking institution that is engaged in a wide range of financial services. The Board believes that there are significant advantages to being part of a global asset management business that offers a wide range of investing expertise and resources, including hundreds of portfolio managers and analysts with research capabilities in many countries throughout the world.

While shareholders may focus primarily on fund performance and fees, the Fund's Board considers these and many other factors, including the quality and integrity of DWS's and DeAMi's personnel and such other issues as back-office operations, fund valuations, and compliance policies and procedures.

**Nature, Quality and Extent of Services.** The Board considered the terms of the Agreements, including the scope of advisory services provided under the Agreements. The Board noted that, under the Agreements, DWS and DeAMi provide portfolio management services to the Fund and that, pursuant to a separate administrative services agreement, DWS provides administrative services to the Fund. The Board considered the experience and skills of senior management and investment personnel, the resources made available to such personnel, the ability of DWS to attract and retain high-quality personnel, and the organizational depth and stability of DWS. The Board reviewed the Fund's performance over short-term and long-term periods and compared those returns to various agreed-upon performance measures, including market indices and a peer universe compiled by the independent fee consultant using information supplied by Lipper Inc. ("Lipper"). The Board also noted that it has put into place a process of identifying "Focus Funds" (e.g., funds performing poorly relative to their benchmark or a peer universe compiled by Lipper), and receives more frequent reporting and information from DWS regarding such funds, along with DWS's remedial plans to address underperformance. The Board believes this process is an effective manner of identifying and addressing underperforming funds. Based on the information provided, the Board noted that for the one-, three- and five-year periods ended December 31, 2009, the Fund's performance (Class A shares) was in the 2nd quartile, 1st quartile and 1st quartile, respectively, of the applicable Lipper universe (the 1st quartile being the best performers and the 4th quartile being the worst performers). The Board also observed that the Fund has outperformed its benchmark in the one-, three- and five-year periods ended December 31, 2009.

On the basis of this evaluation and the ongoing review of investment results by the Board, the Board concluded that the nature, quality and extent of services provided by DWS and DeAMi historically have been and continue to be satisfactory.

**Fees and Expenses.** The Board considered the Fund's investment management fee schedule, sub-advisory fee schedule, operating expenses, and total expense ratios, and comparative information provided by Lipper and the independent fee consultant regarding investment management fee rates paid to other investment advisors by similar funds (1st quartile being the most favorable and 4th quartile being the least favorable). With respect to management fees paid to other investment advisors by similar funds, the Board noted that the contractual fee rates paid by the Fund, which include the 0.10% fee paid to DWS under the Fund's administrative services agreement, were at the median (2nd quartile) of the applicable Lipper peer group (based on Lipper data provided as of December 31, 2009). With respect to the sub-advisory fee paid to DeAMi, the Board noted that the fee is paid by DWS out of its fee and not directly by the Fund. The Board noted that the Fund's Class A shares total (net) operating expenses were expected to be higher than the median (3rd quartile) of the applicable Lipper expense universe (based on Lipper data provided as of December 31, 2009, and analyzing Lipper expense universe Class A expenses less any applicable 12b-1 fees) ("Lipper Universe Expenses"). The Board also reviewed data comparing each share class's total (net) operating expenses to the applicable Lipper Universe Expenses. The Board considered the Fund's management fee rate as compared to fees charged by DWS and certain of its affiliates for comparable mutual funds and considered differences in fund and fee structures between the DWS Funds. The Board also considered how the Fund's total (net) operating expenses compared to the total (net) operating expenses of a more customized peer group selected by Lipper (based on such factors as asset size).

The information considered by the Board as part of its review of management fees included information regarding fees charged by DWS and its affiliates to similar institutional accounts and to similar funds offered primarily to European investors ("DWS Europe funds"), in each case as applicable. The Board observed that advisory fee rates for institutional accounts generally were lower than the management fees charged by similarly managed DWS US mutual funds ("DWS Funds"), but also took note of the differences in services provided to DWS Funds as compared to institutional accounts. In the case of DWS Europe funds, the Board observed that fee rates for DWS Europe funds generally were higher than for similarly managed DWS Funds, but noted that differences in the types of services provided to DWS Funds relative to DWS Europe funds made it difficult to compare such fees.

On the basis of the information provided, the Board concluded that management fees were reasonable and appropriate in light of the nature, quality and extent of services provided by DWS and DeAMi.

**Profitability.** The Board reviewed detailed information regarding revenues received by DWS under the Agreement. The Board considered the estimated costs and pre-tax profits realized by DWS from advising the DWS Funds, as well as estimates of the pre-tax profits attributable to managing the Fund in particular. The Board also received information regarding the estimated enterprise-wide profitability of DWS and its affiliates with respect to all fund services in totality and by fund. The Board reviewed DWS's methodology in allocating its costs to the management of the Fund. Based on the information provided, the Board concluded that the pre-tax profits realized by DWS in connection with the management of the Fund were not unreasonable. The Board also reviewed information regarding the profitability of certain similar investment management firms. The Board noted that while information regarding the profitability of such firms is limited (and in some cases is not necessarily prepared on a comparable basis), DWS and its affiliates' overall profitability with respect to the DWS fund complex (after taking into account distribution and other services provided to the funds by DWS and its affiliates) was lower than the overall profitability levels of many comparable firms for which such data was available.

**Economies of Scale.** The Board considered whether there are economies of scale with respect to the management of the Fund and whether the Fund benefits from any economies of scale. The Board noted that the Fund's management fee schedule includes fee breakpoints. The Board concluded that the Fund's fee schedule represents an appropriate sharing between the Fund and DWS of such economies of scale as may exist in the management of the Fund at current asset levels.

**Other Benefits to DWS and Its Affiliates.** The Board also considered the character and amount of other incidental benefits received by DWS and its affiliates, including any fees received by DWS for administrative services provided to the Fund and any fees received by an affiliate of DWS for distribution services. The Board also considered benefits to DWS related to brokerage and soft-dollar allocations, including allocating brokerage to pay for research generated by parties other than the executing broker dealers, which pertain primarily to funds investing in equity securities, along with the incidental public relations benefits to DWS related to DWS Funds

advertising and cross-selling opportunities among DWS products and services. The Board concluded that management fees were reasonable in light of these fallout benefits.

**Compliance.** The Board considered the significant attention and resources dedicated by DWS to documenting and enhancing its compliance processes in recent years. The Board noted in particular (i) the experience and seniority of both DWS's chief compliance officer and the Fund's chief compliance officer; (ii) the large number of DWS compliance personnel; and (iii) the substantial commitment of resources by DWS and its affiliates to compliance matters.

Based on all of the information considered and the conclusions reached, the Board unanimously (including the Independent Trustees) determined that the continuation of the Agreements is in the best interests of the Fund. In making this determination, the Board did not give particular weight to any single factor identified above. The Board considered these factors over the course of numerous meetings, certain of which were in executive session with only the Independent Trustees and their counsel present. It is possible that individual Trustees may have weighed these factors differently in reaching their individual decisions to approve the continuation of the Agreements.

# Summary of Management Fee Evaluation by Independent Fee Consultant

October 3, 2010

Pursuant to an Order entered into by Deutsche Investment Management Americas and affiliates (collectively, "DeAM") with the Attorney General of New York, I, Thomas H. Mack, have been appointed the Independent Fee Consultant for the DWS Funds (formerly the DWS Scudder Funds). My duties include preparing an annual written evaluation of the management fees DeAM charges the Funds, considering among other factors the management fees charged by other mutual fund companies for like services, management fees DeAM charges other clients for like services, DeAM's costs of supplying services under the management agreements and related profit margins, possible economies of scale if a Fund grows larger, and the nature and quality of DeAM's services, including fund performance. This report summarizes my evaluation for 2010, including my qualifications, the evaluation process for each of the DWS Funds, consideration of certain complex-level factors, and my conclusions. I served in substantially the same capacity in 2007, 2008, and 2009.

## Qualifications

For more than 35 years I have served in various professional capacities within the investment management business. I have held investment analysis and advisory positions, including securities analyst, portfolio strategist and director of investment policy with a large investment firm. I have also performed business management functions, including business development, financial management and marketing research and analysis.

Since 1991, I have been an independent consultant within the asset management industry. I have provided services to over 125 client organizations, including investment managers, mutual fund boards, product distributors and related organizations. Over the past ten years I have completed a number of assignments for mutual fund boards, specifically including assisting boards with management contract renewal.

I hold a Master of Business Administration degree, with highest honors, from Harvard University and Master of Science and Bachelor of Science (highest honors) degrees from the University of California at Berkeley. I am an independent director and audit committee financial expert for two closed-end mutual funds and have served in various leadership and financial oversight capacities with non-profit organizations.

## Evaluation of Fees for each DWS Fund

My work focused primarily on evaluating, fund-by-fund, the fees charged to each of the 118 publicly offered Fund portfolios in the DWS Fund family. For each Fund, I considered each of the key factors mentioned above, as well as any other relevant information. In doing so I worked closely with the Funds' Independent Directors in their annual contract renewal process, as well as in their approval of contracts for several new funds (documented separately).

In evaluating each Fund's fees, I reviewed comprehensive materials provided by or on behalf of DeAM, including expense information prepared by Lipper Analytical, comparative performance information, profitability data, manager histories, and other materials. I also accessed certain additional information from the Lipper and Morningstar databases and drew on my industry knowledge and experience.

To facilitate evaluating this considerable body of information, I prepared for each Fund a document summarizing the key data elements in each area as well as additional analytics discussed below. This made it possible to consider each key data element in the context of the others.

In the course of contract renewal, DeAM agreed to implement a number of fee and expense adjustments requested by the Independent Directors which will favorably impact future fees and expenses, and my evaluation includes the effects of these changes.

### Fees and Expenses Compared with Other Funds

The competitive fee and expense evaluation for each fund focused on two primary comparisons:

- The Fund's contractual management fee (the advisory fee plus the administration fee where applicable) compared with those of a group of typically 12–15 funds in the same Lipper investment category (e.g. Large Capitalization Growth) having similar distribution arrangements and being of similar size.
- The Fund's total expenses compared with a broader universe of funds from the same Lipper investment category and having similar distribution arrangements.

These two comparisons provide a view of not only the level of the fee compared with funds of similar scale but also the total expense the Fund bears for all the services it receives, in comparison with the investment choices available in the Fund's investment category and distribution channel. The principal figure-of-merit used in these comparisons was the subject Fund's percentile ranking against peers.

### DeAM's Fees for Similar Services to Others

DeAM provided management fee schedules for all of its US domiciled fund and non-fund investment management accounts in any of the investment categories where there is a DWS Fund. These similar products included the other DWS Funds, non-fund pooled accounts, institutional accounts and sub-advisory accounts. Using this information, I calculated for each Fund the fee that would be charged to each similar product, at the subject Fund's asset level.

Evaluating information regarding non-fund products is difficult because there are varying levels of services required for different types of accounts, with mutual funds generally requiring considerably more regulatory and administrative types of service as well as having more frequent cash flows than other types of accounts. Also, while mutual fund fees for similar fund products can be expected to be similar, there will be some differences due to different pricing conditions in different distribution channels (e.g. retail funds versus those used in variable insurance products), differences in underlying investment processes and other factors.

**Costs and Profit Margins**

DeAM provided a detailed profitability analysis for each Fund. After making some adjustments so that the presentation would be more comparable to the available industry figures, I reviewed profit margins from investment management alone, from investment management plus other fund services (excluding distribution) provided to the Funds by DeAM (principally shareholder services), and DeAM profits from all sources, including distribution. A later section comments on overall profitability.

**Economies of Scale**

Economies of scale — an expected decline in management cost per dollar of fund assets as fund assets grow — are very rarely quantified and documented because of inherent difficulties in collecting and analyzing relevant data. However, in virtually every investment category that I reviewed, larger funds tend to have lower fees and lower total expenses than smaller funds. To see how each DWS Fund compares with this industry observation, I reviewed:

The trend in Fund assets over the last five years and the accompanying trend in total expenses. This shows if the Fund has grown and, if so, whether total expense (management fees as well as other expenses) have declined as a percent of assets.

Whether the Fund has break-points in its management fee schedule, the extent of the fee reduction built into the schedule and the asset levels where the breaks take effect, and in the case of a sub-advised Fund how the Fund's break-points compare with those of the sub-advisory fee schedule.

How the Fund's contractual fee schedule compares with trends in the industry data. To accomplish this, I constructed a chart showing how actual latest-fiscal-year contractual fees of the Fund and of other similar funds relate to average fund assets, with the subject Fund's contractual fee schedule superimposed.

**Quality of Service — Performance**

The quality-of-service evaluation focused on investment performance, which is the principal result of the investment management service. Each Fund's performance was reviewed over the past 1, 3, 5 and 10 years, as applicable, and compared with that of other funds in the same investment category and with a suitable market index.

In addition, I calculated and reviewed risk-adjusted returns relative to an index of similar mutual funds' returns and a suitable market index. The risk-adjusted returns analysis provides a way of determining the extent to which the Fund's return comparisons are mainly the product of investment value-added (or lack thereof) or alternatively taking considerably more or less risk than is typical in its investment category.

I also received and considered the history of portfolio manager changes for each Fund, as this provided an important context for evaluating the performance results.

## Complex-Level Considerations

While this evaluation was conducted mainly at the individual fund level, there are some issues relating to the reasonableness of fees that can alternatively be considered across the whole fund complex:

I reviewed DeAM's profitability analysis for all DWS Funds, with a view toward determining if the allocation procedures used were reasonable and how profit levels compared with public data for other investment managers.

I considered whether DeAM and affiliates receive any significant ancillary or "fall-out" benefits that should be considered in interpreting the direct profitability results. These would be situations where serving as the investment manager of the Funds is beneficial to another part of the Deutsche Bank organization.

I considered how aggregated DWS Fund expenses had varied over the years, by asset class and in the context of trends in asset levels.

I reviewed the structure of the DeAM organization, trends in staffing levels, and information on compensation of investment management and other professionals compared with industry data.

## Findings

Based on the process and analysis discussed above, which included reviewing a wide range of information from management and external data sources and considering among other factors the fees DeAM charges other clients, the fees charged by other fund managers, DeAM's costs and profits associated with managing the Funds, economies of scale, possible fall-out benefits, and the nature and quality of services provided, in my opinion the management fees charged the DWS Funds are reasonable.

Thomas H. Mack

Thomas H. Mack

# Board Members and Officers

The following table presents certain information regarding the Board Members and Officers of the Trust as of December 31, 2010. Each Board Member's year of birth is set forth in parentheses after his or her name. Unless otherwise noted, (i) each Board Member has engaged in the principal occupation(s) noted in the table for at least the most recent five years, although not necessarily in the same capacity; and (ii) the address of each Independent Board Member is c/o Paul K. Freeman, Independent Chairman, DWS Funds, PO Box 101833, Denver, CO 80250-1833. Except as otherwise noted below, the term of office for each Board Member is until the election and qualification of a successor, or until such Board Member sooner dies, resigns, is removed or as otherwise provided in the governing documents of the fund. Because the fund does not hold an annual meeting of shareholders, each Board Member will hold office for an indeterminate period. The Board Members may also serve in similar capacities with other funds in the fund complex. The Length of Time Served represents the year in which the Board Member joined the board of one or more DWS funds now overseen by the Board.

### Independent Board Members

| Name, Year of Birth, Position with the Fund and Length of Time Served[1] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Paul K. Freeman (1950)<br>Chairperson since 2009<br>Board Member since 1993 | Consultant, World Bank/Inter-American Development Bank; Executive and Governing Council of the Independent Directors Council (education committees); formerly, Project Leader, International Institute for Applied Systems Analysis (1998–2001); Chief Executive Officer, The Eric Group, Inc. (environmental insurance) (1986–1998) | 122 |
| John W. Ballantine (1946)<br>Board Member since 1999 | Retired; formerly, Executive Vice President and Chief Risk Management Officer, First Chicago NBD Corporation/The First National Bank of Chicago (1996–1998); Executive Vice President and Head of International Banking (1995–1996). Directorships: Healthways, Inc. (provider of disease and care management services); Portland General Electric (utility company); Stockwell Capital Investments PLC (private equity). Former Directorships: First Oak Brook Bancshares, Inc. and Oak Brook Bank; Prisma Energy International | 122 |
| Henry P. Becton, Jr. (1943)<br>Board Member since 1990 | Vice Chair and former President, WGBH Educational Foundation. Directorships: Association of Public Television Stations; Lead Director, Becton Dickinson and Company[3] (medical technology company); Lead Director, Belo Corporation[3] (media company); Public Radio International; Public Radio Exchange (PRX); The PBS Foundation. Former Directorships: Boston Museum of Science; American Public Television; Concord Academy; New England Aquarium; Mass. Corporation for Educational Telecommunications; Committee for Economic Development; Public Broadcasting Service | 122 |
| Dawn-Marie Driscoll (1946)<br>Board Member since 1987 | President, Driscoll Associates (consulting firm); Executive Fellow, Center for Business Ethics, Bentley University; formerly, Partner, Palmer & Dodge (1988–1990); Vice President of Corporate Affairs and General Counsel, Filene's (1978–1988). Directorships: Trustee of 22 open-end mutual funds managed by Sun Capital Advisers, Inc. (since 2007); Director of ICI Mutual Insurance Company (since 2007); Advisory Board, Center for Business Ethics, Bentley University; Trustee, Southwest Florida Community Foundation (charitable organization). Former Directorships: Investment Company Institute (audit, executive, nominating committees) and Independent Directors Council (governance, executive committees) | 122 |
| Keith R. Fox (1954)<br>Board Member since 1996 | Managing General Partner, Exeter Capital Partners (a series of private investment funds). Directorships: Progressive International Corporation (kitchen goods importer and distributor); BoxTop Media Inc. (advertising); The Kennel Shop (retailer); former Chairman, National Association of Small Business Investment Companies | 122 |
| Kenneth C. Froewiss (1945)<br>Board Member since 2001 | Adjunct Professor of Finance, NYU Stern School of Business (September 2009–present; Clinical Professor from 1997–September 2009); Member, Finance Committee, Association for Asian Studies (2002–present); Director, Mitsui Sumitomo Insurance Group (US) (2004–present); prior thereto, Managing Director, J.P. Morgan (investment banking firm) (until 1996) | 122 |
| Richard J. Herring (1946)<br>Board Member since 1990 | Jacob Safra Professor of International Banking and Professor, Finance Department, The Wharton School, University of Pennsylvania (since July 1972); Co-Director, Wharton Financial Institutions Center (since July 2000); Co-Chair, U.S. Shadow Financial Regulatory Committee; Executive Director, Financial Economists Roundtable; Director, Japan Equity Fund, Inc. (since September 2007), Thai Capital Fund, Inc. (since September 2007), Singapore Fund, Inc. (since September 2007); Independent Director of Barclays Bank Delaware (since September 2010). Formerly, Vice Dean and Director, Wharton Undergraduate Division (July 1995–June 2000); Director, Lauder Institute of International Management Studies (July 2000–June 2006) | 122 |
| William McClayton (1944)<br>Board Member since 2004+ | Private equity investor (since October 2009); previously, Managing Director, Diamond Management & Technology Consultants, Inc. (global consulting firm) (2001–2009); Directorship: Board of Managers, YMCA of Metropolitan Chicago; formerly: Senior Partner, Arthur Andersen LLP (accounting) (1966–2001); Trustee, Ravinia Festival | 122 |

| Name, Year of Birth, Position with the Fund and Length of Time Served[1] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Rebecca W. Rimel (1951)<br>Board Member since 1995 | President and Chief Executive Officer, The Pew Charitable Trusts (charitable organization) (1994 to present); Trustee, Thomas Jefferson Foundation (charitable organization) (1994 to present); Trustee, Executive Committee, Philadelphia Chamber of Commerce (2001–2007); Director, CardioNet, Inc.[2] (2009–present) (health care). Formerly, Executive Vice President, The Glenmede Trust Company (investment trust and wealth management) (1983–2004); Board Member, Investor Education (charitable organization) (2004–2005); Director, Viasys Health Care[2] (January 2007–June 2007); Trustee, Pro Publica (charitable organization) (2007–2010) | 122 |
| William N. Searcy, Jr. (1946)<br>Board Member since 1993 | Private investor since October 2003; Trustee of 22 open-end mutual funds managed by Sun Capital Advisers, Inc. (since October 1998). Formerly, Pension & Savings Trust Officer, Sprint Corporation[2] (telecommunications) (November 1989–September 2003) | 122 |
| Jean Gleason Stromberg (1943)<br>Board Member since 1997 | Retired. Formerly, Consultant (1997–2001); Director, Financial Markets US Government Accountability Office (1996–1997); Partner, Fulbright & Jaworski, L.L.P. (law firm) (1978–1996). Directorships: The William and Flora Hewlett Foundation. Former Directorships: Service Source, Inc., Mutual Fund Directors Forum (2002–2004), American Bar Retirement Association (funding vehicle for retirement plans) (1987–1990 and 1994–1996) | 122 |
| Robert H. Wadsworth (1940)<br>Board Member since 1999 | President, Robert H. Wadsworth & Associates, Inc. (consulting firm) (1983 to present); Director, The Phoenix Boys Choir Association | 125 |

## Interested Board Member and Officer[4]

| Name, Year of Birth, Position with the Trust/ Corporation and Length of Time Served[1,5] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Ingo Gefeke[7] (1967)<br>Board Member since 2010<br>Executive Vice President since 2010 | Managing Director[3], Deutsche Asset Management; Global Head of Distribution and Product Management, DWS Global Head of Trading and Securities Lending. Member of the Board of Directors of DWS Investment GmbH Frankfurt (since July 2009) and DWS Holding & Service GmbH Frankfurt (since January 2010); formerly, Global Chief Administrative Officer, Deutsche Asset Management (2004–2009); Global Chief Operating Officer, Global Transaction Banking, Deutsche Bank AG, New York (2001–2004); Chief Operating Officer, Global Banking Division Americas, Deutsche Bank AG, New York (1999–2001); Central Management, Global Banking Services, Deutsche Bank AG, Frankfurt (1998–1999); Relationship Management, Deutsche Bank AG, Tokyo, Japan (1997–1998) | 55 |

## Officers[4]

| Name, Year of Birth, Position with the Fund and Length of Time Served[5] | Principal Occupation(s) During Past 5 Years and Other Directorships Held |
|---|---|
| Michael G. Clark[6] (1965)<br>President, 2006–present | Managing Director[3], Deutsche Asset Management (2006–present); President of DWS family of funds; Director, ICI Mutual Insurance Company (since October 2007); formerly, Director of Fund Board Relations (2004–2006) and Director of Product Development (2000–2004), Merrill Lynch Investment Managers; Senior Vice President Operations, Merrill Lynch Asset Management (1999–2000) |
| John Millette[8] (1962)<br>Vice President and Secretary, 1999–present | Director[3], Deutsche Asset Management |
| Paul H. Schubert[6] (1963)<br>Chief Financial Officer, 2004–present<br>Treasurer, 2005–present | Managing Director[3], Deutsche Asset Management (since July 2004); formerly, Executive Director, Head of Mutual Fund Services and Treasurer for UBS Family of Funds (1998–2004); Vice President and Director of Mutual Fund Finance at UBS Global Asset Management (1994–1998) |
| Caroline Pearson[8] (1962)<br>Chief Legal Officer, April 2010–present | Managing Director[3], Deutsche Asset Management; formerly, Assistant Secretary for DWS family of funds (1997–2010) |
| Rita Rubin[9] (1970)<br>Assistant Secretary, 2009–present | Vice President and Counsel, Deutsche Asset Management (since October 2007); formerly, Vice President, Morgan Stanley Investment Management (2004–2007) |
| Paul Antosca[8] (1957)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management (since 2006); Vice President, The Manufacturers Life Insurance Company (U.S.A.) (1990–2006) |
| Jack Clark[8] (1967)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management (since 2007); formerly, Vice President, State Street Corporation (2002–2007) |

| Name, Year of Birth, Position with the Fund and Length of Time Served[5] | Principal Occupation(s) During Past 5 Years and Other Directorships Held |
|---|---|
| Diane Kenneally[8] (1966)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management |
| John Caruso[9] (1965)<br>Anti-Money Laundering Compliance Officer, 2010–present | Managing Director[3], Deutsche Asset Management |
| Robert Kloby[9] (1962)<br>Chief Compliance Officer, 2006–present | Managing Director[3], Deutsche Asset Management |

1 *The length of time served represents the year in which the Board Member joined the board of one or more DWS funds currently overseen by the Board.*

2 *A publicly held company with securities registered pursuant to Section 12 of the Securities Exchange Act of 1934.*

3 *Executive title, not a board directorship.*

4 *As a result of their respective positions held with the Advisor, these individuals are considered "interested persons" of the Advisor within the meaning of the 1940 Act. Interested persons receive no compensation from the fund.*

5 *The length of time served represents the year in which the officer was first elected in such capacity for one or more DWS funds.*

6 *Address: 100 Plaza One, Jersey City, NJ 07311.*

7 *Effective January 11, 2011, Mr. Gefeke, an interested Board Member and Executive Vice President, resigned from the fund's Board and as an officer.*

*The mailing address of Mr. Gefeke is 345 Park Avenue, New York, New York 10154. Mr. Gefeke was an interested Board Member of certain DWS funds by virtue of his positions with Deutsche Asset Management. As an interested person, Mr. Gefeke received no compensation from the fund.*

8 *Address: One Beacon Street, Boston, MA 02108.*

9 *Address: 60 Wall Street, New York, New York 10005.*

*The fund's Statement of Additional Information ("SAI") includes additional information about the Board Members. The SAI is available, without charge, upon request. If you would like to request a copy of the SAI, you may do so by calling the following toll-free number: (800) 728-3337.*

DWS Investments is part of Deutsche Bank's Asset Management division and, within the US, represents the retail asset management activities of Deutsche Bank AG, Deutsche Bank Trust Company Americas, Deutsche Investment Management Americas Inc. and DWS Trust Company.

The views expressed in this report reflect those of the portfolio managers only through the end of the period of the report as stated on the cover. The managers' views are subject to change at any time based on market and other conditions and should not be construed as a recommendation.

This information must be preceded or accompanied by a current prospectus.

Portfolio changes should not be considered recommendations for action by individual investors.

DWS Investments Distributors, Inc.
222 South Riverside Plaza
Chicago, IL 60606
(800) 621-1148

VS2LCV-2 (2/11)

DWS INVESTMENTS
Deutsche Bank Group

DECEMBER 31, 2010

# ANNUAL REPORT

## DWS VARIABLE SERIES II

## DWS Mid Cap Growth VIP

**This report must be preceded or accompanied by a prospectus. To obtain an additional prospectus or summary prospectus, if available, call (800) 728-3337 or your financial representative. We advise you to consider the Fund's objectives, risks, charges and expenses carefully before investing. The summary prospectus and prospectus contain this and other important information about the Fund. Please read the prospectus carefully before you invest.**

*Investments in variable insurance portfolios (VIPs) involve risk. Stocks may decline in value. Bond investments are subject to interest-rate and credit risks. When interest rates rise, bond prices generally fall. Credit risk refers to the ability of an issuer to make timely payments of principal and interest. Investing in derivatives entails special risks relating to liquidity, leverage and credit that may reduce returns and/or increased volatility. Investing in foreign securities, particularly those of emerging markets, presents certain risks, such as currency fluctuations, political and economic changes, and market risks. There are additional risks associated with investing in commodities, high-yield bonds, aggressive growth stocks, non-diversified/ concentrated funds and small- and mid-cap stocks which are more fully explained in the prospectuses. Please read the prospectus for more information.*

*DWS Investments is part of Deutsche Bank's Asset Management division and, within the US, represents the retail asset management activities of Deutsche Bank AG, Deutsche Bank Trust Company Americas, Deutsche Investment Management Americas Inc. and DWS Trust Company.*



DWS INVESTMENTS
Deutsche Bank Group

# Performance Summary

**December 31, 2010**

## DWS Mid Cap Growth VIP

**All performance shown is historical, assumes reinvestment of all dividend and capital gain distributions and does not guarantee future results. Investment return and principal value fluctuate with changing market conditions so that, when redeemed, shares may be worth more or less than their original cost. Current performance may be lower or higher than the performance data quoted. Please contact your participating insurance company for the Fund's most recent month-end performance. Performance doesn't reflect charges and fees ("contract charges") associated with the separate account that invests in the Fund or any variable life insurance policy or variable annuity contract for which the Fund is an investment option. These charges and fees will reduce returns.**

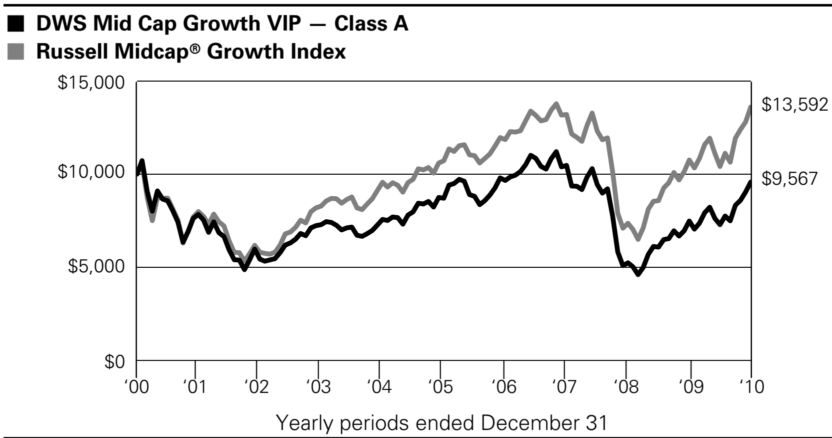
**The gross expense ratio of the Fund, as stated in the fee table of the prospectus dated May 1, 2010 is 1.17% for Class A shares and may differ from the expense ratio disclosed in the Financial Highlights table in this report.**

### Risk Considerations

Stocks of medium-sized companies involve greater risk than securities of larger, more-established companies. Stocks may decline in value. See the prospectus for details.

Fund returns shown for all periods reflect a fee waiver and/or expense reimbursement. Without this waiver/reimbursement, returns would have been lower.

### Growth of an Assumed $10,000 Investment in DWS Mid Cap Growth VIP




*The Russell Midcap® Growth Index is an unmanaged index that measures the performance of those Russell Midcap companies with higher price-to-book ratios and higher forecasted growth values. The stocks are also members of the Russell 1000® Growth Index.*

*Index returns assume reinvestment of dividends and, unlike fund returns, do not reflect any fees or expenses. It is not possible to invest directly into an index.*

### Comparative Results

| DWS Mid Cap Growth VIP | | 1-Year | 3-Year | 5-Year | 10-Year |
|---|---|---|---|---|---|
| **Class A** | Growth of $10,000 | $12,795 | $9,148 | $10,998 | $9,567 |
| | Average annual total return | 27.95% | –2.93% | 1.92% | –0.44% |
| Russell Midcap Growth Index | Growth of $10,000 | $12,638 | $10,294 | $12,692 | $13,592 |
| | Average annual total return | 26.38% | 0.97% | 4.88% | 3.12% |

*The growth of $10,000 is cumulative.*

# Information About Your Fund's Expenses

## DWS Mid Cap Growth VIP

As an investor of the Fund, you incur two types of costs: ongoing expenses and transaction costs. Ongoing expenses include management fees and other Fund expenses. Examples of transaction costs include contract charges, redemption fees and account maintenance fees, which are not shown in this section. The following tables are intended to help you understand your ongoing expenses (in dollars) of investing in the Fund and to help you compare these expenses with the ongoing expenses of investing in other mutual funds. In the most recent six-month period, the Fund limited these expenses; had it not done so, expenses would have been higher. The example in the table is based on an investment of $1,000 invested at the beginning of the six-month period and held for the entire period (July 1, 2010 to December 31, 2010).

The tables illustrate your Fund's expenses in two ways:

- **Actual Fund Return.** This helps you estimate the actual dollar amount of ongoing expenses (but not transaction costs) paid on a $1,000 investment in the Fund using the Fund's actual return during the period. To estimate the expenses you paid over the period, simply divide your account value by $1,000 (for example, an $8,600 account value divided by $1,000 = 8.6), then multiply the result by the number in the "Expenses Paid per $1,000" line under the share class you hold.
- **Hypothetical 5% Fund Return.** This helps you to compare your Fund's ongoing expenses (but not transaction costs) with those of other mutual funds using the Fund's actual expense ratio and a hypothetical rate of return of 5% per year before expenses. Examples using a 5% hypothetical Fund return may be found in the shareholder reports of other mutual funds. The hypothetical account values and expenses may not be used to estimate the actual ending account balance or expenses you paid for the period.

Please note that the expenses shown in these tables are meant to highlight your ongoing expenses only and do not reflect any transaction costs. The "Expenses Paid per $1,000" line of the tables is useful in comparing ongoing expenses only and will not help you determine the relative total expense of owning different funds. If these transaction costs had been included, your costs would have been higher.

**Expenses and Value of a $1,000 Investment** for the six months ended December 31, 2010

| **Actual Fund Return** | **Class A** |
|---|---|
| Beginning Account Value 7/1/10 | $1,000.00 |
| Ending Account Value 12/31/10 | $1,314.70 |
| Expenses Paid per $1,000* | $ 5.83 |

| **Hypothetical 5% Fund Return** | **Class A** |
|---|---|
| Beginning Account Value 7/1/10 | $1,000.00 |
| Ending Account Value 12/31/10 | $1,020.16 |
| Expenses Paid per $1,000* | $ 5.09 |

* *Expenses are equal to the Fund's annualized expense ratio, multiplied by the average account value over the period, multiplied by the number of days in the most recent six-month period, then divided by 365.*

| **Annualized Expense Ratio** | **Class A** |
|---|---|
| DWS Variable Series II — DWS Mid Cap Growth VIP | 1.00% |

For more information, please refer to the Fund's prospectus.

These tables do not reflect charges and fees ("contract charges") associated with the separate account that invests in the Fund of any variable life insurance policy or variable annuity contract for which the Fund is an investment option.

## DWS Mid Cap Growth VIP

The year 2010 began on an optimistic note with a few bright spots in the economy — improving consumer confidence, the government reports showing strong fourth-quarter 2009 gross domestic product (GDP) growth and a six-year high in manufacturing activity — partially offset by growing concerns about the health of the European financial system.[1] By May 2010, the US stock market had entered a period of significant volatility amid regulatory uncertainty (health care and financial reform) and fears of a possible double-dip recession. The market then staged a rebound during the last four months of the year amid increasing confidence that the US Federal Reserve Board's (the Fed's) second round of quantitative easing measures would support asset prices, along with evidence that the US economy was on a path to faster growth in 2011.

For the 12 months ended December 31, 2010, the Fund returned 27.95% (Class A shares, unadjusted for contract charges), compared with the 26.38% return of the Russell Midcap® Growth Index. These strong returns belie the elevated level of investor risk aversion that impacted the global equity markets during much of the summer months as high unemployment, European debt problems, a possible economic "hard landing" within China and some slippage for US economic indicators temporarily dampened enthusiasm for stocks.

The Fund's outperformance of the benchmark came primarily from favorable stock selection. During the period, stock selection was positive within the health care, information technology and consumer staples sectors. Other contributions to returns came from an overweight to energy and an underweight to telecom services.[2] Stock selection in energy and consumer discretionary detracted from performance. In addition, underweight positions in materials, information technology and consumer discretionary weighed on returns.

Joseph Axtell, CFA
Rafaelina M. Lee
*Portfolio Managers*

*The Russell Midcap Growth Index is an unmanaged index that measures the performance of those Russell Midcap companies with higher price-to-book ratios and higher forecasted growth values. The stocks are also members of the Russell 1000® Growth Index.*

*Index returns assume reinvestment of dividends and, unlike fund returns, do not reflect any fees or expenses. It is not possible to invest directly into an index.*

1 *Gross domestic product is the value of goods and services produced in an economy.*

2 *"Overweight" means the Fund holds a higher weighting in a given sector than the benchmark index. "Underweight" means the Fund holds a lower weighting.*

*Portfolio management market commentary is as of December 31, 2010, and may not come to pass. This information is subject to change at any time based on market and other conditions. Past performance does not guarantee future results. Current and future portfolio holdings are subject to risk.*

# Portfolio Summary

## DWS Mid Cap Growth VIP

| **Asset Allocation** (As a % of Investment Portfolio excluding Securities Lending Collateral) | **12/31/10** | **12/31/09** |
|---|---|---|
| Common Stocks | 96% | 98% |
| Cash Equivalents | 4% | 2% |
| | 100% | 100% |

| **Sector Diversification** (As a % of Common Stocks) | **12/31/10** | **12/31/09** |
|---|---|---|
| Information Technology | 21% | 22% |
| Consumer Discretionary | 19% | 18% |
| Industrials | 14% | 14% |
| Health Care | 14% | 12% |
| Energy | 12% | 12% |
| Financials | 8% | 9% |
| Materials | 6% | 8% |
| Consumer Staples | 4% | 3% |
| Telecommunication Services | 2% | 2% |
| | 100% | 100% |

*Asset allocation and sector diversification are subject to change.*

*For more complete details about the Fund's investment portfolio, see page 6.*

Following the Fund's fiscal first and third quarter-end, a complete portfolio holdings listing is filed with the SEC on Form N-Q. The form will be available on the SEC's Web site at www.sec.gov, and it also may be reviewed and copied at the SEC's Public Reference Room in Washington, D.C. Information on the operation of the SEC's Public Reference Room may be obtained by calling (800) SEC-0330. The Fund's portfolio holdings are also posted on www.dws-investments.com from time to time. Please see the Fund's current prospectus for more information.

# Investment Portfolio

December 31, 2010

## DWS Mid Cap Growth VIP

| | Shares | Value ($) |
|---|---|---|
| **Common Stocks 96.6%** | | |
| **Consumer Discretionary 18.1%** | | |
| **Auto Components 2.8%** | | |
| BorgWarner, Inc.* | 5,556 | 402,032 |
| Gentex Corp. | 11,572 | 342,068 |
| | | **744,100** |
| **Hotels Restaurants & Leisure 2.5%** | | |
| Darden Restaurants, Inc. | 8,015 | 372,217 |
| Panera Bread Co. "A"* (a) | 3,000 | 303,630 |
| | | **675,847** |
| **Household Durables 1.0%** | | |
| Jarden Corp. | 8,300 | **256,221** |
| **Internet & Catalog Retail 1.3%** | | |
| Priceline.com, Inc.* | 850 | **339,618** |
| **Specialty Retail 7.4%** | | |
| Advance Auto Parts, Inc. | 5,500 | 363,825 |
| Children's Place Retail Stores, Inc.* | 7,300 | 362,372 |
| Guess?, Inc. | 8,900 | 421,148 |
| Tiffany & Co. (a) | 6,600 | 410,982 |
| Urban Outfitters, Inc.* (a) | 11,500 | 411,815 |
| | | **1,970,142** |
| **Textiles, Apparel & Luxury Goods 3.1%** | | |
| Deckers Outdoor Corp.* | 6,654 | 530,590 |
| Hanesbrands, Inc.* | 11,286 | 286,664 |
| | | **817,254** |
| **Consumer Staples 3.7%** | | |
| **Food Products 1.2%** | | |
| Diamond Foods, Inc. (a) | 5,800 | **308,444** |
| **Household Products 1.0%** | | |
| Church & Dwight Co., Inc. | 3,962 | **273,457** |
| **Personal Products 1.5%** | | |
| Herbalife Ltd. | 6,053 | **413,844** |
| **Energy 11.1%** | | |
| **Energy Equipment & Services 6.7%** | | |
| Cameron International Corp.* | 3,713 | 188,360 |
| Complete Production Services, Inc.* | 9,387 | 277,386 |
| Core Laboratories NV (a) | 2,486 | 221,378 |
| Dresser-Rand Group, Inc.* | 5,050 | 215,080 |
| FMC Technologies, Inc.* | 4,880 | 433,881 |
| McDermott International, Inc.* | 14,000 | 289,660 |
| National Oilwell Varco, Inc. | 2,272 | 152,792 |
| | | **1,778,537** |
| **Oil, Gas & Consumable Fuels 4.4%** | | |
| Alpha Natural Resources, Inc.* | 3,776 | 226,673 |
| Concho Resources, Inc.* | 2,916 | 255,646 |
| Pioneer Natural Resources Co. | 2,080 | 180,586 |
| Ultra Petroleum Corp.* (a) | 4,830 | 230,729 |
| Whiting Petroleum Corp.* | 2,442 | 286,178 |
| | | **1,179,812** |
| **Financials 8.1%** | | |
| **Capital Markets 4.7%** | | |
| Affiliated Managers Group, Inc.* (a) | 1,800 | 178,596 |
| Invesco Ltd. | 5,700 | 137,142 |
| Jefferies Group, Inc. | 8,900 | 237,007 |
| Lazard Ltd. "A" | 4,854 | 191,684 |

| | Shares | Value ($) |
|---|---|---|
| Och-Ziff Capital Management Group "A" (Limited Partnership) | 18,720 | 291,658 |
| TD Ameritrade Holding Corp. (a) | 10,891 | 206,820 |
| | | **1,242,907** |
| **Commercial Banks 1.4%** | | |
| Huntington Bancshares, Inc. | 19,766 | 135,792 |
| Prosperity Bancshares, Inc. | 4,400 | 172,832 |
| Zions Bancorp. | 2,881 | 69,807 |
| | | **378,431** |
| **Diversified Financial Services 1.3%** | | |
| Portfolio Recovery Associates, Inc.* (a) | 4,800 | **360,960** |
| **Insurance 0.7%** | | |
| W.R. Berkley Corp. | 6,500 | **177,970** |
| **Health Care 13.5%** | | |
| **Biotechnology 2.7%** | | |
| Alexion Pharmaceuticals, Inc.* (a) | 2,483 | 200,005 |
| Human Genome Sciences, Inc.* (a) | 6,800 | 162,452 |
| Onyx Pharmaceuticals, Inc.* | 3,763 | 138,742 |
| Regeneron Pharmaceuticals, Inc.* | 6,300 | 206,829 |
| | | **708,028** |
| **Health Care Equipment & Supplies 1.9%** | | |
| Kinetic Concepts, Inc.* | 6,700 | 280,596 |
| Thoratec Corp.* | 7,800 | 220,896 |
| | | **501,492** |
| **Health Care Providers & Services 3.3%** | | |
| AmerisourceBergen Corp. | 8,900 | 303,668 |
| Fresenius Medical Care AG & Co. KGaA (ADR) | 5,230 | 301,719 |
| Laboratory Corp. of America Holdings* (a) | 3,200 | 281,344 |
| | | **886,731** |
| **Health Care Technology 1.7%** | | |
| Cerner Corp.* (a) | 1,599 | 151,489 |
| SXC Health Solutions Corp.* | 7,233 | 310,006 |
| | | **461,495** |
| **Life Sciences Tools & Services 2.4%** | | |
| ICON PLC (ADR)* | 5,824 | 127,546 |
| Life Technologies Corp.* | 5,500 | 305,250 |
| QIAGEN NV* (a) | 10,213 | 199,664 |
| | | **632,460** |
| **Pharmaceuticals 1.5%** | | |
| Questcor Pharmaceuticals, Inc.* | 27,486 | **404,869** |
| **Industrials 13.9%** | | |
| **Aerospace & Defense 1.3%** | | |
| BE Aerospace, Inc.* | 9,400 | **348,082** |
| **Commercial Services & Supplies 1.1%** | | |
| Stericycle, Inc.* (a) | 3,500 | **283,220** |
| **Construction & Engineering 0.4%** | | |
| Aecom Technology Corp.* | 3,712 | **103,825** |
| **Electrical Equipment 2.9%** | | |
| AMETEK, Inc. | 7,446 | 292,255 |
| Babcock & Wilcox Co.* | 4,950 | 126,671 |
| General Cable Corp.* | 10,200 | 357,918 |
| | | **776,844** |

*The accompanying notes are an integral part of the financial statements.*

| | Shares | Value ($) |
|---|---|---|
| **Machinery 4.6%** | | |
| Flowserve Corp. | 1,801 | 214,715 |
| Gardner Denver, Inc. | 4,560 | 313,819 |
| Joy Global, Inc. | 4,000 | 347,000 |
| Terex Corp.* (a) | 11,175 | 346,872 |
| | | **1,222,406** |
| **Professional Services 1.7%** | | |
| FTI Consulting, Inc.* (a) | 5,082 | 189,457 |
| Robert Half International, Inc. | 8,930 | 273,258 |
| | | **462,715** |
| **Road & Rail 1.9%** | | |
| Genesee & Wyoming, Inc. "A"* | 4,960 | 262,632 |
| Kansas City Southern* | 4,945 | 236,668 |
| | | **499,300** |
| **Information Technology 20.6%** | | |
| **Communications Equipment 2.5%** | | |
| F5 Networks, Inc.* | 2,484 | 323,317 |
| Harris Corp. (a) | 2,700 | 122,310 |
| Juniper Networks, Inc.* | 6,166 | 227,649 |
| | | **673,276** |
| **Computers & Peripherals 2.0%** | | |
| NetApp, Inc.* | 5,350 | 294,036 |
| SanDisk Corp.* | 4,728 | 235,738 |
| | | **529,774** |
| **Electronic Equipment, Instruments & Components 0.8%** | | |
| Itron, Inc.* | 3,850 | **213,482** |
| **Internet Software & Services 1.0%** | | |
| Equinix, Inc.* (a) | 3,356 | **272,709** |
| **IT Services 1.3%** | | |
| Cognizant Technology Solutions Corp. "A"* | 4,610 | **337,867** |
| **Semiconductors & Semiconductor Equipment 6.7%** | | |
| Analog Devices, Inc. | 3,500 | 131,845 |
| ARM Holdings PLC (ADR) | 11,965 | 248,274 |
| ASML Holding NV (NY Registered Shares) (a) | 3,669 | 140,669 |
| Broadcom Corp. "A" | 3,682 | 160,351 |
| Cavium Networks, Inc.* (a) | 6,741 | 254,001 |
| First Solar, Inc.* (a) | 1,679 | 218,505 |
| Marvell Technology Group Ltd.* | 13,728 | 254,654 |
| Netlogic Microsystems, Inc.* | 4,200 | 131,922 |
| Novellus Systems, Inc.* | 7,405 | 239,330 |
| | | **1,779,551** |
| **Software 6.3%** | | |
| BMC Software, Inc.* | 2,621 | 123,554 |
| Check Point Software Technologies Ltd.* | 2,905 | 134,385 |
| Concur Technologies, Inc.* | 5,913 | 307,062 |
| MICROS Systems, Inc.* | 2,868 | 125,791 |
| Red Hat, Inc.* | 6,789 | 309,918 |
| Rovi Corp.* (a) | 4,832 | 299,632 |
| Salesforce.com, Inc.* (a) | 2,705 | 357,060 |
| | | **1,657,402** |
| **Materials 5.4%** | | |
| **Chemicals 1.1%** | | |
| Scotts Miracle-Gro Co. "A" | 2,100 | 106,617 |
| Solutia, Inc.* | 7,452 | 171,992 |
| | | **278,609** |
| **Containers & Packaging 0.8%** | | |
| Crown Holdings, Inc.* | 6,589 | **219,941** |
| **Metals & Mining 2.6%** | | |
| Cliffs Natural Resources, Inc. | 3,000 | 234,030 |
| Kinross Gold Corp. | 10,400 | 197,184 |
| Thompson Creek Metals Co., Inc.* | 18,099 | 266,417 |
| | | **697,631** |
| **Paper & Forest Products 0.9%** | | |
| Schweitzer-Mauduit International, Inc. | 3,968 | **249,667** |
| **Telecommunication Services 2.2%** | | |
| **Wireless Telecommunication Services** | | |
| American Tower Corp. "A"* | 6,078 | 313,868 |
| MetroPCS Communications, Inc.* (a) | 21,176 | 267,453 |
| | | **581,321** |
| **Total Common Stocks** (Cost $17,324,405) | | **25,700,241** |

## Securities Lending Collateral 20.0%

| | Shares | Value ($) |
|---|---|---|
| Daily Assets Fund Institutional, 0.27% (b) (c) (Cost $5,310,295) | 5,310,295 | **5,310,295** |

## Cash Equivalents 3.9%

| | Shares | Value ($) |
|---|---|---|
| Central Cash Management Fund, 0.19% (b) (Cost $1,025,897) | 1,025,897 | **1,025,897** |

| | % of Net Assets | Value ($) |
|---|---|---|
| **Total Investment Portfolio** (Cost $23,660,597)† | 120.5 | **32,036,433** |
| **Other Assets and Liabilities, Net** | (20.5) | **(5,439,897)** |
| **Net Assets** | 100.0 | **26,596,536** |

* *Non-income producing security.*

† *The cost for federal income tax purposes was $23,757,711. At December 31, 2010, net unrealized appreciation for all securities based on tax cost was $8,278,722. This consisted of aggregate gross unrealized appreciation for all securities in which there was an excess of value over tax cost of $8,520,038 and aggregate gross unrealized depreciation for all securities in which there was an excess of tax cost over value of $241,316.*

(a) *All or a portion of these securities were on loan (see Notes to Financial Statements). The value of all securities loaned at December 31, 2010 amounted to $5,167,474, which is 19.4% of net assets.*

(b) *Affiliated fund managed by Deutsche Investment Management Americas Inc. The rate shown is the annualized seven-day yield at period end.*

(c) *Represents collateral held in connection with securities lending. Income earned by the Fund is net of borrower rebates.*

*ADR: American Depositary Receipt*

*The accompanying notes are an integral part of the financial statements.*

## Fair Value Measurements

*Various inputs are used in determining the value of the Fund's investments. These inputs are summarized in three broad levels. Level 1 includes quoted prices in active markets for identical securities. Level 2 includes other significant observable inputs (including quoted prices for similar securities, interest rates, prepayment speeds, and credit risk). Level 3 includes significant unobservable inputs (including the Fund's own assumptions in determining the fair value of investments). The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities.*

*The following is a summary of the inputs used as of December 31, 2010 in valuing the Fund's investments. For information on the Fund's policy regarding the valuation of investments, please refer to the Security Valuation section of Note A in the accompanying Notes to Financial Statements.*

| **Assets** | **Level 1** | **Level 2** | **Level 3** | **Total** |
|---|---|---|---|---|
| Common Stocks (d) | $ 25,700,241 | $ — | $ — | $ 25,700,241 |
| Short-Term Investments (d) | 6,336,192 | — | — | 6,336,192 |
| **Total** | **$ 32,036,433** | **$ —** | **$ —** | **$ 32,036,433** |

*There have been no significant transfers between Level 1 and Level 2 fair value measurements during the year ended December 31, 2010.*

(d) *See Investment Portfolio for additional detailed categorizations.*

*The accompanying notes are an integral part of the financial statements.*

# Statement of Assets and Liabilities

as of December 31, 2010

| | | |
|---|---|---|
| **Assets** | | |
| Investments: | | |
| Investments in unaffiliated securities, at value (cost $17,324,405) — including $5,167,474 of securities loaned | $ | 25,700,241 |
| Investment in Daily Assets Fund Institutional (cost $5,310,295)* | | 5,310,295 |
| Investment in Central Cash Management Fund (cost $1,025,897) | | 1,025,897 |
| Total investments, at value (cost $23,660,597) | | 32,036,433 |
| Dividends receivable | | 3,385 |
| Interest receivable | | 815 |
| Foreign taxes recoverable | | 319 |
| Other assets | | 124 |
| Total assets | | 32,041,076 |
| **Liabilities** | | |
| Payable upon return of securities loaned | | 5,310,295 |
| Payable for Fund shares redeemed | | 50,783 |
| Accrued management fee | | 20,245 |
| Other accrued expenses and payables | | 63,217 |
| Total liabilities | | 5,444,540 |
| **Net assets, at value** | **$** | **26,596,536** |
| **Net Assets Consist of** | | |
| Net unrealized appreciation (depreciation) on investments | | 8,375,836 |
| Accumulated net realized gain (loss) | | (25,844,555) |
| Paid-in capital | | 44,065,255 |
| **Net assets, at value** | **$** | **26,596,536** |
| **Class A** | | |
| **Net Asset Value,** offering and redemption price per share ($26,596,536 ÷ 2,135,742 outstanding shares of beneficial interest, no par value, unlimited number of shares authorized) | **$** | **12.45** |

* *Represents collateral on securities loaned.*

# Statement of Operations

for the year ended December 31, 2010

| | | |
|---|---|---|
| **Investment Income** | | |
| Dividends (net of foreign taxes withheld of $1,411) | $ | 141,436 |
| Income distributions — Central Cash Management Fund | | 1,047 |
| Securities lending income, including income from Daily Assets Fund Institutional, net of borrower rebates | | 8,700 |
| Total income | | 151,183 |
| Expenses: | | |
| Management fee | | 149,048 |
| Administration fee | | 22,413 |
| Services to shareholders | | 887 |
| Custodian fee | | 9,826 |
| Legal fees | | 9,140 |
| Audit and tax fees | | 46,898 |
| Trustees' fees and expenses | | 3,099 |
| Reports to shareholders | | 13,510 |
| Other | | 3,824 |
| Total expenses before expense reductions | | 258,645 |
| Expense reductions | | (24,596) |
| Total expenses after expense reductions | | 234,049 |
| **Net investment income (loss)** | | **(82,866)** |
| **Realized and Unrealized Gain (Loss)** | | |
| Net realized gain (loss) from investments | | 2,083,999 |
| Change in net unrealized appreciation (depreciation) on investments | | 3,665,748 |
| **Net gain (loss)** | | **5,749,747** |
| **Net increase (decrease) in net assets resulting from operations** | **$** | **5,666,881** |

*The accompanying notes are an integral part of the financial statements.*

# Statement of Changes in Net Assets

| | Years Ended December 31, | |
|---|---|---|
| **Increase (Decrease) in Net Assets** | **2010** | **2009** |
| Operations: | | |
| Net investment income (loss) | $ (82,866) | $ (40,620) |
| Net realized gain (loss) | 2,083,999 | (3,073,291) |
| Change in net unrealized appreciation (depreciation) | 3,665,748 | 10,072,701 |
| Net increase (decrease) in net assets resulting from operations | 5,666,881 | 6,958,790 |
| Fund share transactions: | | |
| **Class A** | | |
| Proceeds from shares sold | 3,568,315 | 2,976,222 |
| Payments for shares redeemed | (5,044,677) | (5,876,870) |
| Shares converted* | — | 17,354 |
| Net increase (decrease) in net assets from Class A share transactions | (1,476,362) | (2,883,294) |
| **Class B** | | |
| Payments for shares redeemed | — | (64) |
| Shares converted* | — | (17,354) |
| Net increase (decrease) in net assets from Class B share transactions | — | (17,418) |
| **Increase (decrease) in net assets** | 4,190,519 | 4,058,078 |
| Net assets at beginning of period | 22,406,017 | 18,347,939 |
| Net assets at end of period (including net investment income and accumulated net investment loss of $0 and $4,978, respectively) | **$ 26,596,536** | **$ 22,406,017** |

| **Other Information** | | |
|---|---|---|
| **Class A** | | |
| Shares outstanding at beginning of period | 2,302,964 | 2,694,618 |
| Shares sold | 322,729 | 374,687 |
| Shares redeemed | (489,951) | (769,440) |
| Shares converted* | — | 3,099 |
| Net increase (decrease) in Class A shares | (167,222) | (391,654) |
| Shares outstanding at end of period | **2,135,742** | **2,302,964** |
| **Class B** | | |
| Shares outstanding at beginning of period | — | 3,171 |
| Shares redeemed | — | (10) |
| Shares converted* | — | (3,161) |
| Net increase (decrease) in Class B shares | — | (3,171) |
| Shares outstanding at end of period | **—** | **—** |

* *On March 6, 2009, Class B shares converted into Class A shares.*

*The accompanying notes are an integral part of the financial statements.*

# Financial Highlights

## Class A

| Years Ended December 31, | 2010 | 2009 | 2008 | 2007 | 2006 |
|---|---|---|---|---|---|
| **Selected Per Share Data** | | | | | |
| **Net asset value, beginning of period** | **$ 9.73** | **$ 6.80** | **$13.61** | **$12.56** | **$11.32** |
| *Income (loss) from investment operations:* | | | | | |
| Net investment income (loss)[a] | (.04) | (.02) | (.02) | (.05) | (.06)[c] |
| Net realized and unrealized gain (loss) | 2.76 | 2.95 | (6.79) | 1.10 | 1.30 |
| **Total from investment operations** | 2.72 | 2.93 | (6.81) | 1.05 | 1.24 |
| **Net asset value, end of period** | **$12.45** | **$ 9.73** | **$ 6.80** | **$13.61** | **$12.56** |
| Total Return (%)[b] | 27.95 | 43.09 | (50.04) | 8.36 | 10.95[c] |
| **Ratios to Average Net Assets and Supplemental Data** | | | | | |
| Net assets, end of period ($ millions) | 27 | 22 | 18 | 51 | 53 |
| Ratio of expenses before expense reductions (%) | 1.15 | 1.17 | 1.17 | 1.05 | 1.03 |
| Ratio of expenses after expense reductions (%) | 1.04 | .92 | 1.02 | .90 | .93 |
| Ratio of net investment income (loss) (%) | (.37) | (.21) | (.19) | (.38) | (.51)[c] |
| Portfolio turnover rate (%) | 57 | 89 | 82 | 68 | 46 |

a *Based on average shares outstanding during the period.*

b *Total return would have been lower had certain expenses not been reduced.*

c *Includes non-recurring income from the Advisor recorded as a result of an administrative proceeding regarding disclosure of brokerage allocation practices in connection with sales of DWS Funds. The non-recurring income resulted in an increase in net investment income of $0.003 per share and an increase in the ratio of net investment income of 0.03%. Excluding this non-recurring income, total return would have been 0.03% lower.*

# Notes to Financial Statements

## A. Organization and Significant Accounting Policies

DWS Variable Series II (the "Trust") is registered under the Investment Company Act of 1940, as amended (the "1940 Act"), as an open-end management investment company organized as a Massachusetts business trust. The Trust offers seventeen funds (hereinafter referred to individually as "Fund" or collectively as "Funds"). The Fund is classified as a diversified open-end management investment company.

The Trust's financial statements are prepared in accordance with accounting principles generally accepted in the United States of America which require the use of management estimates. Actual results could differ from those estimates. The policies described below are followed consistently by the Trust in the preparation of its financial statements.

**Security Valuation.** Investments are stated at value determined as of the close of regular trading on the New York Stock Exchange on each day the exchange is open for trading.

Various inputs are used in determining the value of the Fund's investments. These inputs are summarized in three broad levels. Level 1 includes quoted prices in active markets for identical securities. Level 2 includes other significant observable inputs (including quoted prices for similar securities, interest rates, prepayment speeds, and credit risk). Level 3 includes significant unobservable inputs (including the Fund's own assumptions in determining the fair value of investments). The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities.

Equity securities are valued at the most recent sale price or official closing price reported on the exchange (US or foreign) or over-the-counter market on which they trade and are categorized as Level 1 securities. Securities for which no sales are reported are valued at the calculated mean between the most recent bid and asked quotations on the relevant market or, if a mean cannot be determined, at the most recent bid quotation.

Money market instruments purchased with an original or remaining maturity of sixty days or less, maturing at par, are valued at amortized cost, which approximates value, and are categorized as Level 2. Investments in open-end investment companies are valued at their net asset value each business day and are categorized as Level 1.

Securities and other assets for which market quotations are not readily available or for which the above valuation procedures are deemed not to reflect fair value are valued in a manner that is intended to reflect their fair value as determined in accordance with procedures approved by the Board and are generally categorized as Level 3. In accordance with the Fund's valuation procedures, factors used in determining value may include, but are not limited to, the type of the security; the size of the holding; the initial cost of the security; the existence of any contractual restrictions on the security's disposition; the price and extent of public trading in similar securities of the issuer or of comparable companies; quotations or evaluated prices from broker-dealers and/or pricing services; information obtained from the issuer, analysts, and/or the appropriate stock exchange (for exchange-traded securities); an analysis of the company's or issuer's financial statements; an evaluation of the forces that influence the issuer and the market(s) in which the security is purchased and sold and with respect to debt securities; the maturity, coupon, creditworthiness, currency denomination and the movement of the market in which the security is normally traded. The value determined under these procedures may differ from published values for the same securities.

Disclosure about the classification of fair value measurements is included in a table following the Fund's Investment Portfolio.

**Securities Lending.** The Fund lends securities to certain financial institutions. The Fund retains beneficial ownership of the securities it has loaned and continues to receive interest and dividends paid by the issuer of securities and to participate in any changes in their market value. The Fund requires the borrowers of the securities to maintain collateral with the Fund consisting of either cash or liquid, unencumbered assets having a value at least equal to the value of the securities loaned. When the collateral falls below specified amounts, the lending agent will use its best effort to obtain additional collateral on the next business day to meet required amounts under the security lending agreement. The Fund may invest the cash collateral into a joint trading account in an affiliated money market fund pursuant to Exemptive Orders issued by the SEC. The Fund receives compensation for lending its securities either in the form of fees or by earning interest on invested cash collateral net of borrower rebates and fees paid to a lending agent. Either the Fund or the borrower may terminate the loan. There may be risks of delay and costs in recovery of securities or even loss of rights in the collateral should the borrower of the securities fail financially. The Fund is also subject to all investment risks associated with the reinvestment of any cash collateral received, including, but not limited to, interest rate, credit and liquidity risk associated with such investments.

**Taxes.** The Fund's policy is to comply with the requirements of the Internal Revenue Code, as amended, which are applicable to regulated investment companies and to distribute all of its taxable income to its shareholders.

At December 31, 2010, the Fund had an approximate net tax basis capital loss carryforward which may be applied against any realized net taxable capital gains of each succeeding year until fully utilized or until the following expiration dates, whichever occurs first:

| Fund | Capital Loss Carryforward ($) | Expiration Date | Capital Loss Carryforward Utilized ($) |
|---|---|---|---|
| DWS Mid Cap Growth VIP | 18,281,000 | 12/31/2011 | 1,874,000 |
| | 935,000 | 12/31/2016 | |
| | 6,533,000 | 12/31/2017 | |

The Fund has reviewed the tax positions for the open tax years as of December 31, 2010 and has determined that no provision for income tax is required in the Fund's financial statements. The Fund's federal tax returns for the prior three fiscal years remain open subject to examination by the Internal Revenue Service.

**Distribution of Income and Gains.** Distributions of net investment income of the Fund, if any, are made annually. Net realized gains from investment transactions, in excess of available capital loss carryforwards, would be taxable to the Fund if not distributed and, therefore, will be distributed to shareholders at least annually. The Fund may also make additional distributions for tax purposes if necessary.

The timing and characterization of certain income and capital gains distributions are determined annually in accordance with federal tax regulations which may differ from accounting principles generally accepted in the United States of America. These differences primarily relate to net operating losses and certain securities sold at a loss. As a result, net investment income (loss) and net realized gain (loss) on investment transactions for a reporting period may differ significantly from distributions during such period. Accordingly, the Fund may periodically make reclassifications among certain of its capital accounts without impacting the net asset value of the Fund.

At December 31, 2010, the Fund's components of distributable earnings on a tax basis were as follows:

| Fund | Capital Loss Carryforwards ($) | Unrealized Appreciation (Depreciation) on Investments ($) |
|---|---|---|
| DWS Mid Cap Growth VIP | (25,749,000) | 8,278,722 |

**Expenses.** Expenses of the Trust arising in connection with a specific fund are allocated to that fund. Other Trust expenses which cannot be directly attributed to a fund are apportioned among the funds in the Trust.

**Contingencies.** In the normal course of business, the Fund may enter into contracts with service providers that contain general indemnification clauses. The Fund's maximum exposure under these arrangements is unknown as this would involve future claims that may be made against the Fund that have not yet been made. However, based on experience, the Fund expects the risk of loss to be remote.

**Other.** Investment transactions are accounted for on a trade date plus one basis for daily net asset value calculations. However, for financial reporting purposes, investment transactions are reported on trade date. Interest income is recorded on the accrual basis. Dividend income is recorded on the ex-dividend date net of foreign withholding taxes. Realized gains and losses from investment transactions are recorded on an identified cost basis.

## B. Purchases and Sales of Securities

During the year ended December 31, 2010, purchases and sales of investment transactions (excluding short-term investments) were as follows:

| Fund | Purchases ($) | Sales ($) |
|---|---|---|
| DWS Mid Cap Growth VIP | 12,373,056 | 14,480,595 |

## C. Related Parties

**Management Agreement.** Under the Investment Management Agreement with Deutsche Investment Management Americas Inc. ("DIMA" or the "Advisor"), an indirect, wholly owned subsidiary of Deutsche Bank AG, the Advisor directs the investments of the Fund in accordance with its investment objectives, policies and restrictions. The Advisor determines the securities, instruments and other contracts relating to investments to be purchased, sold or entered into by the Fund.

Under the Investment Management Agreement with the Advisor, the fee is equivalent to the annual rates shown below of the Fund's average daily net assets, computed and accrued daily and payable monthly:

| **Fund** | **Annual Management Fee Rate** |
|---|---|
| DWS Mid Cap Growth VIP | |
| $0–$250 million | .665% |
| next $750 million | .635% |
| next $1.5 billion | .615% |
| next $2.5 billion | .595% |
| next $2.5 billion | .565% |
| next $2.5 billion | .555% |
| next $2.5 billion | .545% |
| over $12.5 billion | .535% |

For the period from January 1, 2010 through September 30, 2010, the Advisor had contractually agreed to waive its fee and/or reimburse certain operating expenses to the extent necessary to maintain the operating expenses (excluding certain expenses such as extraordinary expenses, taxes, brokerage and interest expense) of the class as follows:

| **Fund** | **Annual Rate** |
|---|---|
| DWS Mid Cap Growth VIP | |
| Class A | 1.09% |

For the period from October 1, 2010 through September 30, 2011, the Advisor has contractually agreed to waive its fee and/or reimburse certain operating expenses to the extent necessary to maintain the operating expenses (excluding certain expenses such as extraordinary expenses, taxes, brokerage and interest expense) of the class as follows:

| **Fund** | **Annual Rate** |
|---|---|
| DWS Mid Cap Growth VIP | |
| Class A | .97% |

Accordingly, for the year ended December 31, 2010, the total management fee, management fee waived and effective management fee rate were as follows:

| **Fund** | **Total Aggregated ($)** | **Waived ($)** | **Annual Effective Rate** |
|---|---|---|---|
| DWS Mid Cap Growth VIP | 149,048 | 24,596 | .56% |

**Administration Fee.** Pursuant to an Administrative Services Agreement, DIMA provides most administrative services to the Fund. For all services provided under the Administrative Services Agreement, the Fund pays DIMA an annual fee ("Administration Fee") of 0.10% of the Fund's average daily net assets, computed and accrued daily and payable monthly. For the year ended December 31, 2010, the Administration Fee was as follows:

| **Fund** | **Total Aggregated ($)** | **Unpaid at December 31, 2010 ($)** |
|---|---|---|
| DWS Mid Cap Growth VIP | 22,413 | 2,228 |

**Typesetting and Filing Service Fees.** Under an agreement with DIMA, DIMA is compensated for providing typesetting and certain regulatory filing services to the Fund. For the year ended December 31, 2010, the amount charged to the Fund by DIMA included in the Statement of Operations under "reports to shareholders" was as follows:

| **Fund** | **Amount ($)** | **Unpaid at December 31, 2010 ($)** |
|---|---|---|
| DWS Mid Cap Growth VIP | 11,630 | 3,135 |

**Trustees' Fees and Expenses.** The Fund paid each Trustee not affiliated with the Advisor retainer fees plus specified amounts for various committee services and for the Board Chairperson.

**Affiliated Cash Management Vehicles.** The Fund may invest uninvested cash balances in Central Cash Management Fund, which is managed by the Advisor. The Fund indirectly bears their proportionate share of the expenses of the underlying money market funds. Central Cash Management Fund does not pay the Advisor an investment management fee. Central Cash Management Fund seeks a high level of current income consistent with liquidity and the preservation of capital.

### D. Ownership of the Fund

At December 31, 2010, the beneficial ownership in the Fund was as follows:

**DWS Mid Cap Growth VIP:** Two Participating Insurance Companies were owners of record of 10% or more of the total outstanding Class A shares of the Fund, each owning 63% and 35%.

### E. Line of Credit

The Trust and other affiliated fund (the "Participants") share in a $450 million revolving credit facility provided by a syndication of banks. The Fund may borrow for temporary or emergency purposes, including the meeting of redemption requests that otherwise might require the untimely disposition of securities. The Participants are charged an annual commitment fee which is allocated based on net assets, among each of the Participants. Interest is calculated at a rate per annum equal to the sum of the Federal Funds Rate plus 1.25 percent plus if LIBOR exceeds the Federal Funds Rate the amount of such excess. The Fund may borrow up to a maximum of 33 percent of its net assets under the agreement.

### F. Subsequent Event

On January 12, 2011, the Board of the following Acquired Fund approved, in principle, the merger of the Acquired Fund into the Acquiring Fund. Completion of the merger is subject to a number of conditions. The merger is expected to be completed on or about May 1, 2011.

| Acquired Fund | Acquiring Fund |
|---|---|
| DWS Variable Series II — DWS Mid Cap Growth VIP | DWS Variable Series II — DWS Small Cap Growth VIP |

In addition, on January 12, 2011, the Board approved changes to the name and strategy of DWS Small Cap Growth VIP. Effective on or about May 1, 2011, DWS Small Cap Growth VIP's investment objective will change from maximum appreciation of investors capital to long-term capital appreciation. In connection with the implementation of the new investment objective, the name will change from DWS Small Cap Growth VIP to DWS Small Mid Cap Growth VIP. In addition, the Russell 2500 Growth Index will replace the Russell 2000 Growth Index as the benchmark index because the Advisor believes that it better reflects the new investment strategy. For a description of the new investment objective, please see the supplement dated January 19, 2011 to the Fund's current prospectus posted on www.dws-investments.com.

# Report of Independent Registered Public Accounting Firm

**To the Board of Trustees and Shareholders of DWS Variable Series II:**

We have audited the accompanying statement of assets and liabilities of DWS Mid Cap Growth VIP, one of the funds constituting the DWS Variable Series II (the "Trust"), including the investment portfolio, as of December 31, 2010, and the related statement of operations, the statement of changes in net assets and the financial highlights for each of the periods indicated therein. These financial statements and financial highlights are the responsibility of the Trust's management. Our responsibility is to express an opinion on these financial statements and financial highlights based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements and financial highlights are free of material misstatement. We were not engaged to perform an audit of the Trust's internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Trust's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements and financial highlights, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our procedures included confirmation of securities owned as of December 31, 2010, by correspondence with the custodian and brokers. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements and financial highlights referred to above present fairly, in all material respects, the financial position of the aforementioned fund of the DWS Variable Series II at December 31, 2010, the results of its operations, the changes in its net assets and the financial highlights for each of the periods indicated therein, in conformity with U.S. generally accepted accounting principles.

Ernst & Young LLP

Boston, Massachusetts
February 14, 2011

## Tax Information

**(Unaudited)**

Please consult a tax advisor if you have questions about federal or state income tax laws, or on how to prepare your tax returns. If you have specific questions about your account, please contact your insurance provider.

## Proxy Voting

The Trust's policies and procedures for voting proxies for portfolio securities and information about how the Trust voted proxies related to its portfolio securities during the 12-month period ended June 30 are available on our Web site — www.dws-investments.com (click on "proxy voting" at the bottom of the page) — or on the SEC's Web site — www.sec.gov. To obtain a written copy of the Trust's policies and procedures without charge, upon request, call us toll free at (800) 728-3337.

# Investment Management Agreement Approval

## DWS Mid Cap Growth VIP

The Board of Trustees, including the Independent Trustees, approved the renewal of your Fund's investment management agreement (the "Agreement") with Deutsche Investment Management Americas Inc. ("DWS") in September 2010.

In terms of the process that the Board followed prior to approving the Agreement, shareholders should know that:

- In September 2010, all but one of the Fund's Trustees were independent of DWS and its affiliates.
- The Trustees meet frequently to discuss fund matters. Each year, the Trustees dedicate substantial time to contract review matters. Over the course of several months, the Board's Contract Committee, in coordination with the Board's Equity Oversight Committee, reviewed comprehensive materials received from DWS, independent third parties and independent counsel. These materials included an analysis of the Fund's performance, fees and expenses, and profitability compiled by the Fund's independent fee consultant. The Board also received extensive information throughout the year regarding performance of the Fund.
- The Independent Trustees regularly meet privately with their independent counsel to discuss contract review and other matters. In addition, the Independent Trustees were also advised by the Fund's independent fee consultant in the course of their review of the Fund's contractual arrangements and considered a comprehensive report prepared by the independent fee consultant in connection with their deliberations (the "IFC Report").
- In connection with reviewing the Agreement, the Board also reviewed the terms of the Fund's distribution agreement, administrative services agreement, transfer agency agreement and other material service agreements.
- Based on its evaluation of the information provided, the Contract Committee presented its findings and recommendations to the Independent Trustees as a group. The Independent Trustees reviewed the Contract Committee's findings and recommendations and presented their recommendations to the full Board.

In connection with the contract review process, the Contract Committee and the Board considered the factors discussed below, among others. The Board also considered that DWS and its predecessors have managed the Fund since its inception, and the Board believes that a long-term relationship with a capable, conscientious advisor is in the best interests of the Fund. The Board considered, generally, that shareholders chose to invest or remain invested in the Fund knowing that DWS managed the Fund, and that the Agreement was approved by the Fund's shareholders. DWS is part of Deutsche Bank, a major global banking institution that is engaged in a wide range of financial services. The Board believes that there are significant advantages to being part of a global asset management business that offers a wide range of investing expertise and resources, including hundreds of portfolio managers and analysts with research capabilities in many countries throughout the world.

While shareholders may focus primarily on fund performance and fees, the Fund's Board considers these and many other factors, including the quality and integrity of DWS's personnel and such other issues as back-office operations, fund valuations, and compliance policies and procedures.

**Nature, Quality and Extent of Services.** The Board considered the terms of the Agreement, including the scope of advisory services provided under the Agreement. The Board noted that, under the Agreement, DWS provides portfolio management services to the Fund and that, pursuant to a separate administrative services agreement, DWS provides administrative services to the Fund. The Board considered the experience and skills of senior management and investment personnel, the resources made available to such personnel, the ability of DWS to attract and retain high-quality personnel, and the organizational depth and stability of DWS. The Board reviewed the Fund's performance over short-term and long-term periods and compared those returns to various agreed-upon performance measures, including market indices and a peer universe compiled by the independent fee consultant using information supplied by Lipper Inc. ("Lipper"). The Board also noted that it has put into place a process of identifying "Focus Funds" (e.g., funds performing poorly relative to their benchmark or a peer universe compiled by Lipper), and receives more frequent reporting and information from DWS regarding such funds, along with DWS's remedial plans to address underperformance. The Board believes this process is an effective manner of identifying and addressing underperforming funds. Based on the information provided, the Board noted that for the one-, three- and five-year periods ended December 31, 2009, the Fund's performance (Class A shares) was in the 2nd quartile, 4th quartile and 4th quartile, respectively, of the applicable Lipper universe (the 1st quartile being the best performers and the 4th quartile being the worst performers). The Board also observed that the Fund has underperformed its benchmark in the one-, three- and five-year periods ended December 31, 2009.

On the basis of this evaluation and the ongoing review of investment results by the Board, the Board concluded that the nature, quality and extent of services provided by DWS historically have been and continue to be satisfactory.

**Fees and Expenses.** The Board considered the Fund's investment management fee schedule, operating expenses, and total expense ratios, and comparative information provided by Lipper and the independent fee consultant regarding investment management fee rates paid to other investment advisors by similar funds (1st quartile being the most favorable and 4th quartile being the least favorable). With respect to management fees paid to other investment advisors by similar funds, the Board noted that the contractual fee rates paid by the Fund, which include the 0.10% fee paid to DWS under the Fund's administrative services agreement, were at the median (2nd quartile) of the applicable Lipper peer group (based on Lipper data provided as of December 31, 2009). The Board noted that the Fund's Class A shares total (net) operating expenses were expected to be higher than the median (4th quartile) of the applicable Lipper expense universe (based on Lipper data provided as of December 31, 2009, and analyzing Lipper expense universe Class A expenses less any applicable 12b-1 fees) ("Lipper Universe Expenses"). The Board considered the Fund's management fee rate as compared to fees charged by DWS and certain of its affiliates for comparable mutual funds and considered differences in fund and fee structures between the DWS Funds. The Board also considered how the Fund's total (net) operating expenses compared to the total (net) operating expenses of a more customized peer group selected by Lipper (based on such factors as asset size). The Board also noted that the expense limitation agreed to by DWS helped to ensure that the Fund's total (net) operating expenses would remain competitive.

The information considered by the Board as part of its review of management fees included information regarding fees charged by DWS and its affiliates to similar institutional accounts and to similar funds offered primarily to European investors ("DWS Europe funds"), in each case as applicable. The Board observed that advisory fee rates for institutional accounts generally were lower than the management fees charged by similarly managed DWS US mutual funds ("DWS Funds"), but also took note of the differences in services provided to DWS Funds as compared to institutional accounts. In the case of DWS Europe funds, the Board observed that fee rates for DWS Europe funds generally were higher than for similarly managed DWS Funds, but noted that differences in the types of services provided to DWS Funds relative to DWS Europe funds made it difficult to compare such fees.

On the basis of the information provided, the Board concluded that management fees were reasonable and appropriate in light of the nature, quality and extent of services provided by DWS.

**Profitability.** The Board reviewed detailed information regarding revenues received by DWS under the Agreement. The Board considered the estimated costs and pre-tax profits realized by DWS from advising the DWS Funds, as well as estimates of the pre-tax profits attributable to managing the Fund in particular. The Board also received information regarding the estimated enterprise-wide profitability of DWS and its affiliates with respect to all fund services in totality and by fund. The Board reviewed DWS's methodology in allocating its costs to the management of the Fund. Based on the information provided, the Board concluded that the pre-tax profits realized by DWS in connection with the management of the Fund were not unreasonable. The Board also reviewed information regarding the profitability of certain similar investment management firms. The Board noted that while information regarding the profitability of such firms is limited (and in some cases is not necessarily prepared on a comparable basis), DWS and its affiliates' overall profitability with respect to the DWS fund complex (after taking into account distribution and other services provided to the funds by DWS and its affiliates) was lower than the overall profitability levels of many comparable firms for which such data was available.

**Economies of Scale.** The Board considered whether there are economies of scale with respect to the management of the Fund and whether the Fund benefits from any economies of scale. The Board noted that the Fund's management fee schedule includes fee breakpoints. The Board concluded that the Fund's fee schedule represents an appropriate sharing between the Fund and DWS of such economies of scale as may exist in the management of the Fund at current asset levels.

**Other Benefits to DWS and Its Affiliates.** The Board also considered the character and amount of other incidental benefits received by DWS and its affiliates, including any fees received by DWS for administrative services provided to the Fund and any fees received by an affiliate of DWS for distribution services. The Board also considered benefits to DWS related to brokerage and soft-dollar allocations, including allocating brokerage to pay for research generated by parties other than the executing broker dealers, which pertain primarily to funds investing in equity securities, along with the incidental public relations benefits to DWS related to DWS Funds advertising and cross-selling opportunities among DWS products and services. The Board concluded that management fees were reasonable in light of these fallout benefits.

**Compliance.** The Board considered the significant attention and resources dedicated by DWS to documenting and enhancing its compliance processes in recent years. The Board noted in particular (i) the experience and seniority of both DWS's chief compliance officer and the Fund's chief compliance officer; (ii) the large number of

DWS compliance personnel; and (iii) the substantial commitment of resources by DWS and its affiliates to compliance matters.

Based on all of the information considered and the conclusions reached, the Board unanimously (including the Independent Trustees) determined that the continuation of the Agreement is in the best interests of the Fund. In making this determination, the Board did not give particular weight to any single factor identified above. The Board considered these factors over the course of numerous meetings, certain of which were in executive session with only the Independent Trustees and their counsel present. It is possible that individual Trustees may have weighed these factors differently in reaching their individual decisions to approve the continuation of the Agreement.

# Summary of Management Fee Evaluation by Independent Fee Consultant

October 3, 2010

Pursuant to an Order entered into by Deutsche Investment Management Americas and affiliates (collectively, "DeAM") with the Attorney General of New York, I, Thomas H. Mack, have been appointed the Independent Fee Consultant for the DWS Funds (formerly the DWS Scudder Funds). My duties include preparing an annual written evaluation of the management fees DeAM charges the Funds, considering among other factors the management fees charged by other mutual fund companies for like services, management fees DeAM charges other clients for like services, DeAM's costs of supplying services under the management agreements and related profit margins, possible economies of scale if a Fund grows larger, and the nature and quality of DeAM's services, including fund performance. This report summarizes my evaluation for 2010, including my qualifications, the evaluation process for each of the DWS Funds, consideration of certain complex-level factors, and my conclusions. I served in substantially the same capacity in 2007, 2008, and 2009.

## Qualifications

For more than 35 years I have served in various professional capacities within the investment management business. I have held investment analysis and advisory positions, including securities analyst, portfolio strategist and director of investment policy with a large investment firm. I have also performed business management functions, including business development, financial management and marketing research and analysis.

Since 1991, I have been an independent consultant within the asset management industry. I have provided services to over 125 client organizations, including investment managers, mutual fund boards, product distributors and related organizations. Over the past ten years I have completed a number of assignments for mutual fund boards, specifically including assisting boards with management contract renewal.

I hold a Master of Business Administration degree, with highest honors, from Harvard University and Master of Science and Bachelor of Science (highest honors) degrees from the University of California at Berkeley. I am an independent director and audit committee financial expert for two closed-end mutual funds and have served in various leadership and financial oversight capacities with non-profit organizations.

## Evaluation of Fees for each DWS Fund

My work focused primarily on evaluating, fund-by-fund, the fees charged to each of the 118 publicly offered Fund portfolios in the DWS Fund family. For each Fund, I considered each of the key factors mentioned above, as well as any other relevant information. In doing so I worked closely with the Funds' Independent Directors in their annual contract renewal process, as well as in their approval of contracts for several new funds (documented separately).

In evaluating each Fund's fees, I reviewed comprehensive materials provided by or on behalf of DeAM, including expense information prepared by Lipper Analytical, comparative performance information, profitability data, manager histories, and other materials. I also accessed certain additional information from the Lipper and Morningstar databases and drew on my industry knowledge and experience.

To facilitate evaluating this considerable body of information, I prepared for each Fund a document summarizing the key data elements in each area as well as additional analytics discussed below. This made it possible to consider each key data element in the context of the others.

In the course of contract renewal, DeAM agreed to implement a number of fee and expense adjustments requested by the Independent Directors which will favorably impact future fees and expenses, and my evaluation includes the effects of these changes.

### Fees and Expenses Compared with Other Funds

The competitive fee and expense evaluation for each fund focused on two primary comparisons:

- The Fund's contractual management fee (the advisory fee plus the administration fee where applicable) compared with those of a group of typically 12–15 funds in the same Lipper investment category (e.g. Large Capitalization Growth) having similar distribution arrangements and being of similar size.
- The Fund's total expenses compared with a broader universe of funds from the same Lipper investment category and having similar distribution arrangements.

These two comparisons provide a view of not only the level of the fee compared with funds of similar scale but also the total expense the Fund bears for all the services it receives, in comparison with the investment choices available in the Fund's investment category and distribution channel. The principal figure-of-merit used in these comparisons was the subject Fund's percentile ranking against peers.

### DeAM's Fees for Similar Services to Others

DeAM provided management fee schedules for all of its US domiciled fund and non-fund investment management accounts in any of the investment categories where there is a DWS Fund. These similar products included the other DWS Funds, non-fund pooled accounts, institutional accounts and sub-advisory accounts. Using this information, I calculated for each Fund the fee that would be charged to each similar product, at the subject Fund's asset level.

Evaluating information regarding non-fund products is difficult because there are varying levels of services required for different types of accounts, with mutual funds generally requiring considerably more regulatory and administrative types of service as well as having more frequent cash flows than other types of accounts. Also, while mutual fund fees for similar fund products can be expected to be similar, there will be some differences due to different pricing conditions in different distribution channels (e.g. retail funds versus those used in variable insurance products), differences in underlying investment processes and other factors.

**Costs and Profit Margins**

DeAM provided a detailed profitability analysis for each Fund. After making some adjustments so that the presentation would be more comparable to the available industry figures, I reviewed profit margins from investment management alone, from investment management plus other fund services (excluding distribution) provided to the Funds by DeAM (principally shareholder services), and DeAM profits from all sources, including distribution. A later section comments on overall profitability.

**Economies of Scale**

Economies of scale — an expected decline in management cost per dollar of fund assets as fund assets grow — are very rarely quantified and documented because of inherent difficulties in collecting and analyzing relevant data. However, in virtually every investment category that I reviewed, larger funds tend to have lower fees and lower total expenses than smaller funds. To see how each DWS Fund compares with this industry observation, I reviewed:

- The trend in Fund assets over the last five years and the accompanying trend in total expenses. This shows if the Fund has grown and, if so, whether total expense (management fees as well as other expenses) have declined as a percent of assets.
- Whether the Fund has break-points in its management fee schedule, the extent of the fee reduction built into the schedule and the asset levels where the breaks take effect, and in the case of a sub-advised Fund how the Fund's break-points compare with those of the sub-advisory fee schedule.
- How the Fund's contractual fee schedule compares with trends in the industry data. To accomplish this, I constructed a chart showing how actual latest-fiscal-year contractual fees of the Fund and of other similar funds relate to average fund assets, with the subject Fund's contractual fee schedule superimposed.

**Quality of Service — Performance**

The quality-of-service evaluation focused on investment performance, which is the principal result of the investment management service. Each Fund's performance was reviewed over the past 1, 3, 5 and 10 years, as applicable, and compared with that of other funds in the same investment category and with a suitable market index.

In addition, I calculated and reviewed risk-adjusted returns relative to an index of similar mutual funds' returns and a suitable market index. The risk-adjusted returns analysis provides a way of determining the extent to which the Fund's return comparisons are mainly the product of investment value-added (or lack thereof) or alternatively taking considerably more or less risk than is typical in its investment category.

I also received and considered the history of portfolio manager changes for each Fund, as this provided an important context for evaluating the performance results.

## Complex-Level Considerations

While this evaluation was conducted mainly at the individual fund level, there are some issues relating to the reasonableness of fees that can alternatively be considered across the whole fund complex:

- I reviewed DeAM's profitability analysis for all DWS Funds, with a view toward determining if the allocation procedures used were reasonable and how profit levels compared with public data for other investment managers.
- I considered whether DeAM and affiliates receive any significant ancillary or "fall-out" benefits that should be considered in interpreting the direct profitability results. These would be situations where serving as the investment manager of the Funds is beneficial to another part of the Deutsche Bank organization.
- I considered how aggregated DWS Fund expenses had varied over the years, by asset class and in the context of trends in asset levels.
- I reviewed the structure of the DeAM organization, trends in staffing levels, and information on compensation of investment management and other professionals compared with industry data.

## Findings

Based on the process and analysis discussed above, which included reviewing a wide range of information from management and external data sources and considering among other factors the fees DeAM charges other clients, the fees charged by other fund managers, DeAM's costs and profits associated with managing the Funds, economies of scale, possible fall-out benefits, and the nature and quality of services provided, in my opinion the management fees charged the DWS Funds are reasonable.

Thomas H. Mack

Thomas H. Mack

# Board Members and Officers

The following table presents certain information regarding the Board Members and Officers of the Trust as of December 31, 2010. Each Board Member's year of birth is set forth in parentheses after his or her name. Unless otherwise noted, (i) each Board Member has engaged in the principal occupation(s) noted in the table for at least the most recent five years, although not necessarily in the same capacity; and (ii) the address of each Independent Board Member is c/o Paul K. Freeman, Independent Chairman, DWS Funds, PO Box 101833, Denver, CO 80250-1833. Except as otherwise noted below, the term of office for each Board Member is until the election and qualification of a successor, or until such Board Member sooner dies, resigns, is removed or as otherwise provided in the governing documents of the fund. Because the fund does not hold an annual meeting of shareholders, each Board Member will hold office for an indeterminate period. The Board Members may also serve in similar capacities with other funds in the fund complex. The Length of Time Served represents the year in which the Board Member joined the board of one or more DWS funds now overseen by the Board.

### Independent Board Members

| Name, Year of Birth, Position with the Fund and Length of Time Served[1] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Paul K. Freeman (1950)<br>Chairperson since 2009<br>Board Member since 1993 | Consultant, World Bank/Inter-American Development Bank; Executive and Governing Council of the Independent Directors Council (education committees); formerly, Project Leader, International Institute for Applied Systems Analysis (1998–2001); Chief Executive Officer, The Eric Group, Inc. (environmental insurance) (1986–1998) | 122 |
| John W. Ballantine (1946)<br>Board Member since 1999 | Retired; formerly, Executive Vice President and Chief Risk Management Officer, First Chicago NBD Corporation/The First National Bank of Chicago (1996–1998); Executive Vice President and Head of International Banking (1995–1996). Directorships: Healthways, Inc. (provider of disease and care management services); Portland General Electric (utility company); Stockwell Capital Investments PLC (private equity). Former Directorships: First Oak Brook Bancshares, Inc. and Oak Brook Bank; Prisma Energy International | 122 |
| Henry P. Becton, Jr. (1943)<br>Board Member since 1990 | Vice Chair and former President, WGBH Educational Foundation. Directorships: Association of Public Television Stations; Lead Director, Becton Dickinson and Company[3] (medical technology company); Lead Director, Belo Corporation[3] (media company); Public Radio International; Public Radio Exchange (PRX); The PBS Foundation. Former Directorships: Boston Museum of Science; American Public Television; Concord Academy; New England Aquarium; Mass. Corporation for Educational Telecommunications; Committee for Economic Development; Public Broadcasting Service | 122 |
| Dawn-Marie Driscoll (1946)<br>Board Member since 1987 | President, Driscoll Associates (consulting firm); Executive Fellow, Center for Business Ethics, Bentley University; formerly, Partner, Palmer & Dodge (1988–1990); Vice President of Corporate Affairs and General Counsel, Filene's (1978–1988). Directorships: Trustee of 22 open-end mutual funds managed by Sun Capital Advisers, Inc. (since 2007); Director of ICI Mutual Insurance Company (since 2007); Advisory Board, Center for Business Ethics, Bentley University; Trustee, Southwest Florida Community Foundation (charitable organization). Former Directorships: Investment Company Institute (audit, executive, nominating committees) and Independent Directors Council (governance, executive committees) | 122 |
| Keith R. Fox (1954)<br>Board Member since 1996 | Managing General Partner, Exeter Capital Partners (a series of private investment funds). Directorships: Progressive International Corporation (kitchen goods importer and distributor); BoxTop Media Inc. (advertising); The Kennel Shop (retailer); former Chairman, National Association of Small Business Investment Companies | 122 |
| Kenneth C. Froewiss (1945)<br>Board Member since 2001 | Adjunct Professor of Finance, NYU Stern School of Business (September 2009–present; Clinical Professor from 1997–September 2009); Member, Finance Committee, Association for Asian Studies (2002–present); Director, Mitsui Sumitomo Insurance Group (US) (2004–present); prior thereto, Managing Director, J.P. Morgan (investment banking firm) (until 1996) | 122 |
| Richard J. Herring (1946)<br>Board Member since 1990 | Jacob Safra Professor of International Banking and Professor, Finance Department, The Wharton School, University of Pennsylvania (since July 1972); Co-Director, Wharton Financial Institutions Center (since July 2000); Co-Chair, U.S. Shadow Financial Regulatory Committee; Executive Director, Financial Economists Roundtable; Director, Japan Equity Fund, Inc. (since September 2007), Thai Capital Fund, Inc. (since September 2007), Singapore Fund, Inc. (since September 2007); Independent Director of Barclays Bank Delaware (since September 2010). Formerly, Vice Dean and Director, Wharton Undergraduate Division (July 1995–June 2000); Director, Lauder Institute of International Management Studies (July 2000–June 2006) | 122 |
| William McClayton (1944)<br>Board Member since 2004+ | Private equity investor (since October 2009); previously, Managing Director, Diamond Management & Technology Consultants, Inc. (global consulting firm) (2001–2009); Directorship: Board of Managers, YMCA of Metropolitan Chicago; formerly: Senior Partner, Arthur Andersen LLP (accounting) (1966–2001); Trustee, Ravinia Festival | 122 |

| Name, Year of Birth, Position with the Fund and Length of Time Served[1] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Rebecca W. Rimel (1951)<br>Board Member since 1995 | President and Chief Executive Officer, The Pew Charitable Trusts (charitable organization) (1994 to present); Trustee, Thomas Jefferson Foundation (charitable organization) (1994 to present); Trustee, Executive Committee, Philadelphia Chamber of Commerce (2001–2007); Director, CardioNet, Inc.[2] (2009–present) (health care). Formerly, Executive Vice President, The Glenmede Trust Company (investment trust and wealth management) (1983–2004); Board Member, Investor Education (charitable organization) (2004–2005); Director, Viasys Health Care[2] (January 2007–June 2007); Trustee, Pro Publica (charitable organization) (2007–2010) | 122 |
| William N. Searcy, Jr. (1946)<br>Board Member since 1993 | Private investor since October 2003; Trustee of 22 open-end mutual funds managed by Sun Capital Advisers, Inc. (since October 1998). Formerly, Pension & Savings Trust Officer, Sprint Corporation[2] (telecommunications) (November 1989–September 2003) | 122 |
| Jean Gleason Stromberg (1943)<br>Board Member since 1997 | Retired. Formerly, Consultant (1997–2001); Director, Financial Markets US Government Accountability Office (1996–1997); Partner, Fulbright & Jaworski, L.L.P. (law firm) (1978–1996). Directorships: The William and Flora Hewlett Foundation. Former Directorships: Service Source, Inc., Mutual Fund Directors Forum (2002–2004), American Bar Retirement Association (funding vehicle for retirement plans) (1987–1990 and 1994–1996) | 122 |
| Robert H. Wadsworth (1940)<br>Board Member since 1999 | President, Robert H. Wadsworth & Associates, Inc. (consulting firm) (1983 to present); Director, The Phoenix Boys Choir Association | 125 |

## Interested Board Member and Officer[4]

| Name, Year of Birth, Position with the Trust/ Corporation and Length of Time Served[1,5] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Ingo Gefeke[7] (1967)<br>Board Member since 2010<br>Executive Vice President since 2010 | Managing Director[3], Deutsche Asset Management; Global Head of Distribution and Product Management, DWS Global Head of Trading and Securities Lending. Member of the Board of Directors of DWS Investment GmbH Frankfurt (since July 2009) and DWS Holding & Service GmbH Frankfurt (since January 2010); formerly, Global Chief Administrative Officer, Deutsche Asset Management (2004–2009); Global Chief Operating Officer, Global Transaction Banking, Deutsche Bank AG, New York (2001–2004); Chief Operating Officer, Global Banking Division Americas, Deutsche Bank AG, New York (1999–2001); Central Management, Global Banking Services, Deutsche Bank AG, Frankfurt (1998–1999); Relationship Management, Deutsche Bank AG, Tokyo, Japan (1997–1998) | 55 |

## Officers[4]

| Name, Year of Birth, Position with the Fund and Length of Time Served[5] | Principal Occupation(s) During Past 5 Years and Other Directorships Held |
|---|---|
| Michael G. Clark[6] (1965)<br>President, 2006–present | Managing Director[3], Deutsche Asset Management (2006–present); President of DWS family of funds; Director, ICI Mutual Insurance Company (since October 2007); formerly, Director of Fund Board Relations (2004–2006) and Director of Product Development (2000–2004), Merrill Lynch Investment Managers; Senior Vice President Operations, Merrill Lynch Asset Management (1999–2000) |
| John Millette[8] (1962)<br>Vice President and Secretary, 1999–present | Director[3], Deutsche Asset Management |
| Paul H. Schubert[6] (1963)<br>Chief Financial Officer, 2004–present<br>Treasurer, 2005–present | Managing Director[3], Deutsche Asset Management (since July 2004); formerly, Executive Director, Head of Mutual Fund Services and Treasurer for UBS Family of Funds (1998–2004); Vice President and Director of Mutual Fund Finance at UBS Global Asset Management (1994–1998) |
| Caroline Pearson[8] (1962)<br>Chief Legal Officer, April 2010–present | Managing Director[3], Deutsche Asset Management; formerly, Assistant Secretary for DWS family of funds (1997–2010) |
| Rita Rubin[9] (1970)<br>Assistant Secretary, 2009–present | Vice President and Counsel, Deutsche Asset Management (since October 2007); formerly, Vice President, Morgan Stanley Investment Management (2004–2007) |
| Paul Antosca[8] (1957)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management (since 2006); Vice President, The Manufacturers Life Insurance Company (U.S.A.) (1990–2006) |
| Jack Clark[8] (1967)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management (since 2007); formerly, Vice President, State Street Corporation (2002–2007) |

| Name, Year of Birth, Position with the Fund and Length of Time Served[5] | Principal Occupation(s) During Past 5 Years and Other Directorships Held |
|---|---|
| Diane Kenneally[8] (1966)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management |
| John Caruso[9] (1965)<br>Anti-Money Laundering Compliance Officer, 2010–present | Managing Director[3], Deutsche Asset Management |
| Robert Kloby[9] (1962)<br>Chief Compliance Officer, 2006–present | Managing Director[3], Deutsche Asset Management |

1 *The length of time served represents the year in which the Board Member joined the board of one or more DWS funds currently overseen by the Board.*

2 *A publicly held company with securities registered pursuant to Section 12 of the Securities Exchange Act of 1934.*

3 *Executive title, not a board directorship.*

4 *As a result of their respective positions held with the Advisor, these individuals are considered "interested persons" of the Advisor within the meaning of the 1940 Act. Interested persons receive no compensation from the fund.*

5 *The length of time served represents the year in which the officer was first elected in such capacity for one or more DWS funds.*

6 *Address: 100 Plaza One, Jersey City, NJ 07311.*

7 *Effective January 11, 2011, Mr. Gefeke, an interested Board Member and Executive Vice President, resigned from the fund's Board and as an officer.*

*The mailing address of Mr. Gefeke is 345 Park Avenue, New York, New York 10154. Mr. Gefeke was an interested Board Member of certain DWS funds by virtue of his positions with Deutsche Asset Management. As an interested person, Mr. Gefeke received no compensation from the fund.*

8 *Address: One Beacon Street, Boston, MA 02108.*

9 *Address: 60 Wall Street, New York, New York 10005.*

*The fund's Statement of Additional Information ("SAI") includes additional information about the Board Members. The SAI is available, without charge, upon request. If you would like to request a copy of the SAI, you may do so by calling the following toll-free number: (800) 728-3337.*

DWS Investments is part of Deutsche Bank's Asset Management division and, within the US, represents the retail asset management activities of Deutsche Bank AG, Deutsche Bank Trust Company Americas, Deutsche Investment Management Americas Inc. and DWS Trust Company.

The views expressed in this report reflect those of the portfolio managers only through the end of the period of the report as stated on the cover. The managers' views are subject to change at any time based on market and other conditions and should not be construed as a recommendation.

This information must be preceded or accompanied by a current prospectus.

Portfolio changes should not be considered recommendations for action by individual investors.

DWS Investments Distributors, Inc.
222 South Riverside Plaza
Chicago, IL 60606
(800) 621-1148

VS2MCG-2 (2/11)

DWS INVESTMENTS
Deutsche Bank Group

DECEMBER 31, 2010

# ANNUAL REPORT

## DWS VARIABLE SERIES II

DWS Money Market VIP

**This report must be preceded or accompanied by a prospectus. To obtain an additional prospectus or summary prospectus, if available, call (800) 728-3337 or your financial representative. We advise you to consider the Fund's objectives, risks, charges and expenses carefully before investing. The summary prospectus and prospectus contain this and other important information about the Fund. Please read the prospectus carefully before you invest.**

*Investments in variable insurance portfolios (VIPs) involve risk. Stocks may decline in value. Bond investments are subject to interest-rate and credit risks. When interest rates rise, bond prices generally fall. Credit risk refers to the ability of an issuer to make timely payments of principal and interest. Investing in derivatives entails special risks relating to liquidity, leverage and credit that may reduce returns and/or increased volatility. Investing in foreign securities, particularly those of emerging markets, presents certain risks, such as currency fluctuations, political and economic changes, and market risks. There are additional risks associated with investing in commodities, high-yield bonds, aggressive growth stocks, non-diversified/ concentrated funds and small- and mid-cap stocks which are more fully explained in the prospectuses. Please read the prospectus for more information.*

*DWS Investments is part of Deutsche Bank's Asset Management division and, within the US, represents the retail asset management activities of Deutsche Bank AG, Deutsche Bank Trust Company Americas, Deutsche Investment Management Americas Inc. and DWS Trust Company.*

*NOT FDIC/NCUA INSURED NO BANK GUARANTEE MAY LOSE VALUE NOT A DEPOSIT*
*NOT INSURED BY ANY FEDERAL GOVERNMENT AGENCY*

DWS INVESTMENTS
Deutsche Bank Group

## DWS Money Market VIP

**All performance shown is historical, assumes reinvestment of all dividend and capital gain distributions and does not guarantee future results. Investment return and principal value fluctuate with changing market conditions so that, when redeemed, shares may be worth more or less than their original cost. Current performance may be lower or higher than the performance data quoted. Please contact your participating insurance company for the Fund's most recent month-end performance. Performance doesn't reflect charges and fees ("contract charges") associated with the separate account that invests in the Fund or any variable life insurance policy or variable annuity contract for which the Fund is an investment option. These charges and fees will reduce returns. The yield quotation more closely reflects the current earnings of the Fund than the total return quotation.**

### Risk Considerations

**An investment in this Fund is not insured or guaranteed by the Federal Deposit Insurance Corporation (FDIC) or by any other government agency. Although the Fund seeks to preserve the value of your investment at $1.00 per share, it is possible to lose money by investing in the Fund. The share price of money market funds can fall below the $1.00 share price.** You should not rely on or expect the Advisor to enter into support agreements or take other actions to maintain the Fund's $1.00 share price. The credit quality of the Fund's holdings can change rapidly in certain markets, and the default of a single holding could have an adverse impact on the Fund's share price. The Fund's share price can also be negatively affected during periods of high redemption pressures and/or illiquid markets. The actions of a few large investors in the Fund may have a significant adverse effect on the share price of the Fund. See the prospectus for specific details regarding the Fund's risk profile.

| Fund's Class A Shares Yield | 7-day current yield |
|---|---|
| December 31, 2010 | 0.01%* |
| December 31, 2009 | 0.02% |

* *The investment advisor has agreed to waive fees/reimburse expenses. This waiver may be changed or terminated at anytime without notice. Without such fee waivers/expense reimbursements, the 7-day current yield would have been –0.14% as of December 31, 2010.*

*Yields are historical, will fluctuate and do not guarantee future performance. The 7-day current yield refers to the income paid by the Fund over a 7-day period expressed as an annual percentage rate of the Fund's shares outstanding.*

# Information About Your Fund's Expenses

## DWS Money Market VIP

As an investor of the Fund, you incur two types of costs: ongoing expenses and transaction costs. Ongoing expenses include management fees and other Fund expenses. Examples of transaction costs include contract charges, redemption fees and account maintenance fees, which are not shown in this section. The following tables are intended to help you understand your ongoing expenses (in dollars) of investing in the Fund and to help you compare these expenses with the ongoing expenses of investing in other mutual funds. In the most recent six-month period the Fund limited these expenses; had it not done so, expenses would have been higher. The example in the table is based on an investment of $1,000 invested at the beginning of the six-month period and held for the entire period (July 1, 2010 to December 31, 2010).

The tables illustrate your Fund's expenses in two ways:

- **Actual Fund Return.** This helps you estimate the actual dollar amount of ongoing expenses (but not transaction costs) paid on a $1,000 investment in the Fund using the Fund's actual return during the period. To estimate the expenses you paid over the period, simply divide your account value by $1,000 (for example, an $8,600 account value divided by $1,000 = 8.6), then multiply the result by the number in the "Expenses Paid per $1,000" line under the share class you hold.
- **Hypothetical 5% Fund Return.** This helps you to compare your Fund's ongoing expenses (but not transaction costs) with those of other mutual funds using the Fund's actual expense ratio and a hypothetical rate of return of 5% per year before expenses. Examples using a 5% hypothetical Fund return may be found in the shareholder reports of other mutual funds. The hypothetical account values and expenses may not be used to estimate the actual ending account balance or expenses you paid for the period.

Please note that the expenses shown in these tables are meant to highlight your ongoing expenses only and do not reflect any transaction costs. The "Expenses Paid per $1,000" line of the tables is useful in comparing ongoing expenses only and will not help you determine the relative total expense of owning different funds. If these transaction costs had been included, your costs would have been higher.

**Expenses and Value of a $1,000 Investment** for the six months ended December 31, 2010

| **Actual Fund Return** | **Class A** |
|---|---|
| Beginning Account Value 7/1/10 | $1,000.00 |
| Ending Account Value 12/31/10 | $1,000.10 |
| Expenses Paid per $1,000* | $ 1.87 |

| **Hypothetical 5% Fund Return** | **Class A** |
|---|---|
| Beginning Account Value 7/1/10 | $1,000.00 |
| Ending Account Value 12/31/10 | $1,023.34 |
| Expenses Paid per $1,000* | $ 1.89 |

* *Expenses are equal to the Fund's annualized expense ratio, multiplied by the average account value over the period, multiplied by the number of days in the most recent six-month period, then divided by 365.*

| **Annualized Expense Ratio** | **Class A** |
|---|---|
| DWS Variable Series II — DWS Money Market VIP | .37% |

For more information, please refer to the Fund's prospectus.

These tables do not reflect charges and fees ("contract charges") associated with the separate account that invests in the Fund or any variable life insurance policy or variable annuity contract for which the Fund is an investment option.

## DWS Money Market VIP

At the start of 2010, the money market yield curve began to change configuration as — for the first time in 12 months — short-term money market rates rose somewhat.[1] The slight increase in rates came in response to several market dynamics, including Congress's raising of the nation's debt ceiling and political and budgetary concerns within peripheral countries in the Eurozone.[2] By mid-June, the crisis in Europe had eased somewhat as the European Central Bank and the International Monetary Fund collaborated in order to offer loans and liquidity facilities to banks in fiscally troubled countries such as Greece, Spain and Italy. In September, investors responded positively to US Federal Reserve Board (the Fed) Chairman Bernanke's statement that the Fed would take additional steps in the form of "quantitative easing" to prop up the US economy as needed. By the close of the year, the Treasury yield curve began to steepen — as fixed-income issues sold off — in response to improved economic data and investor anxiety over possible inflationary pressures.

During the 12-month period ended December 31, 2010, the Fund provided a total return of 0.01% (Class A shares, unadjusted for contract charges), compared with the 0.01% average return for the 102 funds in the Lipper Money Market Variable Annuity Funds category for the same period, according to Lipper Inc.

We were able to maintain a competitive yield for the Fund during the period. (All performance is historical and does not guarantee future results. Yields fluctuate and are not guaranteed.) Over the period, we continued to hold a large percentage of fixed-rate, short-maturity investments. The Fund also held a percentage in floating-rate securities (whose yields adjust periodically in response to changes in interest rates) to track any increases in LIBOR rate levels.[3] Lastly, any investments the Fund has made in slightly longer maturities have been in Treasury, agency and top-quality corporate money market securities. The Fund holds a significant amount of its short-term liquidity in overnight and 7-day investments.

A group of investment professionals is responsible for the day-to-day management of the Fund. These investment professionals have a broad range of experience managing money market funds.

*The Lipper Money Market Variable Annuity Funds category includes funds that invest in high-quality financial instruments rated in the top two grades with dollar-weighted average maturities of less than 90 days, and that intend to keep a constant net asset value. It is not possible to invest directly in a Lipper category. For the 1-, 3-, 5- and 10-year periods, this category's average return was 0.01% (102 funds), 0.81% (99 funds), 2.34% (96 funds) and 2.11% (76 funds), respectively, as of 12/31/10.*

1 *The yield curve is a graphical representation of how yields on bonds of different maturities compare. Normally, yield curves slant up, as bonds with longer maturities typically offer higher yields than short-term bonds.*

2 *The Eurozone refers to a currency union among the European Union member states that have adopted the euro as their sole currency.*

3 *LIBOR, or the London Interbank Offered Rate, is the most widely used benchmark or reference rate for short-term interest rates. LIBOR is the rate of interest at which banks borrow funds from other banks, in large volume, in the international market.*

*Portfolio management market commentary is as of December 31, 2010, and may not come to pass. This information is subject to change at any time based on market and other conditions. Past performance does not guarantee future results. Current and future portfolio holdings are subject to risk.*

# Portfolio Summary

## DWS Money Market VIP

| **Asset Allocation** (As a % of Investment Portfolio) | **12/31/10** | **12/31/09** |
|---|---|---|
| Commercial Paper | 31% | 33% |
| Short-Term Notes | 21% | 21% |
| Repurchase Agreements | 20% | 13% |
| Government & Agency Obligations | 14% | 10% |
| Certificates of Deposit and Bank Notes | 14% | 22% |
| Supranational | — | 1% |
| | 100% | 100% |

| **Weighted Average Maturity*** | | |
|---|---|---|
| DWS Variable Series II — DWS Money Market VIP | 51 days | 48 days |
| First Tier Retail Money Fund Average | 39 days | 47 days |

* *The Fund is compared to its respective iMoneyNet Category: First Tier Retail Money Fund Average — Category includes a widely recognized composite of money market funds that invest in only first tier (highest rating) securities. Portfolio Holdings of First Tier funds include US Treasury, US Other, Repos, Time Deposits, Domestic Bank Obligations, Foreign Bank Obligations, First Tier Commercial Paper, Floating Rate Notes and Asset Backed Commercial Paper.*

*Weighted average maturity, also known as effective maturity, is the weighted average of the bonds held by the Fund taking into consideration any maturity shortening features.*

*Asset allocation and weighted average maturity are subject to change.*

*For more complete details about the Fund's investment portfolio, see page 6.*

Following the Fund's fiscal first and third quarter-end, a complete portfolio holdings listing is filed with the SEC on Form N-Q. In addition, each month, information about the Fund and its portfolio holdings is filed with the SEC on Form N-MFP. The SEC delays the public availability of the information filed on Form N-MFP for 60 days after the end of the reporting period included in the filing. These forms will be available on the SEC's Web site at www.sec.gov, and they may also be reviewed and copied at the SEC's Public Reference Room in Washington, D.C. Information on the operation of the SEC's Public Reference Room may be obtained by calling (800) SEC-0330. The Fund's portfolio holdings are also posted on www.dws-investments.com from time to time. Please see the Fund's current prospectus for more information.

## DWS Money Market VIP

| | Principal Amount ($) | Value ($) |
|---|---|---|
| **Certificates of Deposit and Bank Notes 14.0%** | | |
| Abbey National Treasury Services PLC, 0.46%, 2/2/2011 | 2,000,000 | 2,000,000 |
| Banco Bilbao Vizcaya Argentaria SA, 0.5%, 2/14/2011 | 750,000 | 750,000 |
| Bank of Tokyo-Mitsubishi UFJ Ltd., 0.38%, 5/16/2011 | 2,000,000 | 2,000,000 |
| BNP Paribas: | | |
| 0.41%, 3/17/2011 | 800,000 | 800,017 |
| 0.55%, 5/13/2011 | 750,000 | 750,109 |
| 0.63%, 1/27/2011 | 1,500,000 | 1,500,000 |
| Credit Agricole SA, 0.3%, 1/19/2011 | 2,000,000 | 2,000,000 |
| Dexia Credit Local, 144A, 2.375%, 9/23/2011 | 665,000 | 673,485 |
| International Finance Corp., 3.0%, 11/15/2011 | 500,000 | 511,262 |
| KBC Bank NV: | | |
| 0.4%, 1/18/2011 | 1,000,000 | 1,000,000 |
| 0.4%, 1/19/2011 | 1,000,000 | 1,000,000 |
| Kommuninvest I Sverige, 0.55%, 4/19/2011 | 1,000,000 | 1,000,623 |
| Landeskreditbank Baden-Wuerttemberg Foerderbank, 2.5%, 2/14/2011 | 1,500,000 | 1,503,785 |
| Mizuho Corporate Bank Ltd., 0.3%, 3/7/2011 | 2,000,000 | 2,000,000 |
| Natixis, 0.3%, 1/20/2011 | 3,000,000 | 3,000,000 |
| Nordea Bank Finland PLC: | | |
| 0.26%, 1/12/2011 | 1,500,000 | 1,499,999 |
| 0.27%, 1/12/2011 | 2,000,000 | 2,000,000 |
| 0.44%, 6/30/2011 | 1,000,000 | 1,000,149 |
| Skandinaviska Enskilda Banken AB: | | |
| 0.29%, 1/4/2011 | 1,000,000 | 1,000,000 |
| 0.3%, 2/4/2011 | 1,000,000 | 1,000,000 |
| Societe Generale, 0.41%, 4/26/2011 | 900,000 | 900,000 |
| Sumitomo Mitsui Banking Corp.: | | |
| 0.3%, 1/31/2011 | 1,000,000 | 1,000,000 |
| 0.3%, 3/3/2011 | 2,000,000 | 2,000,000 |
| **Total Certificates of Deposit and Bank Notes** (Cost $30,889,429) | | **30,889,429** |

| | Principal Amount ($) | Value ($) |
|---|---|---|
| **Commercial Paper 30.7%** | | |
| **Issued at Discount**** | | |
| Abbey National North America LLC: | | |
| 0.455%, 2/1/2011 | 2,000,000 | 1,999,216 |
| 0.46%, 2/16/2011 | 1,000,000 | 999,412 |
| 0.9%, 1/19/2011 | 2,000,000 | 1,999,100 |
| Argento Variable Funding: | | |
| 144A, 0.32%, 2/4/2011 | 1,750,000 | 1,749,471 |
| 144A, 0.33%, 1/28/2011 | 1,500,000 | 1,499,629 |
| 144A, 0.36%, 2/9/2011 | 1,500,000 | 1,499,415 |
| 144A, 0.37%, 2/24/2011 | 700,000 | 699,612 |
| ASB Finance Ltd., 0.501%, 2/9/2011 | 1,200,000 | 1,199,350 |
| Banco Bilbao Vizcaya Argentaria SA: | | |
| 0.49%, 2/4/2011 | 1,200,000 | 1,199,445 |
| 0.5%, 2/16/2011 | 700,000 | 699,553 |
| 0.5%, 2/18/2011 | 600,000 | 599,600 |
| BNZ International Funding Ltd., 144A, 0.52%, 1/21/2011 | 2,500,000 | 2,499,278 |
| Caisse D'Amortissement de la Dette Sociale: | | |
| 0.25%, 2/7/2011 | 750,000 | 749,807 |
| 0.26%, 2/22/2011 | 800,000 | 799,700 |
| 0.26%, 3/15/2011 | 1,200,000 | 1,199,367 |
| Cancara Asset Securitisation LLC: | | |
| 144A, 0.3%, 1/10/2011 | 2,000,000 | 1,999,850 |
| 144A, 0.3%, 1/18/2011 | 2,000,000 | 1,999,717 |
| Google, Inc., 0.4%, 9/16/2011 | 800,000 | 797,707 |
| Grampian Funding LLC: | | |
| 144A, 0.3%, 2/11/2011 | 1,000,000 | 999,658 |
| 144A, 0.34%, 1/10/2011 | 1,000,000 | 999,915 |
| 144A, 0.36%, 2/3/2011 | 1,250,000 | 1,249,588 |
| 144A, 0.36%, 2/11/2011 | 1,500,000 | 1,499,385 |
| 144A, 0.37%, 2/17/2011 | 1,150,000 | 1,149,445 |
| 144A, 0.37%, 3/1/2011 | 1,500,000 | 1,499,090 |
| Johnson & Johnson: | | |
| 144A, 0.18%, 1/18/2011 | 800,000 | 799,932 |
| 144A, 0.22%, 4/7/2011 | 1,750,000 | 1,748,973 |
| Kells Funding LLC: | | |
| 144A, 0.3%, 3/18/2011 | 1,200,000 | 1,199,240 |
| 144A, 0.31%, 3/21/2011 | 2,000,000 | 1,998,639 |
| Kreditanstalt fuer Wiederaufbau: | | |
| 144A, 0.23%, 2/15/2011 | 800,000 | 799,770 |
| 144A, 0.245%, 2/24/2011 | 800,000 | 799,706 |
| Nieuw Amsterdam Receivables Corp., 144A, 0.27%, 1/6/2011 | 1,000,000 | 999,963 |
| NRW.Bank: | | |
| 0.27%, 1/4/2011 | 1,150,000 | 1,149,974 |
| 0.32%, 3/8/2011 | 1,350,000 | 1,349,208 |
| 0.42%, 3/31/2011 | 2,400,000 | 2,397,508 |
| 0.43%, 3/31/2011 | 750,000 | 749,203 |
| Oesterreichische Kontrollbank AG, 0.245%, 2/28/2011 | 800,000 | 799,684 |
| PepsiCo, Inc, 0.18%, 2/11/2011 | 2,300,000 | 2,299,529 |
| Regency Markets No. 1 LLC, 144A, 0.27%, 1/20/2011 | 2,375,000 | 2,374,662 |
| Romulus Funding Corp., 144A, 0.36%, 1/13/2011 | 2,000,000 | 1,999,760 |
| Santander Central Hispano Finance Delaware, Inc., 0.5%, 3/11/2011 | 1,350,000 | 1,348,706 |
| Shell International Finance BV: | | |
| 0.4%, 5/2/2011 | 800,000 | 798,924 |
| 0.5%, 2/4/2011 | 800,000 | 799,622 |
| Societe de Prise de Participation de l'Etat, 144A, 0.24%, 2/24/2011 | 800,000 | 799,712 |
| Societe Generale North America, Inc., 0.33%, 2/1/2011 | 1,000,000 | 999,716 |
| Standard Chartered Bank: | | |
| 0.3%, 2/22/2011 | 1,200,000 | 1,199,480 |
| 0.33%, 1/13/2011 | 2,000,000 | 1,999,780 |

*The accompanying notes are an integral part of the financial statements.*

| | Principal Amount ($) | Value ($) |
|---|---|---|
| Straight-A Funding LLC, 144A, 0.25%, 3/10/2011 | 1,200,000 | 1,199,433 |
| Swedbank AB, 0.31%, 1/5/2011 | 1,150,000 | 1,149,960 |
| Toyota Motor Credit Corp., 0.25%, 1/13/2011 | 2,000,000 | 1,999,833 |
| Victory Receivables Corp., 144A, 0.29%, 1/31/2011 | 2,200,000 | 2,199,468 |
| **Total Commercial Paper** (Cost $67,546,695) | | **67,546,695** |

## Short Term Notes* 21.3%

| | Principal Amount ($) | Value ($) |
|---|---|---|
| Abbey National Treasury Services PLC: | | |
| 0.439%, 3/7/2011 | 1,000,000 | 1,000,000 |
| 0.59%, 11/2/2011 | 1,000,000 | 1,000,000 |
| Australia & New Zealand Banking Group Ltd., 144A, 0.43%, 1/20/2012 | 1,200,000 | 1,200,000 |
| Bank of Nova Scotia: | | |
| 0.37%, 9/12/2011 | 800,000 | 800,000 |
| 0.45%, 12/8/2011 | 800,000 | 800,000 |
| Barclays Bank PLC: | | |
| 0.58%, 7/19/2011 | 2,000,000 | 2,000,000 |
| 0.66%, 4/21/2011 | 2,200,000 | 2,200,000 |
| BNP Paribas, 0.538%, 4/26/2011 | 1,800,000 | 1,800,000 |
| Canadian Imperial Bank of Commerce: | | |
| 0.28%, 5/12/2011 | 1,400,000 | 1,400,000 |
| 0.29%, 4/26/2011 | 1,000,000 | 1,000,000 |
| 0.46%, 4/26/2011 | 2,000,000 | 2,000,000 |
| Commonwealth Bank of Australia, 144A, 0.323%, 1/3/2011 | 1,380,000 | 1,380,000 |
| DnB NOR Bank ASA, 144A, 0.295%, 4/26/2011 | 1,500,000 | 1,500,000 |
| Intesa Sanpaolo SpA, 0.37%, 10/27/2011 | 1,000,000 | 1,000,000 |
| JPMorgan Chase Bank NA, 0.26%, 5/31/2011 | 1,300,000 | 1,300,000 |
| Kells Funding LLC, 144A, 0.4%, 12/1/2011 | 1,000,000 | 1,000,000 |
| National Australia Bank Ltd.: | | |
| 144A, 0.29%, 1/27/2011 | 1,000,000 | 1,000,000 |
| 0.322%, 6/10/2011 | 1,500,000 | 1,500,000 |
| Nordea Bank Finland PLC: | | |
| 0.589%, 10/14/2011 | 2,000,000 | 2,004,577 |
| 0.589%, 10/20/2011 | 2,000,000 | 2,004,688 |
| Rabobank Nederland NV: | | |
| 0.262%, 3/11/2011 | 1,800,000 | 1,800,000 |
| 144A, 1.79%, 4/7/2011 | 4,000,000 | 4,000,000 |
| Royal Bank of Canada: | | |
| 0.26%, 2/24/2011 | 675,000 | 675,000 |
| 0.41%, 8/12/2011 | 1,200,000 | 1,200,000 |
| Societe Generale: | | |
| 0.42%, 4/21/2011 | 900,000 | 900,000 |
| 0.42%, 5/19/2011 | 2,200,000 | 2,200,000 |
| Toronto-Dominion Bank, 0.265%, 2/4/2011 | 1,500,000 | 1,500,000 |
| Westpac Banking Corp.: | | |
| 0.289%, 4/14/2011 | 1,800,000 | 1,800,000 |
| 0.3%, 1/10/2011 | 1,300,000 | 1,300,000 |
| 0.307%, 6/1/2011 | 2,000,000 | 2,000,000 |
| 0.46%, 1/10/2012 | 1,500,000 | 1,500,000 |
| **Total Short Term Notes** (Cost $46,764,265) | | **46,764,265** |

## Government & Agency Obligations 14.2%

### Foreign Government Obligations 0.4%

| | Principal Amount ($) | Value ($) |
|---|---|---|
| Kingdom of Denmark, 2.75%, 11/15/2011 | 1,000,000 | **1,020,058** |

### Other Government Related (a) 1.0%

| | Principal Amount ($) | Value ($) |
|---|---|---|
| European Investment Bank: | | |
| 0.23%, 2/16/2011 | 800,000 | 799,765 |
| 2.625%, 5/16/2011 | 750,000 | 756,392 |
| 2.625%, 11/15/2011 | 600,000 | 611,562 |
| | | **2,167,719** |

### US Government Sponsored Agencies 5.4%

| | Principal Amount ($) | Value ($) |
|---|---|---|
| Federal Farm Credit Bank, 0.241%*, 11/2/2011 | 750,000 | 749,969 |
| Federal Home Loan Bank: | | |
| 0.24%, 10/28/2011 | 1,800,000 | 1,799,054 |
| 0.25%, 10/28/2011 | 750,000 | 749,949 |
| 0.269%**, 9/12/2011 | 2,500,000 | 2,495,237 |
| 0.4%, 1/4/2011 | 700,000 | 699,999 |
| 0.43%, 2/22/2011 | 800,000 | 800,002 |
| 0.54%, 5/24/2011 | 1,100,000 | 1,100,034 |
| Federal National Mortgage Association: | | |
| 0.161%*, 7/27/2011 | 1,200,000 | 1,199,551 |
| 0.284%**, 1/18/2011 | 1,500,000 | 1,499,787 |
| 4.68%, 6/15/2011 | 750,000 | 764,946 |
| | | **11,858,528** |

### US Treasury Obligations 7.4%

| | Principal Amount ($) | Value ($) |
|---|---|---|
| US Treasury Bills: | | |
| 0.16%**, 3/10/2011 | 2,000,000 | 1,999,396 |
| 0.217%**, 10/20/2011 | 1,000,000 | 998,236 |
| US Treasury Notes: | | |
| 1.0%, 9/30/2011 | 2,000,000 | 2,010,794 |
| 1.0%, 10/31/2011 | 1,000,000 | 1,006,244 |
| 1.125%, 6/30/2011 | 2,500,000 | 2,508,627 |
| 1.125%, 12/15/2011 | 1,200,000 | 1,209,364 |
| 4.5%, 2/28/2011 | 650,000 | 654,239 |
| 4.625%, 8/31/2011 | 1,800,000 | 1,851,794 |
| 4.625%, 10/31/2011 | 1,000,000 | 1,035,746 |
| 4.75%, 3/31/2011 | 2,300,000 | 2,325,601 |
| 5.125%, 6/30/2011 | 650,000 | 665,784 |
| | | **16,265,825** |
| **Total Government & Agency Obligations** (Cost $31,312,130) | | **31,312,130** |

## Repurchase Agreements 20.5%

| | Principal Amount ($) | Value ($) |
|---|---|---|
| Banc of America Securities LLC, 0.25%, dated 12/31/2010, to be repurchased at $20,526,652 on 1/3/2011 (b) | 20,526,224 | 20,526,224 |
| JPMorgan Securities, Inc., 0.17%, dated 12/31/2010, to be repurchased at $14,447,499 on 1/3/2011 (c) | 14,447,294 | 14,447,294 |
| JPMorgan Securities, Inc., 0.20%, dated 12/31/2010, to be repurchased at $8,000,133 on 1/3/2011 (d) | 8,000,000 | 8,000,000 |
| The Goldman Sachs & Co., 0.17%, dated 12/31/2010, to be repurchased at $2,000,028 on 1/3/2011 (e) | 2,000,000 | 2,000,000 |
| **Total Repurchase Agreements** (Cost $44,973,518) | | **44,973,518** |

*The accompanying notes are an integral part of the financial statements.*

| | % of Net Assets | Value ($) |
|---|---|---|
| **Total Investment Portfolio** (Cost $221,486,037)[†] | 100.7 | **221,486,037** |
| **Other Assets and Liabilities, Net** | (0.7) | **(1,569,492)** |
| **Net Assets** | 100.0 | **219,916,545** |

* *These securities are shown at their current rate as of December 31, 2010. Floating rate securities' yields vary with a designated market index or market rate, such as the coupon-equivalent of the US Treasury bill rate.*

** *Annualized yield at time of purchase; not a coupon rate.*

† *The cost for federal income tax purposes was $221,486,037.*

(a) *Government-backed debt issued by financial companies or government sponsored enterprises.*

(b) *Collateralized by $16,238,000 Federal National Mortgage Association, with various coupon rates from 5.0–7.25%, with various maturity dates of 5/11/2017–5/15/2030 with a value of $20,937,401.*

(c) *Collateralized by $23,120,000 US Treasury STRIPS, maturing on 5/15/2022 with a value of $14,737,612.*

(d) *Collateralized by $8,197,133 Federal National Mortgage Association, 1.75%, maturing on 8/25/2020 with a value of $8,172,037.*

(e) *Collateralized by $1,977,493 Federal Home Loan Mortgage Corp., with various coupon rates from 1.875–4.07%, with various maturity dates of 9/1/2015–6/1/2032 with a value of $2,040,000.*

*144A: Security exempt from registration under Rule 144A of the Securities Act of 1933. These securities may be resold in transactions exempt from registration, normally to qualified institutional buyers.*

*STRIPS: Separate Trading of Registered Interest and Principal Securities*

## Fair Value Measurements

*Various inputs are used in determining the value of the Fund's investments. These inputs are summarized in three broad levels. Level 1 includes quoted prices in active markets for identical securities. Level 2 includes other significant observable inputs (including quoted prices for similar securities, interest rates, prepayment speeds, and credit risk). Level 3 includes significant unobservable inputs (including the Fund's own assumptions in determining the fair value of investments). The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities. Securities held by a money market fund are reflected as Level 2 because the securities are valued at amortized cost (which approximates fair value) and, accordingly, the inputs used to determine value are not quoted prices in an active market.*

*The following is a summary of the inputs used as of December 31, 2010 in valuing the Fund's investments. For information on the Fund's policy regarding the valuation of investments, please refer to the Security Valuation section of Note A in the accompanying Notes to Financial Statements.*

| Assets | Level 1 | Level 2 | Level 3 | Total |
|---|---|---|---|---|
| Investments in Securities (f) | $ — | $ 176,512,519 | $ — | $ 176,512,519 |
| Repurchase Agreements | — | 44,973,518 | — | 44,973,518 |
| **Total** | **$ —** | **$ 221,486,037** | **$ —** | **$ 221,486,037** |

*There have been no transfers between Level 1 and Level 2 fair value measurements during the year ended December 31, 2010.*

(f) *See Investment Portfolio for additional detailed categorizations.*

*The accompanying notes are an integral part of the financial statements.*

# Statement of Assets and Liabilities

as of December 31, 2010

| Assets | | |
|---|---|---|
| Investments: | | |
| Investment in unaffiliated securities, valued at amortized cost | $ | 176,512,519 |
| Repurchase agreements, valued at amortized cost | | 44,973,518 |
| Total investments, valued at amortized cost | | 221,486,037 |
| Cash | | 14 |
| Receivable for Fund shares sold | | 60,705 |
| Due from Advisor | | 15,381 |
| Interest receivable | | 197,386 |
| Other assets | | 1,349 |
| Total assets | | 221,760,872 |

| Liabilities | | |
|---|---|---|
| Payable for Fund shares redeemed | | 1,754,575 |
| Distributions payable | | 1,007 |
| Other accrued expenses and payables | | 88,745 |
| Total liabilities | | 1,844,327 |
| **Net assets, at value** | **$** | **219,916,545** |

| Net Assets Consist of | | |
|---|---|---|
| Distributions in excess of net investment income | | (1,007) |
| Paid-in capital | | 219,917,552 |
| **Net assets, at value** | **$** | **219,916,545** |
| **Class A** | | |
| **Net Asset Value,** offering and redemption price per share ($219,916,545 ÷ 220,001,268 outstanding shares of beneficial interest, no par value, unlimited number of shares authorized) | **$** | **1.00** |

# Statement of Operations

for the year ended December 31, 2010

| Investment Income | | |
|---|---|---|
| Income: | | |
| Interest | $ | 862,229 |
| Expenses: | | |
| Management fee | | 704,427 |
| Administration fee | | 247,168 |
| Services to shareholders | | 1,924 |
| Custodian fee | | 27,571 |
| Professional fees | | 64,438 |
| Trustees' fee and expenses | | 10,980 |
| Reports to shareholders | | 60,076 |
| Other | | 13,636 |
| Total expenses | | 1,130,220 |
| Expense reductions | | (292,806) |
| Total expenses after expense reductions | | 837,414 |
| **Net investment income** | | **24,815** |
| **Net realized gain (loss)** | | **1,201** |
| **Net increase (decrease) in net assets resulting from operations** | **$** | **26,016** |

*The accompanying notes are an integral part of the financial statements.*

# Statement of Changes in Net Assets

| Increase (Decrease) in Net Assets | Years Ended December 31, 2010 | 2009 |
|---|---|---|
| Operations: | | |
| Net investment income | $ 24,815 | $ 1,242,942 |
| Net realized gain (loss) | 1,201 | 23,268 |
| Net increase (decrease) in net assets resulting from operations | 26,016 | 1,266,210 |
| Distributions to shareholders from: | | |
| Net investment income | | |
| Class A | (24,815) | (1,233,793) |
| Class B | — | (37) |
| Total distributions | $ (24,815) | $ (1,233,830) |
| Fund share transactions: | | |
| **Class A** | | |
| Proceeds from shares sold | 111,590,276 | 102,195,146 |
| Shares converted* | — | 41,096 |
| Reinvestment of distributions | 26,864 | 1,523,848 |
| Payments for shares redeemed | (161,340,354) | (231,903,870) |
| Net increase (decrease) in net assets from Class A share transactions | (49,723,214) | (128,143,780) |
| **Class B** | | |
| Proceeds from shares sold | — | 50 |
| Shares converted* | — | (41,096) |
| Reinvestment of distributions | — | 58 |
| Payments for shares redeemed | — | (49) |
| Net increase (decrease) in net assets from Class B share transactions | — | (41,037) |
| **Increase (decrease) in net assets** | (49,722,013) | (128,152,437) |
| Net assets at beginning of period | 269,638,558 | 397,790,995 |
| Net assets at end of period (including distributions in excess of net investment income of $1,007 and $16,402, respectively) | **$ 219,916,545** | **$ 269,638,558** |

| Other Information | | |
|---|---|---|
| **Class A** | | |
| Shares outstanding at beginning of period | 269,724,482 | 397,868,262 |
| Shares sold | 111,590,276 | 102,195,146 |
| Shares converted* | — | 41,096 |
| Shares issued to shareholders in reinvestment of distributions | 26,864 | 1,523,848 |
| Shares redeemed | (161,340,354) | (231,903,870) |
| Net increase (decrease) in Class A shares | (49,723,214) | (128,143,780) |
| Shares outstanding at end of period | **220,001,268** | **269,724,482** |
| **Class B** | | |
| Shares outstanding at beginning of period | — | 41,037 |
| Shares sold | — | 50 |
| Shares converted* | — | (41,096) |
| Shares issued to shareholders in reinvestment of distributions | — | 58 |
| Shares redeemed | — | (49) |
| Net increase (decrease) in Class B shares | — | (41,037) |
| Shares outstanding at end of period | **—** | **—** |

* *On February 3, 2009, Class B shares converted into Class A shares.*

*The accompanying notes are an integral part of the financial statements.*

# Financial Highlights

## Class A

| Years Ended December 31, | 2010 | 2009 | 2008 | 2007 | 2006 |
|---|---|---|---|---|---|
| **Selected Per Share Data** | | | | | |
| **Net asset value, beginning of period** | **$1.000** | **$1.000** | **$1.000** | **$1.000** | **$1.000** |
| *Income from investment operations:* | | | | | |
| Net investment income | .000* | .003 | .026 | .049 | .046 |
| **Total from investment operations** | .000* | .003 | .026 | .049 | .046 |
| *Less distributions from:* | | | | | |
| Net investment income | .000* | (.003) | (.026) | (.049) | (.046) |
| **Net asset value, end of period** | **$1.000** | **$1.000** | **$1.000** | **$1.000** | **$1.000** |
| Total Return (%) | .01[a] | .34 | 2.64[a] | 5.00[a] | 4.65[a] |
| **Ratios to Average Net Assets and Supplemental Data** | | | | | |
| Net assets, end of period ($ millions) | 220 | 270 | 398 | 355 | 294 |
| Ratio of expenses before expense reductions (%) | .46 | .43 | .52 | .46 | .52 |
| Ratio of expenses after expense reductions (%) | .34 | .43 | .50 | .45 | .51 |
| Ratio of net investment income (%) | .01 | .37 | 2.56 | 4.88 | 4.58 |

[a] *Total return would have been lower had certain expenses not been reduced.*

* *Amount is less than $.0005.*

# Notes to Financial Statements

## A. Organization and Significant Accounting Policies

DWS Variable Series II (the "Trust") is registered under the Investment Company Act of 1940, as amended (the "1940 Act"), as an open-end management investment company organized as a Massachusetts business trust. The Trust offers seventeen funds (hereinafter referred to individually as "Fund" or collectively as "Funds"). The Fund is classified as a diversified open-end management investment company.

The Trust's financial statements are prepared in accordance with accounting principles generally accepted in the United States of America which require the use of management estimates. Actual results could differ from those estimates. The policies described below are followed consistently by the Trust in the preparation of its financial statements.

**Security Valuation.** Various inputs are used in determining the value of the Fund's investments. These inputs are summarized in three broad levels. Level 1 includes quoted prices in active markets for identical securities. Level 2 includes other significant observable inputs (including quoted prices for similar securities, interest rates, prepayment speeds, and credit risk). Level 3 includes significant unobservable inputs (including the Fund's own assumptions in determining the fair value of investments). The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities.

The Fund values all securities utilizing the amortized cost method permitted in accordance with Rule 2a-7 under the 1940 Act and certain conditions therein. Under this method, which does not take into account unrealized capital gains or losses on securities, an instrument is initially valued at its cost and thereafter assumes a constant accretion/amortization rate to maturity of any discount or premium. Securities held by a money market fund are reflected as Level 2 because the securities are valued at amortized cost (which approximates fair value) and, accordingly, the inputs used to determine value are not quoted prices in an active market.

Disclosure about the classification of fair value measurements is included in a table following the Fund's Investment Portfolio.

**Repurchase Agreements.** The Fund may enter into repurchase agreements with certain banks and broker/dealers whereby the Fund, through its custodian or sub-custodian bank, receives delivery of the underlying securities, the amount of which at the time of purchase and each subsequent business day is required to be maintained at such a level that the value is equal to at least the principal amount of the repurchase price plus accrued interest. The custodian bank holds the collateral in a separate account until the agreement matures. If the value of the securities falls below the principal amount of the repurchase agreement plus accrued interest, the financial institution deposits additional collateral by the following business day. If the financial institution either fails to deposit the required additional collateral or fails to repurchase the securities as agreed, the Fund has the right to sell the securities and recover any resulting loss from the financial institution. If the financial institution enters into bankruptcy, the Fund's claim on the collateral may be subject to legal proceedings.

**Taxes.** The Fund's policy is to comply with the requirements of the Internal Revenue Code, as amended, which are applicable to regulated investment companies and to distribute all of its taxable income to its shareholders.

The Fund has reviewed the tax positions for the open tax years as of December 31, 2010 and has determined that no provision for income tax is required in the Fund's financial statements. The Fund's federal tax returns for the prior three fiscal years remain open subject to examination by the Internal Revenue Service.

**Distribution of Income and Gains.** Net realized gains from investment transactions, in excess of available capital loss carryforwards, would be taxable to the Fund if not distributed and, therefore, will be distributed to shareholders at least annually. Net investment income of the Fund is declared as a daily dividend and is distributed to shareholders monthly. The Fund may take into account capital gains and losses in its daily dividend declarations. The Fund may also make additional distributions for tax purposes if necessary.

The timing and characterization of certain income and capital gains distributions are determined annually in accordance with federal tax regulations which may differ from accounting principles generally accepted in the United States of America. As a result, net investment income (loss) and net realized gain (loss) on investment transactions for a reporting period may differ from distributions during such period. Accordingly, the Fund may periodically make reclassifications among certain of its capital accounts without impacting the net asset value of the Fund.

The tax character of distributions paid by the Fund is summarized as follows:

| Fund | Distributions from Ordinary Income ($)* Years Ended December 31, 2010 | 2009 |
|---|---|---|
| DWS Money Market VIP | 24,815 | 1,233,830 |

* *For tax purposes, short-term capital gain distributions are considered ordinary income distributions.*

**Expenses.** Expenses of the Trust arising in connection with a specific fund are allocated to that fund. Other Trust expenses which cannot be directly attributed to a fund are apportioned among the funds in the Trust.

**Contingencies.** In the normal course of business, the Fund may enter into contracts with service providers that contain general indemnification clauses. The Fund's maximum exposure under these arrangements is unknown as this would involve future claims that may be made against the Fund that have not yet been made. However, based on experience, the Fund expects the risk of loss to be remote.

**Other.** Investment transactions are accounted for on a trade date. Interest income is recorded on the accrual basis. Realized gains and losses from investment transactions are recorded on an identified cost basis. All discounts and premiums are accreted/amortized for both tax and financial reporting purposes for the Fund.

## B. Related Parties

**Management Agreement.** Under the Investment Management Agreement with Deutsche Investment Management Americas Inc. ("DIMA" or the "Advisor"), an indirect, wholly owned subsidiary of Deutsche Bank AG, the Advisor directs the investments of the Fund in accordance with its investment objectives, policies and restrictions. The Advisor determines the securities, instruments and other contracts relating to investments to be purchased, sold or entered into by the Fund.

Under the Investment Management Agreement with the Advisor, the fee is equivalent to the annual rates shown below of the Fund's average daily net assets, computed and accrued daily and payable monthly:

| Fund | Annual Management Fee Rate |
|---|---|
| DWS Money Market VIP | |
| $0–$500 million | .285% |
| next $500 million | .270% |
| next $1.0 billion | .255% |
| over $2.0 billion | .240% |

For the period from January 1, 2010 through April 30, 2010, the Advisor had contractually agreed to waive its fee and/or reimburse certain operating expenses to the extent necessary to maintain the operating expenses (excluding certain expenses such as extraordinary expenses, taxes, brokerage and interest expense) of the class as follows:

| Fund | Annual Rate |
|---|---|
| DWS Money Market VIP | |
| Class A | .44% |

For the period from May 1, 2010 through January 31, 2011, the Advisor has contractually agreed to waive its fee and/or reimburse certain operating expenses to the extent necessary to maintain the operating expenses (excluding certain expenses such as extraordinary expenses, taxes, brokerage and interest expense) of the class as follows:

| Fund | Annual Rate |
|---|---|
| DWS Money Market VIP | |
| Class A | .51% |

In addition, the Advisor has agreed to voluntarily waive additional expenses for the Fund. The waiver may be changed or terminated at any time without notice. Under this arrangement, the Advisor waived certain expenses of the Fund.

Accordingly, for the year ended December 31, 2010, the total management fee, management fee waived and effective management fee rate were as follows:

| Fund | Total Aggregated ($) | Waived ($) | Annual Effective Rate |
|---|---|---|---|
| DWS Money Market VIP | 704,427 | 292,096 | .17% |

**Administration Fee.** Pursuant to an Administrative Services Agreement, DIMA provides most administrative services to the Fund. For all services provided under the Administrative Services Agreement, the Fund pays DIMA an annual fee ("Administration Fee") of 0.10% of the Fund's average daily net assets, computed and accrued daily and payable monthly. For the year ended December 31, 2010, the Administration Fee was as follows:

| Fund | Total Aggregated ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS Money Market VIP | 247,168 | 19,561 |

**Service Provider Fees.** DWS Investments Service Company ("DISC"), an affiliate of the Advisor, is the transfer agent, dividend-paying agent and shareholder service agent for the Fund. Pursuant to a sub-transfer agency agreement between DISC and DST Systems, Inc. ("DST"), DISC has delegated certain transfer agent, dividend-paying agent and shareholder service agent functions to DST. DISC compensates DST out of the shareholder servicing fee it receives from the Fund. For the year ended December 31, 2010, the amounts charged to the Fund by DISC were as follows:

| Fund | Total Aggregated ($) | Waived ($) |
|---|---|---|
| DWS Money Market VIP Class A | 710 | 710 |

**Typesetting and Filing Service Fees.** Under an agreement with DIMA, DIMA is compensated for providing typesetting and certain regulatory filing services to the Fund. For the year ended December 31, 2010, the amount charged to the Fund by DIMA included in the Statement of Operations under "reports to shareholders" was as follows:

| Fund | Amount ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS Money Market VIP | 10,874 | 1,873 |

**Trustees' Fees and Expenses.** The Fund paid each Trustee not affiliated with the Advisor retainer fees plus specified amounts for various committee services and for the Board Chairperson.

## C. Ownership of the Fund

At December 31, 2010, the beneficial ownership in the Fund was as follows:

**DWS Money Market VIP:** Three Participating Insurance Companies were owners of record of 10% or more of the total outstanding Class A shares of the Fund, each owning 28%, 20% and 15%.

## D. Line of Credit

The Trust and other affiliated fund (the "Participants") share in a $450 million revolving credit facility provided by a syndication of banks. The Fund may borrow for temporary or emergency purposes, including the meeting of redemption requests that otherwise might require the untimely disposition of securities. The Participants are charged an annual commitment fee which is allocated based on net assets, among each of the Participants. Interest is calculated at a rate per annum equal to the sum of the Federal Funds Rate plus 1.25 percent plus if LIBOR exceeds the Federal Funds Rate the amount of such excess. The Fund may borrow up to a maximum of 33 percent of its net assets under the agreement:

# Report of Independent Registered Public Accounting Firm

**To the Board of Trustees and Shareholders of DWS Variable Series II:**

We have audited the accompanying statement of assets and liabilities of DWS Money Market VIP, one of the funds constituting the DWS Variable Series II (the "Trust"), including the investment portfolio, as of December 31, 2010, and the related statement of operations, the statement of changes in net assets and the financial highlights for each of the periods indicated therein. These financial statements and financial highlights are the responsibility of the Trust's management. Our responsibility is to express an opinion on these financial statements and financial highlights based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements and financial highlights are free of material misstatement. We were not engaged to perform an audit of the Trust's internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Trust's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements and financial highlights, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our procedures included confirmation of securities owned as of December 31, 2010, by correspondence with the custodian and brokers or by other appropriate auditing procedures where replies from brokers were not received. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements and financial highlights referred to above present fairly, in all material respects, the financial position of the aforementioned fund of the DWS Variable Series II at December 31, 2010, the results of its operations, the changes in its net assets and the financial highlights for each of the periods indicated therein, in conformity with U.S. generally accepted accounting principles.

Ernst + Young LLP

Boston, Massachusetts
February 14, 2011

## Tax Information

**(Unaudited)**

Please consult a tax advisor if you have questions about federal or state income tax laws, or on how to prepare your tax returns. If you have specific questions about your account, please contact your insurance provider.

## Proxy Voting

The Trust's policies and procedures for voting proxies for portfolio securities and information about how the Trust voted proxies related to its portfolio securities during the 12-month period ended June 30 are available on our Web site — www.dws-investments.com (click on "proxy voting" at the bottom of the page) — or on the SEC's Web site — www.sec.gov. To obtain a written copy of the Trust's policies and procedures without charge, upon request, call us toll free at (800) 728-3337.

# Investment Management Agreement Approval

## DWS Money Market VIP

The Board of Trustees, including the Independent Trustees, approved the renewal of your Fund's investment management agreement (the "Agreement") with Deutsche Investment Management Americas Inc. ("DWS") in September 2010.

In terms of the process that the Board followed prior to approving the Agreement, shareholders should know that:

- In September 2010, all but one of the Fund's Trustees were independent of DWS and its affiliates.
- The Trustees meet frequently to discuss fund matters. Each year, the Trustees dedicate substantial time to contract review matters. Over the course of several months, the Board's Contract Committee, in coordination with the Board's Fixed Income and Quant Oversight Committee, reviewed comprehensive materials received from DWS, independent third parties and independent counsel. These materials included an analysis of the Fund's performance, fees and expenses, and profitability compiled by the Fund's independent fee consultant. The Board also received extensive information throughout the year regarding performance of the Fund.
- The Independent Trustees regularly meet privately with their independent counsel to discuss contract review and other matters. In addition, the Independent Trustees were also advised by the Fund's independent fee consultant in the course of their review of the Fund's contractual arrangements and considered a comprehensive report prepared by the independent fee consultant in connection with their deliberations (the "IFC Report").
- In connection with reviewing the Agreement, the Board also reviewed the terms of the Fund's distribution agreement, administrative services agreement, transfer agency agreement and other material service agreements.
- Based on its evaluation of the information provided, the Contract Committee presented its findings and recommendations to the Independent Trustees as a group. The Independent Trustees reviewed the Contract Committee's findings and recommendations and presented their recommendations to the full Board.

In connection with the contract review process, the Contract Committee and the Board considered the factors discussed below, among others. The Board also considered that DWS and its predecessors have managed the Fund since its inception, and the Board believes that a long-term relationship with a capable, conscientious advisor is in the best interests of the Fund. The Board considered, generally, that shareholders chose to invest or remain invested in the Fund knowing that DWS managed the Fund, and that the Agreement was approved by the Fund's shareholders. DWS is part of Deutsche Bank, a major global banking institution that is engaged in a wide range of financial services. The Board believes that there are significant advantages to being part of a global asset management business that offers a wide range of investing expertise and resources, including hundreds of portfolio managers and analysts with research capabilities in many countries throughout the world.

While shareholders may focus primarily on fund performance and fees, the Fund's Board considers these and many other factors, including the quality and integrity of DWS's personnel and such other issues as back-office operations, fund valuations, and compliance policies and procedures.

**Nature, Quality and Extent of Services.** The Board considered the terms of the Agreement, including the scope of advisory services provided under the Agreement. The Board noted that, under the Agreement, DWS provides portfolio management services to the Fund and that, pursuant to a separate administrative services agreement, DWS provides administrative services to the Fund. The Board considered the experience and skills of senior management and investment personnel, the resources made available to such personnel, the ability of DWS to attract and retain high-quality personnel, and the organizational depth and stability of DWS. The Board reviewed the Fund's performance over short-term and long-term periods and compared those returns to various agreed-upon performance measures, including a peer universe compiled by the independent fee consultant using information supplied by Lipper Inc. ("Lipper"). The Board also noted that it has put into place a process of identifying "Focus Funds" (e.g., funds performing poorly relative to their benchmark or a peer universe compiled by iMoneyNet, Inc.), and receives more frequent reporting and information from DWS regarding such funds, along with DWS's remedial plans to address underperformance. The Board believes this process is an effective manner of identifying and addressing underperforming funds. Based on the information provided, the Board noted that for the one-, three- and five-year periods ended December 31, 2009, the Fund's gross performance (Class A shares) was in the 1st quartile of the applicable Lipper universe (the 1st quartile being the best performers and the 4th quartile being the worst performers).

On the basis of this evaluation and the ongoing review of investment results by the Board, the Board concluded that the nature, quality and extent of services provided by DWS historically have been and continue to be satisfactory.

**Fees and Expenses.** The Board considered the Fund's investment management fee schedule, operating expenses, and total expense ratios, and comparative information provided by Lipper and the independent fee consultant regarding investment management fee rates paid to other investment advisors by similar funds (1st quartile being the most favorable and 4th quartile being the least favorable). With respect to management fees paid to other investment advisors by similar funds, the Board noted that the contractual fee rates paid by the Fund, which include the 0.10% fee paid to DWS under the Fund's administrative services agreement, were lower than the median (2nd quartile) of the applicable Lipper peer group (based on Lipper data provided as of December 31, 2009). The Board noted that the Fund's Class A shares total (net) operating expenses were expected to be lower than the median (2nd quartile) of the applicable Lipper expense universe (based on Lipper data provided as of December 31, 2009, and analyzing Lipper expense universe Class A expenses less any applicable 12b-1 fees) ("Lipper Universe Expenses"). The Board considered the Fund's management fee rate as compared to fees charged by DWS and certain of its affiliates for comparable mutual funds and considered differences in fund and fee structures between DWS Funds. The Board also considered how the Fund's total (net) operating expenses compared to the total (net) operating expenses of a more customized peer group selected by Lipper (based on such factors as asset size). The Board also noted that the expense limitation agreed to by DWS helped to ensure that the Fund's total (net) operating expenses would remain competitive.

The information considered by the Board as part of its review of management fees included information regarding fees charged by DWS and its affiliates to similar institutional accounts and to similar funds offered primarily to European investors ("DWS Europe funds"), in each case as applicable. The Board observed that advisory fee rates for institutional accounts generally were lower than the management fees charged by similarly managed DWS US mutual funds ("DWS Funds"), but also took note of the differences in services provided to DWS Funds as compared to institutional accounts. In the case of DWS Europe funds, the Board observed that fee rates for DWS Europe funds generally were higher than for similarly managed DWS Funds, but noted that differences in the types of services provided to DWS Funds relative to DWS Europe funds made it difficult to compare such fees.

On the basis of the information provided, the Board concluded that management fees were reasonable and appropriate in light of the nature, quality and extent of services provided by DWS.

**Profitability.** The Board reviewed detailed information regarding revenues received by DWS under the Agreement. The Board considered the estimated costs and pre-tax profits realized by DWS from advising the DWS Funds, as well as estimates of the pre-tax profits attributable to managing the Fund in particular. The Board also received information regarding the estimated enterprise-wide profitability of DWS and its affiliates with respect to all fund services in totality and by fund. The Board reviewed DWS's methodology in allocating its costs to the management of the Fund. Based on the information provided, the Board concluded that the pre-tax profits realized by DWS in connection with the management of the Fund were not unreasonable. The Board also reviewed information regarding the profitability of certain similar investment management firms. The Board noted that while information regarding the profitability of such firms is limited (and in some cases is not necessarily prepared on a comparable basis), DWS and its affiliates' overall profitability with respect to the DWS fund complex (after taking into account distribution and other services provided to the funds by DWS and its affiliates) was lower than the overall profitability levels of many comparable firms for which such data was available.

**Economies of Scale.** The Board considered whether there are economies of scale with respect to the management of the Fund and whether the Fund benefits from any economies of scale. The Board noted that the Fund's management fee schedule includes fee breakpoints. The Board concluded that the Fund's fee schedule represents an appropriate sharing between the Fund and DWS of such economies of scale as may exist in the management of the Fund at current asset levels.

**Other Benefits to DWS and Its Affiliates.** The Board also considered the character and amount of other incidental benefits received by DWS and its affiliates, including any fees received by DWS for administrative services provided to the Fund and any fees received by an affiliate of DWS for distribution services. The Board also considered benefits to DWS related to brokerage and soft-dollar allocations, including allocating brokerage to pay for research generated by parties other than the executing broker dealers, which pertain primarily to funds investing in equity securities, along with the incidental public relations benefits to DWS related to DWS Funds advertising and cross-selling opportunities among DWS products and services. The Board concluded that management fees were reasonable in light of these fallout benefits.

**Compliance.** The Board considered the significant attention and resources dedicated by DWS to documenting and enhancing its compliance processes in recent years. The Board noted in particular (i) the experience and seniority of both DWS's chief compliance officer and the Fund's chief compliance officer; (ii) the large number of

DWS compliance personnel; and (iii) the substantial commitment of resources by DWS and its affiliates to compliance matters.

Based on all of the information considered and the conclusions reached, the Board unanimously (including the Independent Trustees) determined that the continuation of the Agreement is in the best interests of the Fund. In making this determination, the Board did not give particular weight to any single factor identified above. The Board considered these factors over the course of numerous meetings, certain of which were in executive session with only the Independent Trustees and their counsel present. It is possible that individual Trustees may have weighed these factors differently in reaching their individual decisions to approve the continuation of the Agreement.

# Summary of Management Fee Evaluation by Independent Fee Consultant

October 3, 2010

Pursuant to an Order entered into by Deutsche Investment Management Americas and affiliates (collectively, "DeAM") with the Attorney General of New York, I, Thomas H. Mack, have been appointed the Independent Fee Consultant for the DWS Funds (formerly the DWS Scudder Funds). My duties include preparing an annual written evaluation of the management fees DeAM charges the Funds, considering among other factors the management fees charged by other mutual fund companies for like services, management fees DeAM charges other clients for like services, DeAM's costs of supplying services under the management agreements and related profit margins, possible economies of scale if a Fund grows larger, and the nature and quality of DeAM's services, including fund performance. This report summarizes my evaluation for 2010, including my qualifications, the evaluation process for each of the DWS Funds, consideration of certain complex-level factors, and my conclusions. I served in substantially the same capacity in 2007, 2008, and 2009.

## Qualifications

For more than 35 years I have served in various professional capacities within the investment management business. I have held investment analysis and advisory positions, including securities analyst, portfolio strategist and director of investment policy with a large investment firm. I have also performed business management functions, including business development, financial management and marketing research and analysis.

Since 1991, I have been an independent consultant within the asset management industry. I have provided services to over 125 client organizations, including investment managers, mutual fund boards, product distributors and related organizations. Over the past ten years I have completed a number of assignments for mutual fund boards, specifically including assisting boards with management contract renewal.

I hold a Master of Business Administration degree, with highest honors, from Harvard University and Master of Science and Bachelor of Science (highest honors) degrees from the University of California at Berkeley. I am an independent director and audit committee financial expert for two closed-end mutual funds and have served in various leadership and financial oversight capacities with non-profit organizations.

## Evaluation of Fees for each DWS Fund

My work focused primarily on evaluating, fund-by-fund, the fees charged to each of the 118 publicly offered Fund portfolios in the DWS Fund family. For each Fund, I considered each of the key factors mentioned above, as well as any other relevant information. In doing so I worked closely with the Funds' Independent Directors in their annual contract renewal process, as well as in their approval of contracts for several new funds (documented separately).

In evaluating each Fund's fees, I reviewed comprehensive materials provided by or on behalf of DeAM, including expense information prepared by Lipper Analytical, comparative performance information, profitability data, manager histories, and other materials. I also accessed certain additional information from the Lipper and Morningstar databases and drew on my industry knowledge and experience.

To facilitate evaluating this considerable body of information, I prepared for each Fund a document summarizing the key data elements in each area as well as additional analytics discussed below. This made it possible to consider each key data element in the context of the others.

In the course of contract renewal, DeAM agreed to implement a number of fee and expense adjustments requested by the Independent Directors which will favorably impact future fees and expenses, and my evaluation includes the effects of these changes.

### Fees and Expenses Compared with Other Funds

The competitive fee and expense evaluation for each fund focused on two primary comparisons:

- The Fund's contractual management fee (the advisory fee plus the administration fee where applicable) compared with those of a group of typically 12–15 funds in the same Lipper investment category (e.g. Large Capitalization Growth) having similar distribution arrangements and being of similar size.
- The Fund's total expenses compared with a broader universe of funds from the same Lipper investment category and having similar distribution arrangements.

These two comparisons provide a view of not only the level of the fee compared with funds of similar scale but also the total expense the Fund bears for all the services it receives, in comparison with the investment choices available in the Fund's investment category and distribution channel. The principal figure-of-merit used in these comparisons was the subject Fund's percentile ranking against peers.

### DeAM's Fees for Similar Services to Others

DeAM provided management fee schedules for all of its US domiciled fund and non-fund investment management accounts in any of the investment categories where there is a DWS Fund. These similar products included the other DWS Funds, non-fund pooled accounts, institutional accounts and sub-advisory accounts. Using this information, I calculated for each Fund the fee that would be charged to each similar product, at the subject Fund's asset level.

Evaluating information regarding non-fund products is difficult because there are varying levels of services required for different types of accounts, with mutual funds generally requiring considerably more regulatory and administrative types of service as well as having more frequent cash flows than other types of accounts. Also, while mutual fund fees for similar fund products can be expected to be similar, there will be some differences due to different pricing conditions in different distribution channels (e.g. retail funds versus those used in variable insurance products), differences in underlying investment processes and other factors.

**Costs and Profit Margins**

DeAM provided a detailed profitability analysis for each Fund. After making some adjustments so that the presentation would be more comparable to the available industry figures, I reviewed profit margins from investment management alone, from investment management plus other fund services (excluding distribution) provided to the Funds by DeAM (principally shareholder services), and DeAM profits from all sources, including distribution. A later section comments on overall profitability.

**Economies of Scale**

Economies of scale — an expected decline in management cost per dollar of fund assets as fund assets grow — are very rarely quantified and documented because of inherent difficulties in collecting and analyzing relevant data. However, in virtually every investment category that I reviewed, larger funds tend to have lower fees and lower total expenses than smaller funds. To see how each DWS Fund compares with this industry observation, I reviewed:

- The trend in Fund assets over the last five years and the accompanying trend in total expenses. This shows if the Fund has grown and, if so, whether total expense (management fees as well as other expenses) have declined as a percent of assets.
- Whether the Fund has break-points in its management fee schedule, the extent of the fee reduction built into the schedule and the asset levels where the breaks take effect, and in the case of a sub-advised Fund how the Fund's break-points compare with those of the sub-advisory fee schedule.
- How the Fund's contractual fee schedule compares with trends in the industry data. To accomplish this, I constructed a chart showing how actual latest-fiscal-year contractual fees of the Fund and of other similar funds relate to average fund assets, with the subject Fund's contractual fee schedule superimposed.

**Quality of Service — Performance**

The quality-of-service evaluation focused on investment performance, which is the principal result of the investment management service. Each Fund's performance was reviewed over the past 1, 3, 5 and 10 years, as applicable, and compared with that of other funds in the same investment category and with a suitable market index.

In addition, I calculated and reviewed risk-adjusted returns relative to an index of similar mutual funds' returns and a suitable market index. The risk-adjusted returns analysis provides a way of determining the extent to which the Fund's return comparisons are mainly the product of investment value-added (or lack thereof) or alternatively taking considerably more or less risk than is typical in its investment category.

I also received and considered the history of portfolio manager changes for each Fund, as this provided an important context for evaluating the performance results.

## Complex-Level Considerations

While this evaluation was conducted mainly at the individual fund level, there are some issues relating to the reasonableness of fees that can alternatively be considered across the whole fund complex:

- I reviewed DeAM's profitability analysis for all DWS Funds, with a view toward determining if the allocation procedures used were reasonable and how profit levels compared with public data for other investment managers.
- I considered whether DeAM and affiliates receive any significant ancillary or "fall-out" benefits that should be considered in interpreting the direct profitability results. These would be situations where serving as the investment manager of the Funds is beneficial to another part of the Deutsche Bank organization.
- I considered how aggregated DWS Fund expenses had varied over the years, by asset class and in the context of trends in asset levels.
- I reviewed the structure of the DeAM organization, trends in staffing levels, and information on compensation of investment management and other professionals compared with industry data.

## Findings

Based on the process and analysis discussed above, which included reviewing a wide range of information from management and external data sources and considering among other factors the fees DeAM charges other clients, the fees charged by other fund managers, DeAM's costs and profits associated with managing the Funds, economies of scale, possible fall-out benefits, and the nature and quality of services provided, in my opinion the management fees charged the DWS Funds are reasonable.

Thomas H. Mack

Thomas H. Mack

# Summary of Administrative Fee Evaluation by Independent Fee Consultant

October 4, 2010

Pursuant to an Order entered into by Deutsche Asset Management (DeAM) with the Attorney General of New York, I, Thomas H. Mack, have been appointed the Independent Fee Consultant for the DWS Funds and have as part of my duties evaluated the reasonableness of a proposed pass-through to the funds of certain reporting costs associated with new regulations for money funds. My evaluation considered the following:

- My recently completed annual evaluation (please see my summary report of October 3, 2010), concluding that the prospective fees and expenses of all the DWS-sponsored money funds are reasonable.
- The fact that in my opinion the services DWS would provide under the combination of the Advisory and proposed Administration Agreements continues to be comparable with those typically provided to competitive funds under their management agreements.
- Management's analysis showing that the maximum total expense ratio impact of this change on any fund share class would be 1.3 basis points, which in my opinion is not material to my conclusions about the reasonableness of expenses.

Based on the foregoing considerations, in my opinion the proposed fees and expenses for the affected DWS-sponsored money funds are reasonable.

Thomas H. Mack

# Board Members and Officers

The following table presents certain information regarding the Board Members and Officers of the Trust as of December 31, 2010. Each Board Member's year of birth is set forth in parentheses after his or her name. Unless otherwise noted, (i) each Board Member has engaged in the principal occupation(s) noted in the table for at least the most recent five years, although not necessarily in the same capacity; and (ii) the address of each Independent Board Member is c/o Paul K. Freeman, Independent Chairman, DWS Funds, PO Box 101833, Denver, CO 80250-1833. Except as otherwise noted below, the term of office for each Board Member is until the election and qualification of a successor, or until such Board Member sooner dies, resigns, is removed or as otherwise provided in the governing documents of the fund. Because the fund does not hold an annual meeting of shareholders, each Board Member will hold office for an indeterminate period. The Board Members may also serve in similar capacities with other funds in the fund complex. The Length of Time Served represents the year in which the Board Member joined the board of one or more DWS funds now overseen by the Board.

### Independent Board Members

| Name, Year of Birth, Position with the Fund and Length of Time Served[1] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Paul K. Freeman (1950)<br>Chairperson since 2009<br>Board Member since 1993 | Consultant, World Bank/Inter-American Development Bank; Executive and Governing Council of the Independent Directors Council (education committees); formerly, Project Leader, International Institute for Applied Systems Analysis (1998–2001); Chief Executive Officer, The Eric Group, Inc. (environmental insurance) (1986–1998) | 122 |
| John W. Ballantine (1946)<br>Board Member since 1999 | Retired; formerly, Executive Vice President and Chief Risk Management Officer, First Chicago NBD Corporation/The First National Bank of Chicago (1996–1998); Executive Vice President and Head of International Banking (1995–1996). Directorships: Healthways, Inc. (provider of disease and care management services); Portland General Electric (utility company); Stockwell Capital Investments PLC (private equity). Former Directorships: First Oak Brook Bancshares, Inc. and Oak Brook Bank; Prisma Energy International | 122 |
| Henry P. Becton, Jr. (1943)<br>Board Member since 1990 | Vice Chair and former President, WGBH Educational Foundation. Directorships: Association of Public Television Stations; Lead Director, Becton Dickinson and Company[3] (medical technology company); Lead Director, Belo Corporation[3] (media company); Public Radio International; Public Radio Exchange (PRX); The PBS Foundation. Former Directorships: Boston Museum of Science; American Public Television; Concord Academy; New England Aquarium; Mass. Corporation for Educational Telecommunications; Committee for Economic Development; Public Broadcasting Service | 122 |
| Dawn-Marie Driscoll (1946)<br>Board Member since 1987 | President, Driscoll Associates (consulting firm); Executive Fellow, Center for Business Ethics, Bentley University; formerly, Partner, Palmer & Dodge (1988–1990); Vice President of Corporate Affairs and General Counsel, Filene's (1978–1988). Directorships: Trustee of 22 open-end mutual funds managed by Sun Capital Advisers, Inc. (since 2007); Director of ICI Mutual Insurance Company (since 2007); Advisory Board, Center for Business Ethics, Bentley University; Trustee, Southwest Florida Community Foundation (charitable organization). Former Directorships: Investment Company Institute (audit, executive, nominating committees) and Independent Directors Council (governance, executive committees) | 122 |
| Keith R. Fox (1954)<br>Board Member since 1996 | Managing General Partner, Exeter Capital Partners (a series of private investment funds). Directorships: Progressive International Corporation (kitchen goods importer and distributor); BoxTop Media Inc. (advertising); The Kennel Shop (retailer); former Chairman, National Association of Small Business Investment Companies | 122 |
| Kenneth C. Froewiss (1945)<br>Board Member since 2001 | Adjunct Professor of Finance, NYU Stern School of Business (September 2009–present; Clinical Professor from 1997–September 2009); Member, Finance Committee, Association for Asian Studies (2002–present); Director, Mitsui Sumitomo Insurance Group (US) (2004–present); prior thereto, Managing Director, J.P. Morgan (investment banking firm) (until 1996) | 122 |
| Richard J. Herring (1946)<br>Board Member since 1990 | Jacob Safra Professor of International Banking and Professor, Finance Department, The Wharton School, University of Pennsylvania (since July 1972); Co-Director, Wharton Financial Institutions Center (since July 2000); Co-Chair, U.S. Shadow Financial Regulatory Committee; Executive Director, Financial Economists Roundtable; Director, Japan Equity Fund, Inc. (since September 2007), Thai Capital Fund, Inc. (since September 2007), Singapore Fund, Inc. (since September 2007); Independent Director of Barclays Bank Delaware (since September 2010). Formerly, Vice Dean and Director, Wharton Undergraduate Division (July 1995–June 2000); Director, Lauder Institute of International Management Studies (July 2000–June 2006) | 122 |
| William McClayton (1944)<br>Board Member since 2004+ | Private equity investor (since October 2009); previously, Managing Director, Diamond Management & Technology Consultants, Inc. (global consulting firm) (2001–2009); Directorship: Board of Managers, YMCA of Metropolitan Chicago; formerly: Senior Partner, Arthur Andersen LLP (accounting) (1966–2001); Trustee, Ravinia Festival | 122 |

| Name, Year of Birth, Position with the Fund and Length of Time Served[1] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Rebecca W. Rimel (1951)<br>Board Member since 1995 | President and Chief Executive Officer, The Pew Charitable Trusts (charitable organization) (1994 to present); Trustee, Thomas Jefferson Foundation (charitable organization) (1994 to present); Trustee, Executive Committee, Philadelphia Chamber of Commerce (2001–2007); Director, CardioNet, Inc.[2] (2009–present) (health care). Formerly, Executive Vice President, The Glenmede Trust Company (investment trust and wealth management) (1983–2004); Board Member, Investor Education (charitable organization) (2004–2005); Director, Viasys Health Care[2] (January 2007–June 2007); Trustee, Pro Publica (charitable organization) (2007–2010) | 122 |
| William N. Searcy, Jr. (1946)<br>Board Member since 1993 | Private investor since October 2003; Trustee of 22 open-end mutual funds managed by Sun Capital Advisers, Inc. (since October 1998). Formerly, Pension & Savings Trust Officer, Sprint Corporation[2] (telecommunications) (November 1989–September 2003) | 122 |
| Jean Gleason Stromberg (1943)<br>Board Member since 1997 | Retired. Formerly, Consultant (1997–2001); Director, Financial Markets US Government Accountability Office (1996–1997); Partner, Fulbright & Jaworski, L.L.P. (law firm) (1978–1996). Directorships: The William and Flora Hewlett Foundation. Former Directorships: Service Source, Inc., Mutual Fund Directors Forum (2002–2004), American Bar Retirement Association (funding vehicle for retirement plans) (1987–1990 and 1994–1996) | 122 |
| Robert H. Wadsworth (1940)<br>Board Member since 1999 | President, Robert H. Wadsworth & Associates, Inc. (consulting firm) (1983 to present); Director, The Phoenix Boys Choir Association | 125 |

## Interested Board Member and Officer[4]

| Name, Year of Birth, Position with the Trust/ Corporation and Length of Time Served[1,5] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Ingo Gefeke[7] (1967)<br>Board Member since 2010<br>Executive Vice President since 2010 | Managing Director[3], Deutsche Asset Management; Global Head of Distribution and Product Management, DWS Global Head of Trading and Securities Lending. Member of the Board of Directors of DWS Investment GmbH Frankfurt (since July 2009) and DWS Holding & Service GmbH Frankfurt (since January 2010); formerly, Global Chief Administrative Officer, Deutsche Asset Management (2004–2009); Global Chief Operating Officer, Global Transaction Banking, Deutsche Bank AG, New York (2001–2004); Chief Operating Officer, Global Banking Division Americas, Deutsche Bank AG, New York (1999–2001); Central Management, Global Banking Services, Deutsche Bank AG, Frankfurt (1998–1999); Relationship Management, Deutsche Bank AG, Tokyo, Japan (1997–1998) | 55 |

## Officers[4]

| Name, Year of Birth, Position with the Fund and Length of Time Served[5] | Principal Occupation(s) During Past 5 Years and Other Directorships Held |
|---|---|
| Michael G. Clark[6] (1965)<br>President, 2006–present | Managing Director[3], Deutsche Asset Management (2006–present); President of DWS family of funds; Director, ICI Mutual Insurance Company (since October 2007); formerly, Director of Fund Board Relations (2004–2006) and Director of Product Development (2000–2004), Merrill Lynch Investment Managers; Senior Vice President Operations, Merrill Lynch Asset Management (1999–2000) |
| John Millette[8] (1962)<br>Vice President and Secretary, 1999–present | Director[3], Deutsche Asset Management |
| Paul H. Schubert[6] (1963)<br>Chief Financial Officer, 2004–present<br>Treasurer, 2005–present | Managing Director[3], Deutsche Asset Management (since July 2004); formerly, Executive Director, Head of Mutual Fund Services and Treasurer for UBS Family of Funds (1998–2004); Vice President and Director of Mutual Fund Finance at UBS Global Asset Management (1994–1998) |
| Caroline Pearson[8] (1962)<br>Chief Legal Officer, April 2010–present | Managing Director[3], Deutsche Asset Management; formerly, Assistant Secretary for DWS family of funds (1997–2010) |
| Rita Rubin[9] (1970)<br>Assistant Secretary, 2009–present | Vice President and Counsel, Deutsche Asset Management (since October 2007); formerly, Vice President, Morgan Stanley Investment Management (2004–2007) |
| Paul Antosca[8] (1957)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management (since 2006); Vice President, The Manufacturers Life Insurance Company (U.S.A.) (1990–2006) |
| Jack Clark[8] (1967)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management (since 2007); formerly, Vice President, State Street Corporation (2002–2007) |

| Name, Year of Birth, Position with the Fund and Length of Time Served[5] | Principal Occupation(s) During Past 5 Years and Other Directorships Held |
|---|---|
| Diane Kenneally[8] (1966)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management |
| John Caruso[9] (1965)<br>Anti-Money Laundering Compliance Officer, 2010–present | Managing Director[3], Deutsche Asset Management |
| Robert Kloby[9] (1962)<br>Chief Compliance Officer, 2006–present | Managing Director[3], Deutsche Asset Management |

1 *The length of time served represents the year in which the Board Member joined the board of one or more DWS funds currently overseen by the Board.*

2 *A publicly held company with securities registered pursuant to Section 12 of the Securities Exchange Act of 1934.*

3 *Executive title, not a board directorship.*

4 *As a result of their respective positions held with the Advisor, these individuals are considered "interested persons" of the Advisor within the meaning of the 1940 Act. Interested persons receive no compensation from the fund.*

5 *The length of time served represents the year in which the officer was first elected in such capacity for one or more DWS funds.*

6 *Address: 100 Plaza One, Jersey City, NJ 07311.*

7 *Effective January 11, 2011, Mr. Gefeke, an interested Board Member and Executive Vice President, resigned from the fund's Board and as an officer.*

*The mailing address of Mr. Gefeke is 345 Park Avenue, New York, New York 10154. Mr. Gefeke was an interested Board Member of certain DWS funds by virtue of his positions with Deutsche Asset Management. As an interested person, Mr. Gefeke received no compensation from the fund.*

8 *Address: One Beacon Street, Boston, MA 02108.*

9 *Address: 60 Wall Street, New York, New York 10005.*

*The fund's Statement of Additional Information ("SAI") includes additional information about the Board Members. The SAI is available, without charge, upon request. If you would like to request a copy of the SAI, you may do so by calling the following toll-free number: (800) 728-3337.*

DWS Investments is part of Deutsche Bank's Asset Management division and, within the US, represents the retail asset management activities of Deutsche Bank AG, Deutsche Bank Trust Company Americas, Deutsche Investment Management Americas Inc. and DWS Trust Company.

The views expressed in this report reflect those of the portfolio managers only through the end of the period of the report as stated on the cover. The managers' views are subject to change at any time based on market and other conditions and should not be construed as a recommendation.

This information must be preceded or accompanied by a current prospectus.

Portfolio changes should not be considered recommendations for action by individual investors.

DWS Investments Distributors, Inc.
222 South Riverside Plaza
Chicago, IL 60606
(800) 621-1148

VS2MM-2 (2/11)

DWS INVESTMENTS
Deutsche Bank Group

DECEMBER 31, 2010

# ANNUAL REPORT

## DWS VARIABLE SERIES II

## DWS Small Cap Growth VIP

**This report must be preceded or accompanied by a prospectus. To obtain an additional prospectus or summary prospectus, if available, call (800) 728-3337 or your financial representative. We advise you to consider the Fund's objectives, risks, charges and expenses carefully before investing. The summary prospectus and prospectus contain this and other important information about the Fund. Please read the prospectus carefully before you invest.**

*Investments in variable insurance portfolios (VIPs) involve risk. Stocks may decline in value. Bond investments are subject to interest-rate and credit risks. When interest rates rise, bond prices generally fall. Credit risk refers to the ability of an issuer to make timely payments of principal and interest. Investing in derivatives entails special risks relating to liquidity, leverage and credit that may reduce returns and/or increased volatility. Investing in foreign securities, particularly those of emerging markets, presents certain risks, such as currency fluctuations, political and economic changes, and market risks. There are additional risks associated with investing in commodities, high-yield bonds, aggressive growth stocks, non-diversified/ concentrated funds and small- and mid-cap stocks which are more fully explained in the prospectuses. Please read the prospectus for more information.*

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*NOT FDIC/NCUA INSURED    NO BANK GUARANTEE    MAY LOSE VALUE    NOT A DEPOSIT*
*NOT INSURED BY ANY FEDERAL GOVERNMENT AGENCY*

DWS INVESTMENTS
Deutsche Bank Group

## DWS Small Cap Growth VIP

**All performance shown is historical, assumes reinvestment of all dividend and capital gain distributions and does not guarantee future results. Investment return and principal value fluctuate with changing market conditions so that, when redeemed, shares may be worth more or less than their original cost. Current performance may be lower or higher than the performance data quoted. Please contact your participating insurance company for the Fund's most recent month-end performance. Performance doesn't reflect charges and fees ("contract charges") associated with the separate account that invests in the Fund or any variable life insurance policy or variable annuity contract for which the Fund is an investment option. These charges and fees will reduce returns.**

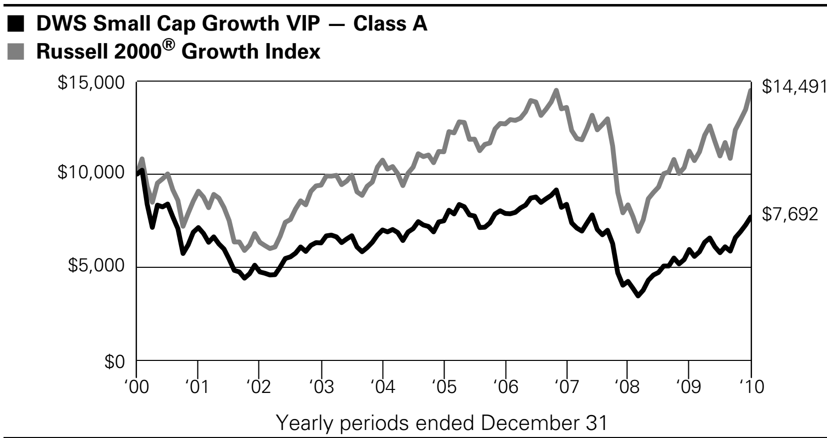
**The gross expense ratio of the Fund, as stated in the fee table of the prospectus dated May 1, 2010 is 0.77% for Class A shares and may differ from the expense ratio disclosed in the Financial Highlights table in this report.**

### Risk Considerations

Stocks of smaller companies involve greater risk than securities of larger, more-established companies. Stocks may decline in value. See the prospectus for details.

Fund returns shown for the 3-year, 5-year and 10-year periods reflect a fee waiver and/or expense reimbursement. Without this waiver/reimbursement, returns would have been lower.

### Growth of an Assumed $10,000 Investment in DWS Small Cap Growth VIP




*The Russell 2000® Growth Index is an unmanaged, capitalization-weighted measure of 2,000 of the smallest capitalized US companies with a greater-than-average growth orientation and whose common stocks trade on the NYSE, NYSE Alternext US (formerly known as "Amex") and Nasdaq.*

*Index returns assume reinvestment of dividends and, unlike fund returns, do not reflect any fees or expenses. It is not possible to invest directly into an index.*

### Comparative Results

| DWS Small Cap Growth VIP | | 1-Year | 3-Year | 5-Year | 10-Year |
|---|---|---|---|---|---|
| **Class A** | Growth of $10,000 | $12,944 | $9,190 | $10,274 | $7,692 |
| | Average annual total return | 29.44% | –2.77% | 0.54% | –2.59% |
| Russell 2000 Growth Index | Growth of $10,000 | $12,909 | $10,668 | $12,944 | $14,491 |
| | Average annual total return | 29.09% | 2.18% | 5.30% | 3.78% |

*The growth of $10,000 is cumulative.*

# Information About Your Fund's Expenses

## DWS Small Cap Growth VIP

As an investor of the Fund, you incur two types of costs: ongoing expenses and transaction costs. Ongoing expenses include management fees and other Fund expenses. Examples of transaction costs include contract charges, redemption fees and account maintenance fees, which are not shown in this section. The following tables are intended to help you understand your ongoing expenses (in dollars) of investing in the Fund and to help you compare these expenses with the ongoing expenses of investing in other mutual funds. The example in the table is based on an investment of $1,000 invested at the beginning of the six-month period and held for the entire period (July 1, 2010 to December 31, 2010).

The tables illustrate your Fund's expenses in two ways:

- **Actual Fund Return.** This helps you estimate the actual dollar amount of ongoing expenses (but not transaction costs) paid on a $1,000 investment in the Fund using the Fund's actual return during the period. To estimate the expenses you paid over the period, simply divide your account value by $1,000 (for example, an $8,600 account value divided by $1,000 = 8.6), then multiply the result by the number in the "Expenses Paid per $1,000" line under the share class you hold.
- **Hypothetical 5% Fund Return.** This helps you to compare your Fund's ongoing expenses (but not transaction costs) with those of other mutual funds using the Fund's actual expense ratio and a hypothetical rate of return of 5% per year before expenses. Examples using a 5% hypothetical Fund return may be found in the shareholder reports of other mutual funds. The hypothetical account values and expenses may not be used to estimate the actual ending account balance or expenses you paid for the period.

Please note that the expenses shown in these tables are meant to highlight your ongoing expenses only and do not reflect any transaction costs. The "Expenses Paid per $1,000" line of the tables is useful in comparing ongoing expenses only and will not help you determine the relative total expense of owning different funds. If these transaction costs had been included, your costs would have been higher.

**Expenses and Value of a $1,000 Investment** for the six months ended December 31, 2010

| **Actual Fund Return** | **Class A** |
|---|---|
| Beginning Account Value 7/1/10 | $1,000.00 |
| Ending Account Value 12/31/10 | $1,333.00 |
| Expenses Paid per $1,000* | $ 4.06 |
| **Hypothetical 5% Fund Return** | **Class A** |
| Beginning Account Value 7/1/10 | $1,000.00 |
| Ending Account Value 12/31/10 | $1,021.73 |
| Expenses Paid per $1,000* | $ 3.52 |

* *Expenses are equal to the Fund's annualized expense ratio, multiplied by the average account value over the period, multiplied by the number of days in the most recent six-month period, then divided by 365.*

| **Annualized Expense Ratio** | **Class A** |
|---|---|
| DWS Variable Series II — DWS Small Cap Growth VIP | .69% |

For more information, please refer to the Fund's prospectus.

These tables do not reflect charges and fees ("contract charges") associated with the separate account that invests in the Fund or any variable life insurance policy or variable annuity contract for which the Fund is an investment option.

## DWS Small Cap Growth VIP

The year 2010 began on an optimistic note with a few bright spots in the economy — improving consumer confidence, the government's report showing strong fourth-quarter 2009 gross domestic product GDP growth and a six-year high in manufacturing activity — partially offset by growing concerns about the health of the European financial system.[1] By May 2010, the US stock market had entered a period of significant volatility amid regulatory uncertainty (health care and financial reform) and fears of a possible double-dip recession. The market then staged a rebound during the last four months of the year amid increasing confidence that the US Federal Reserve Board's (the Fed's) second round of quantitative easing measures would support asset prices, along with evidence that the US economy was on a path to faster growth in 2011.

For the 12 months ended December 31, 2010, the Fund returned 29.44% (Class A shares, unadjusted for contract charges), compared with the 29.09% return of the Russell 2000® Growth Index. These strong returns belie the elevated level of investor risk aversion that impacted the global equity markets during much of the summer months as high unemployment, European debt problems, a possible economic "hard landing" within China and some slippage for US economic indicators temporarily dampened enthusiasm for stocks.

The Fund's outperformance of the benchmark came primarily from favorable stock selection. During the period, stock selection was positive within the health care, information technology and consumer staples sectors. Other contributions to return came from an overweight to energy and an underweight to telecom services.[2] Stock selection in energy and consumer discretionary detracted from performance. In addition, underweight positions in materials, information technology and consumer discretionary weighed on returns.

We continue to maintain a long-term perspective, investing in quality small-cap growth stocks. Effective on or about May 1, 2011, the name of the Fund will be changed to DWS Small Mid Cap Growth VIP. The Fund's investment objective will also change to long-term capital appreciation. For a description of the new investment objective, please see the supplement dated January 19, 2011 to the Fund's current prospectus posted on www.dws-investments.com.

Joseph Axtell, CFA
Rafaelina M. Lee
*Portfolio Managers*

*The Russell 2000 Growth Index is an unmanaged, capitalization-weighted measure of 2,000 of the smallest capitalized US companies with a greater-than-average growth orientation and whose common stocks trade on the NYSE, NYSE Alternext US (formerly known as "Amex") and Nasdaq.*

*Index returns assume reinvestment of dividends and, unlike funds returns, do not reflect any fees or expenses. It is not possible to invest directly into an index.*

1 *Gross domestic product is the value of goods and services produced in an economy.*

2 *"Overweight" means that a Fund holds a higher weighting in a given sector compared with its benchmark index. "Underweight" means that a Fund holds a lower weighting in a given sector.*

*Portfolio management market commentary is as of December 31, 2010, and may not come to pass. This information is subject to change at any time based on market and other conditions. Past performance does not guarantee future results. Current and future portfolio holdings are subject to risk.*

# Portfolio Summary

## DWS Small Cap Growth VIP

| **Asset Allocation** (As a % of Investment Portfolio excluding Securities Lending Collateral) | **12/31/10** | **12/31/09** |
|---|---|---|
| Common Stocks | 97% | 98% |
| Cash Equivalents | 3% | 2% |
| | 100% | 100% |

| **Sector Diversification** (As a % of Common Stocks) | **12/31/10** | **12/31/09** |
|---|---|---|
| Information Technology | 25% | 24% |
| Health Care | 20% | 17% |
| Consumer Discretionary | 16% | 16% |
| Industrials | 16% | 19% |
| Energy | 9% | 9% |
| Financials | 6% | 7% |
| Materials | 5% | 2% |
| Consumer Staples | 3% | 5% |
| Telecommunication Services | — | 1% |
| | 100% | 100% |

*Asset allocation and sector diversification are subject to change.*

*For more complete details about the Fund's investment portfolio, see page 6.*

Following the Fund's fiscal first and third quarter-end, a complete portfolio holdings listing is filed with the SEC on Form N-Q. The form will be available on the SEC's Web site at www.sec.gov, and it also may be reviewed and copied at the SEC's Public Reference Room in Washington, D.C. Information on the operation of the SEC's Public Reference Room may be obtained by calling (800) SEC-0330. The Fund's portfolio holdings are also posted on www.dws-investments.com from time to time. Please see the Fund's current prospectus for more information.

## DWS Small Cap Growth VIP

| | Shares | Value ($) |
|---|---|---|
| **Common Stocks 97.6%** | | |
| **Consumer Discretionary 15.9%** | | |
| **Auto Components 0.9%** | | |
| Gentex Corp. | 27,633 | **816,831** |
| **Diversified Consumer Services 0.6%** | | |
| Capella Education Co.* (a) | 7,900 | **525,982** |
| **Hotels Restaurants & Leisure 1.4%** | | |
| Buffalo Wild Wings, Inc.* | 18,902 | 828,853 |
| Red Robin Gourmet Burgers, Inc.* (a) | 18,900 | 405,783 |
| | | **1,234,636** |
| **Internet & Catalog Retail 0.2%** | | |
| Mecox Lane Ltd. (ADR)* (a) | 22,883 | **169,563** |
| **Media 1.4%** | | |
| Cinemark Holdings, Inc. | 70,334 | **1,212,558** |
| **Specialty Retail 8.5%** | | |
| Advance Auto Parts, Inc. | 19,700 | 1,303,155 |
| Children's Place Retail Stores, Inc.* | 23,300 | 1,156,612 |
| DSW, Inc. "A"* (a) | 39,161 | 1,531,195 |
| Guess?, Inc. | 31,500 | 1,490,580 |
| hhgregg, Inc.* (a) | 44,600 | 934,370 |
| Urban Outfitters, Inc.* | 31,821 | 1,139,510 |
| | | **7,555,422** |
| **Textiles, Apparel & Luxury Goods 2.9%** | | |
| Carter's, Inc.* (a) | 22,600 | 666,926 |
| Deckers Outdoor Corp.* (a) | 12,448 | 992,604 |
| True Religion Apparel, Inc.* (a) | 39,109 | 870,566 |
| | | **2,530,096** |
| **Consumer Staples 3.1%** | | |
| **Food Products** | | |
| Diamond Foods, Inc. (a) | 24,355 | 1,295,199 |
| Green Mountain Coffee Roasters, Inc.* (a) | 43,050 | 1,414,623 |
| | | **2,709,822** |
| **Energy 8.4%** | | |
| **Energy Equipment & Services 2.4%** | | |
| Complete Production Services, Inc.* | 26,075 | 770,516 |
| Dril-Quip, Inc.* | 17,678 | 1,373,934 |
| | | **2,144,450** |
| **Oil, Gas & Consumable Fuels 6.0%** | | |
| Carrizo Oil & Gas, Inc.* (a) | 36,299 | 1,251,952 |
| Clean Energy Fuels Corp.* | 27,300 | 377,832 |
| Cloud Peak Energy, Inc.* | 22,911 | 532,223 |
| Concho Resources, Inc.* | 11,469 | 1,005,487 |
| Northern Oil & Gas, Inc.* | 44,689 | 1,215,988 |
| Rosetta Resources, Inc.* | 24,500 | 922,180 |
| | | **5,305,662** |
| **Financials 5.7%** | | |
| **Capital Markets 1.3%** | | |
| Stifel Financial Corp.* (a) | 17,900 | **1,110,516** |
| **Commercial Banks 0.9%** | | |
| Prosperity Bancshares, Inc. | 21,100 | **828,808** |
| **Consumer Finance 1.9%** | | |
| Dollar Financial Corp.* (a) | 56,842 | **1,627,386** |

| | Shares | Value ($) |
|---|---|---|
| **Diversified Financial Services 1.6%** | | |
| Portfolio Recovery Associates, Inc.* (a) | 19,268 | **1,448,954** |
| **Health Care 19.6%** | | |
| **Biotechnology 5.6%** | | |
| Alexion Pharmaceuticals, Inc.* | 10,651 | 857,938 |
| Halozyme Therapeutics, Inc.* | 106,100 | 840,312 |
| Human Genome Sciences, Inc.* | 20,000 | 477,800 |
| ImmunoGen, Inc.* (a) | 65,600 | 607,456 |
| Onyx Pharmaceuticals, Inc.* | 12,559 | 463,051 |
| Regeneron Pharmaceuticals, Inc.* | 31,600 | 1,037,428 |
| United Therapeutics Corp.* | 10,600 | 670,132 |
| | | **4,954,117** |
| **Health Care Equipment & Supplies 3.4%** | | |
| Accuray, Inc.* | 88,274 | 595,850 |
| Kinetic Concepts, Inc.* | 23,700 | 992,556 |
| NxStage Medical, Inc.* | 19,107 | 475,382 |
| Thoratec Corp.* (a) | 32,500 | 920,400 |
| | | **2,984,188** |
| **Health Care Providers & Services 2.4%** | | |
| ExamWorks Group, Inc.* | 27,635 | 510,695 |
| Gentiva Health Services, Inc.* | 31,400 | 835,240 |
| Universal American Financial Corp. | 40,107 | 820,188 |
| | | **2,166,123** |
| **Health Care Technology 1.9%** | | |
| SXC Health Solutions Corp.* | 40,470 | **1,734,544** |
| **Life Sciences Tools & Services 1.2%** | | |
| ICON PLC (ADR)* | 27,058 | 592,570 |
| QIAGEN NV* (a) | 22,367 | 437,275 |
| | | **1,029,845** |
| **Pharmaceuticals 5.1%** | | |
| Auxilium Pharmaceuticals, Inc.* | 20,048 | 423,013 |
| Flamel Technologies SA (ADR)* (a) | 55,700 | 380,988 |
| Par Pharmaceutical Companies, Inc.* | 25,900 | 997,409 |
| Questcor Pharmaceuticals, Inc.* (a) | 146,192 | 2,153,408 |
| VIVUS, Inc.* (a) | 56,355 | 528,046 |
| | | **4,482,864** |
| **Industrials 15.7%** | | |
| **Aerospace & Defense 2.6%** | | |
| AAR Corp.* | 39,331 | 1,080,423 |
| BE Aerospace, Inc.* | 33,200 | 1,229,396 |
| | | **2,309,819** |
| **Commercial Services & Supplies 0.9%** | | |
| EnerNOC, Inc.* (a) | 34,100 | **815,331** |
| **Construction & Engineering 0.6%** | | |
| MYR Group, Inc.* | 23,600 | **495,600** |
| **Electrical Equipment 1.4%** | | |
| General Cable Corp.* (a) | 34,893 | **1,224,395** |
| **Machinery 6.1%** | | |
| Altra Holdings, Inc.* | 15,383 | 305,506 |
| Ampco-Pittsburgh Corp. | 21,334 | 598,419 |
| Badger Meter, Inc. (a) | 15,702 | 694,343 |
| Columbus McKinnon Corp.* | 28,675 | 582,676 |
| RBC Bearings, Inc.* | 32,677 | 1,277,017 |
| Sauer-Danfoss, Inc.* | 24,876 | 702,747 |
| Terex Corp.* | 39,400 | 1,222,976 |
| | | **5,383,684** |

*The accompanying notes are an integral part of the financial statements.*

| | Shares | Value ($) |
|---|---|---|
| **Professional Services 2.1%** | | |
| FTI Consulting, Inc.* (a) | 17,924 | 668,207 |
| TrueBlue, Inc.* | 68,240 | 1,227,637 |
| | | **1,895,844** |
| **Road & Rail 1.2%** | | |
| Genesee & Wyoming, Inc. "A"* | 19,456 | **1,030,195** |
| **Trading Companies & Distributors 0.8%** | | |
| United Rentals, Inc.* (a) | 30,937 | **703,817** |
| **Information Technology 24.2%** | | |
| **Communications Equipment 3.5%** | | |
| Aruba Networks, Inc.* | 15,850 | 330,948 |
| Comverse Technology, Inc.* | 64,655 | 469,395 |
| Polycom, Inc.* | 24,371 | 949,982 |
| Riverbed Technology, Inc.* (a) | 29,190 | 1,026,612 |
| Sycamore Networks, Inc. | 16,900 | 347,971 |
| | | **3,124,908** |
| **Electronic Equipment, Instruments & Components 0.8%** | | |
| Itron, Inc.* | 12,482 | **692,127** |
| **Internet Software & Services 3.5%** | | |
| Digital River, Inc.* | 29,245 | 1,006,613 |
| GSI Commerce, Inc.* | 35,526 | 824,203 |
| MercadoLibre, Inc.* | 12,509 | 833,725 |
| NIC, Inc. | 45,100 | 437,921 |
| | | **3,102,462** |
| **IT Services 6.9%** | | |
| Cardtronics, Inc.* | 42,700 | 755,790 |
| FleetCor Technologies, Inc.* | 19,144 | 591,932 |
| Forrester Research, Inc. | 40,300 | 1,422,187 |
| iGATE Corp. (a) | 67,043 | 1,321,418 |
| iSoftStone Holdings Ltd. (ADR)* | 25,781 | 468,441 |
| Syntel, Inc. | 18,437 | 881,104 |
| Telvent GIT SA* (a) | 25,117 | 663,591 |
| | | **6,104,463** |
| **Semiconductors & Semiconductor Equipment 3.5%** | | |
| Atheros Communications* | 12,405 | 445,588 |
| Cavium Networks, Inc.* (a) | 31,533 | 1,188,163 |
| Netlogic Microsystems, Inc.* (a) | 23,500 | 738,135 |
| Novellus Systems, Inc.* | 21,144 | 683,374 |
| | | **3,055,260** |
| **Software 6.0%** | | |
| CommVault Systems, Inc.* | 24,732 | 707,830 |
| Concur Technologies, Inc.* (a) | 26,337 | 1,367,681 |
| NICE Systems Ltd. (ADR)* | 23,649 | 825,350 |
| QLIK Technologies, Inc.* | 18,888 | 487,499 |
| Sourcefire, Inc.* | 15,400 | 399,322 |
| Taleo Corp. "A"* | 30,930 | 855,215 |
| TiVo, Inc.* | 30,084 | 259,625 |
| VanceInfo Technologies, Inc. (ADR)* | 12,021 | 415,205 |
| | | **5,317,727** |
| **Materials 5.0%** | | |
| **Chemicals 1.8%** | | |
| Solutia, Inc.* | 42,631 | 983,924 |
| STR Holdings, Inc.* (a) | 32,210 | 644,200 |
| | | **1,628,124** |
| **Metals & Mining 2.3%** | | |
| Molycorp, Inc.* (a) | 14,006 | 698,899 |
| Randgold Resources Ltd. (ADR) (a) | 3,100 | 255,223 |
| Thompson Creek Metals Co., Inc.* | 73,000 | 1,074,560 |
| | | **2,028,682** |
| **Paper & Forest Products 0.9%** | | |
| Schweitzer-Mauduit International, Inc. (a) | 12,681 | **797,889** |
| **Total Common Stocks** (Cost $58,328,703) | | **86,282,694** |

## Securities Lending Collateral 24.8%

| | | |
|---|---|---|
| Daily Assets Fund Institutional, 0.27% (b) (c) (Cost $21,950,973) | 21,950,973 | **21,950,973** |

## Cash Equivalents 2.9%

| | | |
|---|---|---|
| Central Cash Management Fund, 0.19% (b) (Cost $2,532,069) | 2,532,069 | **2,532,069** |

| | % of Net Assets | Value ($) |
|---|---|---|
| **Total Investment Portfolio** (Cost $82,811,745)† | 125.3 | **110,765,736** |
| **Other Assets and Liabilities, Net** | (25.3) | **(22,336,473)** |
| **Net Assets** | 100.0 | **88,429,263** |

* *Non-income producing security.*

† *The cost for federal income tax purposes was $83,216,134. At December 31, 2010, net unrealized appreciation for all securities based on tax cost was $27,549,602. This consisted of aggregate gross unrealized appreciation for all securities in which there was an excess of value over tax cost of $28,627,462 and aggregate gross unrealized depreciation for all securities in which there was an excess of tax cost over value of $1,077,860.*

(a) *All or a portion of these securities were on loan (see Notes to Financial Statements). The value of all securities loaned at December 31, 2010 amounted to $21,144,795, which is 23.9% of net assets.*

(b) *Affiliated fund managed by Deutsche Investment Management Americas Inc. The rate shown is the annualized seven-day yield at period end.*

(c) *Represents collateral held in connection with securities lending. Income earned by the Fund is net of borrower rebates.*

*ADR: American Depositary Receipt*

*The accompanying notes are an integral part of the financial statements.*

### Fair Value Measurements

*Various inputs are used in determining the value of the Fund's investments. These inputs are summarized in three broad levels. Level 1 includes quoted prices in active markets for identical securities. Level 2 includes other significant observable inputs (including quoted prices for similar securities, interest rates, prepayment speeds, and credit risk). Level 3 includes significant unobservable inputs (including the Fund's own assumptions in determining the fair value of investments). The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities.*

*The following is a summary of the inputs used as of December 31, 2010 in valuing the Fund's investments. For information on the Fund's policy regarding the valuation of investments, please refer to the Security Valuation section of Note A in the accompanying Notes to Financial Statements.*

| **Assets** | **Level 1** | **Level 2** | **Level 3** | **Total** |
|---|---|---|---|---|
| Common Stocks (d) | $ 86,282,694 | $ — | $ — | $ 86,282,694 |
| Short-Term Investments (d) | 24,483,042 | — | — | 24,483,042 |
| **Total** | **$ 110,765,736** | **$ —** | **$ —** | **$ 110,765,736** |

*There have been no significant transfers between Level 1 and Level 2 fair value measurements during the year ended December 31, 2010.*

(d) *See Investment Portfolio for additional detailed categorizations.*

*The accompanying notes are an integral part of the financial statements.*

# Statement of Assets and Liabilities

as of December 31, 2010

| **Assets** | | |
|---|---|---|
| Investments: | | |
| Investments in unaffiliated securities, at value (cost $58,328,703) — including $21,144,795 of securities loaned | $ | 86,282,694 |
| Investment in Daily Assets Fund Institutional (cost $21,950,973)* | | 21,950,973 |
| Investment in Central Cash Management Fund (cost $2,532,069) | | 2,532,069 |
| Total investments, at value (cost $82,811,745) | | 110,765,736 |
| Cash | | 10,000 |
| Receivable for Fund shares sold | | 105 |
| Dividends receivable | | 2,288 |
| Interest receivable | | 6,480 |
| Other assets | | 439 |
| Total assets | | 110,785,048 |

| **Liabilities** | | |
|---|---|---|
| Payable upon return of securities loaned | | 21,950,973 |
| Payable for Fund shares redeemed | | 272,959 |
| Accrued management fee | | 42,627 |
| Other accrued expenses and payables | | 89,226 |
| Total liabilities | | 22,355,785 |
| **Net assets, at value** | **$** | **88,429,263** |

| **Net Assets Consist of** | | |
|---|---|---|
| Undistributed net investment income | | 516,412 |
| Net unrealized appreciation (depreciation) on investments | | 27,953,991 |
| Accumulated net realized gain (loss) | | (42,803,640) |
| Paid-in capital | | 102,762,500 |
| **Net assets, at value** | **$** | **88,429,263** |
| **Class A** | | |
| **Net Asset Value,** offering and redemption price per share ($88,429,263 ÷ 6,384,947 outstanding shares of beneficial interest, no par value, unlimited number of shares authorized) | **$** | **13.85** |

* *Represents collateral on securities loaned.*

# Statement of Operations

for the year ended December 31, 2010

| **Investment Income** | | |
|---|---|---|
| Income: | | |
| Dividends (net of foreign taxes withheld of $1,244) | $ | 442,311 |
| Income distributions — Central Cash Management Fund | | 3,293 |
| Securities lending income, including income from Daily Assets Fund Institutional, net of borrower rebates | | 78,166 |
| Total income | | 523,770 |
| Expenses: | | |
| Management fee | | 434,077 |
| Administration fee | | 78,923 |
| Services to shareholders | | 4,365 |
| Custodian fee and other | | 10,831 |
| Legal fees | | 8,644 |
| Audit and tax fees | | 58,410 |
| Trustees' fees and expenses | | 5,538 |
| Reports to shareholders | | 10,959 |
| Total expenses | | 611,747 |
| **Net investment income (loss)** | | **(87,977)** |

| **Realized and Unrealized Gain (Loss)** | | |
|---|---|---|
| Net realized gain (loss) from investments | | 11,959,891 |
| Change in net unrealized appreciation (depreciation) on investments | | 8,823,086 |
| **Net gain (loss)** | | **20,782,977** |
| **Net increase (decrease) in net assets resulting from operations** | **$** | **20,695,000** |

*The accompanying notes are an integral part of the financial statements.*

# Statement of Changes in Net Assets

| Increase (Decrease) in Net Assets | Years Ended December 31, 2010 | 2009 |
|---|---|---|
| Operations: | | |
| Net investment income (loss) | $ (87,977) | $ (146,790) |
| Net realized gain (loss) | 11,959,891 | (20,542,495) |
| Change in net unrealized appreciation (depreciation) | 8,823,086 | 44,155,860 |
| Net increase (decrease) in net assets resulting from operations | 20,695,000 | 23,466,575 |
| Fund share transactions: | | |
| **Class A** | | |
| Proceeds from shares sold | 6,051,148 | 3,738,488 |
| Payments for shares redeemed | (17,902,129) | (17,049,742) |
| Shares converted* | — | 10,873 |
| Net increase (decrease) in net assets from Class A share transactions | (11,850,981) | (13,300,381) |
| **Class B** | | |
| Proceeds from shares sold | — | 244 |
| Payments for shares redeemed | — | (33) |
| Shares converted* | — | (10,873) |
| Net increase (decrease) in net assets from Class B share transactions | — | (10,662) |
| **Increase (decrease) in net assets** | 8,844,019 | 10,155,532 |
| Net assets at beginning of period | 79,585,244 | 69,429,712 |
| Net assets at end of period (including undistributed net investment income of $516,412 and accumulated net investment loss of $14,597, respectively) | **$ 88,429,263** | **$ 79,585,244** |

| Other Information | | |
|---|---|---|
| **Class A** | | |
| Shares outstanding at beginning of period | 7,439,067 | 9,122,504 |
| Shares sold | 517,480 | 442,413 |
| Shares redeemed | (1,571,600) | (2,127,728) |
| Shares converted* | — | 1,878 |
| Net increase (decrease) in Class A shares | (1,054,120) | (1,683,437) |
| Shares outstanding at end of period | **6,384,947** | **7,439,067** |
| **Class B** | | |
| Shares outstanding at beginning of period | — | 1,867 |
| Shares sold | — | 38 |
| Shares redeemed | — | (5) |
| Shares converted* | — | (1,900) |
| Net increase (decrease) in Class B shares | — | (1,867) |
| Shares outstanding at end of period | **—** | **—** |

* *On March 6, 2009, Class B shares converted into Class A shares.*

*The accompanying notes are an integral part of the financial statements.*

# Financial Highlights

## Class A

| Years Ended December 31, | 2010 | 2009 | 2008 | 2007 | 2006 |
|---|---|---|---|---|---|
| **Selected Per Share Data** | | | | | |
| **Net asset value, beginning of period** | **$10.70** | **$ 7.61** | **$15.07** | **$14.19** | **$13.48** |
| *Income (loss) from investment operations:* | | | | | |
| Net investment income (loss)[a] | (.01) | (.02) | (.01) | (.01) | (.04)[c] |
| Net realized and unrealized gain (loss) | 3.16 | 3.11 | (7.45) | .89 | .75 |
| **Total from investment operations** | 3.15 | 3.09 | (7.46) | .88 | .71 |
| **Net asset value, end of period** | **$13.85** | **$10.70** | **$ 7.61** | **$15.07** | **$14.19** |
| Total Return (%) | 29.44 | 40.60 | (49.50)[b] | 6.20[b] | 5.27[b,c] |
| **Ratios to Average Net Assets and Supplemental Data** | | | | | |
| Net assets, end of period ($ millions) | 88 | 80 | 69 | 174 | 208 |
| Ratio of expenses before expense reductions (%) | .78 | .77 | .88 | .75 | .73 |
| Ratio of expenses after expense reductions (%) | .78 | .77 | .85 | .72 | .72 |
| Ratio of net investment income (loss) (%) | (.12) | (.22) | (.04) | (.09) | (.32)[c] |
| Portfolio turnover rate (%) | 64 | 93 | 67 | 67 | 73 |

a *Based on average shares outstanding during the period.*

b *Total return would have been lower had certain expenses not been reduced.*

c *Includes non-recurring income from the Advisor recorded as a result of an administrative proceeding regarding disclosure of brokerage allocation practices in connection with sales of DWS Funds. The non-recurring income resulted in an increase in net investment income of $0.008 per share and an increase in the ratio of net investment income of 0.06%. Excluding this non-recurring income, total return would have been 0.06% lower.*

# Notes to Financial Statements

## A. Organization and Significant Accounting Policies

DWS Variable Series II (the "Trust") is registered under the Investment Company Act of 1940, as amended (the "1940 Act"), as an open-end management investment company organized as a Massachusetts business trust. The Trust offers seventeen funds (hereinafter referred to individually as "Fund" or collectively as "Funds"). The Fund is classified as a diversified open-end management investment company.

The Trust's financial statements are prepared in accordance with accounting principles generally accepted in the United States of America which require the use of management estimates. Actual results could differ from those estimates. The policies described below are followed consistently by the Trust in the preparation of its financial statements.

**Security Valuation.** Investments are stated at value determined as of the close of regular trading on the New York Stock Exchange on each day the exchange is open for trading.

Various inputs are used in determining the value of the Fund's investments. These inputs are summarized in three broad levels. Level 1 includes quoted prices in active markets for identical securities. Level 2 includes other significant observable inputs (including quoted prices for similar securities, interest rates, prepayment speeds, and credit risk). Level 3 includes significant unobservable inputs (including the Fund's own assumptions in determining the fair value of investments). The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities.

Equity securities are valued at the most recent sale price or official closing price reported on the exchange (US or foreign) or over-the-counter market on which they trade and are categorized as Level 1 securities. Securities for which no sales are reported are valued at the calculated mean between the most recent bid and asked quotations on the relevant market or, if a mean cannot be determined, at the most recent bid quotation. For certain international equity securities, in order to adjust for events which may occur between the close of the foreign exchanges and the close of the New York Stock Exchange, a fair valuation model may be used. This fair valuation model takes into account comparisons to the valuation of American Depository Receipts (ADRs), exchange-traded funds, futures contracts and certain indices and these securities are categorized as Level 2.

Money market instruments purchased with an original or remaining maturity of sixty days or less, maturing at par, are valued at amortized cost, which approximates value, and are categorized as Level 2. Investments in open-end investment companies are valued at their net asset value each business day and are categorized as Level 1.

Securities and other assets for which market quotations are not readily available or for which the above valuation procedures are deemed not to reflect fair value are valued in a manner that is intended to reflect their fair value as determined in accordance with procedures approved by the Board and are generally categorized as Level 3. In accordance with the Fund's valuation procedures, factors used in determining value may include, but are not limited to, the type of the security; the size of the holding; the initial cost of the security; the existence of any contractual restrictions on the security's disposition; the price and extent of public trading in similar securities of the issuer or of comparable companies; quotations or evaluated prices from broker-dealers and/or pricing services; information obtained from the issuer, analysts, and/or the appropriate stock exchange (for exchange-traded securities); an analysis of the company's or issuer's financial statements; an evaluation of the forces that influence the issuer and the market(s) in which the security is purchased and sold and with respect to debt securities; the maturity, coupon, creditworthiness, currency denomination and the movement of the market in which the security is normally traded. The value determined under these procedures may differ from published values for the same securities.

Disclosure about the classification of fair value measurements is included in a table following the Fund's Investment Portfolio.

**Securities Lending.** The Fund lends securities to certain financial institutions. The Fund retains beneficial ownership of the securities it has loaned and continues to receive interest and dividends paid by the issuer of securities and to participate in any changes in their market value. The Fund requires the borrowers of the securities to maintain collateral with the Fund consisting of either cash or liquid, unencumbered assets having a value at least equal to the value of the securities loaned. When the collateral falls below specified amounts, the lending agent will use its best effort to obtain additional collateral on the next business day to meet required amounts under the security lending agreement. The Fund may invest the cash collateral into a joint trading account in an affiliated money market fund pursuant to Exemptive Orders issued by the SEC. The Fund receives compensation for lending its securities either in the form of fees or by earning interest on invested cash collateral net of borrower rebates and fees paid to a lending agent. Either the Fund or the borrower may terminate the loan. There may be risks of delay and costs in recovery of securities or even loss of rights in the collateral should the borrower of the securities fail financially. The Fund is also subject to all investment risks associated with the reinvestment of any cash collateral received, including, but not limited to, interest rate, credit and liquidity risk associated with such investments.

**Taxes.** The Fund's policy is to comply with the requirements of the Internal Revenue Code, as amended, which are applicable to regulated investment companies and to distribute all of its taxable income to its shareholders.

At December 31, 2010, the Fund had an approximate net tax basis capital loss carryforward which may be applied against any realized net taxable capital gains of each succeeding year until fully utilized or until the following expiration dates, whichever occurs first:

| Fund | Capital Loss Carryforward ($) | Expiration Date | Capital Loss Carryforward Utilized ($) | Capital Loss Carryforward Expired ($) |
|---|---|---|---|---|
| DWS Small Cap Growth VIP | 8,113,000 | 12/31/2016 | 10,901,000 | 55,922,000 |
| | 34,287,000 | 12/31/2017 | | |

The Fund has reviewed the tax positions for the open tax years as of December 31, 2010 and has determined that no provision for income tax is required in the Fund's financial statements. The Fund's federal tax returns for the prior three fiscal years remain open subject to examination by the Internal Revenue Service.

**Distribution of Income and Gains.** Distributions of net investment income of the Fund, if any, are made annually. Net realized gains from investment transactions, in excess of available capital loss carryforwards, would be taxable to the Fund if not distributed and, therefore, will be distributed to shareholders at least annually. The Fund may also make additional distributions for tax purposes if necessary.

The timing and characterization of certain income and capital gains distributions are determined annually in accordance with federal tax regulations which may differ from accounting principles generally accepted in the United States of America. These differences primarily relate to net operating losses and certain securities sold at a loss. As a result, net investment income (loss) and net realized gain (loss) on investment transactions for a reporting period may differ significantly from distributions during such period. Accordingly, the Fund may periodically make reclassifications among certain of its capital accounts without impacting the net asset value of the Fund.

At December 31, 2010, the Fund's components of distributable earnings on a tax basis were as follows:

| Fund | Undistributed Ordinary Income ($)* | Capital Loss Carryforwards ($) | Unrealized Appreciation (Depreciation) on Investments ($) |
|---|---|---|---|
| DWS Small Cap Growth VIP | 516,412 | (42,400,000) | 27,549,602 |

* *For tax purposes, short-term capital gain distributions are considered ordinary income distributions.*

**Expenses.** Expenses of the Trust arising in connection with a specific fund are allocated to that fund. Other Trust expenses which cannot be directly attributed to a fund are apportioned among the funds in the Trust.

**Contingencies.** In the normal course of business, the Fund may enter into contracts with service providers that contain general indemnification clauses. The Fund's maximum exposure under these arrangements is unknown as this would involve future claims that may be made against the Fund that have not yet been made. However, based on experience, the Fund expects the risk of loss to be remote.

**Other.** Investment transactions are accounted for on a trade date plus one basis for daily net asset value calculations. However, for financial reporting purposes, investment transactions are reported on trade date. Interest income is recorded on the accrual basis. Dividend income is recorded on the ex-dividend date net of foreign withholding taxes. Realized gains and losses from investment transactions are recorded on an identified cost basis.

## B. Purchases and Sales of Securities

During the year ended December 31, 2010, purchases and sales of investment transactions (excluding short-term investments) were as follows:

| Fund | Purchases ($) | Sales ($) |
|---|---|---|
| DWS Small Cap Growth VIP | 49,541,542 | 62,144,300 |

## C. Related Parties

**Management Agreement.** Under the Investment Management Agreement with Deutsche Investment Management Americas Inc. ("DIMA" or the "Advisor"), an indirect, wholly owned subsidiary of Deutsche Bank AG, the Advisor directs the investments of the Fund in accordance with its investment objectives, policies and restrictions. The Advisor determines the securities, instruments and other contracts relating to investments to be purchased, sold or entered into by the Fund.

Under the Investment Management Agreement with the Advisor, the fee is equivalent to the annual rates shown below of the Fund's average daily net assets, computed and accrued daily and payable monthly:

| **Fund** | **Annual Management Fee Rate** |
|---|---|
| DWS Small Cap Growth VIP | |
| $0–$250 million | .550% |
| next $750 million | .525% |
| over $1 billion | .500% |

Accordingly, for the year ended December 31, 2010, the total management fee and effective management fee rate were as follows:

| **Fund** | **Total Aggregated ($)** | **Annual Effective Rate** |
|---|---|---|
| DWS Small Cap Growth VIP | 434,077 | .55% |

**Administration Fee.** Pursuant to an Administrative Services Agreement, DIMA provides most administrative services to the Fund. For all services provided under the Administrative Services Agreement, the Fund pays DIMA an annual fee ("Administration Fee") of 0.10% of the Fund's average daily net assets, computed and accrued daily and payable monthly. For the year ended December 31, 2010, the Administration Fee was as follows:

| **Fund** | **Total Aggregated ($)** | **Unpaid at December 31, 2010 ($)** |
|---|---|---|
| DWS Small Cap Growth VIP | 78,923 | 7,452 |

**Service Provider Fees.** DWS Investments Service Company ("DISC"), an affiliate of the Advisor, is the transfer agent, dividend-paying agent and shareholder service agent for the Fund. Pursuant to a sub-transfer agency agreement between DISC and DST Systems, Inc. ("DST"), DISC has delegated certain transfer agent, dividend-paying agent and shareholder service agent functions to DST. DISC compensates DST out of the shareholder servicing fee it receives from the Fund. For the year ended December 31, 2010, the amounts charged to the Fund by DISC were as follows:

| **Fund** | **Total Aggregated ($)** | **Unpaid at December 31, 2010 ($)** |
|---|---|---|
| DWS Small Cap Growth VIP Class A | 336 | 92 |

**Typesetting and Filing Service Fees.** Under an agreement with DIMA, DIMA is compensated for providing typesetting and certain regulatory filing services to the Fund. For the year ended December 31, 2010, the amount charged to the Fund by DIMA included in the Statement of Operations under "reports to shareholders" was as follows:

| **Fund** | **Amount ($)** | **Unpaid at December 31, 2010 ($)** |
|---|---|---|
| DWS Small Cap Growth VIP | 10,959 | 3,135 |

**Trustees' Fees and Expenses.** The Fund paid each Trustee not affiliated with the Advisor retainer fees plus specified amounts for various committee services and for the Board Chairperson.

**Affiliated Cash Management Vehicles.** The Fund may invest uninvested cash balances in Central Cash Management Fund, which is managed by the Advisor. The Fund indirectly bears their proportionate share of the expenses of the underlying money market funds. Central Cash Management Fund does not pay the Advisor an investment management fee. Central Cash Management Fund seeks a high level of current income consistent with liquidity and the preservation of capital.

## D. Ownership of the Fund

At December 31, 2010, the beneficial ownership in the Fund was as follows:

**DWS Small Cap Growth VIP:**Three Participating Insurance Companies were owners of record of 10% or more of the total outstanding Class A shares of the Fund, each owning 42%, 28% and 25%.

## E. Line of Credit

The Trust and other affiliated fund (the "Participants") share in a $450 million revolving credit facility provided by a syndication of banks. The Fund may borrow for temporary or emergency purposes, including the meeting of redemption requests that otherwise might require the untimely disposition of securities. The Participants are charged an annual commitment fee which is allocated based on net assets, among each of the Participants. Interest is calculated at a rate per annum equal to the sum of the Federal Funds Rate plus 1.25 percent plus if LIBOR exceeds the Federal Funds Rate the amount of such excess. The Fund may borrow up to a maximum of 33 percent of its net assets under the agreement.

## F. Subsequent Events

On January 12, 2011, the Board of the following Acquired Funds approved, in principle, the mergers of the Acquired Funds into the Acquiring Fund. Completion of the mergers is subject to a number of conditions. The mergers are expected to be completed on or about May 1, 2011.

| Acquired Funds | Acquiring Fund |
|---|---|
| DWS Variable Series II — DWS Mid Cap Growth VIP | DWS Variable Series II — DWS Small Cap Growth VIP |
| DWS Variable Series II — DWS Turner Mid Cap Growth VIP | DWS Variable Series II — DWS Small Cap Growth VIP |

In addition, on January 12, 2011, the Board approved changes to the name and strategy of the Fund. Effective on or about May 1, 2011, the Fund's investment objective will change from maximum appreciation of investors capital to long-term capital appreciation. In connection with the implementation of the new investment objective, the name of the Fund will change to DWS Small Mid Cap Growth VIP. In addition, the Russell 2500 Growth Index will replace the Russell 2000 Growth Index as the benchmark index because the Advisor believes that it better reflects the new investment strategy. For a description of the new investment objective, please see the supplement dated January 19, 2011 to the Fund's current prospectus posted on www.dws-investments.com.

# Report of Independent Registered Public Accounting Firm

**To the Board of Trustees and Shareholders of DWS Variable Series II:**

We have audited the accompanying statement of assets and liabilities of DWS Small Cap Growth VIP, one of the funds constituting the DWS Variable Series II (the "Trust"), including the investment portfolio, as of December 31, 2010, and the related statement of operations, the statement of changes in net assets and the financial highlights for each of the periods indicated therein. These financial statements and financial highlights are the responsibility of the Trust's management. Our responsibility is to express an opinion on these financial statements and financial highlights based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements and financial highlights are free of material misstatement. We were not engaged to perform an audit of the Trust's internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Trust's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements and financial highlights, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our procedures included confirmation of securities owned as of December 31, 2010, by correspondence with the custodian and brokers. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements and financial highlights referred to above present fairly, in all material respects, the financial position of the aforementioned fund of the DWS Variable Series II at December 31, 2010, the results of its operations, the changes in its net assets and the financial highlights for each of the periods indicated therein, in conformity with U.S. generally accepted accounting principles.

Ernst + Young LLP

Boston, Massachusetts
February 14, 2011

# Tax Information

**(Unaudited)**

Please consult a tax advisor if you have questions about federal or state income tax laws, or on how to prepare your tax returns. If you have specific questions about your account, please contact your insurance provider.

# Proxy Voting

The Trust's policies and procedures for voting proxies for portfolio securities and information about how the Trust voted proxies related to its portfolio securities during the 12-month period ended June 30 are available on our Web site — www.dws-investments.com (click on "proxy voting" at the bottom of the page) — or on the SEC's Web site — www.sec.gov. To obtain a written copy of the Trust's policies and procedures without charge, upon request, call us toll free at (800) 728-3337.

# Investment Management Agreement Approval

## DWS Small Cap Growth VIP

The Board of Trustees, including the Independent Trustees, approved the renewal of your Fund's investment management agreement (the "Agreement") with Deutsche Investment Management Americas Inc. ("DWS") in September 2010.

In terms of the process that the Board followed prior to approving the Agreement, shareholders should know that:

- In September 2010, all but one of the Fund's Trustees were independent of DWS and its affiliates.
- The Trustees meet frequently to discuss fund matters. Each year, the Trustees dedicate substantial time to contract review matters. Over the course of several months, the Board's Contract Committee, in coordination with the Board's Equity Oversight Committee, reviewed comprehensive materials received from DWS, independent third parties and independent counsel. These materials included an analysis of the Fund's performance, fees and expenses, and profitability compiled by the Fund's independent fee consultant. The Board also received extensive information throughout the year regarding performance of the Fund.
- The Independent Trustees regularly meet privately with their independent counsel to discuss contract review and other matters. In addition, the Independent Trustees were also advised by the Fund's independent fee consultant in the course of their review of the Fund's contractual arrangements and considered a comprehensive report prepared by the independent fee consultant in connection with their deliberations (the "IFC Report").
- In connection with reviewing the Agreement, the Board also reviewed the terms of the Fund's distribution agreement, administrative services agreement, transfer agency agreement and other material service agreements.
- Based on its evaluation of the information provided, the Contract Committee presented its findings and recommendations to the Independent Trustees as a group. The Independent Trustees reviewed the Contract Committee's findings and recommendations and presented their recommendations to the full Board.

In connection with the contract review process, the Contract Committee and the Board considered the factors discussed below, among others. The Board also considered that DWS and its predecessors have managed the Fund since its inception, and the Board believes that a long-term relationship with a capable, conscientious advisor is in the best interests of the Fund. The Board considered, generally, that shareholders chose to invest or remain invested in the Fund knowing that DWS managed the Fund, and that the Agreement was approved by the Fund's shareholders. DWS is part of Deutsche Bank, a major global banking institution that is engaged in a wide range of financial services. The Board believes that there are significant advantages to being part of a global asset management business that offers a wide range of investing expertise and resources, including hundreds of portfolio managers and analysts with research capabilities in many countries throughout the world.

While shareholders may focus primarily on fund performance and fees, the Fund's Board considers these and many other factors, including the quality and integrity of DWS's personnel and such other issues as back-office operations, fund valuations, and compliance policies and procedures.

**Nature, Quality and Extent of Services.** The Board considered the terms of the Agreement, including the scope of advisory services provided under the Agreement. The Board noted that, under the Agreement, DWS provides portfolio management services to the Fund and that, pursuant to a separate administrative services agreement, DWS provides administrative services to the Fund. The Board considered the experience and skills of senior management and investment personnel, the resources made available to such personnel, the ability of DWS to attract and retain high-quality personnel, and the organizational depth and stability of DWS. The Board reviewed the Fund's performance over short-term and long-term periods and compared those returns to various agreed-upon performance measures, including market indices and a peer universe compiled by the independent fee consultant using information supplied by Lipper Inc. ("Lipper"). The Board also noted that it has put into place a process of identifying "Focus Funds" (e.g., funds performing poorly relative to their benchmark or a peer universe compiled by Lipper), and receives more frequent reporting and information from DWS regarding such funds, along with DWS's remedial plans to address underperformance. The Board believes this process is an effective manner of identifying and addressing underperforming funds. Based on the information provided, the Board noted that for the one-, three- and five-year periods ended December 31, 2009, the Fund's performance (Class A shares) was in the 1st quartile, 4th quartile and 4th quartile, respectively, of the applicable Lipper universe (the 1st quartile being the best performers and the 4th quartile being the worst performers). The Board also observed that the Fund has outperformed its benchmark in the one-year period and has underperformed its benchmark in the three- and five-year periods ended December 31, 2009.

On the basis of this evaluation and the ongoing review of investment results by the Board, the Board concluded that the nature, quality and extent of services provided by DWS historically have been and continue to be satisfactory.

**Fees and Expenses.** The Board considered the Fund's investment management fee schedule, operating expenses, and total expense ratios, and comparative information provided by Lipper and the independent fee consultant regarding investment management fee rates paid to other investment advisors by similar funds (1st quartile being the most favorable and 4th quartile being the least favorable). With respect to management fees paid to other investment advisors by similar funds, the Board noted that the contractual fee rates paid by the Fund, which include the 0.10% fee paid to DWS under the Fund's administrative services agreement, were lower than the median (1st quartile) of the applicable Lipper peer group (based on Lipper data provided as of December 31, 2009). The Board noted that the Fund's Class A shares total (net) operating expenses were expected to be lower than the median (1st quartile) of the applicable Lipper expense universe (based on Lipper data provided as of December 31, 2009, and analyzing Lipper expense universe Class A expenses less any applicable 12b-1 fees) ("Lipper Universe Expenses"). The Board considered the Fund's management fee rate as compared to fees charged by DWS and certain of its affiliates for comparable mutual funds and considered differences in fund and fee structures between the DWS Funds. The Board also considered how the Fund's total (net) operating expenses compared to the total (net) operating expenses of a more customized peer group selected by Lipper (based on such factors as asset size).

The information considered by the Board as part of its review of management fees included information regarding fees charged by DWS and its affiliates to similar institutional accounts and to similar funds offered primarily to European investors ("DWS Europe funds"), in each case as applicable. The Board observed that advisory fee rates for institutional accounts generally were lower than the management fees charged by similarly managed DWS US mutual funds ("DWS Funds"), but also took note of the differences in services provided to DWS Funds as compared to institutional accounts. In the case of DWS Europe funds, the Board observed that fee rates for DWS Europe funds generally were higher than for similarly managed DWS Funds, but noted that differences in the types of services provided to DWS Funds relative to DWS Europe funds made it difficult to compare such fees.

On the basis of the information provided, the Board concluded that management fees were reasonable and appropriate in light of the nature, quality and extent of services provided by DWS.

**Profitability.** The Board reviewed detailed information regarding revenues received by DWS under the Agreement. The Board considered the estimated costs and pre-tax profits realized by DWS from advising the DWS Funds, as well as estimates of the pre-tax profits attributable to managing the Fund in particular. The Board also received information regarding the estimated enterprise-wide profitability of DWS and its affiliates with respect to all fund services in totality and by fund. The Board reviewed DWS's methodology in allocating its costs to the management of the Fund. Based on the information provided, the Board concluded that the pre-tax profits realized by DWS in connection with the management of the Fund were not unreasonable. The Board also reviewed information regarding the profitability of certain similar investment management firms. The Board noted that while information regarding the profitability of such firms is limited (and in some cases is not necessarily prepared on a comparable basis), DWS and its affiliates' overall profitability with respect to the DWS fund complex (after taking into account distribution and other services provided to the funds by DWS and its affiliates) was lower than the overall profitability levels of many comparable firms for which such data was available.

**Economies of Scale.** The Board considered whether there are economies of scale with respect to the management of the Fund and whether the Fund benefits from any economies of scale. The Board noted that the Fund's management fee schedule includes fee breakpoints. The Board concluded that the Fund's fee schedule represents an appropriate sharing between the Fund and DWS of such economies of scale as may exist in the management of the Fund at current asset levels.

**Other Benefits to DWS and Its Affiliates.** The Board also considered the character and amount of other incidental benefits received by DWS and its affiliates, including any fees received by DWS for administrative services provided to the Fund and any fees received by an affiliate of DWS for distribution services. The Board also considered benefits to DWS related to brokerage and soft-dollar allocations, including allocating brokerage to pay for research generated by parties other than the executing broker dealers, which pertain primarily to funds investing in equity securities, along with the incidental public relations benefits to DWS related to DWS Funds advertising and cross-selling opportunities among DWS products and services. The Board concluded that management fees were reasonable in light of these fallout benefits.

**Compliance.** The Board considered the significant attention and resources dedicated by DWS to documenting and enhancing its compliance processes in recent years. The Board noted in particular (i) the experience and seniority of both DWS's chief compliance officer and the Fund's chief compliance officer; (ii) the large number of

DWS compliance personnel; and (iii) the substantial commitment of resources by DWS and its affiliates to compliance matters.

Based on all of the information considered and the conclusions reached, the Board unanimously (including the Independent Trustees) determined that the continuation of the Agreement is in the best interests of the Fund. In making this determination, the Board did not give particular weight to any single factor identified above. The Board considered these factors over the course of numerous meetings, certain of which were in executive session with only the Independent Trustees and their counsel present. It is possible that individual Trustees may have weighed these factors differently in reaching their individual decisions to approve the continuation of the Agreement.

# Summary of Management Fee Evaluation by Independent Fee Consultant

October 3, 2010

Pursuant to an Order entered into by Deutsche Investment Management Americas and affiliates (collectively, "DeAM") with the Attorney General of New York, I, Thomas H. Mack, have been appointed the Independent Fee Consultant for the DWS Funds (formerly the DWS Scudder Funds). My duties include preparing an annual written evaluation of the management fees DeAM charges the Funds, considering among other factors the management fees charged by other mutual fund companies for like services, management fees DeAM charges other clients for like services, DeAM's costs of supplying services under the management agreements and related profit margins, possible economies of scale if a Fund grows larger, and the nature and quality of DeAM's services, including fund performance. This report summarizes my evaluation for 2010, including my qualifications, the evaluation process for each of the DWS Funds, consideration of certain complex-level factors, and my conclusions. I served in substantially the same capacity in 2007, 2008, and 2009.

## Qualifications

For more than 35 years I have served in various professional capacities within the investment management business. I have held investment analysis and advisory positions, including securities analyst, portfolio strategist and director of investment policy with a large investment firm. I have also performed business management functions, including business development, financial management and marketing research and analysis.

Since 1991, I have been an independent consultant within the asset management industry. I have provided services to over 125 client organizations, including investment managers, mutual fund boards, product distributors and related organizations. Over the past ten years I have completed a number of assignments for mutual fund boards, specifically including assisting boards with management contract renewal.

I hold a Master of Business Administration degree, with highest honors, from Harvard University and Master of Science and Bachelor of Science (highest honors) degrees from the University of California at Berkeley. I am an independent director and audit committee financial expert for two closed-end mutual funds and have served in various leadership and financial oversight capacities with non-profit organizations.

## Evaluation of Fees for each DWS Fund

My work focused primarily on evaluating, fund-by-fund, the fees charged to each of the 118 publicly offered Fund portfolios in the DWS Fund family. For each Fund, I considered each of the key factors mentioned above, as well as any other relevant information. In doing so I worked closely with the Funds' Independent Directors in their annual contract renewal process, as well as in their approval of contracts for several new funds (documented separately).

In evaluating each Fund's fees, I reviewed comprehensive materials provided by or on behalf of DeAM, including expense information prepared by Lipper Analytical, comparative performance information, profitability data, manager histories, and other materials. I also accessed certain additional information from the Lipper and Morningstar databases and drew on my industry knowledge and experience.

To facilitate evaluating this considerable body of information, I prepared for each Fund a document summarizing the key data elements in each area as well as additional analytics discussed below. This made it possible to consider each key data element in the context of the others.

In the course of contract renewal, DeAM agreed to implement a number of fee and expense adjustments requested by the Independent Directors which will favorably impact future fees and expenses, and my evaluation includes the effects of these changes.

### Fees and Expenses Compared with Other Funds

The competitive fee and expense evaluation for each fund focused on two primary comparisons:

- The Fund's contractual management fee (the advisory fee plus the administration fee where applicable) compared with those of a group of typically 12–15 funds in the same Lipper investment category (e.g. Large Capitalization Growth) having similar distribution arrangements and being of similar size.
- The Fund's total expenses compared with a broader universe of funds from the same Lipper investment category and having similar distribution arrangements.

These two comparisons provide a view of not only the level of the fee compared with funds of similar scale but also the total expense the Fund bears for all the services it receives, in comparison with the investment choices available in the Fund's investment category and distribution channel. The principal figure-of-merit used in these comparisons was the subject Fund's percentile ranking against peers.

### DeAM's Fees for Similar Services to Others

DeAM provided management fee schedules for all of its US domiciled fund and non-fund investment management accounts in any of the investment categories where there is a DWS Fund. These similar products included the other DWS Funds, non-fund pooled accounts, institutional accounts and sub-advisory accounts. Using this information, I calculated for each Fund the fee that would be charged to each similar product, at the subject Fund's asset level.

Evaluating information regarding non-fund products is difficult because there are varying levels of services required for different types of accounts, with mutual funds generally requiring considerably more regulatory and administrative types of service as well as having more frequent cash flows than other types of accounts. Also, while mutual fund fees for similar fund products can be expected to be similar, there will be some differences due to different pricing conditions in different distribution channels (e.g. retail funds versus those used in variable insurance products), differences in underlying investment processes and other factors.

### Costs and Profit Margins

DeAM provided a detailed profitability analysis for each Fund. After making some adjustments so that the presentation would be more comparable to the available industry figures, I reviewed profit margins from investment management alone, from investment management plus other fund services (excluding distribution) provided to the Funds by DeAM (principally shareholder services), and DeAM profits from all sources, including distribution. A later section comments on overall profitability.

### Economies of Scale

Economies of scale — an expected decline in management cost per dollar of fund assets as fund assets grow — are very rarely quantified and documented because of inherent difficulties in collecting and analyzing relevant data. However, in virtually every investment category that I reviewed, larger funds tend to have lower fees and lower total expenses than smaller funds. To see how each DWS Fund compares with this industry observation, I reviewed:

- The trend in Fund assets over the last five years and the accompanying trend in total expenses. This shows if the Fund has grown and, if so, whether total expense (management fees as well as other expenses) have declined as a percent of assets.
- Whether the Fund has break-points in its management fee schedule, the extent of the fee reduction built into the schedule and the asset levels where the breaks take effect, and in the case of a sub-advised Fund how the Fund's break-points compare with those of the sub-advisory fee schedule.
- How the Fund's contractual fee schedule compares with trends in the industry data. To accomplish this, I constructed a chart showing how actual latest-fiscal-year contractual fees of the Fund and of other similar funds relate to average fund assets, with the subject Fund's contractual fee schedule superimposed.

### Quality of Service — Performance

The quality-of-service evaluation focused on investment performance, which is the principal result of the investment management service. Each Fund's performance was reviewed over the past 1, 3, 5 and 10 years, as applicable, and compared with that of other funds in the same investment category and with a suitable market index.

In addition, I calculated and reviewed risk-adjusted returns relative to an index of similar mutual funds' returns and a suitable market index. The risk-adjusted returns analysis provides a way of determining the extent to which the Fund's return comparisons are mainly the product of investment value-added (or lack thereof) or alternatively taking considerably more or less risk than is typical in its investment category.

I also received and considered the history of portfolio manager changes for each Fund, as this provided an important context for evaluating the performance results.

## Complex-Level Considerations

While this evaluation was conducted mainly at the individual fund level, there are some issues relating to the reasonableness of fees that can alternatively be considered across the whole fund complex:

- I reviewed DeAM's profitability analysis for all DWS Funds, with a view toward determining if the allocation procedures used were reasonable and how profit levels compared with public data for other investment managers.
- I considered whether DeAM and affiliates receive any significant ancillary or "fall-out" benefits that should be considered in interpreting the direct profitability results. These would be situations where serving as the investment manager of the Funds is beneficial to another part of the Deutsche Bank organization.
- I considered how aggregated DWS Fund expenses had varied over the years, by asset class and in the context of trends in asset levels.
- I reviewed the structure of the DeAM organization, trends in staffing levels, and information on compensation of investment management and other professionals compared with industry data.

## Findings

Based on the process and analysis discussed above, which included reviewing a wide range of information from management and external data sources and considering among other factors the fees DeAM charges other clients, the fees charged by other fund managers, DeAM's costs and profits associated with managing the Funds, economies of scale, possible fall-out benefits, and the nature and quality of services provided, in my opinion the management fees charged the DWS Funds are reasonable.

Thomas H. Mack

# Board Members and Officers

The following table presents certain information regarding the Board Members and Officers of the Trust as of December 31, 2010. Each Board Member's year of birth is set forth in parentheses after his or her name. Unless otherwise noted, (i) each Board Member has engaged in the principal occupation(s) noted in the table for at least the most recent five years, although not necessarily in the same capacity; and (ii) the address of each Independent Board Member is c/o Paul K. Freeman, Independent Chairman, DWS Funds, PO Box 101833, Denver, CO 80250-1833. Except as otherwise noted below, the term of office for each Board Member is until the election and qualification of a successor, or until such Board Member sooner dies, resigns, is removed or as otherwise provided in the governing documents of the fund. Because the fund does not hold an annual meeting of shareholders, each Board Member will hold office for an indeterminate period. The Board Members may also serve in similar capacities with other funds in the fund complex. The Length of Time Served represents the year in which the Board Member joined the board of one or more DWS funds now overseen by the Board.

### Independent Board Members

| Name, Year of Birth, Position with the Fund and Length of Time Served[1] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Paul K. Freeman (1950)<br>Chairperson since 2009<br>Board Member since 1993 | Consultant, World Bank/Inter-American Development Bank; Executive and Governing Council of the Independent Directors Council (education committees); formerly, Project Leader, International Institute for Applied Systems Analysis (1998–2001); Chief Executive Officer, The Eric Group, Inc. (environmental insurance) (1986–1998) | 122 |
| John W. Ballantine (1946)<br>Board Member since 1999 | Retired; formerly, Executive Vice President and Chief Risk Management Officer, First Chicago NBD Corporation/The First National Bank of Chicago (1996–1998); Executive Vice President and Head of International Banking (1995–1996). Directorships: Healthways, Inc. (provider of disease and care management services); Portland General Electric (utility company); Stockwell Capital Investments PLC (private equity). Former Directorships: First Oak Brook Bancshares, Inc. and Oak Brook Bank; Prisma Energy International | 122 |
| Henry P. Becton, Jr. (1943)<br>Board Member since 1990 | Vice Chair and former President, WGBH Educational Foundation. Directorships: Association of Public Television Stations; Lead Director, Becton Dickinson and Company[3] (medical technology company); Lead Director, Belo Corporation[3] (media company); Public Radio International; Public Radio Exchange (PRX); The PBS Foundation. Former Directorships: Boston Museum of Science; American Public Television; Concord Academy; New England Aquarium; Mass. Corporation for Educational Telecommunications; Committee for Economic Development; Public Broadcasting Service | 122 |
| Dawn-Marie Driscoll (1946)<br>Board Member since 1987 | President, Driscoll Associates (consulting firm); Executive Fellow, Center for Business Ethics, Bentley University; formerly, Partner, Palmer & Dodge (1988–1990); Vice President of Corporate Affairs and General Counsel, Filene's (1978–1988). Directorships: Trustee of 22 open-end mutual funds managed by Sun Capital Advisers, Inc. (since 2007); Director of ICI Mutual Insurance Company (since 2007); Advisory Board, Center for Business Ethics, Bentley University; Trustee, Southwest Florida Community Foundation (charitable organization). Former Directorships: Investment Company Institute (audit, executive, nominating committees) and Independent Directors Council (governance, executive committees) | 122 |
| Keith R. Fox (1954)<br>Board Member since 1996 | Managing General Partner, Exeter Capital Partners (a series of private investment funds). Directorships: Progressive International Corporation (kitchen goods importer and distributor); BoxTop Media Inc. (advertising); The Kennel Shop (retailer); former Chairman, National Association of Small Business Investment Companies | 122 |
| Kenneth C. Froewiss (1945)<br>Board Member since 2001 | Adjunct Professor of Finance, NYU Stern School of Business (September 2009–present; Clinical Professor from 1997–September 2009); Member, Finance Committee, Association for Asian Studies (2002–present); Director, Mitsui Sumitomo Insurance Group (US) (2004–present); prior thereto, Managing Director, J.P. Morgan (investment banking firm) (until 1996) | 122 |
| Richard J. Herring (1946)<br>Board Member since 1990 | Jacob Safra Professor of International Banking and Professor, Finance Department, The Wharton School, University of Pennsylvania (since July 1972); Co-Director, Wharton Financial Institutions Center (since July 2000); Co-Chair, U.S. Shadow Financial Regulatory Committee; Executive Director, Financial Economists Roundtable; Director, Japan Equity Fund, Inc. (since September 2007), Thai Capital Fund, Inc. (since September 2007), Singapore Fund, Inc. (since September 2007); Independent Director of Barclays Bank Delaware (since September 2010). Formerly, Vice Dean and Director, Wharton Undergraduate Division (July 1995–June 2000); Director, Lauder Institute of International Management Studies (July 2000–June 2006) | 122 |
| William McClayton (1944)<br>Board Member since 2004+ | Private equity investor (since October 2009); previously, Managing Director, Diamond Management & Technology Consultants, Inc. (global consulting firm) (2001–2009); Directorship: Board of Managers, YMCA of Metropolitan Chicago; formerly: Senior Partner, Arthur Andersen LLP (accounting) (1966–2001); Trustee, Ravinia Festival | 122 |

| Name, Year of Birth, Position with the Fund and Length of Time Served[1] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Rebecca W. Rimel (1951) Board Member since 1995 | President and Chief Executive Officer, The Pew Charitable Trusts (charitable organization) (1994 to present); Trustee, Thomas Jefferson Foundation (charitable organization) (1994 to present); Trustee, Executive Committee, Philadelphia Chamber of Commerce (2001–2007); Director, CardioNet, Inc.[2] (2009–present) (health care). Formerly, Executive Vice President, The Glenmede Trust Company (investment trust and wealth management) (1983–2004); Board Member, Investor Education (charitable organization) (2004–2005); Director, Viasys Health Care[2] (January 2007–June 2007); Trustee, Pro Publica (charitable organization) (2007–2010) | 122 |
| William N. Searcy, Jr. (1946) Board Member since 1993 | Private investor since October 2003; Trustee of 22 open-end mutual funds managed by Sun Capital Advisers, Inc. (since October 1998). Formerly, Pension & Savings Trust Officer, Sprint Corporation[2] (telecommunications) (November 1989–September 2003) | 122 |
| Jean Gleason Stromberg (1943) Board Member since 1997 | Retired. Formerly, Consultant (1997–2001); Director, Financial Markets US Government Accountability Office (1996–1997); Partner, Fulbright & Jaworski, L.L.P. (law firm) (1978–1996). Directorships: The William and Flora Hewlett Foundation. Former Directorships: Service Source, Inc., Mutual Fund Directors Forum (2002–2004), American Bar Retirement Association (funding vehicle for retirement plans) (1987–1990 and 1994–1996) | 122 |
| Robert H. Wadsworth (1940) Board Member since 1999 | President, Robert H. Wadsworth & Associates, Inc. (consulting firm) (1983 to present); Director, The Phoenix Boys Choir Association | 125 |

## Interested Board Member and Officer[4]

| Name, Year of Birth, Position with the Trust/ Corporation and Length of Time Served[1,5] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Ingo Gefeke[7] (1967) Board Member since 2010 Executive Vice President since 2010 | Managing Director[3], Deutsche Asset Management; Global Head of Distribution and Product Management, DWS Global Head of Trading and Securities Lending. Member of the Board of Directors of DWS Investment GmbH Frankfurt (since July 2009) and DWS Holding & Service GmbH Frankfurt (since January 2010); formerly, Global Chief Administrative Officer, Deutsche Asset Management (2004–2009); Global Chief Operating Officer, Global Transaction Banking, Deutsche Bank AG, New York (2001–2004); Chief Operating Officer, Global Banking Division Americas, Deutsche Bank AG, New York (1999–2001); Central Management, Global Banking Services, Deutsche Bank AG, Frankfurt (1998–1999); Relationship Management, Deutsche Bank AG, Tokyo, Japan (1997–1998) | 55 |

## Officers[4]

| Name, Year of Birth, Position with the Fund and Length of Time Served[5] | Principal Occupation(s) During Past 5 Years and Other Directorships Held |
|---|---|
| Michael G. Clark[6] (1965) President, 2006–present | Managing Director[3], Deutsche Asset Management (2006–present); President of DWS family of funds; Director, ICI Mutual Insurance Company (since October 2007); formerly, Director of Fund Board Relations (2004–2006) and Director of Product Development (2000–2004), Merrill Lynch Investment Managers; Senior Vice President Operations, Merrill Lynch Asset Management (1999–2000) |
| John Millette[8] (1962) Vice President and Secretary, 1999–present | Director[3], Deutsche Asset Management |
| Paul H. Schubert[6] (1963) Chief Financial Officer, 2004–present Treasurer, 2005–present | Managing Director[3], Deutsche Asset Management (since July 2004); formerly, Executive Director, Head of Mutual Fund Services and Treasurer for UBS Family of Funds (1998–2004); Vice President and Director of Mutual Fund Finance at UBS Global Asset Management (1994–1998) |
| Caroline Pearson[8] (1962) Chief Legal Officer, April 2010–present | Managing Director[3], Deutsche Asset Management; formerly, Assistant Secretary for DWS family of funds (1997–2010) |
| Rita Rubin[9] (1970) Assistant Secretary, 2009–present | Vice President and Counsel, Deutsche Asset Management (since October 2007); formerly, Vice President, Morgan Stanley Investment Management (2004–2007) |
| Paul Antosca[8] (1957) Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management (since 2006); Vice President, The Manufacturers Life Insurance Company (U.S.A.) (1990–2006) |
| Jack Clark[8] (1967) Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management (since 2007); formerly, Vice President, State Street Corporation (2002–2007) |

| Name, Year of Birth, Position with the Fund and Length of Time Served[5] | Principal Occupation(s) During Past 5 Years and Other Directorships Held |
|---|---|
| Diane Kenneally[8] (1966)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management |
| John Caruso[9] (1965)<br>Anti-Money Laundering Compliance Officer, 2010–present | Managing Director[3], Deutsche Asset Management |
| Robert Kloby[9] (1962)<br>Chief Compliance Officer, 2006–present | Managing Director[3], Deutsche Asset Management |

1 *The length of time served represents the year in which the Board Member joined the board of one or more DWS funds currently overseen by the Board.*

2 *A publicly held company with securities registered pursuant to Section 12 of the Securities Exchange Act of 1934.*

3 *Executive title, not a board directorship.*

4 *As a result of their respective positions held with the Advisor, these individuals are considered "interested persons" of the Advisor within the meaning of the 1940 Act. Interested persons receive no compensation from the fund.*

5 *The length of time served represents the year in which the officer was first elected in such capacity for one or more DWS funds.*

6 *Address: 100 Plaza One, Jersey City, NJ 07311.*

7 *Effective January 11, 2011, Mr. Gefeke, an interested Board Member and Executive Vice President, resigned from the fund's Board and as an officer.*

*The mailing address of Mr. Gefeke is 345 Park Avenue, New York, New York 10154. Mr. Gefeke was an interested Board Member of certain DWS funds by virtue of his positions with Deutsche Asset Management. As an interested person, Mr. Gefeke received no compensation from the fund.*

8 *Address: One Beacon Street, Boston, MA 02108.*

9 *Address: 60 Wall Street, New York, New York 10005.*

*The fund's Statement of Additional Information ("SAI") includes additional information about the Board Members. The SAI is available, without charge, upon request. If you would like to request a copy of the SAI, you may do so by calling the following toll-free number: (800) 728-3337.*

DWS Investments is part of Deutsche Bank's Asset Management division and, within the US, represents the retail asset management activities of Deutsche Bank AG, Deutsche Bank Trust Company Americas, Deutsche Investment Management Americas Inc. and DWS Trust Company.

The views expressed in this report reflect those of the portfolio managers only through the end of the period of the report as stated on the cover. The managers' views are subject to change at any time based on market and other conditions and should not be construed as a recommendation.

This information must be preceded or accompanied by a current prospectus.

Portfolio changes should not be considered recommendations for action by individual investors.

DWS Investments Distributors, Inc.
222 South Riverside Plaza
Chicago, IL 60606
(800) 621-1148

VS2SCG-2 (2/11)

DWS INVESTMENTS
Deutsche Bank Group

DECEMBER 31, 2010

# ANNUAL REPORT

## DWS VARIABLE SERIES II

## DWS Strategic Income VIP

**This report must be preceded or accompanied by a prospectus. To obtain an additional prospectus or summary prospectus, if available, call (800) 728-3337 or your financial representative. We advise you to consider the Fund's objectives, risks, charges and expenses carefully before investing. The summary prospectus and prospectus contain this and other important information about the Fund. Please read the prospectus carefully before you invest.**

*Investments in variable insurance portfolios (VIPs) involve risk. Stocks may decline in value. Bond investments are subject to interest-rate and credit risks. When interest rates rise, bond prices generally fall. Credit risk refers to the ability of an issuer to make timely payments of principal and interest. Investing in derivatives entails special risks relating to liquidity, leverage and credit that may reduce returns and/or increased volatility. Investing in foreign securities, particularly those of emerging markets, presents certain risks, such as currency fluctuations, political and economic changes, and market risks. There are additional risks associated with investing in commodities, high-yield bonds, aggressive growth stocks, non-diversified/ concentrated funds and small- and mid-cap stocks which are more fully explained in the prospectuses. Please read the prospectus for more information.*

*DWS Investments is part of Deutsche Bank's Asset Management division and, within the US, represents the retail asset management activities of Deutsche Bank AG, Deutsche Bank Trust Company Americas, Deutsche Investment Management Americas Inc. and DWS Trust Company.*

*NOT FDIC/NCUA INSURED    NO BANK GUARANTEE    MAY LOSE VALUE    NOT A DEPOSIT*
*NOT INSURED BY ANY FEDERAL GOVERNMENT AGENCY*

DWS INVESTMENTS
Deutsche Bank Group

# Performance Summary

**December 31, 2010**

## DWS Strategic Income VIP

**All performance shown is historical, assumes reinvestment of all dividend and capital gain distributions and does not guarantee future results. Investment return and principal value fluctuate with changing market conditions so that, when redeemed, shares may be worth more or less than their original cost. Current performance may be lower or higher than the performance data quoted. Please contact your participating insurance company for the Fund's most recent month-end performance. Performance doesn't reflect charges and fees ("contract charges") associated with the separate account that invests in the Fund or any variable life insurance policy or variable annuity contract for which the Fund is an investment option. These charges and fees will reduce returns.**

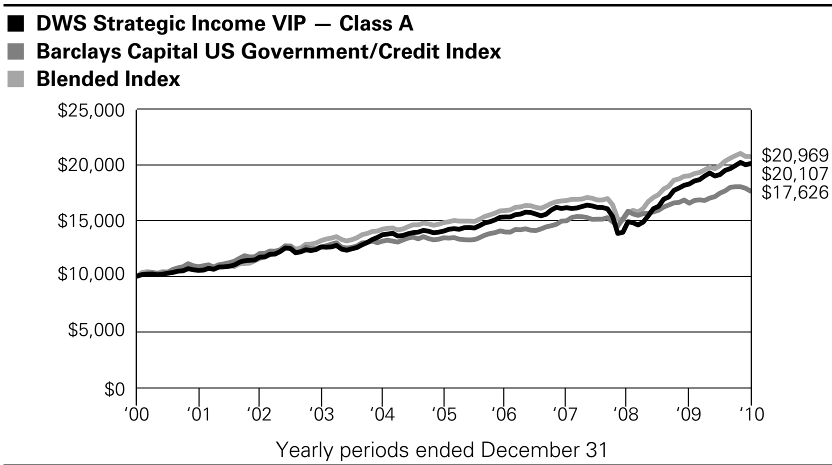
**The gross expense ratio of the Fund, as stated in the fee table of the prospectus dated May 1, 2010 is 0.86% for Class A shares and may differ from the expense ratio disclosed in the Financial Highlights table in this report.**

### Risk Considerations

Bond investments are subject to interest-rate and credit risks. When interest rates rise, bond prices generally fall. Credit risk refers to the ability of an issuer to make timely payments of principal and interest. Investments in lower-quality and non-rated securities present greater risk of loss than investments in higher-quality securities. The Fund may use derivatives, including as part of its global alpha strategy. Investing in derivatives entails special risks relating to liquidity, leverage and credit that may reduce returns and/or increase volatility. Investing in foreign securities, particularly those of emerging markets, presents certain risks, such as currency fluctuations, political and economic changes, and market risks. See the prospectus for details.

Fund returns for all periods shown reflect a fee waiver and/or expense reimbursement. Without this waiver/reimbursement, returns would have been lower.

### Growth of an Assumed $10,000 Investment in DWS Strategic Income VIP




*The Barclays Capital US Government/Credit Index is an unmanaged index comprising intermediate- and long-term government and investment-grade corporate debt securities.*

*The Blended Index consists of the Credit Suisse High Yield Index (35%), Barclays Capital US Government/Credit Index (35%), JPMorgan Emerging Markets Bond Index Global Diversified (15%) and Citigroup Non US Hedged World Government Bond Index ("WGBI") (15%). The Advisor believes this blended benchmark, which is a secondary benchmark, more accurately reflects typical portfolio asset allocations and represents the overall investment process.*

*Index returns, unlike fund returns, do not reflect any fees or expenses. It is not possible to invest directly into an index.*

### Comparative Results

| DWS Strategic Income VIP | | 1-Year | 3-Year | 5-Year | 10-Year |
|---|---|---|---|---|---|
| **Class A** | Growth of $10,000 | $11,005 | $12,460 | $14,317 | $20,107 |
| | Average annual total return | 10.05% | 7.61% | 7.44% | 7.23% |
| Barclays Capital US Government/Credit Index | Growth of $10,000 | $10,659 | $11,777 | $13,105 | $17,626 |
| | Average annual total return | 6.59% | 5.60% | 5.56% | 5.83% |
| Blended Index | Growth of $10,000 | $10,954 | $12,399 | $14,000 | $20,969 |
| | Average annual total return | 9.54% | 7.43% | 6.96% | 7.69% |

*The growth of $10,000 is cumulative.*

# Information About Your Fund's Expenses

## DWS Strategic Income VIP

As an investor of the Fund, you incur two types of costs: ongoing expenses and transaction costs. Ongoing expenses include management fees and other Fund expenses. Examples of transaction costs include contract charges, redemption fees and account maintenance fees, which are not shown in this section. The following tables are intended to help you understand your ongoing expenses (in dollars) of investing in the Fund and to help you compare these expenses with the ongoing expenses of investing in other mutual funds. In the most recent six-month period, the Fund limited these expenses; had it not done so, expenses would have been higher. The example in the table is based on an investment of $1,000 invested at the beginning of the six-month period and held for the entire period (July 1, 2010 to December 31, 2010).

The tables illustrate your Fund's expenses in two ways:

- **Actual Fund Return.** This helps you estimate the actual dollar amount of ongoing expenses (but not transaction costs) paid on a $1,000 investment in the Fund using the Fund's actual return during the period. To estimate the expenses you paid over the period, simply divide your account value by $1,000 (for example, an $8,600 account value divided by $1,000 = 8.6), then multiply the result by the number in the "Expenses Paid per $1,000" line under the share class you hold.
- **Hypothetical 5% Fund Return.** This helps you to compare your Fund's ongoing expenses (but not transaction costs) with those of other mutual funds using the Fund's actual expense ratio and a hypothetical rate of return of 5% per year before expenses. Examples using a 5% hypothetical Fund return may be found in the shareholder reports of other mutual funds. The hypothetical account values and expenses may not be used to estimate the actual ending account balance or expenses you paid for the period.

Please note that the expenses shown in these tables are meant to highlight your ongoing expenses only and do not reflect any transaction costs. The "Expenses Paid per $1,000" line of the tables is useful in comparing ongoing expenses only and will not help you determine the relative total expense of owning different funds. If these transaction costs had been included, your costs would have been higher.

**Expenses and Value of a $1,000 Investment** for the six months ended December 31, 2010

| **Actual Fund Return** | **Class A** |
|---|---|
| Beginning Account Value 7/1/10 | $1,000.00 |
| Ending Account Value 12/31/10 | $1,051.90 |
| Expenses Paid per $1,000* | $ 4.29 |
| **Hypothetical 5% Fund Return** | **Class A** |
| Beginning Account Value 7/1/10 | $1,000.00 |
| Ending Account Value 12/31/10 | $1,021.02 |
| Expenses Paid per $1,000* | $ 4.23 |

* *Expenses are equal to the Fund's annualized expense ratio, multiplied by the average account value over the period, multiplied by the number of days in the most recent six-month period, then divided by 365.*

| **Annualized Expense Ratio** | **Class A** |
|---|---|
| DWS Variable Series II — DWS Strategic Income VIP | .83% |

For more information, please refer to the Fund's prospectus.

These tables do not reflect charges and fees ("contract charges") associated with the separate account that invests in the Fund or any variable life insurance policy or variable annuity contract for which the Fund is an investment option.

# Management Summary

December 31, 2010

## DWS Strategic Income VIP

The Class A shares of the Fund returned 10.05% (unadjusted for contract charges) during the 12-month period ended December 31, 2010. This compares with returns of 9.54% for the Fund's blended benchmark and 6.59% for the Barclays Capital US Government/Credit Index.

The primary positive factor in the Fund's performance was its overweight in high-yield bonds, which outpaced the broader market by a wide margin.[1] We continued to add to this market segment throughout the year, bringing the Fund's weighting in high yield from about 45% at the beginning of 2010 to approximately 55% at year end. Given the outperformance of high-yield bonds, this decision proved helpful to performance. The Fund's weighting in domestic investment-grade bonds also delivered a positive return, thanks to the solid performance of our positions in corporate bonds and mortgage-backed securities.[2] On the negative side, our relative performance in the Fund's domestic segment was held back somewhat by our smaller-than-normal position in commercial mortgage-backed securities.[3]

Turning our attention to the Fund's overseas allocation, our position in emerging-markets debt produced a strong absolute return, which seeks to generate positive returns independent of market direction, but had only a modest impact on performance due to our small average weighting of about 6% to 8% of assets. The Fund's position in non-US developed-market bonds was a modest detractor. While we generated positive performance through our investments in euro-denominated corporate debt, our positions in Greece and Spain weighed significantly on performance during the first half of the year. Our currency positioning and global tactical asset allocation overlay strategy were also modest detractors from performance.[4]

We believe the year ahead will prove challenging for government bonds, given the extremely low absolute yields in the developed markets. In such an environment, we would expect to see continued outperformance from the "spread sectors" such as high-yield and investment-grade corporate bonds.[5] Accordingly, about 80% of the Fund is now invested in these areas — up from about 60% at the start of the year. This allocation includes not just domestic corporates, but also bonds issued by corporations domiciled in Europe, Asia and the emerging markets.

As always, our investment process remains focused on using credit research to identify the most compelling investment opportunities for the Fund. At a time in which government bonds are offering paltry yields, we believe our global, multi-asset-class approach provides us with the best chance to strike this favorable balance over time.

Gary Russell, CFA
William Chepolis, CFA
John D. Ryan
*Portfolio Managers, Deutsche Investment Management Americas Inc.*

Thomas Picciochi
Robert Wang
*Portfolio Managers, QS Investors, LLC*
*Subadvisor to the Fund*

*The Blended Index consists of the Credit Suisse High Yield Index (35%), Barclays Capital US Government/Credit Index (35%), JPMorgan Emerging Markets Bond Index Global Diversified (15%) and Citigroup Non US Hedged WBGI (15%). The Advisor believes this blended benchmark, which is a secondary benchmark, more accurately reflects typical portfolio asset allocations and represents the overall investment process.*

*The Barclays Capital US Government/Credit Index is an unmanaged index comprising intermediate- and long-term government and investment-grade corporate debt securities.*

*Index returns, unlike fund returns, do not reflect any fees or expenses. It is not possible to invest directly into an index.*

1 *"Overweight" means the Fund holds a higher weighting in a given sector or security than the benchmark. "Underweight" means the Fund holds a lower weighting.*

2 *Mortgage-backed securities (MBS) are secured by loans on residential property.*

3 *Commercial mortgage-backed securities (CMBS) are secured by loans on a commercial property.*

4 *The global tactical asset allocation (GTAA) strategy is a total return strategy designed to add value by benefiting from global market inefficiencies. The strategy combines diverse macro investment views to determine the positions, using a disciplined, risk-managed process. The result is a collection of long and short investment positions within global markets designed to generate excess returns that have little correlation to major markets. These positions are then implemented through futures and forward contracts.*

5 *"Spread sectors" refers to all segments of the bond market other than government bonds. They are named as such because they are priced on the yield spread, or difference in yield, relative to Treasuries.*

*Portfolio management market commentary is as of December 31, 2010, and may not come to pass. This information is subject to change at any time based on market and other conditions. Past performance does not guarantee future results. Current and future portfolio holdings are subject to risk.*

# Portfolio Summary

## DWS Strategic Income VIP

| **Asset Allocation** (As a % of Investment Portfolio excluding Securities Lending Collateral) | **12/31/10** | **12/31/09** |
|---|---|---|
| Corporate Bonds | 62% | 62% |
| Government & Agency Obligations | 17% | 18% |
| Cash Equivalents | 5% | 8% |
| Mortgage-Backed Securities Pass-Throughs | 5% | 4% |
| Loan Participations and Assignments | 4% | 3% |
| Collateralized Mortgage Obligations | 3% | 2% |
| Commercial Mortgage-Backed Securities | 3% | 1% |
| Preferred Securities | 1% | 1% |
| Asset Backed | — | 1% |
| | 100% | 100% |

| **Quality** (Excludes Cash Equivalents and Securities Lending Collateral) | **12/31/10** | **12/31/09** |
|---|---|---|
| AAA | 20% | 13% |
| AA | 2% | 9% |
| A | 5% | 7% |
| BBB | 16% | 15% |
| BB | 16% | 20% |
| B | 28% | 23% |
| CCC | 11% | 9% |
| Below CCC | — | 2% |
| Not Rated | 2% | 2% |
| | 100% | 100% |

| **Interest Rate Sensitivity** | **12/31/10** | **12/31/09** |
|---|---|---|
| Effective Maturity | 7.2 years | 6.6 years |
| Effective Duration | 4.7 years | 3.7 years |

*Asset allocation and interest rate sensitivity are subject to change.*

*The quality ratings represent the lower of Moody's Investors Service, Inc. ("Moody's") or Standard & Poor's Corporation ("S&P") credit ratings. The ratings of Moody's and S&P represent their opinions as to the quality of the securities they rate. Ratings are relative and subjective and are not absolute standards of quality. The Fund's credit quality does not remove market risk and is subject to change.*

*Effective maturity is the weighted average of the bonds held by the Fund taking into consideration any maturity shortening features.*

*Effective duration is an approximate measure of the Fund's sensitivity to interest rate changes taking into consideration any maturity shortening features.*

*For more complete details about the Fund's investment portfolio, see page 6.*

Following the Fund's fiscal first and third quarter-end, a complete portfolio holdings listing is filed with the SEC on Form N-Q. The form will be available on the SEC's Web site at www.sec.gov, and it also may be reviewed and copied at the SEC's Public Reference Room in Washington, D.C. Information on the operation of the SEC's Public Reference Room may be obtained by calling (800) SEC-0330. The Fund's portfolio holdings are also posted on www.dws-investments.com from time to time. Please see the Fund's current prospectus for more information.

## DWS Strategic Income VIP

| | Principal Amount ($) (a) | Value ($) |
|---|---|---|
| **Corporate Bonds 64.0%** | | |
| **Consumer Discretionary 7.9%** | | |
| AMC Entertainment, Inc., 8.0%, 3/1/2014 | 105,000 | 106,050 |
| American Achievement Corp., 144A, 10.875%, 4/15/2016 | 110,000 | 112,750 |
| Ameristar Casinos, Inc., 9.25%, 6/1/2014 | 115,000 | 123,050 |
| Asbury Automotive Group, Inc.: | | |
| 7.625%, 3/15/2017 | 65,000 | 65,650 |
| 144A, 8.375%, 11/15/2020 | 80,000 | 82,600 |
| Ashtead Holdings PLC, 144A, 8.625%, 8/1/2015 | 120,000 | 124,350 |
| Avis Budget Car Rental LLC: | | |
| 144A, 8.25%, 1/15/2019 | 95,000 | 95,950 |
| 9.625%, 3/15/2018 | 45,000 | 48,488 |
| Beazer Homes USA, Inc., 144A, 9.125%, 5/15/2019 | 50,000 | 47,500 |
| Bon-Ton Department Stores, Inc., 10.25%, 3/15/2014 | 30,000 | 30,600 |
| Brunswick Corp., 144A, 11.25%, 11/1/2016 | 45,000 | 53,550 |
| Cablevision Systems Corp.: | | |
| 7.75%, 4/15/2018 | 10,000 | 10,475 |
| 144A, 8.0%, 12/15/2018 | 95,000 | 97,850 |
| 8.0%, 4/15/2020 | 10,000 | 10,700 |
| CanWest MediaWorks LP, 144A, 9.25%, 8/1/2015** | 50,000 | 8,500 |
| Carnival Corp., 6.65%, 1/15/2028 | 285,000 | 292,317 |
| Carrols Corp., 9.0%, 1/15/2013 | 30,000 | 30,075 |
| CCO Holdings LLC: | | |
| 7.25%, 10/30/2017 | 90,000 | 91,350 |
| 7.875%, 4/30/2018 | 40,000 | 41,400 |
| 8.125%, 4/30/2020 | 25,000 | 26,313 |
| Cequel Communications Holdings I LLC, 144A, 8.625%, 11/15/2017 | 215,000 | 224,675 |
| Clear Channel Worldwide Holdings, Inc.: | | |
| Series A, 9.25%, 12/15/2017 | 15,000 | 16,313 |
| Series B, 9.25%, 12/15/2017 | 25,000 | 27,375 |
| DineEquity, Inc., 144A, 9.5%, 10/30/2018 | 150,000 | 159,000 |
| DISH DBS Corp.: | | |
| 6.625%, 10/1/2014 | 65,000 | 67,437 |
| 7.125%, 2/1/2016 | 155,000 | 160,037 |
| Fontainebleau Las Vegas Holdings LLC, 144A, 11.0%, 6/15/2015** | 65,000 | 228 |
| Ford Motor Co., 7.45%, 7/16/2031 | 65,000 | 69,631 |
| General Electric Co., 144A, 4.375%, 4/1/2021 | 145,000 | 140,738 |
| Goodyear Tire & Rubber Co., 10.5%, 5/15/2016 | 25,000 | 28,500 |
| Great Canadian Gaming Corp., 144A, 7.25%, 2/15/2015 | 55,000 | 56,237 |
| Group 1 Automotive, Inc., 144A, 3.0%, 3/15/2020 | 65,000 | 80,844 |
| Harrah's Operating Co., Inc.: | | |
| 10.0%, 12/15/2018 | 135,000 | 123,187 |
| 11.25%, 6/1/2017 | 240,000 | 270,000 |
| 144A, 12.75%, 4/15/2018 | 55,000 | 55,275 |
| Hertz Corp.: | | |
| 144A, 7.5%, 10/15/2018 | 155,000 | 160,812 |
| 8.875%, 1/1/2014 | 183,000 | 187,117 |
| Hyundai Motor Manufacturing Czech, 144A, 4.5%, 4/15/2015 | 145,000 | 148,787 |
| Lear Corp.: | | |
| 7.875%, 3/15/2018 | 40,000 | 42,800 |
| 8.125%, 3/15/2020 | 40,000 | 43,500 |
| Limited Brands, Inc., 7.0%, 5/1/2020 | 20,000 | 21,100 |
| Macy's Retail Holdings, Inc., 8.375%, 7/15/2015 | 10,000 | 11,700 |
| Mediacom Broadband LLC, 8.5%, 10/15/2015 | 110,000 | 110,550 |
| Mediacom LLC, 9.125%, 8/15/2019 | 30,000 | 30,600 |
| MGM Resorts International: | | |
| 144A, 9.0%, 3/15/2020 | 65,000 | 71,500 |
| 144A, 10.0%, 11/1/2016 | 15,000 | 15,413 |
| 10.375%, 5/15/2014 | 45,000 | 50,512 |
| 11.125%, 11/15/2017 | 50,000 | 57,500 |
| Michaels Stores, Inc., Step-up Coupon, 0% to 11/1/2011, 13.0% to 11/1/2016 | 25,000 | 24,750 |
| Neiman Marcus Group, Inc., 10.375%, 10/15/2015 | 25,000 | 26,406 |
| Norcraft Holdings LP, 9.75%, 9/1/2012 | 71,000 | 71,444 |
| Penske Automotive Group, Inc., 7.75%, 12/15/2016 | 175,000 | 178,500 |
| PETCO Animal Supplies, Inc., 144A, 9.25%, 12/1/2018 | 60,000 | 63,225 |
| Phillips-Van Heusen Corp., 7.375%, 5/15/2020 | 25,000 | 26,563 |
| Regal Entertainment Group, 9.125%, 8/15/2018 | 25,000 | 26,625 |
| Sabre Holdings Corp., 8.35%, 3/15/2016 | 160,000 | 153,600 |
| Sears Holdings Corp., 144A, 6.625%, 10/15/2018 | 60,000 | 55,950 |
| Seminole Indian Tribe of Florida: | | |
| 144A, 7.75%, 10/1/2017 | 40,000 | 41,300 |
| 144A, 7.804%, 10/1/2020 | 70,000 | 68,215 |
| Simmons Bedding Co., 144A, 11.25%, 7/15/2015 | 50,000 | 54,000 |
| Sirius XM Radio, Inc., 144A, 8.75%, 4/1/2015 | 55,000 | 59,537 |
| Sonic Automotive, Inc.: | | |
| 5.0%, 10/1/2029 | 25,000 | 31,063 |
| Series B, 9.0%, 3/15/2018 | 95,000 | 99,987 |
| Standard Pacific Corp.: | | |
| 8.375%, 5/15/2018 | 10,000 | 10,000 |
| 144A, 8.375%, 5/15/2018 | 65,000 | 65,000 |
| 10.75%, 9/15/2016 | 80,000 | 92,200 |
| Toys "R" Us-Delaware, Inc., 144A, 7.375%, 9/1/2016 | 35,000 | 36,750 |

*The accompanying notes are an integral part of the financial statements.*

| | | Principal Amount ($) (a) | Value ($) |
|---|---|---|---|
| Travelport LLC: | | | |
| 4.921%***, 9/1/2014 | | 45,000 | 39,825 |
| 9.0%, 3/1/2016 | | 65,000 | 62,969 |
| 9.875%, 9/1/2014 | | 45,000 | 43,819 |
| Unitymedia Hessen GmbH & Co., KG, 144A, 8.125%, 12/1/2017 | | 200,000 | 209,000 |
| Univision Communications, Inc., 144A, 7.875%, 11/1/2020 | | 25,000 | 26,250 |
| UPC Holding BV, 144A, 8.0%, 11/1/2016 | EUR | 100,000 | 138,975 |
| Vertis, Inc., 13.5%, 4/1/2014 (PIK)** | | 24,348 | 730 |
| Visant Corp., 144A, 10.0%, 10/1/2017 | | 80,000 | 85,000 |
| Wyndham Worldwide Corp., 5.75%, 2/1/2018 | | 210,000 | 213,536 |
| Wynn Las Vegas LLC, 7.75%, 8/15/2020 | | 50,000 | 54,125 |
| Young Broadcasting, Inc., 8.75%, 1/15/2014** | | 275,000 | 3 |
| | | | **5,990,233** |
| **Consumer Staples 2.2%** | | | |
| Alliance One International, Inc., 10.0%, 7/15/2016 | | 25,000 | 25,625 |
| Altria Group, Inc., 9.95%, 11/10/2038 | | 145,000 | 204,324 |
| B&G Foods, Inc., 7.625%, 1/15/2018 | | 25,000 | 26,313 |
| Central Garden & Pet Co., 8.25%, 3/1/2018 | | 35,000 | 35,437 |
| Darling International, Inc., 144A, 8.5%, 12/15/2018 | | 80,000 | 83,400 |
| Dole Food Co., Inc., 144A, 8.0%, 10/1/2016 | | 35,000 | 36,925 |
| FAGE Dairy Industry SA, 144A, 9.875%, 2/1/2020 | | 85,000 | 85,000 |
| General Nutrition Centers, Inc., 5.75%***, 3/15/2014 (PIK) | | 40,000 | 39,600 |
| NBTY, Inc., 144A, 9.0%, 10/1/2018 | | 25,000 | 26,688 |
| North Atlantic Trading Co., 144A, 10.0%, 3/1/2012 | | 223,000 | 209,620 |
| Pilgrim's Pride Corp., 144A, 7.875%, 12/15/2018 | | 60,000 | 59,700 |
| Reynolds American, Inc., 6.75%, 6/15/2017 | | 200,000 | 223,543 |
| Rite Aid Corp.: | | | |
| 7.5%, 3/1/2017 | | 60,000 | 57,675 |
| 8.0%, 8/15/2020 | | 100,000 | 104,125 |
| Smithfield Foods, Inc.: | | | |
| 7.75%, 7/1/2017 | | 220,000 | 228,800 |
| 144A, 10.0%, 7/15/2014 | | 85,000 | 97,962 |
| Stater Bros. Holdings, Inc., 144A, 7.375%, 11/15/2018 | | 30,000 | 30,750 |
| SUPERVALU, Inc., 8.0%, 5/1/2016 | | 35,000 | 33,513 |
| TreeHouse Foods, Inc., 7.75%, 3/1/2018 | | 25,000 | 27,094 |
| | | | **1,636,094** |
| **Energy 7.4%** | | | |
| Allis-Chalmers Energy, Inc., 9.0%, 1/15/2014 | | 55,000 | 55,825 |
| Anadarko Petroleum Corp., 6.375%, 9/15/2017 | | 215,000 | 234,201 |

| | Principal Amount ($) (a) | Value ($) |
|---|---|---|
| Arch Coal, Inc., 7.25%, 10/1/2020 | 20,000 | 21,100 |
| Atlas Energy Operating Co., LLC, 12.125%, 8/1/2017 | 55,000 | 69,575 |
| Belden & Blake Corp., 8.75%, 7/15/2012 | 310,000 | 296,050 |
| Berry Petroleum Co., 6.75%, 11/1/2020 | 90,000 | 90,450 |
| Bill Barrett Corp., 9.875%, 7/15/2016 | 40,000 | 43,900 |
| BreitBurn Energy Partners LP, 144A, 8.625%, 10/15/2020 | 50,000 | 50,250 |
| Bristow Group, Inc., 7.5%, 9/15/2017 | 70,000 | 73,850 |
| Chaparral Energy, Inc., 8.5%, 12/1/2015 | 230,000 | 234,025 |
| Chesapeake Energy Corp.: | | |
| 6.625%, 8/15/2020 | 60,000 | 59,100 |
| 6.875%, 8/15/2018 | 30,000 | 30,450 |
| 6.875%, 11/15/2020 | 75,000 | 75,937 |
| 7.25%, 12/15/2018 | 100,000 | 103,500 |
| 9.5%, 2/15/2015 | 185,000 | 208,587 |
| CITGO Petroleum Corp., 144A, 11.5%, 7/1/2017 | 105,000 | 117,600 |
| Colorado Interstate Gas Co., 6.8%, 11/15/2015 | 30,000 | 34,561 |
| CONSOL Energy, Inc.: | | |
| 144A, 8.0%, 4/1/2017 | 115,000 | 122,475 |
| 144A, 8.25%, 4/1/2020 | 60,000 | 64,800 |
| Continental Resources, Inc.: | | |
| 144A, 7.125%, 4/1/2021 | 30,000 | 31,500 |
| 7.375%, 10/1/2020 | 35,000 | 37,100 |
| 8.25%, 10/1/2019 | 20,000 | 22,200 |
| Crosstex Energy LP, 8.875%, 2/15/2018 | 55,000 | 58,919 |
| El Paso Corp.: | | |
| 7.25%, 6/1/2018 | 55,000 | 58,878 |
| 9.625%, 5/15/2012 | 132,000 | 140,681 |
| El Paso Pipeline Partners Operating Co., LLC, 6.5%, 4/1/2020 | 155,000 | 162,625 |
| Energy Transfer Equity LP, 7.5%, 10/15/2020 | 35,000 | 36,050 |
| Frontier Oil Corp., 6.875%, 11/15/2018 | 55,000 | 56,100 |
| Genesis Energy LP, 144A, 7.875%, 12/15/2018 | 65,000 | 64,675 |
| Global Geophysical Services, Inc., 10.5%, 5/1/2017 | 130,000 | 129,350 |
| Harvest Operations Corp., 144A, 6.875%, 10/1/2017 | 25,000 | 25,750 |
| Holly Energy Partners LP, 144A, 8.25%, 3/15/2018 | 55,000 | 57,475 |
| Inergy LP, 144A, 7.0%, 10/1/2018 | 60,000 | 60,450 |
| KCS Energy, Inc., 7.125%, 4/1/2012 | 240,000 | 240,600 |
| Linn Energy LLC: | | |
| 144A, 7.75%, 2/1/2021 | 60,000 | 61,500 |
| 144A, 8.625%, 4/15/2020 | 55,000 | 59,263 |
| 11.75%, 5/15/2017 | 75,000 | 85,875 |
| Newfield Exploration Co., 7.125%, 5/15/2018 | 90,000 | 94,725 |
| Nexen, Inc., 5.875%, 3/10/2035 | 75,000 | 69,738 |
| Niska Gas Storage US LLC, 144A, 8.875%, 3/15/2018 | 55,000 | 58,850 |
| OPTI Canada, Inc., 7.875%, 12/15/2014 | 125,000 | 88,281 |

*The accompanying notes are an integral part of the financial statements.*

| | | Principal Amount ($) (a) | Value ($) |
|---|---|---|---|
| Petrohawk Energy Corp.: | | | |
| 7.25%, 8/15/2018 | | 50,000 | 50,500 |
| 7.875%, 6/1/2015 | | 30,000 | 31,238 |
| Plains Exploration & Production Co.: | | | |
| 7.0%, 3/15/2017 | | 60,000 | 61,650 |
| 7.625%, 6/1/2018 | | 110,000 | 115,775 |
| 8.625%, 10/15/2019 | | 55,000 | 60,225 |
| Quicksilver Resources, Inc., 11.75%, 1/1/2016 | | 15,000 | 17,475 |
| Range Resources Corp., 6.75%, 8/1/2020 | | 20,000 | 20,625 |
| Regency Energy Partners LP: | | | |
| 6.875%, 12/1/2018 | | 35,000 | 35,438 |
| 9.375%, 6/1/2016 | | 115,000 | 126,212 |
| Reliance Holdings USA, Inc., 144A, 4.5%, 10/19/2020 | | 250,000 | 238,538 |
| Sabine Pass LNG LP: | | | |
| 7.25%, 11/30/2013 | | 115,000 | 111,837 |
| 7.5%, 11/30/2016 | | 100,000 | 93,750 |
| SandRidge Energy, Inc., 8.625%, 4/1/2015 (PIK) | | 25,000 | 25,594 |
| Southwestern Energy Co., 7.5%, 2/1/2018 | | 85,000 | 95,837 |
| Stone Energy Corp.: | | | |
| 6.75%, 12/15/2014 | | 95,000 | 92,625 |
| 8.625%, 2/1/2017 | | 25,000 | 25,375 |
| Transocean, Inc., 6.5%, 11/15/2020 | | 360,000 | 382,218 |
| Valero Energy Corp., 6.125%, 2/1/2020 | | 160,000 | 169,931 |
| Williams Partners LP, 4.125%, 11/15/2020 | | 190,000 | 179,966 |
| | | | **5,621,630** |

**Financials 16.7%**

| | | Principal Amount ($) (a) | Value ($) |
|---|---|---|---|
| Algoma Acquisition Corp., 144A, 9.875%, 6/15/2015 | | 125,000 | 112,500 |
| Ally Financial, Inc.: | | | |
| 144A, 6.25%, 12/1/2017 | | 95,000 | 95,000 |
| 6.875%, 9/15/2011 | | 297,000 | 305,167 |
| 7.0%, 2/1/2012 | | 185,000 | 191,475 |
| 7.25%, 3/2/2011 | | 455,000 | 457,275 |
| 144A, 7.5%, 9/15/2020 | | 120,000 | 125,850 |
| 8.0%, 3/15/2020 | | 115,000 | 125,637 |
| 8.0%, 11/1/2031 | | 75,000 | 80,813 |
| 8.3%, 2/12/2015 | | 35,000 | 38,500 |
| American International Group, Inc., Series G, 5.6%, 10/18/2016 | | 290,000 | 298,757 |
| Antero Resources Finance Corp., 9.375%, 12/1/2017 | | 10,000 | 10,463 |
| Ashton Woods USA LLC, 144A, Step-up Coupon, 0% to 6/30/2012, 11.0% to 6/30/2015 | | 75,400 | 41,847 |
| Barclays Bank PLC: | | | |
| 5.125%, 1/8/2020 | | 145,000 | 148,082 |
| 5.14%, 10/14/2020 | | 185,000 | 166,453 |
| BBVA Bancomer SA, 144A, 7.25%, 4/22/2020 | | 115,000 | 121,647 |
| Blue Acquisition Sub, Inc., 144A, 9.875%, 10/15/2018 | | 30,000 | 31,950 |
| BP Capital Markets PLC, 4.5%, 10/1/2020 | | 120,000 | 119,711 |
| Bumble Bee Acquisition Corp., 144A, 9.0%, 12/15/2017 | | 130,000 | 135,200 |
| Calpine Construction Finance Co., LP, 144A, 8.0%, 6/1/2016 | | 120,000 | 127,500 |
| Case New Holland, Inc., 7.75%, 9/1/2013 | | 45,000 | 48,375 |
| CIT Group, Inc.: | | | |
| 7.0%, 5/1/2013 | | 80,000 | 81,600 |
| 7.0%, 5/1/2015 | | 105,970 | 106,235 |
| 7.0%, 5/1/2017 | | 355,000 | 355,887 |
| Citigroup Funding, Inc., 5.0%, 4/7/2013 | | 295,000 | 295,000 |
| Credit Agricole SA, 144A, 3.5%, 4/13/2015 | | 171,000 | 172,136 |
| Discover Bank, 7.0%, 4/15/2020 | | 145,000 | 155,881 |
| Dunkin Finance Corp., 144A, 9.625%, 12/1/2018 | | 45,000 | 45,450 |
| E*TRADE Financial Corp., 7.375%, 9/15/2013 | | 120,000 | 119,400 |
| Express LLC, 8.75%, 3/1/2018 | | 45,000 | 47,813 |
| FCE Bank PLC, 9.375%, 1/17/2014 | EUR | 100,000 | 148,663 |
| Ford Motor Credit Co., LLC: | | | |
| 7.25%, 10/25/2011 | | 60,000 | 62,013 |
| 7.375%, 2/1/2011 | | 45,000 | 45,135 |
| 7.5%, 8/1/2012 | | 500,000 | 531,604 |
| 9.875%, 8/10/2011 | | 145,000 | 150,936 |
| GE Capital European Funding, 4.25%, 3/1/2017 | EUR | 290,000 | 393,485 |
| GenOn Escrow Corp., 144A, 9.5%, 10/15/2018 | | 25,000 | 24,844 |
| Giraffe Acquisition Corp., 144A, 9.125%, 12/1/2018 | | 55,000 | 57,338 |
| Hartford Financial Services Group, Inc., 5.5%, 3/30/2020 | | 290,000 | 294,181 |
| Hellas Telecommunications Finance SCA, 144A, 8.985%, 7/15/2015 (PIK)* | EUR | 109,187 | 88 |
| Hexion US Finance Corp., 8.875%, 2/1/2018 | | 340,000 | 363,375 |
| Hospitality Properties Trust, (REIT), 7.875%, 8/15/2014 | | 200,000 | 221,218 |
| Host Hotels & Resorts LP, (REIT), 6.875%, 11/1/2014 | | 165,000 | 169,950 |
| HSBC Finance Corp., 144A, 6.676%, 1/15/2021 | | 120,000 | 121,234 |
| Hutchison Whampoa Finance 09 Ltd., 4.75%, 11/14/2016 | EUR | 150,000 | 208,874 |
| Intergas Finance BV, REG S, 6.875%, 11/4/2011 | | 275,000 | 285,312 |
| International Finance Corp., 5.75%, 3/16/2015 | AUD | 285,000 | 289,497 |
| International Lease Finance Corp.: | | | |
| 144A, 8.625%, 9/15/2015 | | 40,000 | 43,000 |
| 144A, 8.75%, 3/15/2017 | | 180,000 | 193,050 |
| iPayment, Inc., 9.75%, 5/15/2014 | | 45,000 | 42,300 |
| Lincoln National Corp., 7.0%, 6/15/2040 | | 290,000 | 315,367 |
| Lloyds TSB Bank PLC, 144A, 6.5%, 9/14/2020 | | 290,000 | 266,809 |
| Manulife Financial Corp., 4.9%, 9/17/2020 | | 290,000 | 275,987 |
| Morgan Stanley, 3.45%, 11/2/2015 | | 220,000 | 214,490 |

*The accompanying notes are an integral part of the financial statements.*

| | Principal Amount ($) (a) | Value ($) |
|---|---|---|
| Navios Maritime Acquisition Corp., 144A, 8.625%, 11/1/2017 | 25,000 | 25,563 |
| Nielsen Finance LLC: | | |
| Step-up Coupon, 0% to 8/1/2011, 12.5% to 8/1/2016 | 45,000 | 47,250 |
| 144A, 7.75%, 10/15/2018 | 25,000 | 25,875 |
| 11.5%, 5/1/2016 | 20,000 | 23,100 |
| Nomura Holdings, Inc., 6.7%, 3/4/2020 | 90,000 | 96,326 |
| Nuveen Investments, Inc., 10.5%, 11/15/2015 | 130,000 | 132,925 |
| OMEGA Healthcare Investors, Inc., 144A, (REIT), 6.75%, 10/15/2022 | 55,000 | 54,519 |
| Pacific Life Global Funding, 144A, 3.32%***, 2/6/2016 | 386,000 | 382,580 |
| Pinafore LLC, 144A, 9.0%, 10/1/2018 | 40,000 | 43,200 |
| Pinnacle Foods Finance LLC: | | |
| 8.25%, 9/1/2017 | 70,000 | 71,575 |
| 9.25%, 4/1/2015 | 35,000 | 36,444 |
| PNC Bank NA, 6.875%, 4/1/2018 | 180,000 | 205,751 |
| Prudential Financial, Inc., 4.5%, 11/15/2020 | 135,000 | 132,023 |
| Qtel International Finance Ltd., 144A, 4.75%, 2/16/2021 | 200,000 | 190,814 |
| Rainbow National Services LLC, 144A, 10.375%, 9/1/2014 | 13,000 | 13,488 |
| Reynolds Group Issuer, Inc.: | | |
| 144A, 7.125%, 4/15/2019 | 100,000 | 101,750 |
| 144A, 8.5%, 5/15/2018 | 195,000 | 195,975 |
| 144A, 9.0%, 4/15/2019 | 105,000 | 108,806 |
| Roadhouse Financing, Inc., 144A, 10.75%, 10/15/2017 | 40,000 | 43,200 |
| Santander US Debt SA Unipersonal, 144A, 3.724%, 1/20/2015 | 145,000 | 137,382 |
| SLM Corp., 8.0%, 3/25/2020 | 25,000 | 25,348 |
| Societe Generale, 144A, 3.5%, 1/15/2016 | 290,000 | 285,645 |
| Sprint Capital Corp.: | | |
| 7.625%, 1/30/2011 | 50,000 | 50,125 |
| 8.375%, 3/15/2012 | 135,000 | 142,762 |
| Susser Holdings LLC, 8.5%, 5/15/2016 | 30,000 | 32,175 |
| Telecom Italia Capital SA, 4.95%, 9/30/2014 | 174,000 | 178,270 |
| Toys "R" Us Property Co. I, LLC, 10.75%, 7/15/2017 | 50,000 | 57,000 |
| Tropicana Entertainment LLC, 9.625%, 12/15/2014** | 150,000 | 77 |
| UCI Holdco, Inc., 9.25%***, 12/15/2013 (PIK) | 83,525 | 83,316 |
| Ventas Realty LP, (REIT), 3.125%, 11/30/2015 | 95,000 | 91,531 |
| Virgin Media Finance PLC, Series 1, 9.5%, 8/15/2016 | 300,000 | 339,000 |
| Virgin Media Secured Finance PLC, 6.5%, 1/15/2018 | 375,000 | 394,687 |
| WMG Acquisition Corp., 9.5%, 6/15/2016 | 45,000 | 48,263 |
| | | **12,677,099** |

| | Principal Amount ($) (a) | Value ($) |
|---|---|---|
| **Health Care 3.8%** | | |
| Celgene Corp., 3.95%, 10/15/2020 | 170,000 | 161,625 |
| Community Health Systems, Inc., 8.875%, 7/15/2015 | 80,000 | 84,000 |
| DaVita, Inc.: | | |
| 6.375%, 11/1/2018 | 20,000 | 19,900 |
| 6.625%, 11/1/2020 | 20,000 | 19,800 |
| Genzyme Corp., 5.0%, 6/15/2020 | 155,000 | 162,729 |
| Hanger Orthopedic Group, Inc., 7.125%, 11/15/2018 | 25,000 | 24,937 |
| HCA Holdings, Inc., 144A, 7.75%, 5/15/2021 | 105,000 | 105,000 |
| HCA, Inc.: | | |
| 7.875%, 2/15/2020 | 365,000 | 390,550 |
| 8.5%, 4/15/2019 | 45,000 | 49,275 |
| 9.125%, 11/15/2014 | 155,000 | 162,556 |
| 9.25%, 11/15/2016 | 310,000 | 330,731 |
| 9.625%, 11/15/2016 (PIK) | 152,000 | 162,830 |
| IASIS Healthcare LLC, 8.75%, 6/15/2014 | 95,000 | 97,494 |
| Laboratory Corp. of America Holdings, 4.625%, 11/15/2020 | 215,000 | 213,061 |
| Life Technologies Corp., 6.0%, 3/1/2020 | 215,000 | 230,294 |
| Mylan, Inc., 144A, 7.875%, 7/15/2020 | 15,000 | 16,163 |
| The Cooper Companies, Inc., 7.125%, 2/15/2015 | 95,000 | 97,850 |
| Valeant Pharmaceuticals International: | | |
| 144A, 6.75%, 10/1/2017 | 40,000 | 39,800 |
| 144A, 7.0%, 10/1/2020 | 65,000 | 64,187 |
| Vanguard Health Holding Co. II, LLC: | | |
| 8.0%, 2/1/2018 | 55,000 | 56,375 |
| 144A, 8.0%, 2/1/2018 | 45,000 | 45,900 |
| Warner Chilcott Co., LLC, 144A, 7.75%, 9/15/2018 | 75,000 | 75,750 |
| Watson Pharmaceuticals, Inc., 6.125%, 8/15/2019 | 220,000 | 243,615 |
| | | **2,854,422** |
| **Industrials 4.6%** | | |
| Accuride Corp., 144A, 9.5%, 8/1/2018 | 75,000 | 81,187 |
| Actuant Corp., 6.875%, 6/15/2017 | 40,000 | 40,900 |
| AMGH Merger Sub, Inc., 144A, 9.25%, 11/1/2018 | 30,000 | 31,500 |
| ARAMARK Corp., 8.5%, 2/1/2015 | 20,000 | 20,900 |
| Armored Autogroup, Inc., 144A, 9.25%, 11/1/2018 | 105,000 | 104,212 |
| ArvinMeritor, Inc.: | | |
| 8.125%, 9/15/2015 | 55,000 | 57,544 |
| 10.625%, 3/15/2018 | 60,000 | 67,500 |
| BE Aerospace, Inc.: | | |
| 6.875%, 10/1/2020 | 35,000 | 36,138 |
| 8.5%, 7/1/2018 | 105,000 | 114,975 |
| Belden, Inc.: | | |
| 7.0%, 3/15/2017 | 45,000 | 45,563 |
| 9.25%, 6/15/2019 | 40,000 | 43,850 |
| Bombardier, Inc., 144A, 7.75%, 3/15/2020 | 55,000 | 59,262 |

*The accompanying notes are an integral part of the financial statements.*

| | Principal Amount ($) (a) | Value ($) |
|---|---|---|
| Briggs & Stratton Corp., 6.875%, 12/15/2020 | 35,000 | 35,700 |
| Cenveo Corp.: | | |
| 8.875%, 2/1/2018 | 100,000 | 96,750 |
| 144A, 10.5%, 8/15/2016 | 55,000 | 54,038 |
| Clean Harbors, Inc., 7.625%, 8/15/2016 | 32,000 | 34,000 |
| Congoleum Corp., 9.0%, 12/31/2017 (PIK) | 41,250 | 28,437 |
| Corrections Corp. of America, 7.75%, 6/1/2017 | 30,000 | 31,838 |
| DynCorp International, Inc., 144A, 10.375%, 7/1/2017 | 85,000 | 87,125 |
| FTI Consulting, Inc., 144A, 6.75%, 10/1/2020 | 145,000 | 143,912 |
| Garda World Security Corp., 144A, 9.75%, 3/15/2017 | 60,000 | 64,350 |
| Great Lakes Dredge & Dock Co., 7.75%, 12/15/2013 | 50,000 | 50,438 |
| Hutchison Whampoa International 09/19 Ltd., 144A, 5.75%, 9/11/2019 | 225,000 | 240,956 |
| Interline Brands, Inc., 144A, 7.0%, 11/15/2018 | 50,000 | 50,750 |
| K. Hovnanian Enterprises, Inc., 8.875%, 4/1/2012 | 55,000 | 53,900 |
| Kansas City Southern de Mexico SA de CV: | | |
| 7.375%, 6/1/2014 | 115,000 | 120,175 |
| 8.0%, 2/1/2018 | 105,000 | 113,662 |
| Kansas City Southern Railway Co., 8.0%, 6/1/2015 | 100,000 | 107,500 |
| Masco Corp., 7.125%, 3/15/2020 | 145,000 | 151,689 |
| Navios Maritime Holdings, Inc., 9.5%, 12/15/2014 | 75,000 | 78,000 |
| Oshkosh Corp.: | | |
| 8.25%, 3/1/2017 | 10,000 | 10,875 |
| 8.5%, 3/1/2020 | 25,000 | 27,438 |
| Owens Corning, Inc., 9.0%, 6/15/2019 | 217,000 | 254,583 |
| Ply Gem Industries, Inc., 13.125%, 7/15/2014 | 95,000 | 100,937 |
| RailAmerica, Inc., 9.25%, 7/1/2017 | 36,000 | 39,555 |
| RBS Global & Rexnord Corp., 8.5%, 5/1/2018 | 120,000 | 127,500 |
| Sitel LLC, 144A, 11.5%, 4/1/2018 | 95,000 | 78,375 |
| Spirit AeroSystems Holdings, Inc., 144A, 6.75%, 12/15/2020 | 75,000 | 75,187 |
| SPX Corp., 144A, 6.875%, 9/1/2017 | 20,000 | 21,250 |
| Textron, Inc., 7.25%, 10/1/2019 | 145,000 | 166,163 |
| Titan International, Inc., 144A, 7.875%, 10/1/2017 | 160,000 | 168,800 |
| TransDigm, Inc., 144A, 7.75%, 12/15/2018 | 65,000 | 67,275 |
| Tutor Perini Corp., 144A, 7.625%, 11/1/2018 | 55,000 | 55,275 |
| USG Corp., 144A, 9.75%, 8/1/2014 | 45,000 | 47,475 |
| | | **3,487,439** |

| | Principal Amount ($) (a) | Value ($) |
|---|---|---|
| **Information Technology 2.5%** | | |
| Alcatel-Lucent USA, Inc., 6.45%, 3/15/2029 | 70,000 | 55,300 |
| Allen Systems Group, Inc., 144A, 10.5%, 11/15/2016 | 35,000 | 35,263 |
| Amkor Technology, Inc., 7.375%, 5/1/2018 | 45,000 | 46,800 |
| Aspect Software, Inc., 144A, 10.625%, 5/15/2017 | 60,000 | 61,575 |
| CDW LLC, 11.0%, 10/12/2015 | 155,000 | 160,812 |
| Equinix, Inc., 8.125%, 3/1/2018 | 120,000 | 125,400 |
| Fidelity National Information Services, Inc.: | | |
| 144A, 7.625%, 7/15/2017 | 20,000 | 21,050 |
| 144A, 7.875%, 7/15/2020 | 25,000 | 26,438 |
| First Data Corp., 144A, 8.875%, 8/15/2020 | 85,000 | 89,675 |
| Freescale Semiconductor, Inc., 144A, 9.25%, 4/15/2018 | 265,000 | 291,500 |
| Jabil Circuit, Inc., 7.75%, 7/15/2016 | 30,000 | 33,675 |
| L-3 Communications Corp.: | | |
| 5.875%, 1/15/2015 | 105,000 | 106,969 |
| Series B, 6.375%, 10/15/2015 | 80,000 | 82,400 |
| MasTec, Inc., 7.625%, 2/1/2017 | 65,000 | 64,675 |
| NXP BV, 3.039%***, 10/15/2013 | 150,000 | 147,750 |
| SunGard Data Systems, Inc.: | | |
| 144A, 7.375%, 11/15/2018 | 25,000 | 25,125 |
| 10.25%, 8/15/2015 | 225,000 | 236,531 |
| Unisys Corp., 144A, 12.75%, 10/15/2014 | 80,000 | 94,600 |
| Vangent, Inc., 9.625%, 2/15/2015 | 35,000 | 31,675 |
| Western Union Co., 6.2%, 6/21/2040 | 145,000 | 143,446 |
| | | **1,880,659** |
| **Materials 8.1%** | | |
| Agrium, Inc., 6.125%, 1/15/2041 | 290,000 | 307,140 |
| Albemarle Corp., 4.5%, 12/15/2020 | 100,000 | 98,422 |
| Appleton Papers, Inc., 144A, 11.25%, 12/15/2015 | 25,000 | 20,000 |
| ArcelorMittal, 6.125%, 6/1/2018 | 250,000 | 266,372 |
| Ashland, Inc., 9.125%, 6/1/2017 | 55,000 | 63,387 |
| Ball Corp.: | | |
| 7.125%, 9/1/2016 | 30,000 | 32,325 |
| 7.375%, 9/1/2019 | 25,000 | 26,875 |
| Berry Plastics Corp.: | | |
| 9.5%, 5/15/2018 | 65,000 | 65,162 |
| 144A, 9.75%, 1/15/2021 | 80,000 | 79,200 |
| Boise Paper Holdings LLC, 8.0%, 4/1/2020 | 30,000 | 32,100 |
| BWAY Parent Co., Inc., 144A, 10.125%, 11/1/2015 (PIK) | 40,000 | 40,400 |
| Celanese US Holdings LLC, 144A, 6.625%, 10/15/2018 | 35,000 | 36,138 |
| Clearwater Paper Corp., 144A, 7.125%, 11/1/2018 | 65,000 | 67,112 |
| Cliffs Natural Resources, Inc., 6.25%, 10/1/2040 | 290,000 | 282,325 |
| Clondalkin Acquisition BV, 144A, 2.302%***, 12/15/2013 | 75,000 | 71,812 |

*The accompanying notes are an integral part of the financial statements.*

| | | Principal Amount ($) (a) | Value ($) |
|---|---|---|---|
| Corporacion Nacional del Cobre de Chile, 144A, 3.75%, 11/4/2020 | | 130,000 | 123,180 |
| CPG International I, Inc., 10.5%, 7/1/2013 | | 130,000 | 132,600 |
| Crown Americas LLC, 7.625%, 5/15/2017 | | 30,000 | 32,250 |
| Crown European Holdings SA, 144A, 7.125%, 8/15/2018 | EUR | 50,000 | 69,655 |
| Dow Chemical Co.: | | | |
| 8.55%, 5/15/2019 | | 290,000 | 363,442 |
| 9.4%, 5/15/2039 | | 145,000 | 210,457 |
| Essar Steel Algoma, Inc., 144A, 9.375%, 3/15/2015 | | 240,000 | 241,500 |
| Exopack Holding Corp., 11.25%, 2/1/2014 | | 160,000 | 166,000 |
| FMG Resources August 2006 Pty Ltd., 144A, 7.0%, 11/1/2015 | | 25,000 | 25,625 |
| GEO Specialty Chemicals, Inc.: | | | |
| 144A, 7.5%, 3/31/2015 (PIK) | | 120,175 | 103,350 |
| 10.0%, 3/31/2015 | | 119,040 | 108,326 |
| Georgia-Pacific LLC: | | | |
| 144A, 5.4%, 11/1/2020 | | 145,000 | 143,358 |
| 144A, 7.125%, 1/15/2017 | | 35,000 | 37,275 |
| 144A, 8.25%, 5/1/2016 | | 65,000 | 73,369 |
| Graphic Packaging International, Inc.: | | | |
| 7.875%, 10/1/2018 | | 10,000 | 10,475 |
| 9.5%, 6/15/2017 | | 130,000 | 141,862 |
| Greif, Inc., 7.75%, 8/1/2019 | | 195,000 | 213,525 |
| Hexcel Corp., 6.75%, 2/1/2015 | | 280,000 | 285,600 |
| Huntsman International LLC: | | | |
| 8.625%, 3/15/2020 | | 60,000 | 65,250 |
| 144A, 8.625%, 3/15/2021 | | 25,000 | 27,000 |
| International Paper Co., 7.95%, 6/15/2018 | | 145,000 | 172,545 |
| Lyondell Chemical Co., 144A, 8.0%, 11/1/2017 | | 100,000 | 110,625 |
| Millar Western Forest Products Ltd., 7.75%, 11/15/2013 | | 35,000 | 33,163 |
| Momentive Performance Materials, Inc., 144A, 9.0%, 1/15/2021 | | 230,000 | 242,650 |
| Nalco Co., 144A, 6.625%, 1/15/2019 | | 45,000 | 46,013 |
| NewMarket Corp., 7.125%, 12/15/2016 | | 110,000 | 112,475 |
| Novelis, Inc.: | | | |
| 144A, 8.375%, 12/15/2017 | | 140,000 | 144,900 |
| 144A, 8.75%, 12/15/2020 | | 110,000 | 114,125 |
| Owens-Brockway Glass Container, Inc., 7.375%, 5/15/2016 | | 110,000 | 116,875 |
| Radnor Holdings Corp., 11.0%, 3/15/2010** | | 25,000 | 3 |
| Rain CII Carbon LLC, 144A, 8.0%, 12/1/2018 | | 45,000 | 46,125 |
| Silgan Holdings, Inc., 7.25%, 8/15/2016 | | 50,000 | 53,250 |
| Solo Cup Co., 10.5%, 11/1/2013 | | 170,000 | 177,650 |
| Teck Resources Ltd., 4.5%, 1/15/2021 | | 310,000 | 315,181 |
| Texas Industries, Inc., 144A, 9.25%, 8/15/2020 | | 75,000 | 79,687 |
| United States Steel Corp., 7.375%, 4/1/2020 | | 80,000 | 82,000 |
| Viskase Companies, Inc., 144A, 9.875%, 1/15/2018 | | 145,000 | 151,163 |
| Wolverine Tube, Inc., 15.0%, 3/31/2012 (PIK)** | | 91,631 | 49,481 |
| | | | **6,110,780** |
| **Telecommunication Services 7.1%** | | | |
| American Tower Corp., 4.5%, 1/15/2018 | | 270,000 | 267,642 |
| Buccaneer Merger Sub, Inc., 144A, 9.125%, 1/15/2019 | | 25,000 | 25,813 |
| CC Holdings GS V LLC, 144A, 7.75%, 5/1/2017 | | 350,000 | 382,375 |
| Cincinnati Bell, Inc.: | | | |
| 8.375%, 10/15/2020 | | 180,000 | 172,800 |
| 8.75%, 3/15/2018 | | 170,000 | 159,375 |
| Clearwire Communications LLC: | | | |
| 144A, 12.0%, 12/1/2015 | | 20,000 | 21,550 |
| 144A, 12.0%, 12/1/2017 | | 60,000 | 62,100 |
| Cricket Communications, Inc.: | | | |
| 144A, 7.75%, 10/15/2020 | | 250,000 | 238,125 |
| 10.0%, 7/15/2015 | | 100,000 | 107,125 |
| Crown Castle International Corp., 9.0%, 1/15/2015 | | 195,000 | 214,987 |
| Digicel Group Ltd., 144A, 10.5%, 4/15/2018 | | 100,000 | 110,000 |
| Digicel Ltd., 144A, 8.25%, 9/1/2017 | | 300,000 | 307,500 |
| ERC Ireland Preferred Equity Ltd., 144A, 8.05%***, 2/15/2017 (PIK) | EUR | 78,745 | 9,538 |
| Frontier Communications Corp.: | | | |
| 6.25%, 1/15/2013 | | 36,000 | 37,980 |
| 7.875%, 4/15/2015 | | 10,000 | 10,925 |
| 8.25%, 4/15/2017 | | 70,000 | 76,825 |
| 8.5%, 4/15/2020 | | 90,000 | 98,325 |
| 8.75%, 4/15/2022 | | 10,000 | 10,900 |
| Grupo Iusacell Celular SA de CV, 10.0%, 3/31/2012** | | 29,280 | 10,834 |
| Hughes Network Systems LLC, 9.5%, 4/15/2014 | | 150,000 | 154,687 |
| Intelsat Corp., 9.25%, 6/15/2016 | | 380,000 | 410,400 |
| Intelsat Jackson Holdings SA: | | | |
| 144A, 7.25%, 10/15/2020 | | 120,000 | 121,200 |
| 11.25%, 6/15/2016 | | 60,000 | 64,650 |
| Intelsat Luxembourg SA, 11.5%, 2/4/2017 (PIK) | | 200,000 | 221,000 |
| Intelsat Subsidiary Holding Co. SA, 8.875%, 1/15/2015 | | 195,000 | 200,362 |
| iPCS, Inc., 2.412%***, 5/1/2013 | | 35,000 | 33,687 |
| MetroPCS Wireless, Inc.: | | | |
| 6.625%, 11/15/2020 | | 90,000 | 85,725 |
| 7.875%, 9/1/2018 | | 25,000 | 25,938 |
| Nextel Communications, Inc., Series E, 6.875%, 10/31/2013 | | 60,000 | 60,150 |
| Qwest Communications International, Inc.: | | | |
| 144A, 7.125%, 4/1/2018 | | 55,000 | 56,925 |
| 8.0%, 10/1/2015 | | 60,000 | 64,500 |
| Qwest Corp., 7.5%, 10/1/2014 | | 285,000 | 319,200 |

*The accompanying notes are an integral part of the financial statements.*

| | Principal Amount ($) (a) | Value ($) |
|---|---|---|
| SBA Telecommunications, Inc.: | | |
| 8.0%, 8/15/2016 | 35,000 | 37,887 |
| 8.25%, 8/15/2019 | 25,000 | 27,313 |
| Sprint Nextel Corp., 8.375%, 8/15/2017 (b) | 115,000 | 123,337 |
| Telefonica Emisiones SAU, 6.421%, 6/20/2016 | 290,000 | 316,968 |
| Telesat Canada, 11.0%, 11/1/2015 | 180,000 | 202,050 |
| Verizon Communications, Inc., 8.95%, 3/1/2039 | 110,000 | 156,760 |
| West Corp.: | | |
| 144A, 7.875%, 1/15/2019 | 50,000 | 50,875 |
| 144A, 8.625%, 10/1/2018 | 15,000 | 15,900 |
| Windstream Corp.: | | |
| 7.0%, 3/15/2019 | 60,000 | 59,100 |
| 7.875%, 11/1/2017 | 135,000 | 141,919 |
| 8.125%, 9/1/2018 | 70,000 | 73,500 |
| 8.625%, 8/1/2016 | 10,000 | 10,525 |
| | | **5,359,277** |
| **Utilities 3.7%** | | |
| AES Corp.: | | |
| 8.0%, 10/15/2017 | 10,000 | 10,575 |
| 8.0%, 6/1/2020 | 175,000 | 185,500 |
| Calpine Corp.: | | |
| 144A, 7.5%, 2/15/2021 | 80,000 | 78,800 |
| 144A, 7.875%, 7/31/2020 | 95,000 | 96,187 |
| Edison Mission Energy, 7.0%, 5/15/2017 | 65,000 | 51,513 |
| Ferrellgas LP, 144A, 6.5%, 5/1/2021 | 20,000 | 19,500 |
| Korea Gas Corp., 144A, 4.25%, 11/2/2020 | 185,000 | 175,520 |
| Mirant Americas Generation LLC, 8.3%, 5/1/2011 | 230,000 | 233,450 |
| Mirant North America LLC, 7.375%, 12/31/2013 | 60,000 | 61,130 |
| NRG Energy, Inc.: | | |
| 7.25%, 2/1/2014 | 390,000 | 397,800 |
| 7.375%, 2/1/2016 | 660,000 | 676,500 |
| 7.375%, 1/15/2017 | 90,000 | 92,700 |
| 144A, 8.25%, 9/1/2020 | 85,000 | 87,125 |
| Oncor Electric Delivery Co., 144A, 5.25%, 9/30/2040 | 130,000 | 124,871 |
| RRI Energy, Inc., 7.875%, 6/15/2017 | 25,000 | 24,250 |
| San Diego Gas & Electric Co., 6.0%, 6/1/2026 | 180,000 | 207,521 |
| Suburban Propane Partners LP, 7.375%, 3/15/2020 | 15,000 | 16,013 |
| Toledo Edison Co., 7.25%, 5/1/2020 | 230,000 | 271,872 |
| | | **2,810,827** |
| **Total Corporate Bonds** (Cost $47,107,385) | | **48,428,460** |

## Mortgage-Backed Securities Pass-Throughs 5.5%

| | Principal Amount ($) (a) | Value ($) |
|---|---|---|
| Federal National Mortgage Association, 4.0%, 10/1/2023 (c) | 1,000,000 | 1,029,610 |
| Government National Mortgage Association, 4.5%, 7/1/2039 (c) | 3,000,000 | 3,115,078 |
| **Total Mortgage-Backed Securities Pass-Throughs** (Cost $4,088,477) | | **4,144,688** |

## Commercial Mortgage-Backed Securities 3.1%

| | Principal Amount ($) (a) | Value ($) |
|---|---|---|
| Citigroup Commercial Mortgage Trust, "AMP3", Series 2006-C5, 144A, 5.501%, 10/15/2049 | 127,595 | 113,277 |
| Credit Suisse Mortgage Capital Certificates Trust, "A2", Series 2007-C1, 5.268%, 2/15/2040 | 814,000 | 826,456 |
| CS First Boston Mortgage Securities Corp., "H", Series 2002-CKP1, 144A, 7.191%***, 12/15/2035 | 290,000 | 286,115 |
| JPMorgan Chase Commercial Mortgage Securities Corp.: | | |
| "F", Series 2004-LN2, 144A, 5.452%***, 7/15/2041 | 500,000 | 322,735 |
| "A4", Series 2006-LDP7, 5.872%***, 4/15/2045 | 140,000 | 153,105 |
| LB-UBS Commercial Mortgage Trust, "A3", Series 2006-C7, 5.347%, 11/15/2038 | 440,000 | 465,194 |
| Wachovia Bank Commercial Mortgage Trust, "A4", Series 2005-C22, 5.27%***, 12/15/2044 | 140,000 | 150,078 |
| **Total Commercial Mortgage-Backed Securities** (Cost $2,338,559) | | **2,316,960** |

## Collateralized Mortgage Obligations 3.5%

| | Principal Amount ($) (a) | Value ($) |
|---|---|---|
| Banc of America Mortgage Securities, "2A2", Series 2004-A, 3.493%***, 2/25/2034 | 197,420 | 181,352 |
| Bear Stearns Adjustable Rate Mortgage Trust, "2A1", Series 2005-11, 3.436%***, 12/25/2035 | 258,663 | 247,466 |
| Citicorp Mortgage Securities, Inc., "1A7", Series 2006-4, 6.0%, 8/25/2036 | 60,243 | 60,157 |
| Countrywide Home Loans, "2A5", Series 2004-13, 5.75%, 8/25/2034 | 180,689 | 164,321 |
| Federal National Mortgage Association, "BI", Series 2010-13, Interest Only, 5.0%, 12/25/2038 | 445,564 | 63,930 |
| Government National Mortgage Association, "XA", Series 2009-118, 5.0%, 12/20/2039 | 347,329 | 344,906 |
| JPMorgan Mortgage Trust, "2A1", Series 2006-A2, 5.72%***, 4/25/2036 | 711,435 | 655,719 |
| Merrill Lynch Mortgage Investors Trust: | | |
| "2A1A", Series 2005-A9, 2.7%***, 12/25/2035 | 119,270 | 119,090 |
| "2A", Series 2003-A6, 3.19%***, 10/25/2033 | 130,698 | 127,749 |
| Morgan Stanley Mortgage Loan Trust, "5A5", Series 2005-4, 5.5%, 8/25/2035 | 133,860 | 130,053 |
| Vericrest Opportunity Loan Transferee, "M", Series 2010-NPL1, 144A, 6.0%, 5/25/2039 | 149,454 | 146,521 |

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| | | Principal Amount ($) (a) | Value ($) |
|---|---|---|---|
| Washington Mutual Mortgage Pass-Through Certificates Trust, "1A1", Series 2005-AR12, 2.721%***, 10/25/2035 | | 119,151 | 114,132 |
| Wells Fargo Mortgage-Backed Securities Trust: | | | |
| "A3", Series 2005-4, 5.0%, 4/25/2035 | | 115,095 | 114,565 |
| "A19", Series 2006-11, 6.0%, 9/25/2036 | | 124,533 | 124,412 |
| **Total Collateralized Mortgage Obligations** (Cost $2,503,586) | | | **2,594,373** |

## Government & Agency Obligations 17.2%

### Other Government Related (d) 5.3%

| | | Principal Amount ($) (a) | Value ($) |
|---|---|---|---|
| Citibank NA, FDIC Guaranteed, 0.316%***, 5/7/2012 | | 650,000 | 650,528 |
| International Bank for Reconstruction & Development, 5.25%***, 4/9/2025 | | 290,000 | 284,461 |
| JPMorgan Chase & Co., Series 3, FDIC Guaranteed, 0.553%***, 12/26/2012 | | 232,000 | 233,177 |
| Kreditanstalt fuer Wiederaufbau, 1.35%, 1/20/2014 | JPY | 185,000,000 | 2,347,476 |
| Pemex Project Funding Master Trust, 5.75%, 3/1/2018 | | 460,000 | 491,826 |
| | | | **4,007,468** |

### Sovereign Bonds 7.0%

| | | Principal Amount ($) (a) | Value ($) |
|---|---|---|---|
| Federative Republic of Brazil: | | | |
| 8.875%, 10/14/2019 | | 295,000 | 389,400 |
| 12.5%, 1/5/2016 | BRL | 250,000 | 174,398 |
| Government of Canada, 4.5%, 6/1/2015 | CAD | 350,000 | 384,461 |
| Republic of Argentina, 5.83%, 12/31/2033 | ARS | 375 | 176 |
| Republic of El Salvador, 144A, 7.65%, 6/15/2035 | | 156,000 | 164,970 |
| Republic of Lithuania: | | | |
| 144A, 5.125%, 9/14/2017 | | 205,000 | 201,965 |
| 144A, 7.375%, 2/11/2020 | | 195,000 | 215,404 |
| Republic of Panama, 9.375%, 1/16/2023 | | 500,000 | 688,750 |
| Republic of Peru, 7.35%, 7/21/2025 | | 285,000 | 346,703 |
| Republic of Poland, 6.375%, 7/15/2019 | | 345,000 | 386,473 |
| Republic of South Africa, 6.875%, 5/27/2019 | | 220,000 | 257,675 |
| Republic of Uruguay: | | | |
| 7.625%, 3/21/2036 | | 60,000 | 71,250 |
| 9.25%, 5/17/2017 | | 105,000 | 135,450 |
| Republic of Venezuela, 9.25%, 9/15/2027 | | 150,000 | 111,750 |
| Russian Federation, REG S, 7.5%, 3/31/2030 | | 478,731 | 553,652 |
| United Kingdom Treasury Bond, 3.75%, 9/7/2019 | GBP | 750,000 | 1,206,322 |
| | | | **5,288,799** |

### US Government Sponsored Agency 0.1%

| | | Principal Amount ($) (a) | Value ($) |
|---|---|---|---|
| Federal Home Loan Mortgage Corp., 1.125%, 12/15/2011 | | 100,000 | **100,695** |

### US Treasury Obligations 4.8%

| | | Principal Amount ($) (a) | Value ($) |
|---|---|---|---|
| US Treasury Bill, 0.185%****, 3/17/2011 (e) | | 99,000 | 98,978 |
| US Treasury Bond, 4.375%, 5/15/2040 | | 551,000 | 553,667 |
| US Treasury Notes: | | | |
| 0.875%, 2/29/2012 | | 2,250,000 | 2,263,095 |
| 2.625%, 11/15/2020 | | 759,000 | 715,950 |
| | | | **3,631,690** |
| **Total Government & Agency Obligations** (Cost $12,104,046) | | | **13,028,652** |

## Loan Participations and Assignments 3.7%

### Senior Loans*** 3.2%

| | | Principal Amount ($) (a) | Value ($) |
|---|---|---|---|
| Buffets, Inc.: | | | |
| Letter of Credit, First Lien, 7.539%, 4/22/2015 (PIK) | | 11,948 | 9,141 |
| Term Loan B, 12.0%, 4/21/2015 (PIK) | | 69,862 | 65,636 |
| Burger King Corp., New Term Loan B, 6.25%, 10/19/2016 | | 85,000 | 86,410 |
| Charter Communications Operating LLC: | | | |
| Replacement Term Loan, 2.27%, 3/6/2014 | | 18,104 | 17,904 |
| Term Loan, 3.56%, 9/6/2016 | | 208,149 | 205,287 |
| New Term Loan, 7.25%, 3/6/2014 | | 94,108 | 97,945 |
| Clear Channel Communication, Term Loan B, LIBOR plus 3.65%, 1/28/2016 | | 110,000 | 95,920 |
| Dunkin' Brands, Inc., Term Loan B, 5.75%, 11/23/2017 | | 70,000 | 70,943 |
| Ford Motor Co., Term Loan B1, 3.02%, 12/16/2013 | | 183,850 | 183,803 |
| Hawker Beechcraft Acquisition Co., LLC: | | | |
| Term Loan, 2.261%, 3/26/2014 | | 165,210 | 145,300 |
| Letter of Credit, 2.289%, 3/26/2014 | | 9,903 | 8,709 |
| IASIS Healthcare LLC, Term Loan, 5.538%, 6/13/2014 (PIK) | | 109,416 | 105,559 |
| Kabel Deutschland GmbH, Term Loan, 8.272%, 11/19/2014 (PIK) | EUR | 93,849 | 126,321 |
| Momentive Specialty Chemicals, Inc.: | | | |
| Term Loan C1, 2.563%, 5/6/2013 | | 114,379 | 112,556 |
| Term Loan C2, 2.563%, 5/6/2013 | | 58,987 | 58,046 |
| Nuveen Investments, Inc., First Lien, Term Loan, 3.303%, 11/13/2014 | | 115,000 | 110,137 |
| OSI Restaurant Partners LLC: | | | |
| Term Loan, 2.563%, 6/14/2013 | | 11,007 | 10,537 |
| Term Loan B, 2.625%, 6/14/2014 | | 113,924 | 109,062 |
| Pinafore LLC, Term Loan B, 6.25%, 9/29/2016 | | 522,909 | 530,918 |
| Roundy's Supermarkets, Inc., Second Lien, Term Loan, LIBOR plus 8.0%, 4/18/2016 | | 65,000 | 66,097 |

*The accompanying notes are an integral part of the financial statements.*

| | Principal Amount ($) (a) | Value ($) |
|---|---|---|
| Syniverse Technologies, Inc., Term Loan B, LIBOR plus 3.75%, 12/21/2017 | 50,000 | 50,641 |
| Tribune Co., Term Loan B, LIBOR plus 3.0%, 6/4/2014** | 88,875 | 62,124 |
| US Foodservice, Inc., Term Loan B, 2.76%, 7/3/2014 | 84,346 | 77,556 |
| VML US Finance LLC: | | |
| Delayed Draw Term Loan B, 4.8%, 5/25/2012 | 18,154 | 18,177 |
| Term Loan B, 4.8%, 5/27/2013 | 31,429 | 31,469 |
| | | **2,456,198** |
| **Sovereign Loans 0.5%** | | |
| BOM Capital PLC, 144A, 6.699%, 3/11/2015 | 205,000 | 211,150 |
| VTB Bank, 144A, 6.875%, 5/29/2018 | 145,000 | 153,337 |
| | | **364,487** |
| **Total Loan Participations and Assignments** (Cost $2,735,317) | | **2,820,685** |

## Preferred Securities 0.7%

| | Principal Amount ($) (a) | Value ($) |
|---|---|---|
| **Financials 0.6%** | | |
| Capital One Capital VI, 8.875%, 5/15/2040 | 330,000 | 343,613 |
| USB Capital XIII Trust, 6.625%, 12/15/2039 | 145,000 | 148,107 |
| | | **491,720** |
| **Materials 0.1%** | | |
| Hercules, Inc., 6.5%, 6/30/2029 | 95,000 | **73,625** |
| **Total Preferred Securities** (Cost $526,972) | | **565,345** |

## Other Investments 0.0%

| | Units | Value ($) |
|---|---|---|
| **Consumer Discretionary** | | |
| AOT Bedding Super Holdings LLC* (Cost $4,000) | 4 | **4,000** |

## Common Stocks 0.0%

| | Shares | Value ($) |
|---|---|---|
| **Consumer Discretionary 0.0%** | | |
| Buffets Restaurants Holdings, Inc.* | 2,318 | 8,113 |
| Dex One Corp.* | 540 | 4,029 |
| SuperMedia, Inc.* | 99 | 862 |
| Trump Entertainment Resorts, Inc.* | 6 | 109 |
| Vertis Holdings, Inc.* | 940 | 0 |
| | | **13,113** |
| **Industrials 0.0%** | | |
| Congoleum Corp.* | 125,000 | 0 |
| Quad Graphics, Inc.* | 69 | 2,847 |
| | | **2,847** |
| **Materials 0.0%** | | |
| GEO Specialty Chemicals, Inc.* | 2,058 | **1,749** |
| **Total Common Stocks** (Cost $279,466) | | **17,709** |

## Preferred Stock 0.1%

| | Shares | Value ($) |
|---|---|---|
| **Financials** | | |
| Ally Financial, Inc., Series G, 144A, 7.0% (Cost $100,132) | 110 | **103,967** |

## Warrants 0.0%

| | Shares | Value ($) |
|---|---|---|
| **Consumer Discretionary 0.0%** | | |
| Reader's Digest Association, Inc., Expiration Date 2/19/2014* | 159 | **5** |
| **Materials 0.0%** | | |
| Hercules Trust II, Expiration Date 3/31/2029* | 85 | **967** |
| **Total Warrants** (Cost $17,432) | | **972** |

## Call Options Purchased 0.0%

| | Contracts | Value ($) |
|---|---|---|
| Floating Rate — LIBOR, Effective Date 5/16/2011, Expiration Date 5/16/2012, Cap Rate 3.0% (Cost $54,460) | 14,000,000 | **467** |

## Securities Lending Collateral 0.2%

| | Shares | Value ($) |
|---|---|---|
| Daily Assets Fund Institutional, 0.27% (f) (g) (Cost $122,734) | 122,734 | **122,734** |

## Cash Equivalents 5.6%

| | Shares | Value ($) |
|---|---|---|
| Central Cash Management Fund, 0.19% (f) (Cost $4,269,126) | 4,269,126 | **4,269,126** |

| | % of Net Assets | Value ($) |
|---|---|---|
| **Total Investment Portfolio** (Cost $76,251,692)† | 103.6 | **78,418,138** |
| **Other Assets and Liabilities, Net** | (3.6) | **(2,711,284)** |
| **Net Assets** | 100.0 | **75,706,854** |

* *Non-income producing security.*

** *Non-income producing security. Issuer has defaulted on the payment of principal or interest or has filed for bankruptcy. The following table represents bonds and senior loans that are in default:*

| Securities | Coupon | Maturity Date | Principal Amount ($) | | Acquisition Cost ($) | Value ($) |
|---|---|---|---|---|---|---|
| CanWest MediaWorks LP | 9.25% | 8/1/2015 | 50,000 | USD | 50,000 | 8,500 |
| Fontainebleau Las Vegas Holdings LLC | 11.0% | 6/15/2015 | 65,000 | USD | 65,225 | 228 |
| Grupo Iusacell Celular SA de CV | 10.0% | 3/31/2012 | 29,280 | USD | 27,863 | 10,834 |

*The accompanying notes are an integral part of the financial statements.*

| Securities | Coupon | Maturity Date | Principal Amount ($) | | Acquisition Cost ($) | Value ($) |
|---|---|---|---|---|---|---|
| Radnor Holdings Corp. | 11.0% | 3/15/2010 | 25,000 | USD | 15,888 | 3 |
| Tribune Co. | LIBOR plus 3.0% | 6/4/2014 | 88,875 | USD | 88,819 | 62,124 |
| Tropicana Entertainment LLC | 9.625% | 12/15/2014 | 150,000 | USD | 122,979 | 77 |
| Vertis, Inc. | 13.5% | 4/1/2014 | 24,348 | USD | 9,890 | 730 |
| Wolverine Tube, Inc. | 15.0% | 3/31/2012 | 91,631 | USD | 91,631 | 49,481 |
| Young Broadcasting, Inc. | 8.75% | 1/15/2014 | 275,000 | USD | 224,631 | 3 |
| | | | | | **696,926** | **131,980** |

*** *These securities are shown at their current rate as of December 31, 2010. Floating rate securities' yields vary with a designated market index or market rate, such as the coupon-equivalent of the US Treasury bill rate.*

**** *Annualized yield at time of purchase; not a coupon rate.*

† *The cost for federal income tax purposes was $76,320,197. At December 31, 2010, net unrealized appreciation for all securities based on tax cost was $2,097,941. This consisted of aggregate gross unrealized appreciation for all securities in which there was an excess of value over tax cost of $3,741,864 and aggregate gross unrealized depreciation for all securities in which there was an excess of tax cost over value of $1,643,923.*

(a) *Principal amount stated in US dollars unless otherwise noted.*

(b) *All or a portion of these securities were on loan (see Notes to Financial Statements). The value of all securities loaned at December 31, 2010 amounted to $116,902, which is 0.2% of net assets.*

(c) *Delayed delivery security included.*

(d) *Government-backed debt issued by financial companies or government sponsored enterprises.*

(e) *At December 31, 2010, this security has been pledged, in whole or in part, to cover initial margin requirements for open futures contracts.*

(f) *Affiliated fund managed by Deutsche Investment Management Americas Inc. The rate shown is the annualized seven-day yield at period end.*

(g) *Represents collateral held in connection with securities lending. Income earned by the Fund is net of borrower rebates.*

*144A: Security exempt from registration under Rule 144A of the Securities Act of 1933. These securities may be resold in transactions exempt from registration, normally to qualified institutional buyers.*

*FDIC: Federal Deposit Insurance Corp.*

*Interest Only: Interest Only (IO) bonds represent the "interest only" portion of payments on a pool of underlying mortgages or mortgage-backed securities. IO securities are subject to prepayment risk of the pool of underlying mortgages.*

*PIK: Denotes that all or a portion of the income is paid in-kind.*

*REG S: Securities sold under Regulation S may not be offered, sold or delivered within the United States or to, or for the account or benefit of, US persons, except pursuant to an exemption from, or in a transaction not subject to, the registration requirements of the Securities Act of 1933.*

*REIT: Real Estate Investment Trust*

*At December 31, 2010, open futures contracts purchased were as follows:*

| Futures | Currency | Expiration Date | Contracts | Notional Value ($) | Unrealized Appreciation/ (Depreciation) ($) |
|---|---|---|---|---|---|
| 10 Year Australian Treasury Bond | AUD | 3/15/2011 | 34 | 3,592,345 | 26,808 |
| 10 Year US Treasury Note | USD | 3/22/2011 | 47 | 5,660,563 | (153,853) |
| 2 Year US Treasury Note | USD | 3/31/2011 | 74 | 16,199,063 | 11,578 |
| DAX Index | EUR | 3/18/2011 | 1 | 231,414 | (4,326) |
| Federal Republic of Germany Euro-Bund | EUR | 3/8/2011 | 7 | 1,172,162 | 10,009 |
| Federal Republic of Germany Euro-Schatz | EUR | 3/8/2011 | 5 | 728,317 | (811) |
| FTSE 100 Index | GBP | 3/18/2011 | 6 | 551,266 | 5,332 |
| Hang Seng Index | HKD | 1/28/2011 | 1 | 148,080 | 1,988 |
| IBEX 35 Index | EUR | 1/21/2011 | 1 | 130,837 | (3,337) |
| S&P 500 E-Mini Index | USD | 3/18/2011 | 6 | 375,900 | 5,130 |
| TOPIX Index | JPY | 3/11/2011 | 3 | 331,075 | 6,577 |
| United Kingdom Long Gilt Bond | GBP | 3/29/2011 | 16 | 2,980,748 | (5,477) |
| **Total net unrealized depreciation** | | | | | **(100,382)** |

*At December 31, 2010, open futures contracts sold were as follows:*

| Futures | Currency | Expiration Date | Contracts | Notional Value ($) | Unrealized Appreciation/ (Depreciation) ($) |
|---|---|---|---|---|---|
| 10 Year Canadian Government Bond | CAD | 3/22/2011 | 19 | 2,341,989 | (9,848) |
| 10 Year Japanese Government Bond | JPY | 3/10/2011 | 6 | 10,391,181 | (50,690) |
| AEX Index | EUR | 1/21/2011 | 2 | 189,648 | (1,550) |

*The accompanying notes are an integral part of the financial statements.*

| Futures | Currency | Expiration Date | Contracts | Notional Value ($) | Unrealized Appreciation/ (Depreciation) ($) |
|---|---|---|---|---|---|
| ASX SPI 200 Index | AUD | 3/17/2011 | 3 | 362,838 | 3,375 |
| CAC 40 Index | EUR | 1/21/2011 | 3 | 152,719 | 3,668 |
| DJ Euro Stoxx 50 Index | EUR | 3/18/2011 | 11 | 410,698 | 10,437 |
| Federal Republic of Germany Euro-Bund | EUR | 3/8/2011 | 42 | 7,032,973 | 45,686 |
| FTSE MIB Index | EUR | 3/18/2011 | 2 | 269,999 | 7,416 |
| Russell 2000 E-Mini Index | USD | 3/18/2011 | 1 | 78,230 | (865) |
| S&P TSX 60 Index | CAD | 3/17/2011 | 1 | 154,300 | (2,547) |
| **Total net unrealized appreciation** | | | | | **5,082** |

*At December 31, 2010, open written interest rate option contracts were as follows:*

| Effective/ Expiration Date | Cash Flows Paid | Contract Amount | Strike Rate (%) | Value ($) | Premiums Received ($) | Unrealized Depreciation ($) |
|---|---|---|---|---|---|---|
| Call Option<br>5/16/2011<br>5/16/2012 | 30-year USD Swap Rate —<br>10-year USD Swap Rate | 29,000,000 | 0.6 | (35,163) | 30,740 | **(4,423)** |

*At December 31, 2010, open credit default swap contracts sold were as follows:*

| Effective/ Expiration Date | Notional Amount ($) (i) | Fixed Cash Flows Received | Underlying Debt Obligation/Quality Rating (h) | Value ($) | Upfront Payments Paid/ (Received) ($) | Unrealized Appreciation/ (Depreciation) ($) |
|---|---|---|---|---|---|---|
| 9/21/2009<br>12/20/2014 | 290,000[1] | 1.0% | Berkshire Hathaway Finance Corp.,<br>4.625%, 10/15/2013, AA | (1,114) | (7,340) | 6,226 |
| 6/21/2010<br>9/20/2013 | 70,000[2] | 5.0% | Ford Motor Co.,<br>6.5%, 8/1/2018, B | 7,023 | 858 | 6,165 |
| 6/21/2010<br>9/20/2015 | 90,000[3] | 5.0% | Ford Motor Co.,<br>6.5%, 8/1/2018, B | 10,162 | (1,604) | 11,766 |
| 3/22/2010<br>6/20/2015 | 290,000[4] | 1.0% | Freeport-McMoRan Copper & Gold, Inc.,<br>8.375%, 4/1/2017, BBB- | (138) | (1,646) | 1,508 |
| 9/20/2010<br>12/20/2015 | 1,630,000[5] | 1.0% | Markit iTraxx SovX Western Europe | (78,525) | (50,148) | (28,377) |
| **Total net unrealized depreciation** | | | | | | **(2,712)** |

(h) *The quality ratings represent the lower of Moody's Investors Service, Inc. ("Moody's") or Standard & Poor's Corporation ("S&P") credit ratings and are unaudited.*

(i) *The maximum potential amount of future undiscounted payments that the Fund could be required to make under a credit default swap contract would be the notional amount of the contract. These potential amounts would be partially offset by any recovery values of the referenced debt obligation or net amounts received from the settlement of buy protection credit default swap contracts entered into by the Fund for the same referenced debt obligation.*

*At December 31, 2010, open interest rate swaps contracts were as follows:*

| Effective/ Expiration Date | Notional Amount ($) | Cash Flows Paid by the Fund | Cash Flows Received by the Fund | Value ($) | Upfront Payments Paid ($) | Unrealized Depreciation ($) |
|---|---|---|---|---|---|---|
| 10/27/2010<br>10/27/2020 | 1,500,000[4] | Fixed — 4.12% | Floating — LIBOR | (109,121) | 525 | (109,646) |
| 11/24/2010<br>11/24/2020 | 1,300,000[6] | Fixed — 3.96% | Floating — LIBOR | (71,822) | 591 | (72,413) |
| 10/28/2010<br>10/28/2025 | 140,000[4] | Fixed — 4.138% | Floating — LIBOR | (4,412) | — | (4,412) |
| 11/1/2010<br>11/1/2025 | 240,000[6] | Fixed — 4.292% | Floating — LIBOR | (21,668) | — | (21,668) |
| 11/12/2010<br>11/12/2025 | 280,000[4] | Fixed — 4.285% | Floating — LIBOR | (8,155) | — | (8,155) |
| 11/15/2010<br>11/15/2025 | 280,000[6] | Fixed — 4.585% | Floating — LIBOR | (23,555) | — | (23,555) |
| 11/16/2010<br>11/16/2025 | 140,000[4] | Fixed — 4.584% | Floating — LIBOR | (2,817) | — | (2,817) |
| 11/19/2010<br>11/19/2025 | 140,000[6] | Fixed — 4.784% | Floating — LIBOR | (11,110) | — | (11,110) |
| 11/23/2010<br>11/23/2025 | 70,000[4] | Fixed — 4.834% | Floating — LIBOR | (924) | — | (924) |
| **Total unrealized depreciation** | | | | | | **(254,700)** |

*The accompanying notes are an integral part of the financial statements.*

*At December 31, 2010, open total return swap contracts were as follows:*

| Effective/ Expiration Date | Notional Amount ($) | Fixed Cash Flows Paid | Reference Entity | Value ($) | Upfront Payment Paid ($) | Unrealized Appreciation ($) |
|---|---|---|---|---|---|---|
| 5/28/2010<br>6/1/2012 | 2,800,000[2] | 0.45% | Global Interest Rate Strategy Index | 4,545 | 1,867 | **2,678** |

*Counterparties:*

1 *JPMorgan Chase Securities, Inc.*
2 *Citigroup, Inc.*
3 *Bank of America*
4 *Morgan Stanley*
5 *The Goldman Sachs & Co.*
6 *Barclays Bank PLC*

*LIBOR: London InterBank Offered Rate*

*At December 31, 2010, the Fund had the following open forward foreign currency exchange contracts:*

| Contracts to Deliver | | In Exchange For | | Settlement Date | Unrealized Appreciation ($) | Counterparty |
|---|---|---|---|---|---|---|
| EUR | 1,510,000 | USD | 2,091,391 | 1/14/2011 | 69,078 | UBS AG |
| USD | 1,740,512 | CAD | 1,753,000 | 1/25/2011 | 21,681 | Bank of New York Mellon Corp. |
| USD | 1,325,283 | NOK | 7,858,000 | 1/25/2011 | 19,708 | Bank of New York Mellon Corp. |
| USD | 3,376,310 | AUD | 3,420,000 | 1/25/2011 | 109,775 | UBS AG |
| USD | 1,413,474 | SEK | 9,637,000 | 1/25/2011 | 18,182 | HSBC Bank USA |
| USD | 509,540 | JPY | 42,741,000 | 1/25/2011 | 17,047 | Royal Bank of Scotland PLC |
| GBP | 981,000 | USD | 1,532,749 | 1/25/2011 | 3,583 | Royal Bank of Scotland PLC |
| **Total unrealized appreciation** | | | | | **259,054** | |

| Contracts to Deliver | | In Exchange For | | Settlement Date | Unrealized Depreciation ($) | Counterparty |
|---|---|---|---|---|---|---|
| CAD | 236,000 | USD | 235,609 | 1/14/2011 | (1,604) | Credit Suisse |
| EUR | 200,000 | USD | 262,132 | 1/14/2011 | (5,724) | Morgan Stanley |
| EUR | 368,900 | USD | 488,408 | 1/20/2011 | (4,535) | JPMorgan Chase Securities, Inc. |
| EUR | 170,000 | USD | 226,727 | 1/25/2011 | (434) | Royal Bank of Scotland PLC |
| NZD | 2,974,000 | USD | 2,212,269 | 1/25/2011 | (100,137) | UBS AG |
| CHF | 2,415,000 | USD | 2,514,983 | 1/25/2011 | (68,734) | HSBC Bank USA |
| GBP | 925,000 | USD | 1,440,234 | 2/22/2011 | (1,967) | Morgan Stanley |
| JPY | 195,000,000 | USD | 2,325,665 | 2/22/2011 | (79,250) | Morgan Stanley |
| **Total unrealized depreciation** | | | | | **(262,385)** | |

**Currency Abbreviations**

| | | | | | |
|---|---|---|---|---|---|
| ARS | Argentine Peso | EUR | Euro | NOK | Norwegian Krone |
| AUD | Australian Dollar | GBP | British Pound | NZD | New Zealand Dollar |
| BRL | Brazilian Real | HKD | Hong Kong Dollar | SEK | Swedish Krona |
| CAD | Canadian Dollar | JPY | Japanese Yen | USD | United States Dollar |
| CHF | Swiss Franc | | | | |

*For information on the Fund's policy and additional disclosures regarding option contracts, futures contracts, interest rate swap contracts, credit default swap contracts, total return swap contracts and forward foreign currency exchange contracts, please refer to Note B in the accompanying Notes to Financial Statements.*

## Fair Value Measurements

*Various inputs are used in determining the value of the Fund's investments. These inputs are summarized in three broad levels. Level 1 includes quoted prices in active markets for identical securities. Level 2 includes other significant observable inputs (including quoted prices for similar securities, interest rates, prepayment speeds, and credit risk). Level 3 includes significant unobservable inputs (including the Fund's own assumptions in determining the fair value of investments). The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities.*

*The accompanying notes are an integral part of the financial statements.*

*The following is a summary of the inputs used as of December 31, 2010 in valuing the Fund's investments. For information on the Fund's policy regarding the valuation of investments, please refer to the Security Valuation section of Note A in the accompanying Notes to Financial Statements.*

| Assets | Level 1 | Level 2 | Level 3 | Total |
|---|---|---|---|---|
| Fixed Income Investments (j) | | | | |
| Corporate Bonds | $ — | $ 47,884,841 | $ 543,619 | $ 48,428,460 |
| Mortgage-Backed Securities Pass-Throughs | — | 4,144,688 | — | 4,144,688 |
| Commercial Mortgage-Backed Securities | — | 2,316,960 | — | 2,316,960 |
| Collateralized Mortgage Obligations | — | 2,594,373 | — | 2,594,373 |
| Government & Agency Obligations | — | 12,645,213 | 284,461 | 12,929,674 |
| Loan Participations and Assignments | — | 2,820,685 | — | 2,820,685 |
| Preferred Securities | — | 565,345 | — | 565,345 |
| Common Stocks | 15,851 | — | 1,858 | 17,709 |
| Preferred Stock | — | 103,967 | — | 103,967 |
| Warrants | — | — | 972 | 972 |
| Other Investments | — | — | 4,000 | 4,000 |
| Short-Term Investments | 4,391,860 | 98,978 | — | 4,490,838 |
| Derivatives (k) | — | 287,397 | 467 | 287,864 |
| **Total** | **$ 4,407,711** | **$ 73,462,447** | **$ 835,377** | **$ 78,705,535** |
| **Liabilities** | | | | |
| Derivatives (k) | $ (95,300) | $ (545,462) | $ (35,163) | $ (675,925) |
| **Total** | **$ (95,300)** | **$ (545,462)** | **$ (35,163)** | **$ (675,925)** |

*There have been no significant transfers between Level 1 and Level 2 fair value measurements during the year ended December 31, 2010.*

(j) *See Investment Portfolio for additional detailed categorizations.*

(k) *Derivatives include value of open options purchased, unrealized appreciation (depreciation) on open futures contracts, credit default swap contracts, interest rate swap contracts, total return swap contracts, forward foreign currency exchange contracts and written options, at value.*

## Level 3 Reconciliation

*The following is a reconciliation of the Fund's Level 3 investments for which significant unobservable inputs were used in determining value:*

| | Corporate Bonds | Asset-Backed | Government & Agency Obligations | Loan Participations and Assignments | Common Stocks |
|---|---|---|---|---|---|
| **Balance as of December 31, 2009** | $1,399,392 | $ 600,572 | $ — | $ 72,237 | $ 1,749 |
| Total realized gain (loss) | — | 57,024 | — | 3,736 | — |
| Change in unrealized appreciation (depreciation) | 141,636 | (25,710) | (5,539) | 7,898 | (12) |
| Amortization premium/ discount | 16,809 | — | — | 407 | — |
| Net purchases (sales) | (1,000,000) | (631,886) | 290,000 | (84,278) | 121 |
| Transfers into Level 3 | 8,402 (l) | — | — | — | — |
| Transfers (out) of Level 3 | (22,620) (m) | — | — | — | — |
| **Balance as of December 31, 2010** | **$ 543,619** | **$ —** | **$ 284,461** | **$ —** | **$ 1,858** |
| **Net change in unrealized appreciation (depreciation) from investments still held as of December 31, 2010** | **$ (59,208)** | **$ —** | **$ (5,539)** | **$ —** | **$ (12)** |

| | Warrants | Convertible Preferred Stocks | Call Options Purchased | Other Investments | Total | Written Options |
|---|---|---|---|---|---|---|
| **Balance as of December 31, 2009** | $ 625 | $ 0 | $ — | $ — | **$2,074,575** | $ — |
| Total realized gain (loss) | — | (4,191) | — | — | **56,569** | — |
| Change in unrealized appreciation (depreciation) | 347 | 4,191 | (53,993) | 0 | **68,818** | (4,423) |
| Amortization premium/ discount | — | — | — | — | **17,216** | — |
| Net purchases (sales) | — | 0 | 54,460 | 4,000 | **(1,367,583)** | (30,740) |
| Transfers into Level 3 | — | — | — | — | **8,402** | — |
| Transfers (out) of Level 3 | — | — | — | — | **(22,620)** | — |
| **Balance as of December 31, 2010** | **$ 972** | **$ —** | **$ 467** | **$ 4,000** | **$ 835,377** | **$ (35,163)** |
| **Net change in unrealized appreciation (depreciation) from investments still held as of December 31, 2010** | **$ 972** | **$ —** | **$ (53,993)** | **$ 0** | **$ (117,780)** | **$ (4,423)** |

*Transfers between price levels are recognized at the beginning of the reporting period.*

(l) *The investment was transferred from Level 2 to Level 3 because of the lack of observable market data due to a decrease in market activity.*

(m) *The investment was transferred from Level 3 to Level 2 as a result of the availability of a pricing source supported by observable inputs.*

*The accompanying notes are an integral part of the financial statements.*

# Statement of Assets and Liabilities

as of December 31, 2010

| Assets | | |
|---|---|---|
| Investments: | | |
| Investments in unaffiliated securities, at value (cost $71,859,832) — including $116,902 of securities loaned | $ | 74,026,278 |
| Investment in Daily Assets Fund Institutional (cost $122,734)* | | 122,734 |
| Investment in Central Cash Management Fund (cost $4,269,126) | | 4,269,126 |
| Total investments, at value (cost $76,251,692) | | 78,418,138 |
| Cash | | 185,479 |
| Foreign currency, at value (cost $122,513) | | 124,704 |
| Deposit with brokers for open futures contracts | | 918,646 |
| Receivable for investments sold | | 104,426 |
| Interest receivable | | 1,081,310 |
| Upfront payments paid on swaps | | 3,841 |
| Unrealized appreciation on open swap contracts | | 28,343 |
| Unrealized appreciation on open forward foreign currency exchange contracts | | 259,054 |
| Foreign taxes recoverable | | 4,684 |
| Other assets | | 447 |
| Total assets | | 81,129,072 |

| Liabilities | | |
|---|---|---|
| Payable for investments purchased | | 280,508 |
| Payable for investments purchased — delayed delivery securities | | 4,097,602 |
| Payable upon return of securities loaned | | 122,734 |
| Payable for daily variation margin on open futures contracts | | 86,632 |
| Payable for Fund shares redeemed | | 64,777 |
| Options written, at value (premiums received $30,740) | | 35,163 |
| Upfront payments received on swaps | | 60,738 |
| Unrealized depreciation on open swap contracts | | 283,077 |
| Unrealized depreciation on open forward foreign currency exchange contracts | | 262,385 |
| Accrued management fee | | 19,509 |
| Other accrued expenses and payables | | 109,093 |
| Total liabilities | | 5,422,218 |
| **Net assets, at value** | **$** | **75,706,854** |

| Net Assets Consist of | | |
|---|---|---|
| Undistributed net investment income | | 4,058,018 |
| Net unrealized appreciation (depreciation) on: | | |
| Investments | | 2,166,446 |
| Swap contracts | | (254,734) |
| Written options | | (4,423) |
| Futures | | (95,300) |
| Foreign currency | | 8,924 |
| Accumulated net realized gain (loss) | | (944,838) |
| Paid-in capital | | 70,772,761 |
| **Net assets, at value** | **$** | **75,706,854** |
| **Class A** | | |
| **Net Asset Value,** offering and redemption price per share ($75,706,854 ÷ 6,329,747 outstanding shares of beneficial interest, no par value, unlimited number of shares authorized) | **$** | **11.96** |

* *Represents collateral on securities loaned.*

# Statement of Operations

for the year ended December 31, 2010

| Investment Income | | |
|---|---|---|
| Income: | | |
| Interest (net of foreign taxes withheld of $164) | $ | 4,821,293 |
| Income distributions — Central Cash Management Fund | | 10,113 |
| Securities lending income, including income from Daily Assets Fund Institutional, net of borrower rebates | | 2,499 |
| Total income | | 4,833,905 |
| Expenses: | | |
| Management fee | | 410,735 |
| Administration fee | | 74,679 |
| Services to shareholders | | 1,730 |
| Custodian fee | | 70,329 |
| Legal fees | | 17,266 |
| Audit and tax fees | | 66,284 |
| Trustees' fees and expenses | | 5,347 |
| Reports to shareholders | | 17,398 |
| Other | | 42,290 |
| Total expenses before expense reductions | | 706,058 |
| Expense reductions | | (67,414) |
| Total expenses after expense reductions | | 638,644 |
| **Net investment income (loss)** | | **4,195,261** |

| Realized and Unrealized Gain (Loss) | | |
|---|---|---|
| Net realized gain (loss) from: | | |
| Investments | | 1,957,117 |
| Swap contracts | | (37,558) |
| Futures | | 59,063 |
| Foreign currency | | 404,118 |
| | | 2,382,740 |
| Change in net unrealized appreciation (depreciation) on: | | |
| Investments | | 1,121,385 |
| Swap contracts | | (309,862) |
| Written options | | (4,423) |
| Futures | | (1,691) |
| Foreign currency | | (282,893) |
| | | 522,516 |
| **Net gain (loss)** | | **2,905,256** |
| **Net increase (decrease) in net assets resulting from operations** | **$** | **7,100,517** |

*The accompanying notes are an integral part of the financial statements.*

# Statement of Changes in Net Assets

| Increase (Decrease) in Net Assets | Years Ended December 31, 2010 | 2009 |
|---|---|---|
| Operations: | | |
| Net investment income | $ 4,195,261 | $ 4,244,300 |
| Net realized gain (loss) | 2,382,740 | 564,606 |
| Change in net unrealized appreciation (depreciation) | 522,516 | 9,572,764 |
| Net increase (decrease) in net assets resulting from operations | 7,100,517 | 14,381,670 |
| Distributions to shareholders from: | | |
| Net investment income: | | |
| Class A | (4,806,010) | (3,708,667) |
| Fund share transactions: | | |
| **Class A** | | |
| Proceeds from shares sold | 11,245,997 | 9,943,530 |
| Shares converted* | — | 44,195 |
| Reinvestment of distributions | 4,806,010 | 3,708,667 |
| Payments for shares redeemed | (16,514,815) | (23,212,559) |
| Net increase (decrease) in net assets from Class A share transactions | (462,808) | (9,516,167) |
| **Class B** | | |
| Shares converted* | — | (44,195) |
| Payments for shares redeemed | — | (151) |
| Net increase (decrease) in net assets from Class B share transactions | — | (44,346) |
| **Increase (decrease) in net assets** | 1,831,699 | 1,112,490 |
| Net assets at beginning of period | 73,875,155 | 72,762,665 |
| Net assets at end of period (including undistributed net investment income of $4,058,018 and $4,333,267, respectively) | **$ 75,706,854** | **$ 73,875,155** |

| Other Information | | |
|---|---|---|
| **Class A** | | |
| Shares outstanding at beginning of period | 6,362,456 | 7,250,530 |
| Shares sold | 957,272 | 943,043 |
| Shares converted* | — | 4,547 |
| Shares issued to shareholders in reinvestment of distributions | 420,473 | 392,867 |
| Shares redeemed | (1,410,454) | (2,228,531) |
| Net increase (decrease) in Class A shares | (32,709) | (888,074) |
| Shares outstanding at end of period | **6,329,747** | **6,362,456** |
| **Class B** | | |
| Shares outstanding at beginning of period | — | 4,594 |
| Shares converted* | — | (4,579) |
| Shares redeemed | — | (15) |
| Net increase (decrease) in Class B shares | — | (4,594) |
| Shares outstanding at end of period | **—** | **—** |

* *On March 6, 2009, Class B shares converted into Class A shares.*

*The accompanying notes are an integral part of the financial statements.*

# Financial Highlights

## Class A

| Years Ended December 31, | 2010 | 2009 | 2008 | 2007 | 2006 |
|---|---|---|---|---|---|
| **Selected Per Share Data** | | | | | |
| **Net asset value, beginning of period** | **$11.61** | **$10.03** | **$11.70** | **$11.80** | **$11.50** |
| *Income (loss) from investment operations:* | | | | | |
| Net investment income[a] | .66 | .63 | .55 | .63 | .62 |
| Net realized and unrealized gain (loss) | .47 | 1.50 | (1.38) | (.01) | .36 |
| **Total from investment operations** | 1.13 | 2.13 | (.83) | .62 | .98 |
| *Less distributions from:* | | | | | |
| Net investment income | (.78) | (.55) | (.69) | (.72) | (.57) |
| Net realized gains | — | — | (.15) | — | (.11) |
| **Total distributions** | (.78) | (.55) | (.84) | (.72) | (.68) |
| **Net asset value, end of period** | **$11.96** | **$11.61** | **$10.03** | **$11.70** | **$11.80** |
| Total Return (%) | 10.05[b] | 22.73[b] | (7.75)[b] | 5.43[b] | 8.98 |
| **Ratios to Average Net Assets and Supplemental Data** | | | | | |
| Net assets, end of period ($ millions) | 76 | 74 | 73 | 100 | 86 |
| Ratio of expenses before expense reductions (%) | .95 | .86 | .89 | .84 | .85 |
| Ratio of expenses after expense reductions (%) | .86 | .80 | .87 | .83 | .85 |
| Ratio of net investment income (%) | 5.62 | 5.96 | 5.06 | 5.50 | 5.47 |
| Portfolio turnover rate (%) | 167 | 370 | 234 | 147 | 143 |

[a] *Based on average shares outstanding during the period.*

[b] *Total return would have been lower had certain expenses not been reduced.*

# Notes to Financial Statements

## A. Organization and Significant Accounting Policies

DWS Variable Series II (the "Trust") is registered under the Investment Company Act of 1940, as amended (the "1940 Act"), as an open-end management investment company organized as a Massachusetts business trust. The Trust offers seventeen funds (hereinafter referred to individually as "Fund" or collectively as "Funds"). The Fund is classified as a diversified open-end management investment company.

The Trust's financial statements are prepared in accordance with accounting principles generally accepted in the United States of America which require the use of management estimates. Actual results could differ from those estimates. The policies described below are followed consistently by the Trust in the preparation of its financial statements.

**Security Valuation.** Investments are stated at value determined as of the close of regular trading on the New York Stock Exchange on each day the exchange is open for trading.

Various inputs are used in determining the value of the Fund's investments. These inputs are summarized in three broad levels. Level 1 includes quoted prices in active markets for identical securities. Level 2 includes other significant observable inputs (including quoted prices for similar securities, interest rates, prepayment speeds, and credit risk). Level 3 includes significant unobservable inputs (including the Fund's own assumptions in determining the fair value of investments). The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities.

Equity securities are valued at the most recent sale price or official closing price reported on the exchange (US or foreign) or over-the-counter market on which they trade and are categorized as Level 1 securities. Securities for which no sales are reported are valued at the calculated mean between the most recent bid and asked quotations on the relevant market or, if a mean cannot be determined, at the most recent bid quotation.

Debt securities are valued by independent pricing services approved by the Fund's Board. If the pricing services are unable to provide valuations, securities are valued at the most recent bid quotation or evaluated price, as applicable, obtained from one or more broker-dealers. Such services may use various pricing techniques which take into account appropriate factors such as yield, quality, coupon rate, maturity, type of issue, trading characteristics and other data, as well as broker quotes. These securities are generally categorized as Level 2.

Futures contracts are generally valued at the settlement prices established each day on the exchange on which they are traded and are categorized as Level 1.

Forward currency contracts are valued at the prevailing forward exchange rate of the underlying currencies and are categorized as Level 2.

Swap contracts are valued daily based upon prices supplied by a Board approved pricing vendor, if available, and otherwise are valued at the price provided by the broker-dealer. Swap contracts are generally categorized as Level 2.

Exchange-traded options are valued at the last sale price or, in the absence of a sale, the mean between the closing bid and asked prices or at the most recent asked price (bid for purchased options) if no bid or asked price are available. Exchange-traded options are categorized as Level 1. Over-the-counter written or purchased options are valued based upon a price provided by the broker-dealer with which the option, was traded and are generally categorized as Level 3.

Money market instruments purchased with an original or remaining maturity of sixty days or less, maturing at par, are valued at amortized cost, which approximates value, and are categorized as Level 2. Investments in open-end investment companies are valued at their net asset value each business day and are categorized as Level 1.

Securities and other assets for which market quotations are not readily available or for which the above valuation procedures are deemed not to reflect fair value are valued in a manner that is intended to reflect their fair value as determined in accordance with procedures approved by the Board and are generally categorized as Level 3. In accordance with the Fund's valuation procedures, factors used in determining value may include, but are not limited to, the type of the security; the size of the holding; the initial cost of the security; the existence of any contractual restrictions on the security's disposition; the price and extent of public trading in similar securities of the issuer or of comparable companies; quotations or evaluated prices from broker-dealers and/or pricing services; information obtained from the issuer, analysts, and/or the appropriate stock exchange (for exchange-traded securities); an analysis of the company's or issuer's financial statements; an evaluation of the forces that influence the issuer and the market(s) in which the security is purchased and sold and with respect to debt securities; the maturity, coupon, creditworthiness, currency denomination and the movement of the market in which the security is normally traded. The value determined under these procedures may differ from published values for the same securities.

Disclosure about the classification of fair value measurements is included in a table following the Fund's Investment Portfolio.

**Foreign Currency Translations.** The books and records of the Trust are maintained in US dollars. Investment securities and other assets and liabilities denominated in a foreign currency are translated into US dollars at the prevailing exchange rates at period end. Purchases and sales of investment securities, income and expenses are translated into US dollars at the prevailing exchange rates on the respective dates of the transactions.

Net realized and unrealized gains and losses on foreign currency transactions represent net gains and losses between trade and settlement dates on securities transactions, the disposition of forward foreign currency exchange contracts and foreign currencies, and the difference between the amount of net investment income accrued and the US dollar amount actually received. That portion of both realized and unrealized gains and losses on investments that results from fluctuations in foreign currency exchange rates is not separately disclosed but is included with net realized and unrealized gain/appreciation and loss/depreciation on investments.

**Securities Lending.** The Fund lends securities to certain financial institutions. The Fund retains beneficial ownership of the securities it has loaned and continues to receive interest and dividends paid by the issuer of securities and to participate in any changes in their market value. The Fund requires the borrowers of the securities to maintain collateral with the Fund consisting of either cash or liquid, unencumbered assets having a value at least equal to the value of the securities loaned. When the collateral falls below specified amounts, the lending agent will use its best effort to obtain additional collateral on the next business day to meet required amounts under the security lending agreement. The Fund may invest the cash collateral into a joint trading account in an affiliated money market fund pursuant to Exemptive Orders issued by the SEC. The Fund receives compensation for lending its securities either in the form of fees or by earning interest on invested cash collateral net of borrower rebates and fees paid to a lending agent. Either the Fund or the borrower may terminate the loan. There may be risks of delay and costs in recovery of securities or even loss of rights in the collateral should the borrower of the securities fail financially. The Fund is also subject to all investment risks associated with the reinvestment of any cash collateral received, including, but not limited to, interest rate, credit and liquidity risk associated with such investments.

**Loan Participations and Assignments.** The Fund invests in Loan Participations and Assignments. Loan Participations and Assignments are portions of loans originated by banks and sold in pieces to investors. These US dollar-denominated fixed and floating rate loans ("Loans") in which the Fund invests, are arranged between the borrower and one or more financial institutions ("Lenders"). These Loans may take the form of Senior Loans, which are corporate obligations often issued in connection with recapitalizations, acquisitions, leveraged buy-outs and refinancings, and Sovereign Loans, which are debt instruments between a foreign sovereign entity and one or more financial institutions. The Fund invests in such Loans in the form of participations in Loans ("Participations") or assignments of all or a portion of Loans from third parties ("Assignments"). Participations typically result in the Fund having a contractual relationship only with the Lender, not with the borrower. The Fund has the right to receive payments of principal, interest and any fees to which it is entitled from the Lender selling the Participation and only upon receipt by the Lender of the payments from the borrower. In connection with purchasing Participations, the Fund generally has no right to enforce compliance by the borrower with the terms of the loan agreement relating to the Loan, or any rights of set-off against the borrower, and the Fund will not benefit directly from any collateral supporting the Loan in which it has purchased the Participation. As a result, the Fund assumes the credit risk of both the borrower and the Lender that is selling the Participation. Assignments typically result in the Fund having a direct contractual relationship with the borrower, and the Fund may enforce compliance by the borrower with the terms of the loan agreement. All Loan Participations and Assignments involve interest rate risk, liquidity risk and credit risk, including the potential default or insolvency of the borrower.

**When-Issued/Delayed Delivery Securities.** The Fund may purchase securities with delivery or payment to occur at a later date beyond the normal settlement period. At the time the Fund enters into a commitment to purchase a security, the transaction is recorded and the value of the security is reflected in the net asset value. The price of such security and the date when the security will be delivered and paid for are fixed at the time the transaction is negotiated. The value of the security may vary with market fluctuations. No interest accrues to the Fund until payment takes place. At the time the Fund enters into this type of transaction it is required to segregate cash or other liquid assets at least equal to the amount of the commitment.

Certain risks may arise upon entering into when-issued or delayed delivery securities from the potential inability of counterparties to meet the terms of their contracts or if the issuer does not issue the securities due to political, economic, or other factors. Additionally, losses may arise due to changes in the value of the underlying securities.

**Taxes.** The Fund's policy is to comply with the requirements of the Internal Revenue Code, as amended, which are applicable to regulated investment companies and to distribute all of its taxable income to its shareholders.

Additionally, based on the Fund's understanding of the tax rules and rates related to income, gains and transactions for the foreign jurisdictions in which it invests, the Fund will provide for foreign taxes, and where appropriate, deferred foreign taxes.

At December 31, 2010, the Fund had an approximate net tax basis capital loss carryforward which may be applied against any realized net taxable capital gains of each succeeding year until fully utilized or until the following expiration dates, whichever occurs first:

| Fund | Capital Loss Carryforward ($) | Expiration Date | Capital Loss Carryforward Utilized ($) |
|---|---|---|---|
| DWS Strategic Income VIP | 543,000 | 12/31/2017 | 2,458,000 |

In addition, from November 1, 2010 through December 31, 2010, the Fund incurred net realized capital losses. As permitted by tax regulations, the Fund intends to elect to defer these losses and treat them as arising in the fiscal year ended December 31, 2011.

| Fund | |
|---|---|
| DWS Strategic Income VIP | $ 472,000 |

The Fund has reviewed the tax positions for the open tax years as of December 31, 2010 and has determined that no provision for income tax is required in the Fund's financial statements. The Fund's federal tax returns for the prior three fiscal years remain open subject to examination by the Internal Revenue Service.

**Distribution of Income and Gains.** Distributions of net investment income of the Fund, if any, are made annually. Net realized gains from investment transactions, in excess of available capital loss carryforwards, would be taxable to the Fund if not distributed and, therefore, will be distributed to shareholders at least annually. The Fund may also make additional distributions for tax purposes if necessary.

The timing and characterization of certain income and capital gains distributions are determined annually in accordance with federal tax regulations which may differ from accounting principles generally accepted in the United States of America. These differences primarily relate to investments in foreign denominated investments, investments in forward currency contracts, investments in futures contracts, investments in swap contracts and certain securities sold at a loss. As a result, net investment income (loss) and net realized gain (loss) on investment transactions for a reporting period may differ significantly from distributions during such period. Accordingly, the Fund may periodically make reclassifications among certain of its capital accounts without impacting the net asset value of the Fund.

At December 31, 2010, the Fund's components of distributable earnings on a tax basis were as follows:

| Fund | Undistributed Ordinary Income ($)* | Capital Loss Carryforwards ($) | Unrealized Appreciation (Depreciation) on Investments ($) |
|---|---|---|---|
| DWS Strategic Income VIP | 4,050,541 | (543,000) | 2,097,941 |

In addition, the tax character of distributions paid by the Fund is summarized as follows:

| | Distributions from Ordinary Income ($)* | |
|---|---|---|
| | Years Ended December 31, | |
| Fund | 2010 | 2009 |
| DWS Strategic Income VIP | 4,806,010 | 3,708,667 |

* *For tax purposes, short-term capital gain distributions are considered ordinary income distributions.*

**Expenses.** Expenses of the Trust arising in connection with a specific fund are allocated to that fund. Other Trust expenses which cannot be directly attributed to a fund are apportioned among the funds in the Trust.

**Contingencies.** In the normal course of business, the Fund may enter into contracts with service providers that contain general indemnification clauses. The Fund's maximum exposure under these arrangements is unknown as this would involve future claims that may be made against the Fund that have not yet been made. However, based on experience, the Fund expects the risk of loss to be remote.

**Other.** Investment transactions are accounted for on a trade date plus one basis for daily net asset value calculations. However, for financial reporting purposes, investment transactions are reported on trade date. Interest income is recorded on the accrual basis. Realized gains and losses from investment transactions are recorded on an identified cost basis. All discounts and premiums are accreted/amortized for both tax and financial reporting purposes for the Fund, with the exception of securities in default of principal.

## B. Derivative Instruments

**Interest Rate Swap Contracts.** For the year ended December 31, 2010, the Fund entered into interest rate swap transactions to gain exposure to different parts of the yield curve while managing overall duration. The use of interest rate swaps is a highly specialized activity that involves investment techniques and risks different from those associated with ordinary portfolio security transactions. In an interest rate swap, the Fund agrees to pay to the other party to the interest rate swap (which is known as the "counterparty") a fixed rate payment in exchange for the counterparty agreeing to pay to the Fund a variable rate payment, or the Fund agrees to receive from the counterparty a fixed rate payment in exchange for the counterparty agreeing to receive from the Fund a variable rate payment. The payment obligations are based on the notional amount of the swap. Certain risks may arise when entering into swap transactions including counterparty default, liquidity or unfavorable changes in interest rates. In connection with these agreements, securities and or cash may be identified as collateral in accordance with the terms of the swap agreements to provide assets of value and recourse in the event of default. The maximum counterparty credit risk is the net present value of the cash flows to be received from or paid to the counterparty over the term of the interest rate swap contract, to the extent that this amount is beneficial to the Fund, in addition to any related collateral posted to the counterparty by the Fund. This risk may be partially reduced by a master netting arrangement between the Fund and the counterparty. The value of the swap is adjusted daily and the change in value, if any, is recorded as unrealized appreciation or depreciation in the Statement of Assets and Liabilities. An upfront payment made by the Fund is recorded as an asset in the Statement of Assets and Liabilities. An upfront payment received by the Fund is recorded as a liability in the Statement of Assets and Liabilities. Payments received or made at the end of the measurement period are recorded as realized gain or loss in the Statement of Operations.

A summary of the open interest rate swap contracts as of December 31, 2010 is included in a table following the Fund's Investment Portfolio. For the year ended December 31, 2010, the Fund's investment in interest rate swap contracts had a total notional amount generally indicative of a range from approximately $3,600,000 to $4,850,000.

**Credit Default Swap Contracts.** A credit default swap is a contract between a buyer and a seller of protection against pre-defined credit events for the reference entity. For the year ended December 31, 2010, the Fund bought or sold credit default swap contracts to gain exposure to an underlying issuer's credit quality characteristics without directly investing in that issuer, or to hedge the risk of default on Fund securities. As a seller in the credit default swap contract, the Fund is required to pay the par (or other agreed-upon) value of the referenced entity to the counterparty with the occurrence of a credit event by a third party, such as a US or foreign corporate issuer, on the reference entity, which would likely result in a loss to the Fund. In return, the Fund receives from the counterparty a periodic stream of payments over the term of the contract provided that no credit event has occurred. If no credit event occurs, the Fund keeps the stream of payments with no payment obligations. The Fund may also buy credit default swap contracts in order to hedge against the risk of a credit event on debt securities, in which case the Fund functions as the counterparty referenced above. This involves the risk that the contract may expire worthless. It also involves counterparty risk that the seller may fail to satisfy its payment obligations to the Fund with the occurrence of a credit event. When the Fund sells a credit default swap contract it will cover its commitment. This may be achieved by, among other methods, maintaining cash or liquid assets equal to the aggregate notional value of the reference entities for all outstanding credit default swap contracts sold by the Fund.

The value of the credit default swap is adjusted daily and the change in value, if any, is recorded daily as unrealized appreciation or depreciation in the Statement of Assets and Liabilities. An upfront payment made by the Fund is recorded as an asset in the Statement of Assets and Liabilities. An upfront payment received by the Fund is recorded as a liability in the Statement of Assets and Liabilities. Under the terms of the credit default swap contracts, the Fund receives or makes quarterly payments based on a specified interest rate on a fixed notional amount. These payments are recorded as a realized gain or loss in the Statement of Operations. Payments received or made as a result of a credit event or termination of the contract are recognized, net of a proportional amount of the upfront payment, as realized gains or losses in the Statement of Operations.

A summary of the open credit default swap contracts as of December 31, 2010 is included in a table following the Fund's Investment Portfolio. For the year ended December 31, 2010, the Fund's investment in credit default swap contracts purchased had a total notional value generally indicative of a range from $0 to approximately $4,000,000 and the investment in credit default swap contracts sold had a total notional value generally indicative of a range from approximately $580,000 to $2,370,000.

**Total Return Swap Contracts.** Total return swaps involve commitments to pay interest in exchange for a market-linked return based on a notional amount. For the year ended December 31, 2010, the Fund entered into total return swap transactions to enhance potential gain. To the extent the total return of the reference security or index underlying the total return swap exceeds or falls short of the offsetting interest rate obligation, the Fund will receive a payment or make a payment to the counterparty, respectively. Certain risks may arise when entering into swap transactions including counterparty default, liquidity or unfavorable changes in the value of underlying reference security or index. The value of the swap is adjusted daily and the change in value, if any, is recorded as unrealized appreciation or depreciation in the Statement of Assets and Liabilities. An upfront payment made by the Fund is recorded as an asset in the Statement of Assets and Liabilities. An upfront payment received by the Fund is recorded as a liability in the Statement of Assets and Liabilities. Payments received or made at the end of each measurement period are recorded as realized gain or loss in the Statement of Operations.

A summary of the open total return swap contracts as of December 31, 2010 is included in a table following the Fund's Investment Portfolio. For the year ended December 31, 2010, the Fund's investment in total return swap contracts had a total notional amount generally indicative of a range from approximately $2,800,000 to $3,000,000.

**Options.** An option contract is a contract in which the writer (seller) of the option grants the buyer of the option, upon payment of a premium, the right to purchase from (call option), or sell to (put option), the writer a designated instrument at a specified price within a specified period of time. Certain options, including options on indices and interest rate options, will require cash settlement by the Fund if the option is exercised. Interest rate options are comprised of multiple European style options that have periodic exercise dates within the terms of the contract. For the year ended December 31, 2010, the Fund entered into option contracts in order to hedge against potential adverse interest rate movements of portfolio assets.

The liability representing the Fund's obligation under an exchange-traded written option or investment in a purchased option is valued at the last sale price or, in the absence of a sale, the mean between the closing bid and asked prices or at the most recent asked price (bid for purchased options) if no bid and asked price are available. Over-the-counter written or purchased options are valued using dealer-supplied quotations. Gain or loss is recognized when the option contract expires, exercised or is closed.

If the Fund writes a covered call option, the Fund foregoes, in exchange for the premium, the opportunity to profit during the option period from an increase in the market value of the underlying security above the exercise price. If the Fund writes a put option it accepts the risk of a decline in the value of the underlying security below the exercise price. Over-the-counter options have the risk of the potential inability of counterparties to meet the terms of their contracts. The Fund's maximum exposure to purchased options is limited to the premium initially paid. In addition, certain risks may arise upon entering into option contracts including the risk that an illiquid secondary market will limit the Fund's ability to close out an option contract prior to the expiration date and that a change in the value of the option contract may not correlate exactly with changes in the value of the securities or currencies hedged.

A summary of the open option contracts as of December 31, 2010 is included in the Fund's Investment Portfolio. For the year ended December 31, 2010, the Fund's investment in written option contracts had a total value generally indicative of a range from $0 to approximately $53,000 and the investment in purchased option contracts had a total value generally indicative of a range from $0 to approximately $59,000.

**Futures Contracts.** A futures contract is an agreement between a buyer or seller and an established futures exchange or its clearinghouse in which the buyer or seller agrees to take or make a delivery of a specific amount of a financial instrument at a specified price on a specific date (settlement date). For the year ended December 31, 2010, the Fund entered into interest rate futures to gain exposure to different parts of the yield curve while managing overall duration. In addition, the Fund seeks to enhance returns by employing a global tactical asset allocation overlay strategy. The Fund enters into futures contracts on fixed-income securities and equities, including on financial indices and security indices, as part of its global tactical asset allocation overlay strategy. For the year ended December 31, 2010, as part of this strategy, the Fund used futures contracts to attempt to take advantage of short-term and medium-term inefficiencies within the global equity and bond markets.

Futures contracts are valued at the most recent settlement price. Upon entering into a futures contract, the Fund is required to deposit with a financial intermediary cash or securities ("initial margin") in an amount equal to a certain percentage of the face value indicated in the futures contract. Subsequent payments ("variation margin") are made or received by the Fund dependent upon the daily fluctuations in the value and are recorded for financial reporting purposes as unrealized gains or losses by the Fund. Gains or losses are realized when the contract expires or is closed. Since all futures contracts are exchange-traded, counterparty risk is minimized as the exchange's clearinghouse acts as the counterparty, and guarantees the futures against default.

Certain risks may arise upon entering into futures contracts, including the risk that an illiquid market will limit the Fund's ability to close out a futures contract prior to the settlement date and that a change in the value of a futures contract may not correlate exactly with the changes in the value of the underlying hedged security, index or currency. Risk of loss may exceed amounts recognized in the Statement of Assets and Liabilities.

A summary of the open futures contracts as of December 31, 2010 is included in a table following the Fund's Investment Portfolio. For the year ended December 31, 2010, the Fund's investment in futures contracts purchased had a total notional value generally indicative of a range from approximately $19,962,000 to $32,102,000 and the investment in futures contracts sold had a total notional value generally indicative of a range from approximately $13,614,000 to $21,729,000.

**Forward Foreign Currency Exchange Contracts.** A forward foreign currency exchange contract ("forward currency contract") is a commitment to purchase or sell a foreign currency at the settlement date at a negotiated rate. For the year ended December 31, 2010, the Fund entered into forward currency contracts in order to hedge its exposure to changes in foreign currency exchange rates on its foreign currency denominated portfolio holdings and to facilitate transactions in foreign currency denominated securities. In addition, the Fund seeks to enhance returns by employing a global tactical asset allocation overlay strategy. For the year ended December 31, 2010, as part of this strategy, the Fund used forward currency contracts to gain exposure to changes in the value of foreign currencies, and to attempt to take advantage of short-term and medium-term inefficiencies within the currency markets.

Forward currency contracts are valued at the prevailing forward exchange rate of the underlying currencies and unrealized gain (loss) is recorded daily. On the settlement date of the forward currency contract, the Fund records a realized gain or loss equal to the difference between the value of the contract at the time it was opened and the value of the contract at the time it was closed. Certain risks may arise upon entering into forward currency contracts from the potential inability of counterparties to meet the terms of their contracts. The maximum counterparty credit risk to the Fund is measured by the unrealized gain on appreciated contracts. Additionally, when utilizing forward currency contracts to hedge, the Fund gives up the opportunity to profit from favorable exchange rate movements during the term of the contract.

A summary of the open forward currency contracts as of December 31, 2010 is included in a table following the Fund's Investment Portfolio. For the year ended December 31, 2010, the Fund's investment in forward currency contracts US dollars purchased had a total contract value generally indicative of a range from approximately $12,029,000 to $20,192,000 and the investment in forward currency contracts US dollars sold had a total contract value generally indicative of a range from approximately $3,370,000 to $8,365,000.

The following tables summarize the value of the Fund's derivative instruments held as of December 31, 2010 and the related location in the accompanying Statement of Assets and Liabilities, presented by primary underlying risk exposure:

| **Asset Derivatives** | **Purchased Options** | **Forward Contracts** | **Swap Contracts** | **Total** |
|---|---|---|---|---|
| Interest Rate Contracts (a) | $ 467 | $ — | $ 2,678 | $ 3,145 |
| Credit Contracts (a) | — | — | 25,665 | 25,665 |
| Foreign Exchange Contracts (b) | — | 259,054 | — | 259,054 |
| | **$ 467** | **$ 259,054** | **$ 28,343** | **$ 287,864** |

*Each of the above derivatives is located in the following Statement of Assets and Liabilities accounts:*

(a) *Investments in securities, at value (includes purchased options) and unrealized appreciation on open swap contracts*

(b) *Unrealized appreciation on open forward foreign currency exchange contracts*

| **Liability Derivatives** | **Written Options** | **Forward Contracts** | **Swap Contracts** | **Futures Contracts** | **Total** |
|---|---|---|---|---|---|
| Equity Contracts (a) | $ — | $ — | $ — | $ 31,298 | $ 31,298 |
| Interest Rate Contracts (a) | (35,163) | — | (254,700) | (126,598) | (416,461) |
| Credit Contracts (a) | — | — | (28,377) | — | (28,377) |
| Foreign Exchange Contracts (b) | — | (262,385) | — | — | (262,385) |
| | **$ (35,163)** | **$ (262,385)** | **$ (283,077)** | **$ (95,300)** | **$ (675,925)** |

*Each of the above derivatives is located in the following Statement of Assets and Liabilities accounts:*

(a) *Options written, at value, net unrealized appreciation (depreciation) on futures and unrealized depreciation on open swap contracts. Liability of payable for daily variation margin on open futures contracts reflects unsettled variation margin.*

(b) *Unrealized depreciation on open forward foreign currency exchange contracts*

Additionally, the amount of unrealized and realized gains and losses on derivative instruments recognized in Fund earnings during the year ended December 31, 2010 and the related location in the accompanying Statement of Operations is summarized in the following tables by primary underlying risk exposure:

| Realized Gain (Loss) | Purchased Options | Forward Contracts | Swap Contracts | Futures Contracts | Total |
|---|---|---|---|---|---|
| Equity Contracts (a) | $ — | $ — | $ — | $ (421,417) | $ (421,417) |
| Interest Rate Contracts (a) | 38,962 | — | 94,915 | 480,480 | 614,357 |
| Credit Contracts (a) | — | — | (132,473) | — | (132,473) |
| Foreign Exchange Contracts (b) | — | 434,022 | — | — | 434,022 |
| | **$ 38,962** | **$ 434,022** | **$ (37,558)** | **$ 59,063** | **$ 494,489** |

*Each of the above derivatives is located in the following Statement of Operations accounts:*

(a) *Net realized gain (loss) from investments (includes purchased options), swap contracts and futures, respectively*

(b) *Net realized gain (loss) from foreign currency (Statement of Operations includes both forward currency contracts and foreign currency transactions)*

| Change in Net Unrealized Appreciation (Depreciation) | Purchased Options | Written Options | Forward Contracts | Swap Contracts | Futures Contracts | Total |
|---|---|---|---|---|---|---|
| Equity Contracts (a) | $ — | $ — | $ — | $ — | $ 19,172 | $ 19,172 |
| Interest Rate Contracts (a) | (57,941) | (4,423) | — | (308,385) | (20,863) | (391,612) |
| Credit contracts (a) | — | — | — | (1,477) | — | (1,477) |
| Foreign Exchange Contracts (b) | — | — | (279,489) | — | — | (279,489) |
| | **$ (57,941)** | **$ (4,423)** | **$ (279,489)** | **$ (309,862)** | **$ (1,691)** | **$ (653,406)** |

*Each of the above derivatives is located in the following Statement of Operations accounts:*

(a) *Change in net unrealized appreciation (depreciation) on investments (includes purchased options), written options, swap contracts and futures, respectively*

(b) *Change in net unrealized appreciation (depreciation) on foreign currency (Statement of Operations includes both forward currency contracts and foreign currency transactions)*

## C. Purchases and Sales of Securities

During the year ended December 31, 2010, purchases and sales of investment transactions (excluding short-term investments) were as follows:

| Fund | Purchases ($) | Sales ($) |
|---|---|---|
| DWS Strategic Income VIP<br>excluding US Treasury Obligations | 83,860,216 | 81,802,651 |
| US Treasury Obligations | 38,991,537 | 36,504,796 |

For the year ended December 31, 2010, transactions for written options on interest rate swaps were as follows:

| | Contract Amount | Premiums |
|---|---|---|
| Outstanding, beginning of period | — | $ — |
| Options written | 29,000,000 | 30,740 |
| Outstanding, end of period | **29,000,000** | **$ 30,740** |

## D. Related Parties

**Management Agreement.** Under the Investment Management Agreement with Deutsche Investment Management Americas Inc. ("DIMA" or the "Advisor"), an indirect, wholly owned subsidiary of Deutsche Bank AG, the Advisor directs the investments of the Fund in accordance with its investment objectives, policies and restrictions. The Advisor determines the securities, instruments and other contracts relating to investments to be purchased, sold or entered into by the Fund or delegates such responsibility to the Fund's subadvisor.

QS Investors, LLC ("QS Investors") acts as an investment sub-advisor to the Fund. On August 1, 2010, members of the Advisor's Quantitative Strategies Group, including some members of the Fund's portfolio management team, separated from the Advisor and formed QS Investors as a separate investment advisory firm unaffiliated with the Advisor (the "Separation"). As an investment sub-advisor to the Fund, QS Investors manages the assets attributable only to the Fund's Global Tactical Asset Allocation Overlay Strategy. QS Investors is paid by the Advisor, not the Fund, for the services QS Investors provides to the Fund.

Under the Investment Management Agreement with the Advisor, the fee is equivalent to the annual rates shown below of the Fund's average daily net assets, computed and accrued daily and payable monthly:

| Fund | Annual Management Fee Rate |
|---|---|
| DWS Strategic Income VIP | |
| $0–$250 million | .550% |
| next $750 million | .520% |
| next $1.5 billion | .500% |
| next $2.5 billion | .480% |
| next $2.5 billion | .450% |
| next $2.5 billion | .430% |
| next $2.5 billion | .410% |
| over $12.5 billion | .390% |

For the period from January 1, 2010 through September 30, 2010, the Advisor had contractually agreed to waive its fee and/or reimburse certain operating expenses to the extent necessary to maintain the operating expenses (excluding certain expenses such as extraordinary expenses, taxes, brokerage and interest expense) of the class as follows:

| Fund | Annual Rate |
|---|---|
| DWS Strategic Income VIP | |
| Class A | .87% |

For the period from October 1, 2010 through September 30, 2011, the Advisor has contractually agreed to waive its fee and/or reimburse certain operating expenses to the extent necessary to maintain the operating expenses (excluding certain expenses such as extraordinary expenses, taxes, brokerage and interest expense) of the class as follows:

| Fund | Annual Rate |
|---|---|
| DWS Strategic Income VIP | |
| Class A | .78% |

Accordingly, for the year ended December 31, 2010, the total management fee, management fee waived and effective management fee rate were as follows:

| Fund | Total Aggregated ($) | Waived ($) | Annual Effective Rate |
|---|---|---|---|
| DWS Strategic Income VIP | 410,735 | 67,252 | .46% |

**Administration Fee.** Pursuant to an Administrative Services Agreement, DIMA provides most administrative services to the Fund. For all services provided under the Administrative Services Agreement, the Fund pays DIMA an annual fee ("Administration Fee") of 0.10% of the Fund's average daily net assets, computed and accrued daily and payable monthly. For the year ended December 31, 2010, the Administration Fee was as follows:

| Fund | Total Aggregated ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS Strategic Income VIP | 74,679 | 6,418 |

**Service Provider Fees.** DWS Investments Service Company ("DISC"), an affiliate of the Advisor, is the transfer agent, dividend-paying agent and shareholder service agent for the Fund. Pursuant to a sub-transfer agency agreement between DISC and DST Systems, Inc. ("DST"), DISC has delegated certain transfer agent, dividend-paying agent and shareholder service agent functions to DST. DISC compensates DST out of the shareholder servicing fee it receives from the Fund. For the year ended December 31, 2010, the amounts charged to the Fund by DISC were as follows:

| Fund | Total Aggregated ($) | Waived ($) |
|---|---|---|
| DWS Strategic Income VIP Class A | 162 | 162 |

**Typesetting and Filing Service Fees.** Under an agreement with DIMA, DIMA is compensated for providing typesetting and certain regulatory filing services to the Fund. For the year ended December 31, 2010, the amount charged to the Fund by DIMA included in the Statement of Operations under "reports to shareholders" was as follows:

| Fund | Amount ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS Strategic Income VIP | 11,019 | 3,562 |

**Trustees' Fees and Expenses.** The Fund paid each Trustee not affiliated with the Advisor retainer fees plus specified amounts for various committee services and for the Board Chairperson.

**Affiliated Cash Management Vehicles.** The Fund may invest uninvested cash balances in Central Cash Management Fund, which is managed by the Advisor. The Fund indirectly bears their proportionate share of the expenses of the underlying money market funds. Central Cash Management Fund does not pay the Advisor an investment management fee. Central Cash Management Fund seeks a high level of current income consistent with liquidity and the preservation of capital.

## E. Investing in High Yield Securities

The Fund's performance could be hurt if a security declines in credit quality or goes into default, or if an issuer does not make timely payments of interest or principal. Because the issuers of high-yield debt securities or junk bonds (debt securities rated below the fourth-highest category) may be in uncertain financial health, the prices of their debt securities can be more vulnerable to bad economic news, or even the expectation of bad news, than investment-grade debt securities. Because the Fund may invest in securities not paying current interest or in securities already in default, these risks may be more pronounced.

## F. Investing in Emerging Markets

Investing in emerging markets may involve special risks and considerations not typically associated with investing in developed markets. These risks include revaluation of currencies, high rates of inflation or deflation, repatriation restrictions on income and capital, and future adverse political, social and economic developments. Moreover, securities issued in these markets may be less liquid, subject to government ownership controls or delayed settlements, and may have prices that are more volatile or less easily assessed than those of comparable securities of issuers in developed markets.

## G. Ownership of the Fund

At December 31, 2010, the beneficial ownership in the Fund was as follows:

**DWS Strategic Income VIP:** Two Participating Insurance Companies were owners of record of 10% or more of the total outstanding Class A shares of the Fund, each owning 59% and 39%.

## H. Line of Credit

The Trust and other affiliated fund (the "Participants") share in a $450 million revolving credit facility provided by a syndication of banks. The Fund may borrow for temporary or emergency purposes, including the meeting of redemption requests that otherwise might require the untimely disposition of securities. The Participants are charged an annual commitment fee which is allocated based on net assets, among each of the Participants. Interest is calculated at a rate per annum equal to the sum of the Federal Funds Rate plus 1.25 percent plus if LIBOR exceeds the Federal Funds Rate the amount of such excess. The Fund may borrow up to a maximum of 33 percent of its net assets under the agreement.

# Report of Independent Registered Public Accounting Firm

**To the Board of Trustees and Shareholders of DWS Variable Series II:**

We have audited the accompanying statement of assets and liabilities of DWS Strategic Income VIP, one of the funds constituting the DWS Variable Series II (the "Trust"), including the investment portfolio, as of December 31, 2010, and the related statement of operations, the statement of changes in net assets and the financial highlights for each of the periods indicated therein. These financial statements and financial highlights are the responsibility of the Trust's management. Our responsibility is to express an opinion on these financial statements and financial highlights based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements and financial highlights are free of material misstatement. We were not engaged to perform an audit of the Trust's internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Trust's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements and financial highlights, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our procedures included confirmation of securities owned as of December 31, 2010, by correspondence with the custodian and brokers or by other appropriate auditing procedures where replies from brokers were not received. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements and financial highlights referred to above present fairly, in all material respects, the financial position of the aforementioned fund of the DWS Variable Series II at December 31, 2010, the results of its operations, the changes in its net assets and the financial highlights for each of the periods indicated therein, in conformity with U.S. generally accepted accounting principles.

Ernst + Young LLP

Boston, Massachusetts
February 14, 2011

## Tax Information

**(Unaudited)**

Please consult a tax advisor if you have questions about federal or state income tax laws, or on how to prepare your tax returns. If you have specific questions about your account, please contact your insurance provider.

## Proxy Voting

The Trust's policies and procedures for voting proxies for portfolio securities and information about how the Trust voted proxies related to its portfolio securities during the 12-month period ended June 30 are available on our Web site — www.dws-investments.com (click on "proxy voting" at the bottom of the page) — or on the SEC's Web site — www.sec.gov. To obtain a written copy of the Trust's policies and procedures without charge, upon request, call us toll free at (800) 728-3337.

# Investment Management Agreement Approval

### DWS Strategic Income VIP

The Board of Trustees, including the Independent Trustees, approved the renewal of your Fund's investment management agreement (the "Agreement") with Deutsche Investment Management Americas Inc. ("DWS") and sub-advisory agreement (the "Sub-Advisory Agreement" and together with the Agreement the "Agreements") between DWS and QS Investors, LLC ("QS Investors") in September 2010.

In terms of the process that the Board followed prior to approving the Agreements, shareholders should know that:

- In September 2010, all but one of the Fund's Trustees were independent of DWS and its affiliates.
- The Trustees meet frequently to discuss fund matters. Each year, the Trustees dedicate substantial time to contract review matters. Over the course of several months, the Board's Contract Committee, in coordination with the Board's Fixed Income and Quant Oversight Committee, reviewed comprehensive materials received from DWS, independent third parties and independent counsel. These materials included an analysis of the Fund's performance, fees and expenses, and profitability compiled by the Fund's independent fee consultant. The Board also received extensive information throughout the year regarding performance of the Fund.
- The Independent Trustees regularly meet privately with their independent counsel to discuss contract review and other matters. In addition, the Independent Trustees were also advised by the Fund's independent fee consultant in the course of their review of the Fund's contractual arrangements and considered a comprehensive report prepared by the independent fee consultant in connection with their deliberations (the "IFC Report").
- In connection with reviewing the Agreements, the Board also reviewed the terms of the Fund's distribution agreement, administrative services agreement, transfer agency agreement and other material service agreements.
- Based on its evaluation of the information provided, the Contract Committee presented its findings and recommendations to the Independent Trustees as a group. The Independent Trustees reviewed the Contract Committee's findings and recommendations and presented their recommendations to the full Board.

In connection with the contract review process, the Contract Committee and the Board considered the factors discussed below, among others. The Board also considered that DWS and its predecessors have managed the Fund since its inception, and the Board believes that a long-term relationship with a capable, conscientious advisor is in the best interests of the Fund. The Board considered, generally, that shareholders chose to invest or remain invested in the Fund knowing that DWS managed the Fund, and that the Agreement was approved by the Fund's shareholders. DWS is part of Deutsche Bank, a major global banking institution that is engaged in a wide range of financial services. The Board believes that there are significant advantages to being part of a global asset management business that offers a wide range of investing expertise and resources, including hundreds of portfolio managers and analysts with research capabilities in many countries throughout the world.

While shareholders may focus primarily on fund performance and fees, the Fund's Board considers these and many other factors, including the quality and integrity of DWS's and QS Investors' personnel and such other issues as back-office operations, fund valuations, and compliance policies and procedures. In addition, in connection with approving the continuation of the Fund's Sub-Advisory Agreement, the Board noted it had engaged in a comprehensive review of the agreement in connection with its initial approval in May 2010.

**Nature, Quality and Extent of Services.** The Board considered the terms of the Agreements, including the scope of advisory services provided under the Agreements. The Board noted that, under the Agreements, DWS and QS Investors provide portfolio management services to the Fund and that, pursuant to a separate administrative services agreement, DWS provides administrative services to the Fund. The Board considered the experience and skills of senior management and investment personnel, the resources made available to such personnel, the ability of DWS to attract and retain high-quality personnel, and the organizational depth and stability of DWS. The Board reviewed the Fund's performance over short-term and long-term periods and compared those returns to various agreed-upon performance measures, including market indices and a peer universe compiled by the independent fee consultant using information supplied by Lipper Inc. ("Lipper"). The Board also noted that it has put into place a process of identifying "Focus Funds" (e.g., funds performing poorly relative to their benchmark or a peer universe compiled by Lipper), and receives more frequent reporting and information from DWS regarding such funds, along with DWS's remedial plans to address underperformance. The Board believes this process is an effective manner of identifying and addressing underperforming funds. Based on the information provided, the Board noted that for the one-, three- and five-year periods ended December 31, 2009, the Fund's performance (Class A shares) was in the 2nd quartile, 1st quartile and 1st quartile, respectively, of the applicable Lipper universe (the 1st quartile being the best performers and the 4th quartile being the worst performers). The Board also observed that the Fund has outperformed its benchmark in the one-year period and has underperformed its benchmark in the three- and five-year periods ended December 31, 2009.

On the basis of this evaluation and the ongoing review of investment results by the Board, the Board concluded that the nature, quality and extent of services provided by DWS and QS Investors historically have been and continue to be satisfactory.

**Fees and Expenses.** The Board considered the Fund's investment management fee schedule, sub-advisory fee schedule, operating expenses, and total expense ratios, and comparative information provided by Lipper and the independent fee consultant regarding investment management fee rates paid to other investment advisors by similar funds (1st quartile being the most favorable and 4th quartile being the least favorable). With respect to management fees paid to other investment advisors by similar funds, the Board noted that the contractual fee rates paid by the Fund, which include the 0.10% fee paid to DWS under the Fund's administrative services agreement, were at the median (2nd quartile) of the applicable Lipper peer group (based on Lipper data provided as of December 31, 2009). With respect to the sub-advisory fee paid to QS Investors, the Board noted that the fee is paid by DWS out of its fee and not directly by the Fund. The Board noted that the Fund's Class A shares total (net) operating expenses were expected to be higher than the median (4th quartile) of the applicable Lipper expense universe (based on Lipper data provided as of December 31, 2009, and analyzing Lipper expense universe Class A expenses less any applicable 12b-1 fees) ("Lipper Universe Expenses"). The Board considered the Fund's management fee rate as compared to fees charged by DWS and certain of its affiliates for comparable mutual funds and considered differences in fund and fee structures between the DWS Funds. The Board also considered how the Fund's total (net) operating expenses compared to the total (net) operating expenses of a more customized peer group selected by Lipper (based on such factors as asset size). The Board also noted that the expense limitation agreed to by DWS helped to ensure that the Fund's total (net) operating expenses would remain competitive.

The information considered by the Board as part of its review of management fees included information regarding fees charged by DWS and its affiliates to similar institutional accounts and to similar funds offered primarily to European investors ("DWS Europe funds"), in each case as applicable. The Board observed that advisory fee rates for institutional accounts generally were lower than the management fees charged by similarly managed DWS US mutual funds ("DWS Funds"), but also took note of the differences in services provided to DWS Funds as compared to institutional accounts. In the case of DWS Europe funds, the Board observed that fee rates for DWS Europe funds generally were higher than for similarly managed DWS Funds, but noted that differences in the types of services provided to DWS Funds relative to DWS Europe funds made it difficult to compare such fees.

On the basis of the information provided, the Board concluded that management fees were reasonable and appropriate in light of the nature, quality and extent of services provided by DWS and QS Investors.

**Profitability.** The Board reviewed detailed information regarding revenues received by DWS under the Agreement. The Board considered the estimated costs and pre-tax profits realized by DWS from advising the DWS Funds, as well as estimates of the pre-tax profits attributable to managing the Fund in particular. The Board also received information regarding the estimated enterprise-wide profitability of DWS and its affiliates with respect to all fund services in totality and by fund. The Board reviewed DWS's methodology in allocating its costs to the management of the Fund. Based on the information provided, the Board concluded that the pre-tax profits realized by DWS in connection with the management of the Fund were not unreasonable. The Board also reviewed information regarding the profitability of certain similar investment management firms. The Board noted that while information regarding the profitability of such firms is limited (and in some cases is not necessarily prepared on a comparable basis), DWS and its affiliates' overall profitability with respect to the DWS fund complex (after taking into account distribution and other services provided to the funds by DWS and its affiliates) was lower than the overall profitability levels of many comparable firms for which such data was available. The Board did not consider the profitability of QS Investors with respect to the Fund. The Board noted that DWS pays QS Investors' fee out of its management fee, and its understanding that the Fund's sub-advisory fee schedule was the product of an arm's length negotiation with DWS.

**Economies of Scale.** The Board considered whether there are economies of scale with respect to the management of the Fund and whether the Fund benefits from any economies of scale. The Board noted that the Fund's management fee schedule includes fee breakpoints. The Board concluded that the Fund's fee schedule represents an appropriate sharing between the Fund and DWS of such economies of scale as may exist in the management of the Fund at current asset levels.

**Other Benefits to DWS and QS Investors and Their Affiliates.** The Board also considered the character and amount of other incidental benefits received by DWS and QS Investors and their affiliates, including any fees received by DWS for administrative services provided to the Fund and any fees received by an affiliate of DWS for distribution services. The Board also considered benefits to DWS and QS Investors related to brokerage and soft-dollar allocations, including allocating brokerage to pay for research generated by parties other than the executing broker dealers, which pertain primarily to funds investing in equity securities, along with the incidental public relations benefits to DWS and QS Investors related to DWS Funds advertising and cross-selling opportunities among DWS products and services. The Board concluded that management fees were reasonable in light of these fallout benefits.

**Compliance.** The Board considered the significant attention and resources dedicated by DWS to documenting and enhancing its compliance processes in recent years. The Board noted in particular (i) the experience and seniority of both DWS's chief compliance officer and the Fund's chief compliance officer; (ii) the large number of DWS compliance personnel; and (iii) the substantial commitment of resources by DWS and its affiliates to compliance matters. The Board also considered the attention and resources dedicated by DWS to the oversight of the investment sub-advisor's compliance program and compliance with the applicable fund policies and procedures.

Based on all of the information considered and the conclusions reached, the Board unanimously (including the Independent Trustees) determined that the continuation of the Agreements is in the best interests of the Fund. In making this determination, the Board did not give particular weight to any single factor identified above. The Board considered these factors over the course of numerous meetings, certain of which were in executive session with only the Independent Trustees and their counsel present. It is possible that individual Trustees may have weighed these factors differently in reaching their individual decisions to approve the continuation of the Agreements.

# Summary of Management Fee Evaluation by Independent Fee Consultant

October 3, 2010

Pursuant to an Order entered into by Deutsche Investment Management Americas and affiliates (collectively, "DeAM") with the Attorney General of New York, I, Thomas H. Mack, have been appointed the Independent Fee Consultant for the DWS Funds (formerly the DWS Scudder Funds). My duties include preparing an annual written evaluation of the management fees DeAM charges the Funds, considering among other factors the management fees charged by other mutual fund companies for like services, management fees DeAM charges other clients for like services, DeAM's costs of supplying services under the management agreements and related profit margins, possible economies of scale if a Fund grows larger, and the nature and quality of DeAM's services, including fund performance. This report summarizes my evaluation for 2010, including my qualifications, the evaluation process for each of the DWS Funds, consideration of certain complex-level factors, and my conclusions. I served in substantially the same capacity in 2007, 2008, and 2009.

## Qualifications

For more than 35 years I have served in various professional capacities within the investment management business. I have held investment analysis and advisory positions, including securities analyst, portfolio strategist and director of investment policy with a large investment firm. I have also performed business management functions, including business development, financial management and marketing research and analysis.

Since 1991, I have been an independent consultant within the asset management industry. I have provided services to over 125 client organizations, including investment managers, mutual fund boards, product distributors and related organizations. Over the past ten years I have completed a number of assignments for mutual fund boards, specifically including assisting boards with management contract renewal.

I hold a Master of Business Administration degree, with highest honors, from Harvard University and Master of Science and Bachelor of Science (highest honors) degrees from the University of California at Berkeley. I am an independent director and audit committee financial expert for two closed-end mutual funds and have served in various leadership and financial oversight capacities with non-profit organizations.

## Evaluation of Fees for each DWS Fund

My work focused primarily on evaluating, fund-by-fund, the fees charged to each of the 118 publicly offered Fund portfolios in the DWS Fund family. For each Fund, I considered each of the key factors mentioned above, as well as any other relevant information. In doing so I worked closely with the Funds' Independent Directors in their annual contract renewal process, as well as in their approval of contracts for several new funds (documented separately).

In evaluating each Fund's fees, I reviewed comprehensive materials provided by or on behalf of DeAM, including expense information prepared by Lipper Analytical, comparative performance information, profitability data, manager histories, and other materials. I also accessed certain additional information from the Lipper and Morningstar databases and drew on my industry knowledge and experience.

To facilitate evaluating this considerable body of information, I prepared for each Fund a document summarizing the key data elements in each area as well as additional analytics discussed below. This made it possible to consider each key data element in the context of the others.

In the course of contract renewal, DeAM agreed to implement a number of fee and expense adjustments requested by the Independent Directors which will favorably impact future fees and expenses, and my evaluation includes the effects of these changes.

### Fees and Expenses Compared with Other Funds

The competitive fee and expense evaluation for each fund focused on two primary comparisons:

- The Fund's contractual management fee (the advisory fee plus the administration fee where applicable) compared with those of a group of typically 12–15 funds in the same Lipper investment category (e.g. Large Capitalization Growth) having similar distribution arrangements and being of similar size.
- The Fund's total expenses compared with a broader universe of funds from the same Lipper investment category and having similar distribution arrangements.

These two comparisons provide a view of not only the level of the fee compared with funds of similar scale but also the total expense the Fund bears for all the services it receives, in comparison with the investment choices available in the Fund's investment category and distribution channel. The principal figure-of-merit used in these comparisons was the subject Fund's percentile ranking against peers.

### DeAM's Fees for Similar Services to Others

DeAM provided management fee schedules for all of its US domiciled fund and non-fund investment management accounts in any of the investment categories where there is a DWS Fund. These similar products included the other DWS Funds, non-fund pooled accounts, institutional accounts and sub-advisory accounts. Using this information, I calculated for each Fund the fee that would be charged to each similar product, at the subject Fund's asset level.

Evaluating information regarding non-fund products is difficult because there are varying levels of services required for different types of accounts, with mutual funds generally requiring considerably more regulatory and administrative types of service as well as having more frequent cash flows than other types of accounts. Also, while mutual fund fees for similar fund products can be expected to be similar, there will be some differences due to different pricing conditions in different distribution channels (e.g. retail funds versus those used in variable insurance products), differences in underlying investment processes and other factors.

**Costs and Profit Margins**

DeAM provided a detailed profitability analysis for each Fund. After making some adjustments so that the presentation would be more comparable to the available industry figures, I reviewed profit margins from investment management alone, from investment management plus other fund services (excluding distribution) provided to the Funds by DeAM (principally shareholder services), and DeAM profits from all sources, including distribution. A later section comments on overall profitability.

**Economies of Scale**

Economies of scale — an expected decline in management cost per dollar of fund assets as fund assets grow — are very rarely quantified and documented because of inherent difficulties in collecting and analyzing relevant data. However, in virtually every investment category that I reviewed, larger funds tend to have lower fees and lower total expenses than smaller funds. To see how each DWS Fund compares with this industry observation, I reviewed:

The trend in Fund assets over the last five years and the accompanying trend in total expenses. This shows if the Fund has grown and, if so, whether total expense (management fees as well as other expenses) have declined as a percent of assets.

Whether the Fund has break-points in its management fee schedule, the extent of the fee reduction built into the schedule and the asset levels where the breaks take effect, and in the case of a sub-advised Fund how the Fund's break-points compare with those of the sub-advisory fee schedule.

How the Fund's contractual fee schedule compares with trends in the industry data. To accomplish this, I constructed a chart showing how actual latest-fiscal-year contractual fees of the Fund and of other similar funds relate to average fund assets, with the subject Fund's contractual fee schedule superimposed.

**Quality of Service — Performance**

The quality-of-service evaluation focused on investment performance, which is the principal result of the investment management service. Each Fund's performance was reviewed over the past 1, 3, 5 and 10 years, as applicable, and compared with that of other funds in the same investment category and with a suitable market index.

In addition, I calculated and reviewed risk-adjusted returns relative to an index of similar mutual funds' returns and a suitable market index. The risk-adjusted returns analysis provides a way of determining the extent to which the Fund's return comparisons are mainly the product of investment value-added (or lack thereof) or alternatively taking considerably more or less risk than is typical in its investment category.

I also received and considered the history of portfolio manager changes for each Fund, as this provided an important context for evaluating the performance results.

## Complex-Level Considerations

While this evaluation was conducted mainly at the individual fund level, there are some issues relating to the reasonableness of fees that can alternatively be considered across the whole fund complex:

I reviewed DeAM's profitability analysis for all DWS Funds, with a view toward determining if the allocation procedures used were reasonable and how profit levels compared with public data for other investment managers.

I considered whether DeAM and affiliates receive any significant ancillary or "fall-out" benefits that should be considered in interpreting the direct profitability results. These would be situations where serving as the investment manager of the Funds is beneficial to another part of the Deutsche Bank organization.

I considered how aggregated DWS Fund expenses had varied over the years, by asset class and in the context of trends in asset levels.

I reviewed the structure of the DeAM organization, trends in staffing levels, and information on compensation of investment management and other professionals compared with industry data.

## Findings

Based on the process and analysis discussed above, which included reviewing a wide range of information from management and external data sources and considering among other factors the fees DeAM charges other clients, the fees charged by other fund managers, DeAM's costs and profits associated with managing the Funds, economies of scale, possible fall-out benefits, and the nature and quality of services provided, in my opinion the management fees charged the DWS Funds are reasonable.

Thomas H. Mack

Thomas H. Mack

# Board Members and Officers

The following table presents certain information regarding the Board Members and Officers of the Trust as of December 31, 2010. Each Board Member's year of birth is set forth in parentheses after his or her name. Unless otherwise noted, (i) each Board Member has engaged in the principal occupation(s) noted in the table for at least the most recent five years, although not necessarily in the same capacity; and (ii) the address of each Independent Board Member is c/o Paul K. Freeman, Independent Chairman, DWS Funds, PO Box 101833, Denver, CO 80250-1833. Except as otherwise noted below, the term of office for each Board Member is until the election and qualification of a successor, or until such Board Member sooner dies, resigns, is removed or as otherwise provided in the governing documents of the fund. Because the fund does not hold an annual meeting of shareholders, each Board Member will hold office for an indeterminate period. The Board Members may also serve in similar capacities with other funds in the fund complex. The Length of Time Served represents the year in which the Board Member joined the board of one or more DWS funds now overseen by the Board.

### Independent Board Members

| Name, Year of Birth, Position with the Fund and Length of Time Served[1] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Paul K. Freeman (1950)<br>Chairperson since 2009<br>Board Member since 1993 | Consultant, World Bank/Inter-American Development Bank; Executive and Governing Council of the Independent Directors Council (education committees); formerly, Project Leader, International Institute for Applied Systems Analysis (1998–2001); Chief Executive Officer, The Eric Group, Inc. (environmental insurance) (1986–1998) | 122 |
| John W. Ballantine (1946)<br>Board Member since 1999 | Retired; formerly, Executive Vice President and Chief Risk Management Officer, First Chicago NBD Corporation/The First National Bank of Chicago (1996–1998); Executive Vice President and Head of International Banking (1995–1996). Directorships: Healthways, Inc. (provider of disease and care management services); Portland General Electric (utility company); Stockwell Capital Investments PLC (private equity). Former Directorships: First Oak Brook Bancshares, Inc. and Oak Brook Bank; Prisma Energy International | 122 |
| Henry P. Becton, Jr. (1943)<br>Board Member since 1990 | Vice Chair and former President, WGBH Educational Foundation. Directorships: Association of Public Television Stations; Lead Director, Becton Dickinson and Company[3] (medical technology company); Lead Director, Belo Corporation[3] (media company); Public Radio International; Public Radio Exchange (PRX); The PBS Foundation. Former Directorships: Boston Museum of Science; American Public Television; Concord Academy; New England Aquarium; Mass. Corporation for Educational Telecommunications; Committee for Economic Development; Public Broadcasting Service | 122 |
| Dawn-Marie Driscoll (1946)<br>Board Member since 1987 | President, Driscoll Associates (consulting firm); Executive Fellow, Center for Business Ethics, Bentley University; formerly, Partner, Palmer & Dodge (1988–1990); Vice President of Corporate Affairs and General Counsel, Filene's (1978–1988). Directorships: Trustee of 22 open-end mutual funds managed by Sun Capital Advisers, Inc. (since 2007); Director of ICI Mutual Insurance Company (since 2007); Advisory Board, Center for Business Ethics, Bentley University; Trustee, Southwest Florida Community Foundation (charitable organization). Former Directorships: Investment Company Institute (audit, executive, nominating committees) and Independent Directors Council (governance, executive committees) | 122 |
| Keith R. Fox (1954)<br>Board Member since 1996 | Managing General Partner, Exeter Capital Partners (a series of private investment funds). Directorships: Progressive International Corporation (kitchen goods importer and distributor); BoxTop Media Inc. (advertising); The Kennel Shop (retailer); former Chairman, National Association of Small Business Investment Companies | 122 |
| Kenneth C. Froewiss (1945)<br>Board Member since 2001 | Adjunct Professor of Finance, NYU Stern School of Business (September 2009–present; Clinical Professor from 1997–September 2009); Member, Finance Committee, Association for Asian Studies (2002–present); Director, Mitsui Sumitomo Insurance Group (US) (2004–present); prior thereto, Managing Director, J.P. Morgan (investment banking firm) (until 1996) | 122 |
| Richard J. Herring (1946)<br>Board Member since 1990 | Jacob Safra Professor of International Banking and Professor, Finance Department, The Wharton School, University of Pennsylvania (since July 1972); Co-Director, Wharton Financial Institutions Center (since July 2000); Co-Chair, U.S. Shadow Financial Regulatory Committee; Executive Director, Financial Economists Roundtable; Director, Japan Equity Fund, Inc. (since September 2007), Thai Capital Fund, Inc. (since September 2007), Singapore Fund, Inc. (since September 2007); Independent Director of Barclays Bank Delaware (since September 2010). Formerly, Vice Dean and Director, Wharton Undergraduate Division (July 1995–June 2000); Director, Lauder Institute of International Management Studies (July 2000–June 2006) | 122 |
| William McClayton (1944)<br>Board Member since 2004+ | Private equity investor (since October 2009); previously, Managing Director, Diamond Management & Technology Consultants, Inc. (global consulting firm) (2001–2009); Directorship: Board of Managers, YMCA of Metropolitan Chicago; formerly: Senior Partner, Arthur Andersen LLP (accounting) (1966–2001); Trustee, Ravinia Festival | 122 |

| Name, Year of Birth, Position with the Fund and Length of Time Served[1] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Rebecca W. Rimel (1951)<br>Board Member since 1995 | President and Chief Executive Officer, The Pew Charitable Trusts (charitable organization) (1994 to present); Trustee, Thomas Jefferson Foundation (charitable organization) (1994 to present); Trustee, Executive Committee, Philadelphia Chamber of Commerce (2001–2007); Director, CardioNet, Inc.[2] (2009–present) (health care). Formerly, Executive Vice President, The Glenmede Trust Company (investment trust and wealth management) (1983–2004); Board Member, Investor Education (charitable organization) (2004–2005); Director, Viasys Health Care[2] (January 2007–June 2007); Trustee, Pro Publica (charitable organization) (2007–2010) | 122 |
| William N. Searcy, Jr. (1946)<br>Board Member since 1993 | Private investor since October 2003; Trustee of 22 open-end mutual funds managed by Sun Capital Advisers, Inc. (since October 1998). Formerly, Pension & Savings Trust Officer, Sprint Corporation[2] (telecommunications) (November 1989–September 2003) | 122 |
| Jean Gleason Stromberg (1943)<br>Board Member since 1997 | Retired. Formerly, Consultant (1997–2001); Director, Financial Markets US Government Accountability Office (1996–1997); Partner, Fulbright & Jaworski, L.L.P. (law firm) (1978–1996). Directorships: The William and Flora Hewlett Foundation. Former Directorships: Service Source, Inc., Mutual Fund Directors Forum (2002–2004), American Bar Retirement Association (funding vehicle for retirement plans) (1987–1990 and 1994–1996) | 122 |
| Robert H. Wadsworth<br>(1940)<br>Board Member since 1999 | President, Robert H. Wadsworth & Associates, Inc. (consulting firm) (1983 to present); Director, The Phoenix Boys Choir Association | 125 |

## Interested Board Member and Officer[4]

| Name, Year of Birth, Position with the Trust/ Corporation and Length of Time Served[1,5] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Ingo Gefeke[7] (1967)<br>Board Member since 2010<br>Executive Vice President since 2010 | Managing Director[3], Deutsche Asset Management; Global Head of Distribution and Product Management, DWS Global Head of Trading and Securities Lending. Member of the Board of Directors of DWS Investment GmbH Frankfurt (since July 2009) and DWS Holding & Service GmbH Frankfurt (since January 2010); formerly, Global Chief Administrative Officer, Deutsche Asset Management (2004–2009); Global Chief Operating Officer, Global Transaction Banking, Deutsche Bank AG, New York (2001–2004); Chief Operating Officer, Global Banking Division Americas, Deutsche Bank AG, New York (1999–2001); Central Management, Global Banking Services, Deutsche Bank AG, Frankfurt (1998–1999); Relationship Management, Deutsche Bank AG, Tokyo, Japan (1997–1998) | 55 |

## Officers[4]

| Name, Year of Birth, Position with the Fund and Length of Time Served[5] | Principal Occupation(s) During Past 5 Years and Other Directorships Held |
|---|---|
| Michael G. Clark[6] (1965)<br>President, 2006–present | Managing Director[3], Deutsche Asset Management (2006–present); President of DWS family of funds; Director, ICI Mutual Insurance Company (since October 2007); formerly, Director of Fund Board Relations (2004–2006) and Director of Product Development (2000–2004), Merrill Lynch Investment Managers; Senior Vice President Operations, Merrill Lynch Asset Management (1999–2000) |
| John Millette[8] (1962)<br>Vice President and Secretary, 1999–present | Director[3], Deutsche Asset Management |
| Paul H. Schubert[6] (1963)<br>Chief Financial Officer, 2004–present<br>Treasurer, 2005–present | Managing Director[3], Deutsche Asset Management (since July 2004); formerly, Executive Director, Head of Mutual Fund Services and Treasurer for UBS Family of Funds (1998–2004); Vice President and Director of Mutual Fund Finance at UBS Global Asset Management (1994–1998) |
| Caroline Pearson[8] (1962)<br>Chief Legal Officer, April 2010–present | Managing Director[3], Deutsche Asset Management; formerly, Assistant Secretary for DWS family of funds (1997–2010) |
| Rita Rubin[9] (1970)<br>Assistant Secretary, 2009–present | Vice President and Counsel, Deutsche Asset Management (since October 2007); formerly, Vice President, Morgan Stanley Investment Management (2004–2007) |
| Paul Antosca[8] (1957)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management (since 2006); Vice President, The Manufacturers Life Insurance Company (U.S.A.) (1990–2006) |
| Jack Clark[8] (1967)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management (since 2007); formerly, Vice President, State Street Corporation (2002–2007) |

| Name, Year of Birth, Position with the Fund and Length of Time Served[5] | Principal Occupation(s) During Past 5 Years and Other Directorships Held |
|---|---|
| Diane Kenneally[8] (1966)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management |
| John Caruso[9] (1965)<br>Anti-Money Laundering Compliance Officer, 2010–present | Managing Director[3], Deutsche Asset Management |
| Robert Kloby[9] (1962)<br>Chief Compliance Officer, 2006–present | Managing Director[3], Deutsche Asset Management |

1 *The length of time served represents the year in which the Board Member joined the board of one or more DWS funds currently overseen by the Board.*

2 *A publicly held company with securities registered pursuant to Section 12 of the Securities Exchange Act of 1934.*

3 *Executive title, not a board directorship.*

4 *As a result of their respective positions held with the Advisor, these individuals are considered "interested persons" of the Advisor within the meaning of the 1940 Act. Interested persons receive no compensation from the fund.*

5 *The length of time served represents the year in which the officer was first elected in such capacity for one or more DWS funds.*

6 *Address: 100 Plaza One, Jersey City, NJ 07311.*

7 *Effective January 11, 2011, Mr. Gefeke, an interested Board Member and Executive Vice President, resigned from the fund's Board and as an officer.*

*The mailing address of Mr. Gefeke is 345 Park Avenue, New York, New York 10154. Mr. Gefeke was an interested Board Member of certain DWS funds by virtue of his positions with Deutsche Asset Management. As an interested person, Mr. Gefeke received no compensation from the fund.*

8 *Address: One Beacon Street, Boston, MA 02108.*

9 *Address: 60 Wall Street, New York, New York 10005.*

*The fund's Statement of Additional Information ("SAI") includes additional information about the Board Members. The SAI is available, without charge, upon request. If you would like to request a copy of the SAI, you may do so by calling the following toll-free number: (800) 728-3337.*

# Notes

DWS Investments is part of Deutsche Bank's Asset Management division and, within the US, represents the retail asset management activities of Deutsche Bank AG, Deutsche Bank Trust Company Americas, Deutsche Investment Management Americas Inc. and DWS Trust Company.

The views expressed in this report reflect those of the portfolio managers only through the end of the period of the report as stated on the cover. The managers' views are subject to change at any time based on market and other conditions and should not be construed as a recommendation.

This information must be preceded or accompanied by a current prospectus.

Portfolio changes should not be considered recommendations for action by individual investors.

DWS Investments Distributors, Inc.
222 South Riverside Plaza
Chicago, IL 60606
(800) 621-1148

VS2SI-2 (2/11)

DWS INVESTMENTS
Deutsche Bank Group

DECEMBER 31, 2010

# ANNUAL REPORT

## DWS VARIABLE SERIES II

## DWS Strategic Value VIP

**This report must be preceded or accompanied by a prospectus. To obtain an additional prospectus or summary prospectus, if available, call (800) 728-3337 or your financial representative. We advise you to consider the Fund's objectives, risks, charges and expenses carefully before investing. The summary prospectus and prospectus contain this and other important information about the Fund. Please read the prospectus carefully before you invest.**

*Investments in variable insurance portfolios (VIPs) involve risk. Stocks may decline in value. Bond investments are subject to interest-rate and credit risks. When interest rates rise, bond prices generally fall. Credit risk refers to the ability of an issuer to make timely payments of principal and interest. Investing in derivatives entails special risks relating to liquidity, leverage and credit that may reduce returns and/or increased volatility. Investing in foreign securities, particularly those of emerging markets, presents certain risks, such as currency fluctuations, political and economic changes, and market risks. There are additional risks associated with investing in commodities, high-yield bonds, aggressive growth stocks, non-diversified/ concentrated funds and small- and mid-cap stocks which are more fully explained in the prospectuses. Please read the prospectus for more information.*

*DWS Investments is part of Deutsche Bank's Asset Management division and, within the US, represents the retail asset management activities of Deutsche Bank AG, Deutsche Bank Trust Company Americas, Deutsche Investment Management Americas Inc. and DWS Trust Company.*



DWS INVESTMENTS
Deutsche Bank Group

# Performance Summary

December 31, 2010

## DWS Strategic Value VIP

**All performance shown is historical, assumes reinvestment of all dividend and capital gain distributions and does not guarantee future results. Investment return and principal value fluctuate with changing market conditions so that, when redeemed, shares may be worth more or less than their original cost. Current performance may be lower or higher than the performance data quoted. Please contact your participating insurance company for the Fund's most recent month-end performance. Performance doesn't reflect charges and fees ("contract charges") associated with the separate account that invests in the Fund or any variable life insurance policy or variable annuity contract for which the Fund is an investment option. These charges and fees will reduce returns. While all share classes have the same underlying portfolio, their performance will differ.**

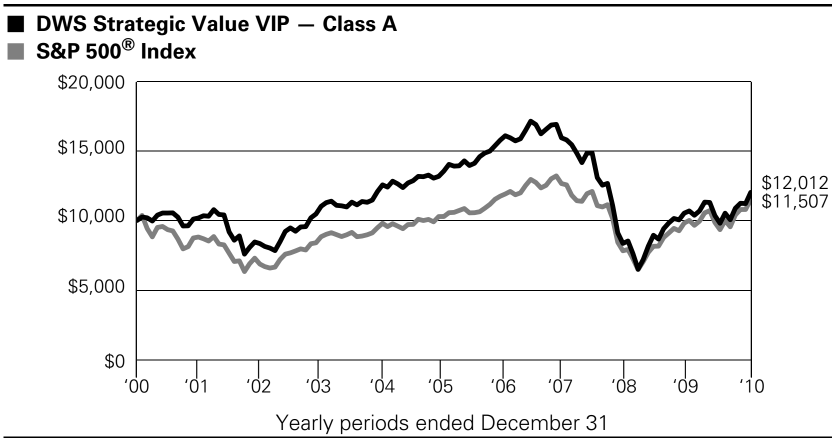
**The gross expense ratios of the Fund, as stated in the fee table of the prospectus dated May 1, 2010 are 0.80% and 1.11% for Class A and Class B shares, respectively, and may differ from the expense ratios disclosed in the Financial Highlights tables in this report.**

### Risk Considerations

Investing in derivatives entails special risks relating to liquidity, leverage and credit that may reduce returns and/or increase volatility. Stocks may decline in value. See the prospectus for details.

Fund returns for all periods shown reflect a fee waiver and/or expense reimbursement. Without this waiver/reimbursement, returns would have been lower.

### Growth of an Assumed $10,000 Investment in DWS Strategic Value VIP




*The Standard & Poor's 500® (S&P 500) Index is an unmanaged, capitalization-weighted index of 500 stocks. The index is designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries.*

*Index returns assume reinvestment of dividends and, unlike fund returns, do not reflect any fees or expenses. It is not possible to invest directly into an index.*

### Comparative Results

| DWS Strategic Value VIP | | 1-Year | 3-Year | 5-Year | 10-Year |
|---|---|---|---|---|---|
| **Class A** | Growth of $10,000 | $11,252 | $7,617 | $8,875 | $12,012 |
| | Average annual total return | 12.52% | –8.68% | –2.36% | 1.85% |
| S&P 500 Index | Growth of $10,000 | $11,506 | $9,168 | $11,199 | $11,507 |
| | Average annual total return | 15.06% | –2.86% | 2.29% | 1.41% |

| DWS Strategic Value VIP | | 1-Year | 3-Year | 5-Year | Life of Class* |
|---|---|---|---|---|---|
| **Class B** | Growth of $10,000 | $11,213 | $7,543 | $8,721 | $12,809 |
| | Average annual total return | 12.13% | –8.97% | –2.70% | 2.95% |
| S&P 500 Index | Growth of $10,000 | $11,506 | $9,168 | $11,199 | $15,038 |
| | Average annual total return | 15.06% | –2.86% | 2.29% | 4.92% |

*The growth of $10,000 is cumulative.*

* *The Fund commenced offering Class B shares on July 1, 2002. Index returns began on June 30, 2002.*

# Information About Your Fund's Expenses

## DWS Strategic Value VIP

As an investor of the Fund, you incur two types of costs: ongoing expenses and transaction costs. Ongoing expenses include management fees, distribution and service (12b-1) fees and other Fund expenses. Examples of transaction costs include contract charges, redemption fees and account maintenance fees, which are not shown in this section. The following tables are intended to help you understand your ongoing expenses (in dollars) of investing in the Fund and to help you compare these expenses with the ongoing expenses of investing in other mutual funds. The example in the table is based on an investment of $1,000 invested at the beginning of the six-month period and held for the entire period (July 1, 2010 to December 31, 2010).

The tables illustrate your Fund's expenses in two ways:

- **Actual Fund Return.** This helps you estimate the actual dollar amount of ongoing expenses (but not transaction costs) paid on a $1,000 investment in the Fund using the Fund's actual return during the period. To estimate the expenses you paid over the period, simply divide your account value by $1,000 (for example, an $8,600 account value divided by $1,000 = 8.6), then multiply the result by the number in the "Expenses Paid per $1,000" line under the share class you hold.
- **Hypothetical 5% Fund Return.** This helps you to compare your Fund's ongoing expenses (but not transaction costs) with those of other mutual funds using the Fund's actual expense ratio and a hypothetical rate of return of 5% per year before expenses. Examples using a 5% hypothetical Fund return may be found in the shareholder reports of other mutual funds. The hypothetical account values and expenses may not be used to estimate the actual ending account balance or expenses you paid for the period.

Please note that the expenses shown in these tables are meant to highlight your ongoing expenses only and do not reflect any transaction costs. The "Expenses Paid per $1,000" line of the tables is useful in comparing ongoing expenses only and will not help you determine the relative total expense of owning different funds. If these transaction costs had been included, your costs would have been higher.

**Expenses and Value of a $1,000 Investment** for the six months ended December 31, 2010

| **Actual Fund Return** | **Class A** | **Class B** |
|---|---|---|
| Beginning Account Value 7/1/10 | $1,000.00 | $1,000.00 |
| Ending Account Value 12/31/10 | $1,226.20 | $1,223.70 |
| Expenses Paid per $1,000* | $ 4.71 | $ 6.56 |
| **Hypothetical 5% Fund Return** | **Class A** | **Class B** |
| Beginning Account Value 7/1/10 | $1,000.00 | $1,000.00 |
| Ending Account Value 12/31/10 | $1,020.97 | $1,019.31 |
| Expenses Paid per $1,000* | $ 4.28 | $ 5.96 |

* *Expenses are equal to the Fund's annualized expense ratio for each share class, multiplied by the average account value over the period, multiplied by the number of days in the most recent six-month period, then divided by 365.*

| **Annualized Expense Ratios** | **Class A** | **Class B** |
|---|---|---|
| DWS Variable Series II — DWS Strategic Value VIP | .84% | 1.17% |

For more information, please refer to the Fund's prospectus.

These tables do not reflect charges and fees ("contract charges") associated with the separate account that invests in the Fund or any variable life insurance policy or variable annuity contract for which the Fund is an investment option.

# Management Summary

December 31, 2010

## DWS Strategic Value VIP

The US equity market performed well during the past year, gaining 15.06% as measured by the Fund's benchmark, the Standard & Poor's 500® (S&P 500) Index. The Class A shares of the Fund returned 12.52% (unadjusted for contract charges).

The most important factor in the Fund's underperformance was the pro-cyclical bias we held throughout the year. By "pro-cyclical," we mean that we tilted the Fund toward the areas of the market most likely to benefit from an improving economy. This approach worked well during the first three months of the Fund's fiscal year, and again in the fourth quarter rally. However, our pro-cyclical tilt proved to be a significant negative in the April–August 2010 interval, during which elevated concerns about the possibility of a "double-dip" recession weighed heavily on the more economically sensitive areas of the market. Unfortunately, this more than offset the outperformance we generated during the other parts of the year. Other important factors in our underperformance included our underweight in the consumer discretionary sector and our relatively conservative positioning in technology.[1]

On the plus side, we added value in the energy sector, thanks to both an overweight position and strong stock selection. Our stock selection in the health care, consumer staples and industrials sectors also was additive to performance.

We are disappointed that the Fund failed to keep pace with the benchmark during the past year, but we remain confident in its positioning as we head into 2011. We are focused on owning stocks with high free cash flow, a metric that has correlated with outperformance for individual stocks over time. Free cash flow strength opens the door for a variety of positive developments, including increased dividends, share buybacks and the potential to be acquired at a premium by a competitor. While high free cash flows did not necessarily lead to outperformance for individual stocks during the past year, we believe that the best time to add exposure to a time-tested investment style is when it is out of favor.

In the wake of a financial shock as large as what we experienced in 2008–2009, the process of recovery is bound to be uneven. The result, inevitably, is periodic instability such as what we witnessed in the April–August 2010 time frame.

Thomas Schuessler, PhD
Volker Dosch
Oliver Pfeil, PhD
*Portfolio Managers*

*The Standard & Poor's 500 (S&P 500) Index is an unmanaged, capitalization-weighted index of 500 stocks. The index is designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries.*

*Index returns assume reinvestment of dividends and, unlike fund returns, do not reflect any fees or expenses. It is not possible to invest directly into an index.*

1 *"Overweight" means the Fund holds a higher weighting in a given sector or security than the benchmark. "Underweight" means the Fund holds a lower weighting.*

*Portfolio management market commentary is as of December 31, 2010, and may not come to pass. This information is subject to change at any time based on market and other conditions. Past performance does not guarantee future results. Current and future portfolio holdings are subject to risk.*

# Portfolio Summary

## DWS Strategic Value VIP

| **Asset Allocation** (As a % of Investment Portfolio excluding Securities Lending Collateral) | **12/31/10** | **12/31/09** |
|---|---|---|
| Common Stocks | 98% | 98% |
| Cash Equivalents | 2% | 2% |
| | 100% | 100% |

| **Sector Diversification** (As a % of Common Stocks) | **12/31/10** | **12/31/09** |
|---|---|---|
| Energy | 22% | 13% |
| Financials | 16% | 16% |
| Information Technology | 15% | 15% |
| Industrials | 11% | 12% |
| Consumer Discretionary | 10% | 7% |
| Health Care | 9% | 14% |
| Consumer Staples | 7% | 12% |
| Telecommunication Services | 4% | 6% |
| Materials | 3% | 4% |
| Utilities | 3% | 1% |
| | 100% | 100% |

*Asset allocation and sector diversification are subject to change.*

*For more complete details about the Fund's investment portfolio, see page 6.*

Following the Fund's fiscal first and third quarter-end, a complete portfolio holdings listing is filed with the SEC on Form N-Q. The form will be available on the SEC's Web site at www.sec.gov, and it also may be reviewed and copied at the SEC's Public Reference Room in Washington, D.C. Information on the operation of the SEC's Public Reference Room may be obtained by calling (800) SEC-0330. The Fund's portfolio holdings are also posted on www.dws-investments.com from time to time. Please see the Fund's current prospectus for more information.

## DWS Strategic Value VIP

| | Shares | Value ($) |
|---|---|---|
| **Common Stocks 98.3%** | | |
| **Consumer Discretionary 10.0%** | | |
| **Automobiles 1.0%** | | |
| General Motors Co.* | 73,980 | **2,726,903** |
| **Hotels Restaurants & Leisure 2.2%** | | |
| McDonald's Corp. | 62,115 | 4,767,947 |
| MGM Resorts International* (a) | 80,000 | 1,188,000 |
| | | **5,955,947** |
| **Household Durables 0.4%** | | |
| Newell Rubbermaid, Inc. | 60,000 | **1,090,800** |
| **Leisure Equipment & Products 0.8%** | | |
| Mattel, Inc. | 87,213 | **2,217,826** |
| **Media 1.6%** | | |
| Time Warner, Inc. | 131,875 | **4,242,419** |
| **Multiline Retail 1.5%** | | |
| Target Corp. | 64,560 | **3,881,993** |
| **Specialty Retail 1.1%** | | |
| Bed Bath & Beyond, Inc.* | 30,000 | 1,474,500 |
| Lowe's Companies, Inc. | 55,829 | 1,400,191 |
| | | **2,874,691** |
| **Textiles, Apparel & Luxury Goods 1.4%** | | |
| VF Corp. (a) | 43,799 | **3,774,598** |
| **Consumer Staples 7.0%** | | |
| **Beverages 1.5%** | | |
| PepsiCo, Inc. | 61,068 | **3,989,572** |
| **Food & Staples Retailing 2.0%** | | |
| CVS Caremark Corp. | 88,016 | 3,060,316 |
| Safeway, Inc. (a) | 108,536 | 2,440,975 |
| | | **5,501,291** |
| **Tobacco 3.5%** | | |
| Altria Group, Inc. | 205,453 | 5,058,253 |
| Philip Morris International, Inc. | 73,109 | 4,279,070 |
| | | **9,337,323** |
| **Energy 21.4%** | | |
| **Energy Equipment & Services 5.6%** | | |
| Ensco PLC (ADR) | 73,117 | 3,902,985 |
| National Oilwell Varco, Inc. | 43,893 | 2,951,804 |
| Transocean Ltd.* (a) | 58,269 | 4,050,278 |
| Weatherford International Ltd.* (a) | 181,327 | 4,134,256 |
| | | **15,039,323** |
| **Oil, Gas & Consumable Fuels 15.8%** | | |
| Apache Corp. | 48,056 | 5,729,717 |
| Chevron Corp. | 65,658 | 5,991,292 |
| ConocoPhillips | 114,579 | 7,802,830 |
| Exxon Mobil Corp. | 43,803 | 3,202,875 |
| Hess Corp. | 80,468 | 6,159,021 |
| Marathon Oil Corp. | 131,664 | 4,875,518 |
| Nexen, Inc. | 97,451 | 2,231,628 |
| Occidental Petroleum Corp. | 29,367 | 2,880,903 |
| Williams Companies, Inc. | 135,158 | 3,341,106 |
| | | **42,214,890** |
| **Financials 15.3%** | | |
| **Capital Markets 1.8%** | | |
| Janus Capital Group, Inc. | 80,000 | 1,037,600 |
| Legg Mason, Inc. | 30,000 | 1,088,100 |
| The Goldman Sachs Group, Inc. | 16,213 | 2,726,378 |
| | | **4,852,078** |
| **Commercial Banks 3.0%** | | |
| Royal Bank of Canada | 50,000 | 2,618,000 |
| Wells Fargo & Co. | 172,565 | 5,347,789 |
| | | **7,965,789** |
| **Consumer Finance 1.0%** | | |
| Capital One Financial Corp. (a) | 63,978 | **2,722,904** |
| **Diversified Financial Services 5.6%** | | |
| Citigroup, Inc.* | 1,057,545 | 5,002,188 |
| JPMorgan Chase & Co. | 233,319 | 9,897,392 |
| | | **14,899,580** |
| **Insurance 3.9%** | | |
| Hartford Financial Services Group, Inc. (a) | 154,087 | 4,081,765 |
| Lincoln National Corp. | 130,684 | 3,634,322 |
| MetLife, Inc. | 61,167 | 2,718,261 |
| | | **10,434,348** |
| **Thrifts & Mortgage Finance 0.0%** | | |
| Washington Mutual, Inc.* | 1,394,944 | **78,954** |
| **Health Care 8.9%** | | |
| **Biotechnology 0.9%** | | |
| Amgen, Inc.* | 43,291 | **2,376,676** |
| **Health Care Providers & Services 3.5%** | | |
| Aetna, Inc. | 99,770 | 3,043,983 |
| UnitedHealth Group, Inc. | 83,959 | 3,031,759 |
| WellPoint, Inc.* | 58,337 | 3,317,042 |
| | | **9,392,784** |
| **Life Sciences Tools & Services 1.1%** | | |
| Thermo Fisher Scientific, Inc.* | 51,917 | **2,874,125** |
| **Pharmaceuticals 3.4%** | | |
| Abbott Laboratories | 52,809 | 2,530,079 |
| Mylan, Inc.* | 174,984 | 3,697,412 |
| Novartis AG (ADR) (a) | 48,184 | 2,840,447 |
| | | **9,067,938** |
| **Industrials 10.4%** | | |
| **Aerospace & Defense 5.4%** | | |
| Honeywell International, Inc. | 76,520 | 4,067,803 |
| ITT Corp. (a) | 58,665 | 3,057,033 |
| United Technologies Corp. | 94,868 | 7,468,009 |
| | | **14,592,845** |
| **Construction & Engineering 0.9%** | | |
| URS Corp.* | 58,652 | **2,440,510** |
| **Industrial Conglomerates 1.5%** | | |
| General Electric Co. | 226,206 | **4,137,308** |
| **Machinery 1.6%** | | |
| Deere & Co. | 50,053 | **4,156,902** |
| **Road & Rail 1.0%** | | |
| CSX Corp. | 41,068 | **2,653,403** |
| **Information Technology 14.8%** | | |
| **Communications Equipment 1.0%** | | |
| Cisco Systems, Inc.* | 135,000 | **2,731,050** |
| **Computers & Peripherals 3.4%** | | |
| Hewlett-Packard Co. | 179,144 | 7,541,962 |
| Lexmark International, Inc. "A"* | 45,000 | 1,566,900 |
| | | **9,108,862** |

*The accompanying notes are an integral part of the financial statements.*

| | Shares | Value ($) |
|---|---|---|
| **Electronic Equipment, Instruments & Components 0.5%** | | |
| Corning, Inc. | 70,000 | **1,352,400** |
| **IT Services 2.5%** | | |
| Accenture PLC "A" | 102,451 | 4,967,849 |
| Computer Sciences Corp. | 33,254 | 1,649,398 |
| | | **6,617,247** |
| **Office Electronics 1.6%** | | |
| Xerox Corp. | 373,129 | **4,298,447** |
| **Semiconductors & Semiconductor Equipment 1.0%** | | |
| Micron Technology, Inc.* (a) | 331,290 | **2,656,946** |
| **Software 4.8%** | | |
| BMC Software, Inc.* | 65,869 | 3,105,065 |
| Microsoft Corp. | 354,564 | 9,899,427 |
| | | **13,004,492** |
| **Materials 3.4%** | | |
| **Metals & Mining** | | |
| Agnico-Eagle Mines Ltd. (a) | 21,894 | 1,679,270 |
| BHP Billiton Ltd. (ADR) (a) | 20,000 | 1,858,400 |
| Freeport-McMoRan Copper & Gold, Inc. | 23,244 | 2,791,372 |
| Kinross Gold Corp. | 146,385 | 2,775,459 |
| | | **9,104,501** |
| **Telecommunication Services 4.5%** | | |
| **Diversified Telecommunication Services 2.8%** | | |
| AT&T, Inc. | 146,263 | 4,297,207 |
| CenturyLink, Inc. (a) | 65,928 | 3,043,896 |
| | | **7,341,103** |
| **Wireless Telecommunication Services 1.7%** | | |
| Vodafone Group PLC (ADR) (a) | 175,281 | **4,632,677** |
| **Utilities 2.6%** | | |
| **Electric Utilities 0.6%** | | |
| FirstEnergy Corp. (a) | 43,893 | **1,624,919** |
| **Multi-Utilities 2.0%** | | |
| PG&E Corp. | 58,501 | 2,798,688 |
| Sempra Energy | 48,382 | 2,539,087 |
| | | **5,337,775** |
| **Total Common Stocks** (Cost $225,572,465) | | **263,304,139** |

## Securities Lending Collateral 14.9%

| | Shares | Value ($) |
|---|---|---|
| Daily Assets Fund Institutional, 0.27% (b) (c) (Cost $39,865,520) | 39,865,520 | **39,865,520** |

## Cash Equivalents 2.1%

| | Shares | Value ($) |
|---|---|---|
| Central Cash Management Fund, 0.19% (b) (Cost $5,724,962) | 5,724,962 | **5,724,962** |

| | % of Net Assets | Value ($) |
|---|---|---|
| **Total Investment Portfolio** (Cost $271,162,947)† | 115.3 | **308,894,621** |
| **Other Assets and Liabilities, Net** | (15.3) | **(40,966,695)** |
| **Net Assets** | 100.0 | **267,927,926** |

* *Non-income producing security.*

† *The cost for federal income tax purposes was $272,059,584. At December 31, 2010, net unrealized appreciation for all securities based on tax cost was $36,835,037. This consisted of aggregate gross unrealized appreciation for all securities in which there was an excess of value over tax cost of $50,605,721 and aggregate gross unrealized depreciation for all securities in which there was an excess of tax cost over value of $13,770,684.*

(a) *All or a portion of these securities were on loan (see Notes to Financial Statements). The value of all securities loaned at December 31, 2010 amounted to $38,874,375, which is 14.5% of net assets.*

(b) *Affiliated fund managed by Deutsche Investment Management Americas Inc. The rate shown is the annualized seven-day yield at period end.*

(c) *Represents collateral held in connection with securities lending. Income earned by the Fund is net of borrower rebates.*

*ADR: American Depositary Receipt*

### Fair Value Measurements

*Various inputs are used in determining the value of the Fund's investments. These inputs are summarized in three broad levels. Level 1 includes quoted prices in active markets for identical securities. Level 2 includes other significant observable inputs (including quoted prices for similar securities, interest rates, prepayment speeds, and credit risk). Level 3 includes significant unobservable inputs (including the Fund's own assumptions in determining the fair value of investments). The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities.*

*The following is a summary of the inputs used as of December 31, 2010 in valuing the Fund's investments. For information on the Fund's policy regarding the valuation of investments, please refer to the Security Valuation section of Note A in the accompanying Notes to Financial Statements.*

| Assets | Level 1 | Level 2 | Level 3 | Total |
|---|---|---|---|---|
| Common Stocks (d) | $ 263,304,139 | $ — | $ — | $ 263,304,139 |
| Short-Term Investments (d) | 45,590,482 | — | — | 45,590,482 |
| **Total** | **$ 308,894,621** | **$ —** | **$ —** | **$ 308,894,621** |

*There have been no significant transfers between Level 1 and Level 2 fair value measurements during the year ended December 31, 2010.*

(d) *See Investment Portfolio for additional detailed categorizations.*

*The accompanying notes are an integral part of the financial statements.*

# Statement of Assets and Liabilities

as of December 31, 2010

| **Assets** | | |
|---|---|---|
| Investments: | | |
| Investments in unaffiliated securities, at value (cost $225,572,465) — including $38,874,375 of securities loaned | $ | 263,304,139 |
| Investment in Daily Assets Fund Institutional (cost $39,865,520)* | | 39,865,520 |
| Investment in Central Cash Management Fund (cost $5,724,962) | | 5,724,962 |
| Total investments at value (cost $271,162,947) | | 308,894,621 |
| Receivable for Fund shares sold | | 803 |
| Dividends receivable | | 426,895 |
| Interest receivable | | 2,761 |
| Foreign taxes recoverable | | 2,107 |
| Other assets | | 1,438 |
| Total assets | | 309,328,625 |
| **Liabilities** | | |
| Payable upon return of securities loaned | | 39,865,520 |
| Payable for Fund shares redeemed | | 154,974 |
| Payable for investments purchased | | 1,085,769 |
| Accrued management fee | | 149,132 |
| Other accrued expenses and payables | | 145,304 |
| Total liabilities | | 41,400,699 |
| **Net assets, at value** | **$** | **267,927,926** |
| **Net Assets Consist of** | | |
| Undistributed net investment income | | 3,522,893 |
| Net unrealized appreciation (depreciation) on: | | |
| Investments | | 37,731,674 |
| Foreign currency | | 64 |
| Accumulated net realized gain (loss) | | (141,564,092) |
| Paid-in capital | | 368,237,387 |
| **Net assets, at value** | **$** | **267,927,926** |
| **Class A** | | |
| **Net Asset Value,** offering and redemption price per share ($266,068,810 ÷ 32,742,109 outstanding shares of beneficial interest, no par value, unlimited number of shares authorized) | **$** | **8.13** |
| **Class B** | | |
| **Net Asset Value,** offering and redemption price per share ($1,859,116 ÷ 228,157 outstanding shares of beneficial interest, no par value, unlimited number of shares authorized) | **$** | **8.15** |

* *Represents collateral on securities loaned.*

# Statement of Operations

for the year ended December 31, 2010

| **Investment Income** | | |
|---|---|---|
| Income: | | |
| Dividends (net of foreign taxes withheld of $43,360) | $ | 5,932,680 |
| Income distributions — Central Cash Management Fund | | 19,988 |
| Securities lending income, including income from Daily Assets Fund Institutional, net of borrower rebates | | 32,898 |
| Total income | | 5,985,566 |
| Expenses: | | |
| Management fee | | 1,756,021 |
| Administration fee | | 264,774 |
| Services to shareholders | | 20,135 |
| Distribution service fee (Class B) | | 4,271 |
| Record keeping fees (Class B) | | 940 |
| Custodian fee | | 17,404 |
| Professional fees | | 65,688 |
| Trustees' fees and expenses | | 9,696 |
| Reports to shareholders | | 69,429 |
| Other | | 13,801 |
| Total expenses before expense reductions | | 2,222,159 |
| Expense reductions | | (36,423) |
| Total expenses after expense reductions | | 2,185,736 |
| **Net investment income (loss)** | | **3,799,830** |
| **Realized and Unrealized Gain (Loss)** | | |
| Net realized gain (loss) from: | | |
| Investments | | 17,969,063 |
| Foreign currency | | 351 |
| Payments by Affiliates (see Note F) | | 289,394 |
| | | 18,258,808 |
| Change in net unrealized appreciation (depreciation) on: | | |
| Investments | | 8,466,003 |
| Foreign currency | | 64 |
| | | 8,466,067 |
| **Net gain (loss)** | | **26,724,875** |
| **Net increase (decrease) in net assets resulting from operations** | **$** | **30,524,705** |

*The accompanying notes are an integral part of the financial statements.*

# Statement of Changes in Net Assets

| Increase (Decrease) in Net Assets | Years Ended December 31, 2010 | 2009 |
|---|---|---|
| Operations: | | |
| Net investment income (loss) | $ 3,799,830 | $ 5,183,044 |
| Net realized gain (loss) | 18,258,808 | (11,128,319) |
| Change in net unrealized appreciation (depreciation) | 8,466,067 | 65,208,508 |
| Net increase (decrease) in net assets resulting from operations | 30,524,705 | 59,263,233 |
| Distributions to shareholders from: | | |
| Net investment income: | | |
| Class A | (5,244,990) | (12,778,810) |
| Class B | (28,738) | (81,600) |
| Total distributions | (5,273,728) | (12,860,410) |
| Fund share transactions: | | |
| **Class A** | | |
| Proceeds from shares sold | 4,504,378 | 5,209,923 |
| Reinvestment of distributions | 5,244,990 | 12,778,810 |
| Payments for shares redeemed | (50,438,746) | (90,662,545) |
| Net increase (decrease) in net assets from Class A share transactions | (40,689,378) | (72,673,812) |
| **Class B** | | |
| Proceeds from shares sold | 431,727 | 544,525 |
| Reinvestment of distributions | 28,738 | 81,600 |
| Payments for shares redeemed | (713,355) | (1,038,519) |
| Net increase (decrease) in net assets from Class B share transactions | (252,890) | (412,394) |
| **Increase (decrease) in net assets** | (15,691,291) | (26,683,383) |
| Net assets at beginning of period | 283,619,217 | 310,302,600 |
| Net assets at end of period (including undistributed net investment income of $3,522,893 and $4,996,440, respectively) | **$ 267,927,926** | **$ 283,619,217** |

| Other Information | | |
|---|---|---|
| **Class A** | | |
| Shares outstanding at beginning of period | 38,269,626 | 49,642,073 |
| Shares sold | 610,579 | 874,127 |
| Shares issued to shareholders in reinvestment of distributions | 674,163 | 2,576,373 |
| Shares redeemed | (6,812,259) | (14,822,947) |
| Net increase (decrease) in Class A shares | (5,527,517) | (11,372,447) |
| Shares outstanding at end of period | **32,742,109** | **38,269,626** |
| **Class B** | | |
| Shares outstanding at beginning of period | 265,888 | 327,546 |
| Shares sold | 56,800 | 86,408 |
| Shares issued to shareholders in reinvestment of distributions | 3,675 | 16,352 |
| Shares redeemed | (98,206) | (164,418) |
| Net increase (decrease) in Class B shares | (37,731) | (61,658) |
| Shares outstanding at end of period | **228,157** | **265,888** |

*The accompanying notes are an integral part of the financial statements.*

# Financial Highlights

## Class A

| Years Ended December 31, | 2010 | 2009 | 2008 | 2007 | 2006 |
|---|---|---|---|---|---|
| **Selected Per Share Data** | | | | | |
| **Net asset value, beginning of period** | **$ 7.36** | **$ 6.21** | **$14.40** | **$15.02** | **$13.41** |
| *Income (loss) from investment operations:* | | | | | |
| Net investment income (loss)[a] | .11 | .12 | .22 | .29 | .27 |
| Net realized and unrealized gain (loss) | .81 | 1.31 | (5.80) | (.56) | 2.21 |
| **Total from investment operations** | .92 | 1.43 | (5.58) | (.27) | 2.48 |
| *Less distributions from:* | | | | | |
| Net investment income | (.15) | (.28) | (.36) | (.22) | (.28) |
| Net realized gains | — | — | (2.25) | (.13) | (.59) |
| **Total distributions** | (.15) | (.28) | (2.61) | (.35) | (.87) |
| **Net asset value, end of period** | **$ 8.13** | **$ 7.36** | **$ 6.21** | **$14.40** | **$15.02** |
| Total Return (%) | 12.52[b] | 25.30[b] | (45.98)[b] | (1.86) | 18.74 |
| **Ratios to Average Net Assets and Supplemental Data** | | | | | |
| Net assets, end of period ($ millions) | 266 | 282 | 308 | 792 | 992 |
| Ratio of expenses before expense reductions (%) | .84 | .80 | .81 | .78 | .77 |
| Ratio of expenses after expense reductions(%) | .82 | .76 | .80 | .78 | .77 |
| Ratio of net investment income (%) | 1.44 | 1.89 | 2.21 | 1.94 | 1.87 |
| Portfolio turnover rate (%) | 87 | 91 | 28 | 27 | 20 |

[a] *Based on average shares outstanding during the period.*

[b] *Total return would have been lower had certain expenses not been reduced.*

## Class B

| Years Ended December 31, | 2010 | 2009 | 2008 | 2007 | 2006 |
|---|---|---|---|---|---|
| **Selected Per Share Data** | | | | | |
| **Net asset value, beginning of period** | **$ 7.38** | **$ 6.22** | **$14.41** | **$15.02** | **$13.39** |
| *Income (loss) from investment operations:* | | | | | |
| Net investment income (loss)[a] | .08 | .10 | .16 | .24 | .22 |
| Net realized and unrealized gain (loss) | .81 | 1.32 | (5.79) | (.56) | 2.19 |
| **Total from investment operations** | .89 | 1.42 | (5.63) | (.32) | 2.41 |
| *Less distributions from:* | | | | | |
| Net investment income | (.12) | (.26) | (.31) | (.16) | (.19) |
| Net realized gains | — | — | (2.25) | (.13) | (.59) |
| **Total distributions** | (.12) | (.26) | (2.56) | (.29) | (.78) |
| **Net asset value, end of period** | **$ 8.15** | **$ 7.38** | **$ 6.22** | **$14.41** | **$15.02** |
| Total Return (%)[b] | 12.13 | 24.94 | (46.16) | (2.19) | 18.21 |
| **Ratios to Average Net Assets and Supplemental Data** | | | | | |
| Net assets, end of period ($ millions) | 2 | 2 | 2 | 37 | 191 |
| Ratio of expenses before expense reduction (%) | 1.15 | 1.11 | 1.21 | 1.15 | 1.16 |
| Ratio of expenses after expense reduction (%) | 1.14 | 1.08 | 1.17 | 1.13 | 1.16 |
| Ratio of net investment income (%) | 1.12 | 1.57 | 1.84 | 1.59 | 1.48 |
| Portfolio turnover rate (%) | 87 | 91 | 28 | 27 | 20 |

[a] *Based on average shares outstanding during the period.*

[b] *Total return would have been lower had certain expenses not been reduced.*

# Notes to Financial Statements

## A. Organization and Significant Accounting Policies

DWS Variable Series II (the "Trust") is registered under the Investment Company Act of 1940, as amended (the "1940 Act"), as an open-end management investment company organized as a Massachusetts business trust. The Trust offers seventeen funds (hereinafter referred to individually as "Fund" or collectively as "Funds"). The Fund is classified as a diversified open-end management investment company.

**Multiple Classes of Shares of Beneficial Interest.** Certain Funds of the Trust offer two classes of shares (Class A shares and Class B shares). Sales of Class B shares are subject to record keeping fees up to 0.15% and Rule 12b-1 fees under the 1940 Act equal to an annual rate of 0.25%, of the average daily net assets of the Class B shares of the applicable Fund. Class A shares are not subject to such fees.

Investment income, realized and unrealized gains and losses, and certain fund-level expenses and expense reductions, if any, are borne pro rata on the basis of relative net assets by the holders of all classes of shares except that each class bears certain expenses unique to that class (including the applicable Rule 12b-1 fee and record keeping fees). Differences in class-level expenses may result in payment of different per share dividends by class. All shares have equal rights with respect to voting subject to class-specific arrangements.

The Trust's financial statements are prepared in accordance with accounting principles generally accepted in the United States of America which require the use of management estimates. Actual results could differ from those estimates. The policies described below are followed consistently by the Trust in the preparation of its financial statements.

**Security Valuation.** Investments are stated at value determined as of the close of regular trading on the New York Stock Exchange on each day the exchange is open for trading.

Various inputs are used in determining the value of the Fund's investments. These inputs are summarized in three broad levels. Level 1 includes quoted prices in active markets for identical securities. Level 2 includes other significant observable inputs (including quoted prices for similar securities, interest rates, prepayment speeds, and credit risk). Level 3 includes significant unobservable inputs (including the Fund's own assumptions in determining the fair value of investments). The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities.

Equity securities are valued at the most recent sale price or official closing price reported on the exchange (US or foreign) or over-the-counter market on which they trade and are categorized as Level 1 securities. Securities for which no sales are reported are valued at the calculated mean between the most recent bid and asked quotations on the relevant market or, if a mean cannot be determined, at the most recent bid quotation.

Money market instruments purchased with an original or remaining maturity of sixty days or less, maturing at par, are valued at amortized cost, which approximates value, and are categorized as Level 2. Investments in open-end investment companies are valued at their net asset value each business day and are categorized as Level 1.

Securities and other assets for which market quotations are not readily available or for which the above valuation procedures are deemed not to reflect fair value are valued in a manner that is intended to reflect their fair value as determined in accordance with procedures approved by the Board and are generally categorized as Level 3. In accordance with the Fund's valuation procedures, factors used in determining value may include, but are not limited to, the type of the security; the size of the holding; the initial cost of the security; the existence of any contractual restrictions on the security's disposition; the price and extent of public trading in similar securities of the issuer or of comparable companies; quotations or evaluated prices from broker-dealers and/or pricing services; information obtained from the issuer, analysts, and/or the appropriate stock exchange (for exchange-traded securities); an analysis of the company's or issuer's financial statements; an evaluation of the forces that influence the issuer and the market(s) in which the security is purchased and sold and with respect to debt securities; the maturity, coupon, creditworthiness, currency denomination and the movement of the market in which the security is normally traded. The value determined under these procedures may differ from published values for the same securities.

Disclosure about the classification of fair value measurements is included in a table following the Fund's Investment Portfolio.

**Securities Lending.** The Fund lends securities to certain financial institutions. The Fund retains beneficial ownership of the securities it has loaned and continues to receive interest and dividends paid by the issuer of securities and to participate in any changes in their market value. The Fund requires the borrowers of the securities to maintain collateral with the Fund consisting of either cash or liquid, unencumbered assets having a value at least equal to the value of the securities loaned. When the collateral falls below specified amounts, the lending agent will use its best effort to obtain additional collateral on the next business day to meet required amounts under the security lending agreement. The Fund may invest the cash collateral into a joint trading account in an affiliated money market fund pursuant to Exemptive Orders issued by the SEC. The Fund receives compensation for lending its securities either in the form of fees or by earning interest on invested cash collateral net of borrower rebates and fees paid to a lending agent. Either the Fund or the borrower may terminate the loan. There may be risks of delay and costs in recovery of securities or even loss of rights in the collateral should the borrower of the securities fail financially. The Fund is also subject to all investment risks associated with the reinvestment of any cash collateral received, including, but not limited to, interest rate, credit and liquidity risk associated with such investments.

**Taxes.** The Fund's policy is to comply with the requirements of the Internal Revenue Code, as amended, which are applicable to regulated investment companies and to distribute all of its taxable income to its shareholders.

At December 31, 2010, the Fund had an approximate net tax basis capital loss carryforward which may be applied against any realized net taxable capital gains of each succeeding year until fully utilized or until the following expiration dates, whichever occurs first:

| Fund | Capital Loss Carryforward ($) | Expiration Date | Capital Loss Carryforward Utilized ($) |
|---|---|---|---|
| DWS Strategic Value VIP | 52,455,000 | 12/31/2016 | 15,988,000 |
| | 88,212,000 | 12/31/2017 | |

The Fund has reviewed the tax positions for the open tax years as of December 31, 2010 and has determined that no provision for income tax is required in the Fund's financial statements. The Fund's federal tax returns for the prior three fiscal years remain open subject to examination by the Internal Revenue Service.

**Distribution of Income and Gains.** Distributions of net investment income of the Fund, if any, are made annually. Net realized gains from investment transactions, in excess of available capital loss carryforwards, would be taxable to the Fund if not distributed and, therefore, will be distributed to shareholders at least annually. The Fund may also make additional distributions for tax purposes if necessary.

The timing and characterization of certain income and capital gains distributions are determined annually in accordance with federal tax regulations which may differ from accounting principles generally accepted in the United States of America. These differences primarily relate to certain securities sold at a loss. As a result, net investment income (loss) and net realized gain (loss) on investment transactions for a reporting period may differ significantly from distributions during such period. Accordingly, the Fund may periodically make reclassifications among certain of its capital accounts without impacting the net asset value of the Fund.

At December 31, 2010, the Fund's components of distributable earnings on a tax basis were as follows:

| Fund | Undistributed Ordinary Income ($)* | Capital Loss Carryforwards ($) | Unrealized Appreciation (Depreciation) on Investments ($) |
|---|---|---|---|
| DWS Strategic Value VIP | 3,522,893 | (140,667,000) | 36,835,037 |

In addition, the tax character of distributions paid by the Fund is summarized as follows:

| | Distributions from Ordinary Income ($)* | |
|---|---|---|
| | Years Ended December 31, | |
| Fund | 2010 | 2009 |
| DWS Strategic Value VIP | 5,273,728 | 12,860,410 |

* *For tax purposes, short-term capital gain distributions are considered ordinary income distributions.*

**Expenses.** Expenses of the Trust arising in connection with a specific fund are allocated to that fund. Other Trust expenses which cannot be directly attributed to a fund are apportioned among the funds in the Trust.

**Contingencies.** In the normal course of business, the Fund may enter into contracts with service providers that contain general indemnification clauses. The Fund's maximum exposure under these arrangements is unknown as this would involve future claims that may be made against the Fund that have not yet been made. However, based on experience, the Fund expects the risk of loss to be remote.

**Other.** Investment transactions are accounted for on a trade date plus one basis for daily net asset value calculations. However, for financial reporting purposes, investment transactions are reported on trade date. Interest income is recorded on the accrual basis. Dividend income is recorded on the ex-dividend date net of foreign withholding taxes. Realized gains and losses from investment transactions are recorded on an identified cost basis.

## B. Purchases and Sales of Securities

During the year ended December 31, 2010, purchases and sales of investment transactions (excluding short-term investments) were as follows:

| Fund | Purchases ($) | Sales ($) |
|---|---|---|
| DWS Strategic Value VIP | 218,849,807 | 258,849,951 |

## C. Related Parties

**Management Agreement.** Under the Investment Management Agreement with Deutsche Investment Management Americas Inc. ("DIMA" or the "Advisor"), an indirect, wholly owned subsidiary of Deutsche Bank AG, the Advisor directs the investments of the Fund in accordance with its investment objectives, policies and restrictions. The Advisor determines the securities, instruments and other contracts relating to investments to be purchased, sold or entered into by the Fund.

Under the Investment Management Agreement with the Advisor, the fee is equivalent to the annual rates shown below of the Fund's average daily net assets, computed and accrued daily and payable monthly:

| Fund | Annual Management Fee Rate |
|---|---|
| DWS Strategic Value VIP | |
| $0–$250 million | .665% |
| next $750 million | .635% |
| next $1.5 billion | .615% |
| next $2.5 billion | .595% |
| next $2.5 billion | .565% |
| next $2.5 billion | .555% |
| next $2.5 billion | .545% |
| over $12.5 billion | .535% |

For the period from January 1, 2010 through April 30, 2010, the Advisor had contractually agreed to waive its fee and/or reimburse certain operating expenses to the extent necessary to maintain the operating expenses (excluding certain expenses such as extraordinary expenses, taxes, brokerage and interest expense) of each class as follows:

| Fund | Annual Rate |
|---|---|
| DWS Strategic Value VIP | |
| Class A | .78% |
| Class B | 1.11% |

Accordingly, for the year ended December 31, 2010, the total management fee, management fee waived and effective management fee rate were as follows:

| Fund | Total Aggregated ($) | Waived ($) | Annual Effective Rate |
|---|---|---|---|
| DWS Strategic Value VIP | 1,756,021 | 35,990 | .65% |

**Administration Fee.** Pursuant to an Administrative Services Agreement, DIMA provides most administrative services to the Fund. For all services provided under the Administrative Services Agreement, the Fund pays DIMA an annual fee ("Administration Fee") of 0.10% of the Fund's average daily net assets, computed and accrued daily and payable monthly. For the year ended December 31, 2010, the Administration Fee was as follows:

| Fund | Total Aggregated ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS Strategic Value VIP | 264,774 | 22,475 |

**Service Provider Fees.** DWS Investments Service Company ("DISC"), an affiliate of the Advisor, is the transfer agent, dividend-paying agent and shareholder service agent for the Fund. Pursuant to a sub-transfer agency agreement between DISC and DST Systems, Inc. ("DST"), DISC has delegated certain transfer agent, dividend-paying agent and shareholder service agent functions to DST. DISC compensates DST out of the shareholder servicing fee it receives from the Fund. For the year ended December 31, 2010, the amounts charged to the Fund by DISC were as follows:

| Fund | Total Aggregated ($) | Waived ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|---|
| DWS Strategic Value VIP Class A | 433 | 433 | — |
| DWS Strategic Value VIP Class B | 197 | — | 48 |

**Distribution Service Agreement**. Under the Fund's Class B 12b-1 plans, DWS Investments Distributors, Inc. ("DIDI") received a fee ("Distribution Service Fee") of 0.25% of average daily net assets of Class B shares. For the year ended December 31, 2010, the Distribution Service Fee was as follows:

| Fund | Total Aggregated ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS Strategic Value VIP | 4,271 | 393 |

**Typesetting and Filing Service Fees.** Under an agreement with DIMA, DIMA is compensated for providing typesetting and certain regulatory filing services to the Fund. For the year ended December 31, 2010, the amount charged to the Fund by DIMA included in the Statement of Operations under "reports to shareholders" was as follows:

| Fund | Amount ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS Strategic Value VIP | 13,417 | 4,180 |

**Trustees' Fees and Expenses.** The Fund paid each Trustee not affiliated with the Advisor retainer fees plus specified amounts for various committee services and for the Board Chairperson.

**Affiliated Cash Management Vehicles.** The Fund may invest uninvested cash balances in Central Cash Management Fund, which is managed by the Advisor. The Fund indirectly bears their proportionate share of the expenses of the underlying money market funds. Central Cash Management Fund does not pay the Advisor an investment management fee. Central Cash Management Fund seeks a high level of current income consistent with liquidity and the preservation of capital.

## D. Ownership of the Fund

At December 31, 2010, the beneficial ownership in the Fund was as follows:

**DWS Strategic Value VIP:** Two Participating Insurance Companies were owners of record of 10% or more of the total outstanding Class A shares of the Fund, each owning 56% and 30%. Five Participating Insurance Companies were owners of record of 10% or more of the total outstanding Class B shares of the Fund, each owning 26%, 25%, 15%, 11% and 11%.

## E. Line of Credit

The Trust and other affiliated fund (the "Participants") share in a $450 million revolving credit facility provided by a syndication of banks. The Fund may borrow for temporary or emergency purposes, including the meeting of redemption requests that otherwise might require the untimely disposition of securities. The Participants are charged an annual commitment fee which is allocated based on net assets, among each of the Participants. Interest is calculated at a rate per annum equal to the sum of the Federal Funds Rate plus 1.25 percent plus if LIBOR exceeds the Federal Funds Rate the amount of such excess. The Fund may borrow up to a maximum of 33 percent of its net assets under the agreement.

## F. Payments by Affiliates

During the year ended December 31, 2010, the Advisor agreed to reimburse the Fund $289,394 for losses incurred on trades executed incorrectly. The amount of the reimbursement is 0.11% of the Fund's average net assets.

## G. Subsequent Event

On January 12, 2011, the Board of the following Acquired Fund approved, in principle, the merger of the Acquired Fund into the Acquiring Fund. Completion of the merger is subject to a number of conditions. The merger is expected to be completed on or about May 1, 2011.

| Acquired Fund | Acquiring Fund |
|---|---|
| DWS Variable Series II — DWS Strategic Value VIP | DWS Variable Series II — DWS Large Cap Value VIP |

# Report of Independent Registered Public Accounting Firm

**To the Board of Trustees and Shareholders of DWS Variable Series II:**

We have audited the accompanying statement of assets and liabilities of DWS Strategic Value VIP, one of the funds constituting the DWS Variable Series II (the "Trust"), including the investment portfolio, as of December 31, 2010, and the related statement of operations, the statement of changes in net assets and the financial highlights for each of the periods indicated therein. These financial statements and financial highlights are the responsibility of the Trust's management. Our responsibility is to express an opinion on these financial statements and financial highlights based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements and financial highlights are free of material misstatement. We were not engaged to perform an audit of the Trust's internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Trust's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements and financial highlights, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our procedures included confirmation of securities owned as of December 31, 2010, by correspondence with the custodian and brokers or by other appropriate auditing procedures where replies from brokers were not received. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements and financial highlights referred to above present fairly, in all material respects, the financial position of the aforementioned fund of the DWS Variable Series II at December 31, 2010, the results of its operations, the changes in its net assets and the financial highlights for each of the periods indicated therein, in conformity with U.S. generally accepted accounting principles.

Ernst + Young LLP

Boston, Massachusetts
February 14, 2011

# Tax Information

**(Unaudited)**

For corporate shareholders, the following percentage of income dividends paid during the Fund's fiscal year ended December 31, 2010 qualified for the dividends received deduction:

| Fund | Dividends Received % |
|---|---|
| DWS Strategic Value VIP | 100 |

Please consult a tax advisor if you have questions about federal or state income tax laws, or on how to prepare your tax returns. If you have specific questions about your account, please contact your insurance provider.

# Proxy Voting

The Trust's policies and procedures for voting proxies for portfolio securities and information about how the Trust voted proxies related to its portfolio securities during the 12-month period ended June 30 are available on our Web site — www.dws-investments.com (click on "proxy voting" at the bottom of the page) — or on the SEC's Web site — www.sec.gov. To obtain a written copy of the Trust's policies and procedures without charge, upon request, call us toll free at (800) 728-3337.

# Investment Management Agreement Approval

## DWS Strategic Value VIP

The Board of Trustees, including the Independent Trustees, approved the renewal of your Fund's investment management agreement (the "Agreement") with Deutsche Investment Management Americas Inc. ("DWS") in September 2010.

In terms of the process that the Board followed prior to approving the Agreement, shareholders should know that:

- In September 2010, all but one of the Fund's Trustees were independent of DWS and its affiliates.
- The Trustees meet frequently to discuss fund matters. Each year, the Trustees dedicate substantial time to contract review matters. Over the course of several months, the Board's Contract Committee, in coordination with the Board's Equity Oversight Committee, reviewed comprehensive materials received from DWS, independent third parties and independent counsel. These materials included an analysis of the Fund's performance, fees and expenses, and profitability compiled by the Fund's independent fee consultant. The Board also received extensive information throughout the year regarding performance of the Fund.
- The Independent Trustees regularly meet privately with their independent counsel to discuss contract review and other matters. In addition, the Independent Trustees were also advised by the Fund's independent fee consultant in the course of their review of the Fund's contractual arrangements and considered a comprehensive report prepared by the independent fee consultant in connection with their deliberations (the "IFC Report").
- In connection with reviewing the Agreement, the Board also reviewed the terms of the Fund's Rule 12b-1 plan, distribution agreement, administrative services agreement, transfer agency agreement and other material service agreements.
- Based on its evaluation of the information provided, the Contract Committee presented its findings and recommendations to the Independent Trustees as a group. The Independent Trustees reviewed the Contract Committee's findings and recommendations and presented their recommendations to the full Board.

In connection with the contract review process, the Contract Committee and the Board considered the factors discussed below, among others. The Board also considered that DWS and its predecessors have managed the Fund since its inception, and the Board believes that a long-term relationship with a capable, conscientious advisor is in the best interests of the Fund. The Board considered, generally, that shareholders chose to invest or remain invested in the Fund knowing that DWS managed the Fund, and that the Agreement was approved by the Fund's shareholders. DWS is part of Deutsche Bank, a major global banking institution that is engaged in a wide range of financial services. The Board believes that there are significant advantages to being part of a global asset management business that offers a wide range of investing expertise and resources, including hundreds of portfolio managers and analysts with research capabilities in many countries throughout the world.

While shareholders may focus primarily on fund performance and fees, the Fund's Board considers these and many other factors, including the quality and integrity of DWS's personnel and such other issues as back-office operations, fund valuations, and compliance policies and procedures.

**Nature, Quality and Extent of Services.** The Board considered the terms of the Agreement, including the scope of advisory services provided under the Agreement. The Board noted that, under the Agreement, DWS provides portfolio management services to the Fund and that, pursuant to a separate administrative services agreement, DWS provides administrative services to the Fund. The Board considered the experience and skills of senior management and investment personnel, the resources made available to such personnel, the ability of DWS to attract and retain high-quality personnel, and the organizational depth and stability of DWS. The Board reviewed the Fund's performance over short-term and long-term periods and compared those returns to various agreed-upon performance measures, including market indices and a peer universe compiled by the independent fee consultant using information supplied by Lipper Inc. ("Lipper"). The Board also noted that it has put into place a process of identifying "Focus Funds" (e.g., funds performing poorly relative to their benchmark or a peer universe compiled by Lipper), and receives more frequent reporting and information from DWS regarding such funds, along with DWS's remedial plans to address underperformance. The Board believes this process is an effective manner of identifying and addressing underperforming funds. Based on the information provided, the Board noted that for the one, three- and five-year periods ended December 31, 2009, the Fund's performance (Class A shares) was in the 2nd quartile, 4th quartile and 4th quartile, respectively, of the applicable Lipper universe (the 1st quartile being the best performers and the 4th quartile being the worst performers). The Board also observed that the Fund has underperformed its benchmark in the one-, three- and five-year periods ended December 31, 2009.

On the basis of this evaluation and the ongoing review of investment results by the Board, the Board concluded that the nature, quality and extent of services provided by DWS historically have been and continue to be satisfactory.

**Fees and Expenses.** The Board considered the Fund's investment management fee schedule, operating expenses, and total expense ratios, and comparative information provided by Lipper and the independent fee consultant regarding investment management fee rates paid to other investment advisors by similar funds (1st quartile being the most favorable and 4th quartile being the least favorable). With respect to management fees paid to other investment advisors by similar funds, the Board noted that the contractual fee rates paid by the Fund, which include the 0.10% fee paid to DWS under the Fund's administrative services agreement, were higher than the median (3rd quartile) of the applicable Lipper peer group (based on Lipper data provided as of December 31, 2009). The Board noted that the Fund's Class A shares total (net) operating expenses were expected to be higher than the median (3rd quartile) of the applicable Lipper expense universe (based on Lipper data provided as of December 31, 2009, and analyzing Lipper expense universe Class A expenses less any applicable 12b-1 fees) ("Lipper Universe Expenses"). The Board also reviewed data comparing each share class's total (net) operating expenses to the applicable Lipper Universe Expenses. The Board considered the Fund's management fee rate as compared to fees charged by DWS and certain of its affiliates for comparable mutual funds and considered differences in fund and fee structures between the DWS Funds. The Board also considered how the Fund's total (net) operating expenses compared to the total (net) operating expenses of a more customized peer group selected by Lipper (based on such factors as asset size).

The information considered by the Board as part of its review of management fees included information regarding fees charged by DWS and its affiliates to similar institutional accounts and to similar funds offered primarily to European investors ("DWS Europe funds"), in each case as applicable. The Board observed that advisory fee rates for institutional accounts generally were lower than the management fees charged by similarly managed DWS US mutual funds ("DWS Funds"), but also took note of the differences in services provided to DWS Funds as compared to institutional accounts. In the case of DWS Europe funds, the Board observed that fee rates for DWS Europe funds generally were higher than for similarly managed DWS Funds, but noted that differences in the types of services provided to DWS Funds relative to DWS Europe funds made it difficult to compare such fees.

On the basis of the information provided, the Board concluded that management fees were reasonable and appropriate in light of the nature, quality and extent of services provided by DWS.

**Profitability.** The Board reviewed detailed information regarding revenues received by DWS under the Agreement. The Board considered the estimated costs and pre-tax profits realized by DWS from advising the DWS Funds, as well as estimates of the pre-tax profits attributable to managing the Fund in particular. The Board also received information regarding the estimated enterprise-wide profitability of DWS and its affiliates with respect to all fund services in totality and by fund. The Board reviewed DWS's methodology in allocating its costs to the management of the Fund. Based on the information provided, the Board concluded that the pre-tax profits realized by DWS in connection with the management of the Fund were not unreasonable. The Board also reviewed information regarding the profitability of certain similar investment management firms. The Board noted that while information regarding the profitability of such firms is limited (and in some cases is not necessarily prepared on a comparable basis), DWS and its affiliates' overall profitability with respect to the DWS fund complex (after taking into account distribution and other services provided to the funds by DWS and its affiliates) was lower than the overall profitability levels of many comparable firms for which such data was available.

**Economies of Scale.** The Board considered whether there are economies of scale with respect to the management of the Fund and whether the Fund benefits from any economies of scale. The Board noted that the Fund's management fee schedule includes fee breakpoints. The Board concluded that the Fund's fee schedule represents an appropriate sharing between the Fund and DWS of such economies of scale as may exist in the management of the Fund at current asset levels.

**Other Benefits to DWS and Its Affiliates.** The Board also considered the character and amount of other incidental benefits received by DWS and its affiliates, including any fees received by DWS for administrative services provided to the Fund and any fees received by an affiliate of DWS for distribution services. The Board also considered benefits to DWS related to brokerage and soft-dollar allocations, including allocating brokerage to pay for research generated by parties other than the executing broker dealers, which pertain primarily to funds investing in equity securities, along with the incidental public relations benefits to DWS related to DWS Funds advertising and cross-selling opportunities among DWS products and services. The Board concluded that management fees were reasonable in light of these fallout benefits.

**Compliance.** The Board considered the significant attention and resources dedicated by DWS to documenting and enhancing its compliance processes in recent years. The Board noted in particular (i) the experience and seniority of both DWS's chief compliance officer and the Fund's chief compliance officer; (ii) the large number of

DWS compliance personnel; and (iii) the substantial commitment of resources by DWS and its affiliates to compliance matters.

Based on all of the information considered and the conclusions reached, the Board unanimously (including the Independent Trustees) determined that the continuation of the Agreement is in the best interests of the Fund. In making this determination, the Board did not give particular weight to any single factor identified above. The Board considered these factors over the course of numerous meetings, certain of which were in executive session with only the Independent Trustees and their counsel present. It is possible that individual Trustees may have weighed these factors differently in reaching their individual decisions to approve the continuation of the Agreement.

# Summary of Management Fee Evaluation by Independent Fee Consultant

October 3, 2010

Pursuant to an Order entered into by Deutsche Investment Management Americas and affiliates (collectively, "DeAM") with the Attorney General of New York, I, Thomas H. Mack, have been appointed the Independent Fee Consultant for the DWS Funds (formerly the DWS Scudder Funds). My duties include preparing an annual written evaluation of the management fees DeAM charges the Funds, considering among other factors the management fees charged by other mutual fund companies for like services, management fees DeAM charges other clients for like services, DeAM's costs of supplying services under the management agreements and related profit margins, possible economies of scale if a Fund grows larger, and the nature and quality of DeAM's services, including fund performance. This report summarizes my evaluation for 2010, including my qualifications, the evaluation process for each of the DWS Funds, consideration of certain complex-level factors, and my conclusions. I served in substantially the same capacity in 2007, 2008, and 2009.

## Qualifications

For more than 35 years I have served in various professional capacities within the investment management business. I have held investment analysis and advisory positions, including securities analyst, portfolio strategist and director of investment policy with a large investment firm. I have also performed business management functions, including business development, financial management and marketing research and analysis.

Since 1991, I have been an independent consultant within the asset management industry. I have provided services to over 125 client organizations, including investment managers, mutual fund boards, product distributors and related organizations. Over the past ten years I have completed a number of assignments for mutual fund boards, specifically including assisting boards with management contract renewal.

I hold a Master of Business Administration degree, with highest honors, from Harvard University and Master of Science and Bachelor of Science (highest honors) degrees from the University of California at Berkeley. I am an independent director and audit committee financial expert for two closed-end mutual funds and have served in various leadership and financial oversight capacities with non-profit organizations.

## Evaluation of Fees for each DWS Fund

My work focused primarily on evaluating, fund-by-fund, the fees charged to each of the 118 publicly offered Fund portfolios in the DWS Fund family. For each Fund, I considered each of the key factors mentioned above, as well as any other relevant information. In doing so I worked closely with the Funds' Independent Directors in their annual contract renewal process, as well as in their approval of contracts for several new funds (documented separately).

In evaluating each Fund's fees, I reviewed comprehensive materials provided by or on behalf of DeAM, including expense information prepared by Lipper Analytical, comparative performance information, profitability data, manager histories, and other materials. I also accessed certain additional information from the Lipper and Morningstar databases and drew on my industry knowledge and experience.

To facilitate evaluating this considerable body of information, I prepared for each Fund a document summarizing the key data elements in each area as well as additional analytics discussed below. This made it possible to consider each key data element in the context of the others.

In the course of contract renewal, DeAM agreed to implement a number of fee and expense adjustments requested by the Independent Directors which will favorably impact future fees and expenses, and my evaluation includes the effects of these changes.

### Fees and Expenses Compared with Other Funds

The competitive fee and expense evaluation for each fund focused on two primary comparisons:

- The Fund's contractual management fee (the advisory fee plus the administration fee where applicable) compared with those of a group of typically 12–15 funds in the same Lipper investment category (e.g. Large Capitalization Growth) having similar distribution arrangements and being of similar size.
- The Fund's total expenses compared with a broader universe of funds from the same Lipper investment category and having similar distribution arrangements.

These two comparisons provide a view of not only the level of the fee compared with funds of similar scale but also the total expense the Fund bears for all the services it receives, in comparison with the investment choices available in the Fund's investment category and distribution channel. The principal figure-of-merit used in these comparisons was the subject Fund's percentile ranking against peers.

### DeAM's Fees for Similar Services to Others

DeAM provided management fee schedules for all of its US domiciled fund and non-fund investment management accounts in any of the investment categories where there is a DWS Fund. These similar products included the other DWS Funds, non-fund pooled accounts, institutional accounts and sub-advisory accounts. Using this information, I calculated for each Fund the fee that would be charged to each similar product, at the subject Fund's asset level.

Evaluating information regarding non-fund products is difficult because there are varying levels of services required for different types of accounts, with mutual funds generally requiring considerably more regulatory and administrative types of service as well as having more frequent cash flows than other types of accounts. Also, while mutual fund fees for similar fund products can be expected to be similar, there will be some differences due to different pricing conditions in different distribution channels (e.g. retail funds versus those used in variable insurance products), differences in underlying investment processes and other factors.

**Costs and Profit Margins**

DeAM provided a detailed profitability analysis for each Fund. After making some adjustments so that the presentation would be more comparable to the available industry figures, I reviewed profit margins from investment management alone, from investment management plus other fund services (excluding distribution) provided to the Funds by DeAM (principally shareholder services), and DeAM profits from all sources, including distribution. A later section comments on overall profitability.

**Economies of Scale**

Economies of scale — an expected decline in management cost per dollar of fund assets as fund assets grow — are very rarely quantified and documented because of inherent difficulties in collecting and analyzing relevant data. However, in virtually every investment category that I reviewed, larger funds tend to have lower fees and lower total expenses than smaller funds. To see how each DWS Fund compares with this industry observation, I reviewed:

- The trend in Fund assets over the last five years and the accompanying trend in total expenses. This shows if the Fund has grown and, if so, whether total expense (management fees as well as other expenses) have declined as a percent of assets.
- Whether the Fund has break-points in its management fee schedule, the extent of the fee reduction built into the schedule and the asset levels where the breaks take effect, and in the case of a sub-advised Fund how the Fund's break-points compare with those of the sub-advisory fee schedule.
- How the Fund's contractual fee schedule compares with trends in the industry data. To accomplish this, I constructed a chart showing how actual latest-fiscal-year contractual fees of the Fund and of other similar funds relate to average fund assets, with the subject Fund's contractual fee schedule superimposed.

**Quality of Service — Performance**

The quality-of-service evaluation focused on investment performance, which is the principal result of the investment management service. Each Fund's performance was reviewed over the past 1, 3, 5 and 10 years, as applicable, and compared with that of other funds in the same investment category and with a suitable market index.

In addition, I calculated and reviewed risk-adjusted returns relative to an index of similar mutual funds' returns and a suitable market index. The risk-adjusted returns analysis provides a way of determining the extent to which the Fund's return comparisons are mainly the product of investment value-added (or lack thereof) or alternatively taking considerably more or less risk than is typical in its investment category.

I also received and considered the history of portfolio manager changes for each Fund, as this provided an important context for evaluating the performance results.

## Complex-Level Considerations

While this evaluation was conducted mainly at the individual fund level, there are some issues relating to the reasonableness of fees that can alternatively be considered across the whole fund complex:

- I reviewed DeAM's profitability analysis for all DWS Funds, with a view toward determining if the allocation procedures used were reasonable and how profit levels compared with public data for other investment managers.
- I considered whether DeAM and affiliates receive any significant ancillary or "fall-out" benefits that should be considered in interpreting the direct profitability results. These would be situations where serving as the investment manager of the Funds is beneficial to another part of the Deutsche Bank organization.
- I considered how aggregated DWS Fund expenses had varied over the years, by asset class and in the context of trends in asset levels.
- I reviewed the structure of the DeAM organization, trends in staffing levels, and information on compensation of investment management and other professionals compared with industry data.

## Findings

Based on the process and analysis discussed above, which included reviewing a wide range of information from management and external data sources and considering among other factors the fees DeAM charges other clients, the fees charged by other fund managers, DeAM's costs and profits associated with managing the Funds, economies of scale, possible fall-out benefits, and the nature and quality of services provided, in my opinion the management fees charged the DWS Funds are reasonable.

Thomas H. Mack

Thomas H. Mack

# Board Members and Officers

The following table presents certain information regarding the Board Members and Officers of the Trust as of December 31, 2010. Each Board Member's year of birth is set forth in parentheses after his or her name. Unless otherwise noted, (i) each Board Member has engaged in the principal occupation(s) noted in the table for at least the most recent five years, although not necessarily in the same capacity; and (ii) the address of each Independent Board Member is c/o Paul K. Freeman, Independent Chairman, DWS Funds, PO Box 101833, Denver, CO 80250-1833. Except as otherwise noted below, the term of office for each Board Member is until the election and qualification of a successor, or until such Board Member sooner dies, resigns, is removed or as otherwise provided in the governing documents of the fund. Because the fund does not hold an annual meeting of shareholders, each Board Member will hold office for an indeterminate period. The Board Members may also serve in similar capacities with other funds in the fund complex. The Length of Time Served represents the year in which the Board Member joined the board of one or more DWS funds now overseen by the Board.

### Independent Board Members

| Name, Year of Birth, Position with the Fund and Length of Time Served[1] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Paul K. Freeman (1950)<br>Chairperson since 2009<br>Board Member since 1993 | Consultant, World Bank/Inter-American Development Bank; Executive and Governing Council of the Independent Directors Council (education committees); formerly, Project Leader, International Institute for Applied Systems Analysis (1998–2001); Chief Executive Officer, The Eric Group, Inc. (environmental insurance) (1986–1998) | 122 |
| John W. Ballantine (1946)<br>Board Member since 1999 | Retired; formerly, Executive Vice President and Chief Risk Management Officer, First Chicago NBD Corporation/The First National Bank of Chicago (1996–1998); Executive Vice President and Head of International Banking (1995–1996). Directorships: Healthways, Inc. (provider of disease and care management services); Portland General Electric (utility company); Stockwell Capital Investments PLC (private equity). Former Directorships: First Oak Brook Bancshares, Inc. and Oak Brook Bank; Prisma Energy International | 122 |
| Henry P. Becton, Jr. (1943)<br>Board Member since 1990 | Vice Chair and former President, WGBH Educational Foundation. Directorships: Association of Public Television Stations; Lead Director, Becton Dickinson and Company[3] (medical technology company); Lead Director, Belo Corporation[3] (media company); Public Radio International; Public Radio Exchange (PRX); The PBS Foundation. Former Directorships: Boston Museum of Science; American Public Television; Concord Academy; New England Aquarium; Mass. Corporation for Educational Telecommunications; Committee for Economic Development; Public Broadcasting Service | 122 |
| Dawn-Marie Driscoll (1946)<br>Board Member since 1987 | President, Driscoll Associates (consulting firm); Executive Fellow, Center for Business Ethics, Bentley University; formerly, Partner, Palmer & Dodge (1988–1990); Vice President of Corporate Affairs and General Counsel, Filene's (1978–1988). Directorships: Trustee of 22 open-end mutual funds managed by Sun Capital Advisers, Inc. (since 2007); Director of ICI Mutual Insurance Company (since 2007); Advisory Board, Center for Business Ethics, Bentley University; Trustee, Southwest Florida Community Foundation (charitable organization). Former Directorships: Investment Company Institute (audit, executive, nominating committees) and Independent Directors Council (governance, executive committees) | 122 |
| Keith R. Fox (1954)<br>Board Member since 1996 | Managing General Partner, Exeter Capital Partners (a series of private investment funds). Directorships: Progressive International Corporation (kitchen goods importer and distributor); BoxTop Media Inc. (advertising); The Kennel Shop (retailer); former Chairman, National Association of Small Business Investment Companies | 122 |
| Kenneth C. Froewiss (1945)<br>Board Member since 2001 | Adjunct Professor of Finance, NYU Stern School of Business (September 2009–present; Clinical Professor from 1997–September 2009); Member, Finance Committee, Association for Asian Studies (2002–present); Director, Mitsui Sumitomo Insurance Group (US) (2004–present); prior thereto, Managing Director, J.P. Morgan (investment banking firm) (until 1996) | 122 |
| Richard J. Herring (1946)<br>Board Member since 1990 | Jacob Safra Professor of International Banking and Professor, Finance Department, The Wharton School, University of Pennsylvania (since July 1972); Co-Director, Wharton Financial Institutions Center (since July 2000); Co-Chair, U.S. Shadow Financial Regulatory Committee; Executive Director, Financial Economists Roundtable; Director, Japan Equity Fund, Inc. (since September 2007), Thai Capital Fund, Inc. (since September 2007), Singapore Fund, Inc. (since September 2007); Independent Director of Barclays Bank Delaware (since September 2010). Formerly, Vice Dean and Director, Wharton Undergraduate Division (July 1995–June 2000); Director, Lauder Institute of International Management Studies (July 2000–June 2006) | 122 |
| William McClayton (1944)<br>Board Member since 2004+ | Private equity investor (since October 2009); previously, Managing Director, Diamond Management & Technology Consultants, Inc. (global consulting firm) (2001–2009); Directorship: Board of Managers, YMCA of Metropolitan Chicago; formerly: Senior Partner, Arthur Andersen LLP (accounting) (1966–2001); Trustee, Ravinia Festival | 122 |

| Name, Year of Birth, Position with the Fund and Length of Time Served[1] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Rebecca W. Rimel (1951)<br>Board Member since 1995 | President and Chief Executive Officer, The Pew Charitable Trusts (charitable organization) (1994 to present); Trustee, Thomas Jefferson Foundation (charitable organization) (1994 to present); Trustee, Executive Committee, Philadelphia Chamber of Commerce (2001–2007); Director, CardioNet, Inc.[2] (2009–present) (health care). Formerly, Executive Vice President, The Glenmede Trust Company (investment trust and wealth management) (1983–2004); Board Member, Investor Education (charitable organization) (2004–2005); Director, Viasys Health Care[2] (January 2007–June 2007); Trustee, Pro Publica (charitable organization) (2007–2010) | 122 |
| William N. Searcy, Jr. (1946)<br>Board Member since 1993 | Private investor since October 2003; Trustee of 22 open-end mutual funds managed by Sun Capital Advisers, Inc. (since October 1998). Formerly, Pension & Savings Trust Officer, Sprint Corporation[2] (telecommunications) (November 1989–September 2003) | 122 |
| Jean Gleason Stromberg (1943)<br>Board Member since 1997 | Retired. Formerly, Consultant (1997–2001); Director, Financial Markets US Government Accountability Office (1996–1997); Partner, Fulbright & Jaworski, L.L.P. (law firm) (1978–1996). Directorships: The William and Flora Hewlett Foundation. Former Directorships: Service Source, Inc., Mutual Fund Directors Forum (2002–2004), American Bar Retirement Association (funding vehicle for retirement plans) (1987–1990 and 1994–1996) | 122 |
| Robert H. Wadsworth (1940)<br>Board Member since 1999 | President, Robert H. Wadsworth & Associates, Inc. (consulting firm) (1983 to present); Director, The Phoenix Boys Choir Association | 125 |

## Interested Board Member and Officer[4]

| Name, Year of Birth, Position with the Trust/ Corporation and Length of Time Served[1,5] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Ingo Gefeke[7] (1967)<br>Board Member since 2010<br>Executive Vice President since 2010 | Managing Director[3], Deutsche Asset Management; Global Head of Distribution and Product Management, DWS Global Head of Trading and Securities Lending. Member of the Board of Directors of DWS Investment GmbH Frankfurt (since July 2009) and DWS Holding & Service GmbH Frankfurt (since January 2010); formerly, Global Chief Administrative Officer, Deutsche Asset Management (2004–2009); Global Chief Operating Officer, Global Transaction Banking, Deutsche Bank AG, New York (2001–2004); Chief Operating Officer, Global Banking Division Americas, Deutsche Bank AG, New York (1999–2001); Central Management, Global Banking Services, Deutsche Bank AG, Frankfurt (1998–1999); Relationship Management, Deutsche Bank AG, Tokyo, Japan (1997–1998) | 55 |

## Officers[4]

| Name, Year of Birth, Position with the Fund and Length of Time Served[5] | Principal Occupation(s) During Past 5 Years and Other Directorships Held |
|---|---|
| Michael G. Clark[6] (1965)<br>President, 2006–present | Managing Director[3], Deutsche Asset Management (2006–present); President of DWS family of funds; Director, ICI Mutual Insurance Company (since October 2007); formerly, Director of Fund Board Relations (2004–2006) and Director of Product Development (2000–2004), Merrill Lynch Investment Managers; Senior Vice President Operations, Merrill Lynch Asset Management (1999–2000) |
| John Millette[8] (1962)<br>Vice President and Secretary, 1999–present | Director[3], Deutsche Asset Management |
| Paul H. Schubert[6] (1963)<br>Chief Financial Officer, 2004–present<br>Treasurer, 2005–present | Managing Director[3], Deutsche Asset Management (since July 2004); formerly, Executive Director, Head of Mutual Fund Services and Treasurer for UBS Family of Funds (1998–2004); Vice President and Director of Mutual Fund Finance at UBS Global Asset Management (1994–1998) |
| Caroline Pearson[8] (1962)<br>Chief Legal Officer, April 2010–present | Managing Director[3], Deutsche Asset Management; formerly, Assistant Secretary for DWS family of funds (1997–2010) |
| Rita Rubin[9] (1970)<br>Assistant Secretary, 2009–present | Vice President and Counsel, Deutsche Asset Management (since October 2007); formerly, Vice President, Morgan Stanley Investment Management (2004–2007) |
| Paul Antosca[8] (1957)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management (since 2006); Vice President, The Manufacturers Life Insurance Company (U.S.A.) (1990–2006) |
| Jack Clark[8] (1967)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management (since 2007); formerly, Vice President, State Street Corporation (2002–2007) |

| Name, Year of Birth, Position with the Fund and Length of Time Served[5] | Principal Occupation(s) During Past 5 Years and Other Directorships Held |
|---|---|
| Diane Kenneally[8] (1966)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management |
| John Caruso[9] (1965)<br>Anti-Money Laundering Compliance Officer, 2010–present | Managing Director[3], Deutsche Asset Management |
| Robert Kloby[9] (1962)<br>Chief Compliance Officer, 2006–present | Managing Director[3], Deutsche Asset Management |

1 *The length of time served represents the year in which the Board Member joined the board of one or more DWS funds currently overseen by the Board.*

2 *A publicly held company with securities registered pursuant to Section 12 of the Securities Exchange Act of 1934.*

3 *Executive title, not a board directorship.*

4 *As a result of their respective positions held with the Advisor, these individuals are considered "interested persons" of the Advisor within the meaning of the 1940 Act. Interested persons receive no compensation from the fund.*

5 *The length of time served represents the year in which the officer was first elected in such capacity for one or more DWS funds.*

6 *Address: 100 Plaza One, Jersey City, NJ 07311.*

7 *Effective January 11, 2011, Mr. Gefeke, an interested Board Member and Executive Vice President, resigned from the fund's Board and as an officer.*

*The mailing address of Mr. Gefeke is 345 Park Avenue, New York, New York 10154. Mr. Gefeke was an interested Board Member of certain DWS funds by virtue of his positions with Deutsche Asset Management. As an interested person, Mr. Gefeke received no compensation from the fund.*

8 *Address: One Beacon Street, Boston, MA 02108.*

9 *Address: 60 Wall Street, New York, New York 10005.*

*The fund's Statement of Additional Information ("SAI") includes additional information about the Board Members. The SAI is available, without charge, upon request. If you would like to request a copy of the SAI, you may do so by calling the following toll-free number: (800) 728-3337.*

# Notes

DWS Investments is part of Deutsche Bank's Asset Management division and, within the US, represents the retail asset management activities of Deutsche Bank AG, Deutsche Bank Trust Company Americas, Deutsche Investment Management Americas Inc. and DWS Trust Company.

The views expressed in this report reflect those of the portfolio managers only through the end of the period of the report as stated on the cover. The managers' views are subject to change at any time based on market and other conditions and should not be construed as a recommendation.

This information must be preceded or accompanied by a current prospectus.

Portfolio changes should not be considered recommendations for action by individual investors.

DWS Investments Distributors, Inc.
222 South Riverside Plaza
Chicago, IL 60606
(800) 621-1148

VS2SV-2 (2/11)

DWS INVESTMENTS
Deutsche Bank Group

DECEMBER 31, 2010

# ANNUAL REPORT

## DWS VARIABLE SERIES II

## DWS Technology VIP

**This report must be preceded or accompanied by a prospectus. To obtain an additional prospectus or summary prospectus, if available, call (800) 728-3337 or your financial representative. We advise you to consider the Fund's objectives, risks, charges and expenses carefully before investing. The summary prospectus and prospectus contain this and other important information about the Fund. Please read the prospectus carefully before you invest.**

*Investments in variable insurance portfolios (VIPs) involve risk. Stocks may decline in value. Bond investments are subject to interest-rate and credit risks. When interest rates rise, bond prices generally fall. Credit risk refers to the ability of an issuer to make timely payments of principal and interest. Investing in derivatives entails special risks relating to liquidity, leverage and credit that may reduce returns and/or increased volatility. Investing in foreign securities, particularly those of emerging markets, presents certain risks, such as currency fluctuations, political and economic changes, and market risks. There are additional risks associated with investing in commodities, high-yield bonds, aggressive growth stocks, non-diversified/ concentrated funds and small- and mid-cap stocks which are more fully explained in the prospectuses. Please read the prospectus for more information.*



DWS INVESTMENTS
Deutsche Bank Group

## DWS Technology VIP

**All performance shown is historical, assumes reinvestment of all dividend and capital gain distributions and does not guarantee future results. Investment return and principal value fluctuate with changing market conditions so that, when redeemed, shares may be worth more or less than their original cost. Current performance may be lower or higher than the performance data quoted. Please contact your participating insurance company for the Fund's most recent month-end performance. Performance doesn't reflect charges and fees ("contract charges") associated with the separate account that invests in the Fund or any variable life insurance policy or variable annuity contract for which the Fund is an investment option. These charges and fees will reduce returns. While all share classes have the same underlying portfolio, their performance will differ.**

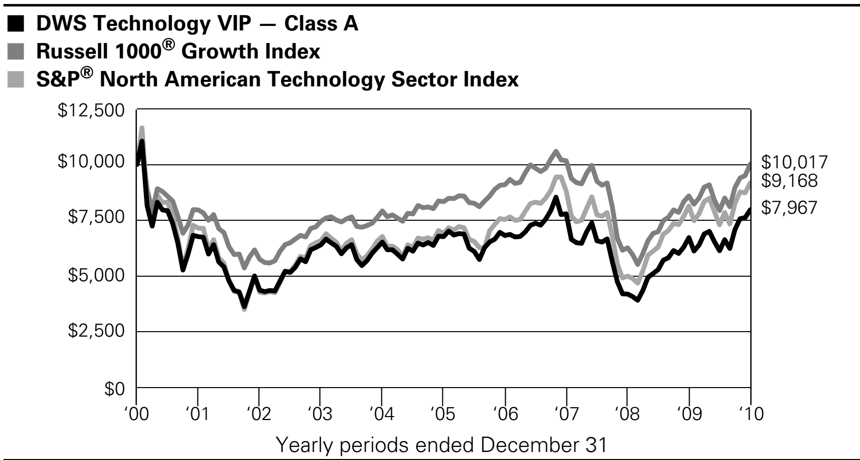
**The gross expense ratios of the Fund, as stated in the fee table of the prospectus dated May 1, 2010 are 0.84% and 1.18% for Class A and Class B shares, respectively, and may differ from the expense ratios disclosed in the Financial Highlights tables in this report.**

### Risk Considerations

Any Fund that concentrates in a particular segment of the market will generally be more volatile than a fund that invests more broadly. This Fund is non-diversified and can take larger positions in fewer issues, increasing its potential risk. Stocks may decline in value. See the prospectus for details.

Fund returns shown during the 3-year, 5-year and 10-year periods reflect a fee waiver and/or expense reimbursement for Class A shares. Without this waiver/reimbursement, returns would have been lower.

### Growth of an Assumed $10,000 Investment in DWS Technology VIP




*The Russell 1000® Growth Index is an unmanaged index that consists of those stocks in the Russell 1000 Index with higher price-to-book ratios and higher forecasted growth values.*

*The S&P North American Technology Sector Index is the technology subindex of the S&P North American Sector Indices. The S&P North American Technology Sector Index family is designed as equity benchmarks for US-traded technology-related securities.*

*Index returns assume reinvestment of dividends and, unlike fund returns, do not reflect any fees or expenses. It is not possible to invest directly into an index.*

### Comparative Results

| DWS Technology VIP | | 1-Year | 3-Year | 5-Year | 10-Year |
|---|---|---|---|---|---|
| **Class A** | Growth of $10,000 | $11,866 | $10,237 | $11,789 | $7,967 |
| | Average annual total return | 18.66% | 0.79% | 3.35% | –2.25% |
| Russell 1000 Growth Index | Growth of $10,000 | $11,671 | $9,858 | $12,023 | $10,017 |
| | Average annual total return | 16.71% | –0.47% | 3.75% | 0.02% |
| S&P North American Technology Sector Index | Growth of $10,000 | $11,265 | $10,417 | $13,276 | $9,168 |
| | Average annual total return | 12.65% | 1.37% | 5.83% | –0.86% |

| DWS Technology VIP | | 1-Year | 3-Year | 5-Year | Life of Class* |
|---|---|---|---|---|---|
| **Class B** | Growth of $10,000 | $11,769 | $10,104 | $11,553 | $16,857 |
| | Average annual total return | 17.96% | 0.35% | 2.93% | 6.34% |
| Russell 1000 Growth Index | Growth of $10,000 | $11,671 | $9,858 | $12,023 | $15,890 |
| | Average annual total return | 16.71% | –0.47% | 3.75% | 5.60% |
| S&P North American Technology Sector Index | Growth of $10,000 | $11,265 | $10,417 | $13,276 | $19,158 |
| | Average annual total return | 12.65% | 1.37% | 5.83% | 7.94% |

*The growth of $10,000 is cumulative.*

* *The Fund commenced offering Class B shares on July 1, 2002. Index returns began on June 30, 2002.*

# Information About Your Fund's Expenses

## DWS Technology VIP

As an investor of the Fund, you incur two types of costs: ongoing expenses and transaction costs. Ongoing expenses include management fees, distribution and service (12b-1) fees and other Fund expenses. Examples of transaction costs include contract charges, redemption fees and account maintenance fees, which are not shown in this section. The following tables are intended to help you understand your ongoing expenses (in dollars) of investing in the Fund and to help you compare these expenses with the ongoing expenses of investing in other mutual funds. The example in the table is based on an investment of $1,000 invested at the beginning of the six-month period and held for the entire period (July 1, 2010 to December 31, 2010).

The tables illustrate your Fund's expenses in two ways:

- **Actual Fund Return.** This helps you estimate the actual dollar amount of ongoing expenses (but not transaction costs) paid on a $1,000 investment in the Fund using the Fund's actual return during the period. To estimate the expenses you paid over the period, simply divide your account value by $1,000 (for example, an $8,600 account value divided by $1,000 = 8.6), then multiply the result by the number in the "Expenses Paid per $1,000" line under the share class you hold.
- **Hypothetical 5% Fund Return.** This helps you to compare your Fund's ongoing expenses (but not transaction costs) with those of other mutual funds using the Fund's actual expense ratio and a hypothetical rate of return of 5% per year before expenses. Examples using a 5% hypothetical Fund return may be found in the shareholder reports of other mutual funds. The hypothetical account values and expenses may not be used to estimate the actual ending account balance or expenses you paid for the period.

Please note that the expenses shown in these tables are meant to highlight your ongoing expenses only and do not reflect any transaction costs. The "Expenses Paid per $1,000" line of the tables is useful in comparing ongoing expenses only and will not help you determine the relative total expense of owning different funds. If these transaction costs had been included, your costs would have been higher.

**Expenses and Value of a $1,000 Investment** for the six months ended December 31, 2010

| **Actual Fund Return** | **Class A** | **Class B** |
|---|---|---|
| Beginning Account Value 7/1/10 | $1,000.00 | $1,000.00 |
| Ending Account Value 12/31/10 | $1,300.10 | $1,297.60 |
| Expenses Paid per $1,000* | $ 5.45 | $ 7.76 |

| **Hypothetical 5% Fund Return** | **Class A** | **Class B** |
|---|---|---|
| Beginning Account Value 7/1/10 | $1,000.00 | $1,000.00 |
| Ending Account Value 12/31/10 | $1,020.47 | $1,018.45 |
| Expenses Paid per $1,000* | $ 4.79 | $ 6.82 |

* *Expenses are equal to the Fund's annualized expense ratio for each share class, multiplied by the average account value over the period, multiplied by the number of days in the most recent six-month period, then divided by 365.*

| **Annualized Expense Ratios** | **Class A** | **Class B** |
|---|---|---|
| DWS Variable Series II — DWS Technology VIP | .94% | 1.34% |

For more information, please refer to the Fund's prospectus.

These tables do not reflect charges and fees ("contract charges") associated with the separate account that invests in the Fund or any variable life insurance policy or variable annuity contract for which the Fund is an investment option.

## DWS Technology VIP

Technology stocks produced double-digit returns during 2010 — as measured by the 12.65% gain of the Fund's benchmark, the S&P® North American Technology Sector Index — but underperformed the 15.06% return of the Standard & Poor's 500® (S&P 500) Index. The Class A shares of the Fund returned 18.66% (unadjusted for contract charges), outperforming the benchmark by a wide margin.

The Fund's strong performance was largely attributable to the effectiveness of our individual stock selection. Of the many stocks that stood out as winners, the largest contributor was Isilon Systems, Inc.,* a vendor of data storage systems suitable for very large files. The stock performed well due to the effectiveness of the company's new sales strategy, rising demand for its storage products and takeover speculation. Also among the Fund's top contributors were LogMeIn, Inc.,* Apple Inc., Ariba, Inc. and F5 Networks, Inc.

On the negative side, our performance was hurt by an overweight position in Hewlett-Packard Co.[1] The stock lagged the broader sector by a wide margin due to the forced departure of esteemed CEO Mark Hurd and the Board's unexpected choice of former SAP CEO Leo Apotheker as his replacement. Other detractors of note included Comverse Technology, Inc. and Google, Inc.

We believe the tech sector continues to present a mix of defensive and offensive characteristics, making it attractive at a time of an uncertain economic outlook. The tech sector also provides investors with the opportunity to take part in a number of compelling longer-term themes. For instance, we favor companies participating in technological trends with significant potential impact on the overall economy, such as cloud computing, mobile data, business analytics and online advertising. Many companies related to these themes are likely to become potential targets for further merger and acquisition (M&A) activity, creating opportunities for bottom-up investors.

Frederic L. Fayolle, CFA
*Lead Portfolio Manager*

Clark Chang
Walter Holick
*Portfolio Managers*

*The S&P North American Technology Sector Index is an unmanaged, capitalization-weighted index based on a universe of technology-related stocks.*

*The Standard & Poor's 500 (S&P 500) Index is an unmanaged, capitalization-weighted index of 500 stocks. The index is designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries.*

*Index returns assume reinvestment of dividends and, unlike fund returns, do not reflect any fees or expenses. It is not possible to invest directly into an index.*

1 *"Overweight" means the Fund holds a higher weighting in a given sector or security than the benchmark. "Underweight" means the Fund holds a lower weighting.*

* *Not held in the portfolio as of December 31, 2010.*

*Portfolio management market commentary is as of December 31, 2010, and may not come to pass. This information is subject to change at any time based on market and other conditions. Past performance does not guarantee future results. Current and future portfolio holdings are subject to risk.*

# Portfolio Summary

## DWS Technology VIP

| **Asset Allocation** (As a % of Investment Portfolio excluding Securities Lending Collateral) | **12/31/10** | **12/31/09** |
|---|---|---|
| Common Stocks | 99% | 98% |
| Cash Equivalents | 1% | 2% |
| | 100% | 100% |

| **Sector Diversification** (As a % of Common Stocks) | **12/31/10** | **12/31/09** |
|---|---|---|
| Information Technology: | | |
| Computers & Peripherals | 22% | 25% |
| Software | 18% | 18% |
| Communications Equipment | 17% | 17% |
| Semiconductors & Semiconductor Equipment | 16% | 16% |
| Internet Software & Services | 14% | 14% |
| IT Services | 9% | 7% |
| Electronic Equipment, Instruments & Components | 1% | 2% |
| Consumer Discretionary: | | |
| Hotel Restaurants & Leisure | 0% | — |
| Internet & Catalog Retail | 3% | 1% |
| | 100% | 100% |

*Asset allocation and sector diversification are subject to change.*

*For more complete details about the Fund's investment portfolio, see page 6.*

Following the Fund's fiscal first and third quarter-end, a complete portfolio holdings listing is filed with the SEC on Form N-Q. The form will be available on the SEC's Web site at www.sec.gov, and it also may be reviewed and copied at the SEC's Public Reference Room in Washington, D.C. Information on the operation of the SEC's Public Reference Room may be obtained by calling (800) SEC-0330. The Fund's portfolio holdings are also posted on www.dws-investments.com from time to time. Please see the Fund's current prospectus for more information.

# Investment Portfolio

**December 31, 2010**

## DWS Technology VIP

| | Shares | Value ($) |
|---|---|---|
| **Common Stocks 99.3%** | | |
| **Consumer Discretionary 3.1%** | | |
| **Hotels Restaurants & Leisure 0.3%** | | |
| Ctrip.com International Ltd. (ADR)* | 6,070 | **245,532** |
| **Internet & Catalog Retail 2.8%** | | |
| Amazon.com, Inc.* | 7,210 | 1,297,800 |
| Priceline.com, Inc.* | 1,950 | 779,122 |
| | | **2,076,922** |
| **Information Technology 96.2%** | | |
| **Communications Equipment 17.2%** | | |
| Acme Packet, Inc.* | 7,523 | 399,923 |
| Aviat Networks, Inc.* | 2,463 | 12,487 |
| Cisco Systems, Inc.* | 183,760 | 3,717,465 |
| Comverse Technology, Inc.* | 126,644 | 919,435 |
| F5 Networks, Inc.* | 8,850 | 1,151,916 |
| Juniper Networks, Inc.* (a) | 29,800 | 1,100,216 |
| Motorola, Inc.* | 59,350 | 538,304 |
| Polycom, Inc.* (a) | 23,810 | 928,114 |
| QUALCOMM, Inc. | 77,996 | 3,860,022 |
| Research In Motion Ltd.* | 6,460 | 375,520 |
| | | **13,003,402** |
| **Computers & Peripherals 22.2%** | | |
| Apple, Inc.* | 29,370 | 9,473,587 |
| EMC Corp.* (a) | 93,957 | 2,151,615 |
| Gemalto NV | 7,700 | 327,670 |
| Hewlett-Packard Co. | 90,770 | 3,821,417 |
| QLogic Corp.* | 3,660 | 62,293 |
| SanDisk Corp.* | 17,290 | 862,079 |
| Xyratex Ltd.* | 7,848 | 128,001 |
| | | **16,826,662** |
| **Electronic Equipment, Instruments & Components 1.0%** | | |
| Corning, Inc. | 39,250 | **758,310** |
| **Internet Software & Services 13.6%** | | |
| Akamai Technologies, Inc.* | 6,720 | 316,176 |
| Digital River, Inc.* | 16,620 | 572,060 |
| eBay, Inc.* | 10,450 | 290,824 |
| Equinix, Inc.* | 2,710 | 220,215 |
| Google, Inc. "A"* | 9,450 | 5,613,017 |
| LogMeIn, Inc.* (a) | 24,313 | 1,078,038 |
| Open Text Corp.* (a) | 3,400 | 156,604 |
| QuinStreet, Inc.* (a) | 27,888 | 535,728 |
| Telecity Group PLC* | 40,505 | 297,064 |
| Tencent Holdings Ltd. | 18,080 | 397,756 |
| VistaPrint NV* (a) | 3,030 | 139,380 |
| Yahoo!, Inc.* (a) | 41,070 | 682,994 |
| | | **10,299,856** |
| **IT Services 8.9%** | | |
| Accenture PLC "A" | 9,820 | 476,172 |
| Amdocs Ltd.* | 8,580 | 235,693 |
| Cognizant Technology Solutions Corp. "A"* | 25,390 | 1,860,833 |
| Fiserv, Inc.* | 10,400 | 609,024 |
| FleetCor Technologies, Inc.* | 4,920 | 152,126 |
| International Business Machines Corp. | 12,740 | 1,869,722 |
| iSoftStone Holdings Ltd. (ADR)* | 4,530 | 82,310 |
| MasterCard, Inc. "A" | 960 | 215,146 |
| Teradata Corp.* | 22,861 | 940,959 |
| Visa, Inc. "A" (a) | 4,610 | 324,452 |
| | | **6,766,437** |
| **Semiconductors & Semiconductor Equipment 15.7%** | | |
| Aixtron SE (a) | 10,660 | 393,643 |
| Altera Corp. (a) | 11,660 | 414,863 |
| Applied Materials, Inc. | 24,000 | 337,200 |
| ASML Holding NV (NY Registered Shares) (a) | 14,190 | 544,044 |
| Avago Technologies Ltd. | 17,129 | 487,663 |
| Broadcom Corp. "A" | 20,310 | 884,500 |
| Cavium Networks, Inc.* (a) | 7,010 | 264,137 |
| Cirrus Logic, Inc.* | 21,400 | 341,972 |
| Inphi Corp.* | 1,940 | 38,975 |
| Integrated Device Technology, Inc.* | 74,600 | 496,836 |
| Intel Corp. | 152,879 | 3,215,045 |
| KLA-Tencor Corp. | 12,740 | 492,273 |
| Marvell Technology Group Ltd.* | 17,900 | 332,045 |
| MaxLinear, Inc. "A"* (a) | 22,300 | 239,948 |
| Microchip Technology, Inc. (a) | 8,270 | 282,917 |
| Microsemi Corp.* | 14,290 | 327,241 |
| Netlogic Microsystems, Inc.* | 13,880 | 435,971 |
| Novellus Systems, Inc.* (a) | 16,910 | 546,531 |
| NXP Semiconductors NV* | 10,220 | 213,905 |
| Texas Instruments, Inc. (a) | 49,900 | 1,621,750 |
| | | **11,911,459** |
| **Software 17.6%** | | |
| Activision Blizzard, Inc. | 36,210 | 450,452 |
| Adobe Systems, Inc.* | 20,990 | 646,072 |
| ANSYS, Inc.* | 5,160 | 268,681 |
| Ariba, Inc.* | 55,660 | 1,307,453 |
| BMC Software, Inc.* | 19,040 | 897,546 |
| Check Point Software Technologies Ltd.* | 11,080 | 512,561 |
| Citrix Systems, Inc.* | 4,770 | 326,316 |
| Informatica Corp.* (a) | 20,790 | 915,384 |
| Longtop Financial Technologies Ltd. (ADR)* | 4,900 | 177,282 |
| Microsoft Corp. | 127,410 | 3,557,287 |
| Oracle Corp. | 87,010 | 2,723,413 |
| QLIK Technologies, Inc.* | 7,958 | 205,396 |
| RealD, Inc.* | 976 | 25,298 |
| Rovi Corp.* (a) | 3,150 | 195,332 |
| Salesforce.com, Inc.* (a) | 1,560 | 205,920 |
| Symantec Corp.* | 18,560 | 310,694 |
| Taleo Corp. "A"* | 10,890 | 301,109 |
| VanceInfo Technologies, Inc. (ADR)* | 8,160 | 281,846 |
| | | **13,308,042** |
| **Total Common Stocks** (Cost $42,878,738) | | **75,196,622** |
| **Securities Lending Collateral 12.3%** | | |
| Daily Assets Fund Institutional, 0.27% (b) (c) (Cost $9,321,665) | 9,321,665 | **9,321,665** |

*The accompanying notes are an integral part of the financial statements.*

| | Shares | Value ($) |
|---|---|---|
| **Cash Equivalents 0.9%** | | |
| Central Cash Management Fund, 0.19% (b) (Cost $675,065) | 675,065 | **675,065** |

| | % of Net Assets | Value ($) |
|---|---|---|
| **Total Investment Portfolio** (Cost $52,875,468)† | 112.5 | **85,193,352** |
| **Other Assets and Liabilities, Net** | (12.5) | **(9,493,284)** |
| **Net Assets** | 100.0 | **75,700,068** |

* *Non-income producing security.*

† *The cost for federal income tax purposes was $56,197,483. At December 31, 2010, net unrealized appreciation for all securities based on tax cost was $28,995,869. This consisted of aggregate gross unrealized appreciation for all securities in which there was an excess of value over tax cost of $32,698,880 and aggregate gross unrealized depreciation for all securities in which there was an excess of tax cost over value of $3,703,011.*

(a) *All or a portion of these securities were on loan (see Notes to Financial Statements). The value of all securities loaned at December 31, 2010 amounted to $9,072,813, which is 12.0% of net assets.*

(b) *Affiliated fund managed by Deutsche Investment Management Americas Inc. The rate shown is the annualized seven-day yield at period end.*

(c) *Represents collateral held in connection with securities lending. Income earned by the Fund is net of borrower rebates.*

*ADR: American Depositary Receipt*

## Fair Value Measurements

*Various inputs are used in determining the value of the Fund's investments. These inputs are summarized in three broad levels. Level 1 includes quoted prices in active markets for identical securities. Level 2 includes other significant observable inputs (including quoted prices for similar securities, interest rates, prepayment speeds, and credit risk). Level 3 includes significant unobservable inputs (including the Fund's own assumptions in determining the fair value of investments). The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities.*

*The following is a summary of the inputs used as of December 31, 2010 in valuing the Fund's investments. For information on the Fund's policy regarding the valuation of investments, please refer to the Security Valuation section of Note A in the accompanying Notes to Financial Statements.*

| **Assets** | **Level 1** | **Level 2** | **Level 3** | **Total** |
|---|---|---|---|---|
| Common Stocks (d) | | | | |
| Consumer Discretionary | $ 2,322,454 | $ — | $ — | $ 2,322,454 |
| Information Technology | 71,458,035 | 1,416,133 | — | 72,874,168 |
| Short-Term Investments (d) | 9,996,730 | — | — | 9,996,730 |
| **Total** | **$ 83,777,219** | **$ 1,416,133** | **$ —** | **$ 85,193,352** |

*There have been no significant transfers between Level 1 and Level 2 fair value measurements during the year ended December 31, 2010.*

(d) *See Investment Portfolio for additional detailed categorizations.*

*The accompanying notes are an integral part of the financial statements.*

# Statement of Assets and Liabilities

as of December 31, 2010

| | | |
|---|---|---|
| **Assets** | | |
| Investments: | | |
| Investments in unaffiliated securities, at value (cost $42,878,738) — including $9,072,813 of securities loaned | $ | 75,196,622 |
| Investment in Daily Assets Fund Institutional (cost $9,321,665)* | | 9,321,665 |
| Investment in Central Cash Management Fund (cost $675,065) | | 675,065 |
| Total investments, at value (cost $52,875,468) | | 85,193,352 |
| Cash | | 3,103 |
| Foreign currency, at value (cost $9,181) | | 9,138 |
| Receivable for Fund shares sold | | 128 |
| Interest receivable | | 4,770 |
| Other assets | | 406 |
| Total assets | | 85,210,897 |
| **Liabilities** | | |
| Payable upon return of securities loaned | | 9,321,665 |
| Payable for Fund shares redeemed | | 72,412 |
| Accrued management fee | | 42,305 |
| Other accrued expenses and payables | | 74,447 |
| Total liabilities | | 9,510,829 |
| **Net assets, at value** | **$** | **75,700,068** |
| **Net Assets Consist of** | | |
| Distributions in excess of net investment income | | (79) |
| Net unrealized appreciation (depreciation) on: | | |
| Investments | | 32,317,884 |
| Foreign currency | | (43) |
| Accumulated net realized gain (loss) | | (108,783,810) |
| Paid-in capital | | 152,166,116 |
| **Net assets, at value** | **$** | **75,700,068** |
| **Class A** | | |
| **Net Asset Value,** offering and redemption price per share ($75,572,811 ÷ 6,893,997 outstanding shares of beneficial interest, no par value, unlimited number of shares authorized) | **$** | **10.96** |
| **Class B** | | |
| **Net Asset Value,** offering and redemption price per share ($127,257 ÷ 11,963 outstanding shares of beneficial interest, no par value, unlimited number of shares authorized) | **$** | **10.64** |

* *Represents collateral on securities loaned.*

# Statement of Operations

for the year ended December 31, 2010

| | | |
|---|---|---|
| **Investment Income** | | |
| Income: | | |
| Dividends (net of foreign taxes withheld of $607) | $ | 442,108 |
| Income distributions — Central Cash Management Fund | | 974 |
| Securities lending income, including income from Daily Assets Fund Institutional, net of borrower rebates | | 29,747 |
| Total income | | 472,829 |
| Expenses: | | |
| Management fee | | 484,850 |
| Administration fee | | 72,910 |
| Services to shareholders | | 2,813 |
| Distribution service fee (Class B) | | 2,449 |
| Record keeping fees (Class B) | | 962 |
| Custodian fee | | 10,843 |
| Legal fees | | 9,743 |
| Audit and tax fees | | 52,788 |
| Trustees' fees and expenses | | 5,376 |
| Reports to shareholders | | 24,990 |
| Other | | 17,141 |
| Total expenses | | 684,865 |
| **Net investment income (loss)** | | **(212,036)** |
| **Realized and Unrealized Gain (Loss)** | | |
| Net realized gain (loss) from: | | |
| Investments | | 7,855,733 |
| Foreign currency | | 3,739 |
| Payments by affiliate (see Note F) | | 1,507 |
| | | 7,860,979 |
| Change in net unrealized appreciation (depreciation) on: | | |
| Investments | | 4,413,329 |
| Foreign currency | | (5,229) |
| | | 4,408,100 |
| **Net gain (loss)** | | **12,269,079** |
| **Net increase (decrease) in net assets resulting from operations** | **$** | **12,057,043** |

*The accompanying notes are an integral part of the financial statements.*

# Statement of Changes in Net Assets

| Increase (Decrease) in Net Assets | Years Ended December 31, 2010 | 2009 |
|---|---|---|
| Operations: | | |
| Net investment income (loss) | $ (212,036) | $ 43,997 |
| Net realized gain (loss) | 7,860,979 | (13,132,543) |
| Net unrealized appreciation (depreciation) | 4,408,100 | 45,141,538 |
| Net increase (decrease) in net assets resulting from operations | 12,057,043 | 32,052,992 |
| Distributions to shareholders from: | | |
| Net investment income: | | |
| Class A | (30,198) | — |
| Fund share transactions: | | |
| **Class A** | | |
| Proceeds from shares sold | 4,885,683 | 8,267,890 |
| Reinvestment of distributions | 30,198 | — |
| Payments for shares redeemed | (19,283,343) | (20,829,816) |
| Net increase (decrease) in net assets from Class A share transactions | (14,367,462) | (12,561,926) |
| **Class B** | | |
| Proceeds from shares sold | 154,027 | 696,779 |
| Payments for shares redeemed | (2,934,016) | (561,458) |
| Net increase (decrease) in net assets from Class B share transactions | (2,779,989) | 135,321 |
| **Increase (decrease) in net assets** | (5,120,606) | 19,626,387 |
| Net assets at beginning of period | 80,820,674 | 61,194,287 |
| Net assets at end of period (including distributions in excess of net investment income and undistributed net investment income of $79 and $24,841, respectively) | **$ 75,700,068** | **$ 80,820,674** |

| **Other Information** | | |
|---|---|---|
| **Class A** | | |
| Shares outstanding at beginning of period | 8,447,123 | 10,336,451 |
| Shares sold | 509,793 | 1,071,894 |
| Shares issued to shareholders in reinvestment of distributions | 3,065 | — |
| Shares redeemed | (2,065,984) | (2,961,222) |
| Net increase (decrease) in Class A shares | (1,553,126) | (1,889,328) |
| Shares outstanding at end of period | **6,893,997** | **8,447,123** |
| **Class B** | | |
| Shares outstanding at beginning of period | 309,078 | 290,168 |
| Shares sold | 17,099 | 100,046 |
| Shares redeemed | (314,214) | (81,136) |
| Net increase (decrease) in Class B shares | (297,115) | 18,910 |
| Shares outstanding at end of period | **11,963** | **309,078** |

*The accompanying notes are an integral part of the financial statements.*

# Financial Highlights

## Class A

| Years Ended December 31, | 2010 | 2009 | 2008 | 2007 | 2006 |
|---|---|---|---|---|---|
| **Selected Per Share Data** | | | | | |
| **Net asset value, beginning of period** | **$ 9.24** | **$ 5.76** | **$10.71** | **$ 9.37** | **$ 9.30** |
| *Income (loss) from investment operations:* | | | | | |
| Net investment income (loss)[a] | (.03) | .01 | (.00)* | (.02) | (.01)[c] |
| Net realized and unrealized gain (loss) | 1.75 | 3.47 | (4.95) | 1.36 | .08 |
| **Total from investment operations** | 1.72 | 3.48 | (4.95) | 1.34 | .07 |
| *Less distributions from:* | | | | | |
| Net investment income | (.00)* | — | — | — | — |
| **Net asset value, end of period** | **$10.96** | **$ 9.24** | **$ 5.76** | **$10.71** | **$ 9.37** |
| Total Return (%) | 18.66 | 60.42 | (46.22)[b] | 14.30 | .75[c] |
| **Ratios to Average Net Assets and Supplemental Data** | | | | | |
| Net assets, end of period ($ millions) | 76 | 78 | 60 | 153 | 165 |
| Ratio of expenses before expense reductions (%) | .93 | .84 | 1.01 | .91 | .89 |
| Ratio of expenses after expense reductions (%) | .93 | .84 | 1.00 | .91 | .89 |
| Ratio of net investment income (loss) (%) | (.29) | .08 | (.01) | (.15) | (.12)[c] |
| Portfolio turnover rate (%) | 23 | 45 | 71 | 91 | 49 |

a *Based on average shares outstanding during the period.*

b *Total return would have been lower had certain expenses not been reduced.*

c *Includes non-recurring income from the Advisor recorded as a result of an administrative proceeding regarding disclosure of brokerage allocation practices in connection with sales of DWS Funds. The non-recurring income resulted in an increase in net investment income of $0.017 per share and an increase in the ratio of net investment income of 0.18%. Excluding this non-recurring income, total return would have been 0.19% lower.*

* *Amount is less than $0.005.*

## Class B

| Years Ended December 31, | 2010 | 2009 | 2008 | 2007 | 2006 |
|---|---|---|---|---|---|
| **Selected Per Share Data** | | | | | |
| **Net asset value, beginning of period** | **$ 9.02** | **$ 5.64** | **$10.53** | **$ 9.25** | **$ 9.21** |
| *Income (loss) from investment operations:* | | | | | |
| Net investment income (loss)[a] | (.06) | (.02) | (.03) | (.05) | (.04)[c] |
| Net realized and unrealized gain (loss) | 1.68 | 3.40 | (4.86) | 1.33 | .08 |
| **Total from investment operations** | 1.62 | 3.38 | (4.89) | 1.28 | .04 |
| **Net asset value, end of period** | **$10.64** | **$ 9.02** | **$ 5.64** | **$10.53** | **$ 9.25** |
| Total Return (%) | 17.96 | 59.93 | (46.44)[b] | 13.84 | .43[c] |
| **Ratios to Average Net Assets and Supplemental Data** | | | | | |
| Net assets, end of period ($ millions) | .1 | 3 | 2 | 3 | 14 |
| Ratio of expenses before expense reductions (%) | 1.29 | 1.18 | 1.35 | 1.29 | 1.28 |
| Ratio of expenses after expense reductions (%) | 1.29 | 1.18 | 1.35 | 1.29 | 1.28 |
| Ratio of net investment income (loss) (%) | (.64) | (.27) | (.35) | (.53) | (.51)[c] |
| Portfolio turnover rate (%) | 23 | 45 | 71 | 91 | 49 |

a *Based on average shares outstanding during the period.*

b *Total return would have been lower had certain expenses not been reduced.*

c *Includes non-recurring income from the Advisor recorded as a result of an administrative proceeding regarding disclosure of brokerage allocation practices in connection with sales of DWS Funds. The non-recurring income resulted in an increase in net investment income of $0.017 per share and an increase in the ratio of net investment income of 0.18%. Excluding this non-recurring income, total return would have been 0.19% lower.*

# Notes to Financial Statements

## A. Organization and Significant Accounting Policies

DWS Variable Series II (the "Trust") is registered under the Investment Company Act of 1940, as amended (the "1940 Act"), as an open-end management investment company organized as a Massachusetts business trust. The Trust offers seventeen funds (hereinafter referred to individually as "Fund" or collectively as "Funds"). The Fund is classified as a non-diversified, open-end management investment company.

**Multiple Classes of Shares of Beneficial Interest.** Certain Funds of the Trust offer two classes of shares (Class A shares and Class B shares). Sales of Class B shares are subject to record keeping fees up to 0.15% and Rule 12b-1 fees under the 1940 Act equal to an annual rate of 0.25%, of the average daily net assets of the Class B shares of the applicable Fund. Class A shares are not subject to such fees.

Investment income, realized and unrealized gains and losses, and certain fund-level expenses and expense reductions, if any, are borne pro rata on the basis of relative net assets by the holders of all classes of shares except that each class bears certain expenses unique to that class (including the applicable Rule 12b-1 fee and record keeping fees). Differences in class-level expenses may result in payment of different per share dividends by class. All shares have equal rights with respect to voting subject to class-specific arrangements.

The Trust's financial statements are prepared in accordance with accounting principles generally accepted in the United States of America which require the use of management estimates. Actual results could differ from those estimates. The policies described below are followed consistently by the Trust in the preparation of its financial statements.

**Security Valuation.** Investments are stated at value determined as of the close of regular trading on the New York Stock Exchange on each day the exchange is open for trading.

Various inputs are used in determining the value of the Fund's investments. These inputs are summarized in three broad levels. Level 1 includes quoted prices in active markets for identical securities. Level 2 includes other significant observable inputs (including quoted prices for similar securities, interest rates, prepayment speeds, and credit risk). Level 3 includes significant unobservable inputs (including the Fund's own assumptions in determining the fair value of investments). The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities.

Equity securities are valued at the most recent sale price or official closing price reported on the exchange (US or foreign) or over-the-counter market on which they trade and are categorized as Level 1 securities. Securities for which no sales are reported are valued at the calculated mean between the most recent bid and asked quotations on the relevant market or, if a mean cannot be determined, at the most recent bid quotation. For certain international equity securities, in order to adjust for events which may occur between the close of the foreign exchanges and the close of the New York Stock Exchange, a fair valuation model may be used. This fair valuation model takes into account comparisons to the valuation of American Depository Receipts (ADRs), exchange-traded funds, futures contracts and certain indices and these securities are categorized as Level 2.

Money market instruments purchased with an original or remaining maturity of sixty days or less, maturing at par, are valued at amortized cost, which approximates value, and are categorized as Level 2. Investments in open-end investment companies are valued at their net asset value each business day and are categorized as Level 1.

Securities and other assets for which market quotations are not readily available or for which the above valuation procedures are deemed not to reflect fair value are valued in a manner that is intended to reflect their fair value as determined in accordance with procedures approved by the Board and are generally categorized as Level 3. In accordance with the Fund's valuation procedures, factors used in determining value may include, but are not limited to, the type of the security; the size of the holding; the initial cost of the security; the existence of any contractual restrictions on the security's disposition; the price and extent of public trading in similar securities of the issuer or of comparable companies; quotations or evaluated prices from broker-dealers and/or pricing services; information obtained from the issuer, analysts, and/or the appropriate stock exchange (for exchange-traded securities); an analysis of the company's or issuer's financial statements; an evaluation of the forces that influence the issuer and the market(s) in which the security is purchased and sold and with respect to debt securities; the maturity, coupon, creditworthiness, currency denomination and the movement of the market in which the security is normally traded. The value determined under these procedures may differ from published values for the same securities.

Disclosure about the classification of fair value measurements is included in a table following the Fund's Investment Portfolio.

**Foreign Currency Translations.** The books and records of the Trust are maintained in US dollars. Investment securities and other assets and liabilities denominated in a foreign currency are translated into US dollars at the prevailing exchange rates at period end. Purchases and sales of investment securities, income and expenses are translated into US dollars at the prevailing exchange rates on the respective dates of the transactions.

Net realized and unrealized gains and losses on foreign currency transactions represent net gains and losses between trade and settlement dates on securities transactions, the disposition of forward foreign currency exchange contracts and foreign currencies, and the difference between the amount of net investment income accrued and the US dollar amount actually received. That portion of both realized and unrealized gains and losses on investments that results from fluctuations in foreign currency exchange rates is not separately disclosed but is included with net realized and unrealized gain/appreciation and loss/depreciation on investments.

**Securities Lending.** The Fund lends securities to certain financial institutions. The Fund retains beneficial ownership of the securities it has loaned and continues to receive interest and dividends paid by the issuer of securities and to participate in any changes in their market value. The Fund requires the borrowers of the securities to maintain collateral with the Fund consisting of either cash or liquid, unencumbered assets having a value at least equal to the value of the securities loaned. When the collateral falls below specified amounts, the lending agent will use its best effort to obtain additional collateral on the next business day to meet required amounts under the security lending agreement. The Fund may invest the cash collateral into a joint trading account in an affiliated money market fund pursuant to Exemptive Orders issued by the SEC. The Fund receives compensation for lending its securities either in the form of fees or by earning interest on invested cash collateral net of borrower rebates and fees paid to a lending agent. Either the Fund or the borrower may terminate the loan. There may be risks of delay and costs in recovery of securities or even loss of rights in the collateral should the borrower of the securities fail financially. The Fund is also subject to all investment risks associated with the reinvestment of any cash collateral received, including, but not limited to, interest rate, credit and liquidity risk associated with such investments.

**Taxes.** The Fund's policy is to comply with the requirements of the Internal Revenue Code, as amended, which are applicable to regulated investment companies and to distribute all of its taxable income to its shareholders.

At December 31, 2010, the Fund had an approximate net tax basis capital loss carryforward which may be applied against any realized net taxable capital gains of each succeeding year until fully utilized or until the following expiration dates, whichever occurs first:

| Fund | Capital Loss Carryforward ($) | Expiration Date | Capital Loss Carryforward Utilized ($) | Capital Loss Carryforward Expired ($) |
|---|---|---|---|---|
| DWS Technology VIP | 71,516,000 | 12/31/2011 | 6,205,000 | 87,294,000 |
| | 13,148,000 | 12/31/2016 | | |
| | 20,753,000 | 12/31/2017 | | |

The Fund has reviewed the tax positions for the open tax years as of December 31, 2010 and has determined that no provision for income tax is required in the Fund's financial statements. The Fund's federal tax returns for the prior three fiscal years remain open subject to examination by the Internal Revenue Service.

**Distribution of Income and Gains.** Distributions of net investment income of the Fund , if any, are made annually. Net realized gains from investment transactions, in excess of available capital loss carryforwards, would be taxable to the Fund if not distributed and, therefore, will be distributed to shareholders at least annually. The Fund may also make additional distributions for tax purposes if necessary.

The timing and characterization of certain income and capital gains distributions are determined annually in accordance with federal tax regulations which may differ from accounting principles generally accepted in the United States of America. These differences primarily relate to net operating losses and certain securities sold at a loss. As a result, net investment income (loss) and net realized gain (loss) on investment transactions for a reporting period may differ significantly from distributions during such period. Accordingly, the Fund may periodically make reclassifications among certain of its capital accounts without impacting the net asset value of the Fund.

At December 31, 2010, the Fund's components of distributable earnings on a tax basis were as follows:

| Fund | Capital Loss Carryforwards ($) | Unrealized Appreciation (Depreciation) on Investments ($) |
|---|---|---|
| DWS Technology VIP | (105,417,000) | 28,995,869 |

In addition, the tax character of distributions paid by the Fund is summarized as follows:

| Fund | Distributions from Ordinary Income ($)* Years Ended December 31, 2010 | 2009 |
|---|---|---|
| DWS Technology VIP | 30,198 | — |

* *For tax purposes, short-term capital gain distributions are considered ordinary income distributions.*

**Expenses.** Expenses of the Trust arising in connection with a specific fund are allocated to that fund. Other Trust expenses which cannot be directly attributed to a fund are apportioned among the funds in the Trust.

**Contingencies.** In the normal course of business, the Fund may enter into contracts with service providers that contain general indemnification clauses. The Fund's maximum exposure under these arrangements is unknown as this would involve future claims that may be made against the Fund that have not yet been made. However, based on experience, the Fund expects the risk of loss to be remote.

**Other.** Investment transactions are accounted for on a trade date plus one basis for daily net asset value calculations. However, for financial reporting purposes, investment transactions are reported on trade date. Interest income is recorded on the accrual basis. Dividend income is recorded on the ex-dividend date net of foreign withholding taxes. Realized gains and losses from investment transactions are recorded on an identified cost basis.

## B. Purchases and Sales of Securities

During the year ended December 31, 2010, purchases and sales of investment transactions (excluding short-term investments) were as follows:

| Fund | Purchases ($) | Sales ($) |
|---|---|---|
| DWS Technology VIP | 16,212,693 | 32,717,685 |

## C. Related Parties

**Management Agreement.** Under the Investment Management Agreement with Deutsche Investment Management Americas Inc. ("DIMA" or the "Advisor"), an indirect, wholly owned subsidiary of Deutsche Bank AG, the Advisor directs the investments of the Fund in accordance with its investment objectives, policies and restrictions. The Advisor determines the securities, instruments and other contracts relating to investments to be purchased, sold or entered into by the Fund.

Under the Investment Management Agreement with the Advisor, the fee is equivalent to the annual rates shown below of the Fund's average daily net assets, computed and accrued daily and payable monthly:

| Fund | Annual Management Fee Rate |
|---|---|
| DWS Technology VIP | |
| $0–$250 million | .665% |
| next $750 million | .635% |
| next $1.5 billion | .615% |
| next $2.5 billion | .595% |
| next $2.5 billion | .565% |
| next $2.5 billion | .555% |
| next $2.5 billion | .545% |
| over $12.5 billion | .535% |

Accordingly, for the year ended December 31, 2010, the total management fee and effective management fee rate were as follows:

| Fund | Total Aggregated ($) | Annual Effective Rate |
|---|---|---|
| DWS Technology VIP | 484,850 | .665% |

**Administration Fee.** Pursuant to an Administrative Services Agreement, DIMA provides most administrative services to the Fund. For all services provided under the Administrative Services Agreement, the Fund pays DIMA an annual fee ("Administration Fee") of 0.10% of the Fund's average daily net assets, computed and accrued daily and payable monthly. For the year ended December 31, 2010, the Administration Fee was as follows:

| Fund | Total Aggregated ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS Technology VIP | 72,910 | 6,462 |

**Service Provider Fees.** DWS Investments Service Company ("DISC"), an affiliate of the Advisor, is the transfer agent, dividend-paying agent and shareholder service agent for the Fund. Pursuant to a sub-transfer agency agreement between DISC and DST Systems, Inc. ("DST"), DISC has delegated certain transfer agent, dividend-paying agent and shareholder service agent functions to DST. DISC compensates DST out of the shareholder servicing fee it receives from the Fund. For the year ended December 31, 2010, the amounts charged to the Fund by DISC were as follows:

| Fund | Total Aggregated ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS Technology VIP Class A | 134 | 35 |
| DWS Technology VIP Class B | 107 | 24 |

**Distribution Service Agreement**. Under the Fund's Class B 12b-1 plans, DWS Investments Distributors, Inc. ("DIDI") received a fee ("Distribution Service Fee") of 0.25% of average daily net assets of Class B shares. For the year ended December 31, 2010, the Distribution Service Fee was as follows:

| Fund | Total Aggregated ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS Technology VIP | 2,449 | 31 |

**Typesetting and Filing Service Fees.** Under an agreement with DIMA, DIMA is compensated for providing typesetting and certain regulatory filing services to the Fund. For the year ended December 31, 2010, the amount charged to the Fund by DIMA included in the Statement of Operations under "reports to shareholders" was as follows:

| Fund | Amount ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS Technology VIP | 11,852 | 2,738 |

**Trustees' Fees and Expenses.** The Fund paid each Trustee not affiliated with the Advisor retainer fees plus specified amounts for various committee services and for the Board Chairperson.

**Affiliated Cash Management Vehicles.** The Fund may invest uninvested cash balances in Central Cash Management Fund, which is managed by the Advisor. The Fund indirectly bears their proportionate share of the expenses of the underlying money market funds. Central Cash Management Fund does not pay the Advisor an investment management fee. Central Cash Management Fund seeks a high level of current income consistent with liquidity and the preservation of capital.

## D. Ownership of the Fund

At December 31, 2010, the beneficial ownership in the Fund was as follows:

**DWS Technology VIP:** Two Participating Insurance Companies were owners of record of 10% or more of the total outstanding Class A shares of the Fund, each owning 57% and 37%. Two Participating Insurance Companies were owners of record of 10% or more of the total outstanding Class B shares of the Fund, owning 79% and 12%.

## E. Line of Credit

The Trust and other affiliated fund (the "Participants") share in a $450 million revolving credit facility provided by a syndication of banks. The Fund may borrow for temporary or emergency purposes, including the meeting of redemption requests that otherwise might require the untimely disposition of securities. The Participants are charged an annual commitment fee which is allocated based on net assets, among each of the Participants. Interest is calculated at a rate per annum equal to the sum of the Federal Funds Rate plus 1.25 percent plus if LIBOR exceeds the Federal Funds Rate the amount of such excess. The Fund may borrow up to a maximum of 20 percent of its net assets under the agreement.

## F. Payments by Affiliates

During the year ended December 31, 2010, the Advisor agreed to reimburse the Fund $1,507 for losses incurred on trades executed incorrectly. The amount of the reimbursement is less than 0.01% of the Fund's average net assets.

## G. Subsequent Event

On January 12, 2011, the Board of the following Acquired Fund approved, in principle, the merger of the Acquired Fund into the Acquiring Fund. Completion of the merger is subject to a number of conditions, including approval by shareholders of the Fund at a shareholder meeting expected to be held in April 2011.

| Acquired Fund | Acquiring Fund |
|---|---|
| DWS Variable Series II — DWS Technology VIP | DWS Variable Series I — DWS Capital Growth VIP |

# Report of Independent Registered Public Accounting Firm

**To the Board of Trustees and Shareholders of DWS Variable Series II:**

We have audited the accompanying statement of assets and liabilities of DWS Technology VIP, one of the funds constituting the DWS Variable Series II (the "Trust"), including the investment portfolio, as of December 31, 2010, and the related statement of operations, the statement of changes in net assets and the financial highlights for each of the periods indicated therein. These financial statements and financial highlights are the responsibility of the Trust's management. Our responsibility is to express an opinion on these financial statements and financial highlights based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements and financial highlights are free of material misstatement. We were not engaged to perform an audit of the Trust's internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Trust's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements and financial highlights, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our procedures included confirmation of securities owned as of December 31, 2010, by correspondence with the custodian and brokers. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements and financial highlights referred to above present fairly, in all material respects, the financial position of the aforementioned fund of the DWS Variable Series II at December 31, 2010, the results of its operations, the changes in its net assets and the financial highlights for each of the periods indicated therein, in conformity with U.S. generally accepted accounting principles.

Ernst + Young LLP

Boston, Massachusetts
February 14, 2011

# Tax Information

**(Unaudited)**

For corporate shareholders, the following percentage of income dividends paid during the Fund's fiscal year ended December 31, 2010 qualified for the dividends received deduction:

| Fund | Dividends Received % |
|---|---|
| DWS Technology VIP | 100 |

Please consult a tax advisor if you have questions about federal or state income tax laws, or on how to prepare your tax returns. If you have specific questions about your account, please contact your insurance provider.

# Proxy Voting

The Trust's policies and procedures for voting proxies for portfolio securities and information about how the Trust voted proxies related to its portfolio securities during the 12-month period ended June 30 are available on our Web site — www.dws-investments.com (click on "proxy voting" at the bottom of the page) — or on the SEC's Web site — www.sec.gov. To obtain a written copy of the Trust's policies and procedures without charge, upon request, call us toll free at (800) 728-3337.

# Investment Management Agreement Approval

## DWS Technology VIP

The Board of Trustees, including the Independent Trustees, approved the renewal of your Fund's investment management agreement (the "Agreement") with Deutsche Investment Management Americas Inc. ("DWS") in September 2010.

In terms of the process that the Board followed prior to approving the Agreement, shareholders should know that:

- In September 2010, all but one of the Fund's Trustees were independent of DWS and its affiliates.
- The Trustees meet frequently to discuss fund matters. Each year, the Trustees dedicate substantial time to contract review matters. Over the course of several months, the Board's Contract Committee, in coordination with the Board's Equity Oversight Committee, reviewed comprehensive materials received from DWS, independent third parties and independent counsel. These materials included an analysis of the Fund's performance, fees and expenses, and profitability compiled by the Fund's independent fee consultant. The Board also received extensive information throughout the year regarding performance of the Fund.
- The Independent Trustees regularly meet privately with their independent counsel to discuss contract review and other matters. In addition, the Independent Trustees were also advised by the Fund's independent fee consultant in the course of their review of the Fund's contractual arrangements and considered a comprehensive report prepared by the independent fee consultant in connection with their deliberations (the "IFC Report").
- In connection with reviewing the Agreement, the Board also reviewed the terms of the Fund's Rule 12b-1 plan, distribution agreement, administrative services agreement, transfer agency agreement and other material service agreements.
- Based on its evaluation of the information provided, the Contract Committee presented its findings and recommendations to the Independent Trustees as a group. The Independent Trustees reviewed the Contract Committee's findings and recommendations and presented their recommendations to the full Board.

In connection with the contract review process, the Contract Committee and the Board considered the factors discussed below, among others. The Board also considered that DWS and its predecessors have managed the Fund since its inception, and the Board believes that a long-term relationship with a capable, conscientious advisor is in the best interests of the Fund. The Board considered, generally, that shareholders chose to invest or remain invested in the Fund knowing that DWS managed the Fund, and that the Agreement was approved by the Fund's shareholders. DWS is part of Deutsche Bank, a major global banking institution that is engaged in a wide range of financial services. The Board believes that there are significant advantages to being part of a global asset management business that offers a wide range of investing expertise and resources, including hundreds of portfolio managers and analysts with research capabilities in many countries throughout the world.

While shareholders may focus primarily on fund performance and fees, the Fund's Board considers these and many other factors, including the quality and integrity of DWS's personnel and such other issues as back-office operations, fund valuations, and compliance policies and procedures.

**Nature, Quality and Extent of Services.** The Board considered the terms of the Agreement, including the scope of advisory services provided under the Agreement. The Board noted that, under the Agreement, DWS provides portfolio management services to the Fund and that, pursuant to a separate administrative services agreement, DWS provides administrative services to the Fund. The Board considered the experience and skills of senior management and investment personnel, the resources made available to such personnel, the ability of DWS to attract and retain high-quality personnel, and the organizational depth and stability of DWS. The Board reviewed the Fund's performance over short-term and long-term periods and compared those returns to various agreed-upon performance measures, including market indices and a peer universe compiled by the independent fee consultant using information supplied by Lipper Inc. ("Lipper"). The Board also noted that it has put into place a process of identifying "Focus Funds" (e.g., funds performing poorly relative to their benchmark or a peer universe compiled by Lipper), and receives more frequent reporting and information from DWS regarding such funds, along with DWS's remedial plans to address underperformance. The Board believes this process is an effective manner of identifying and addressing underperforming funds. Based on the information provided, the Board noted that for the one-, three- and five-year periods ended December 31, 2009, the Fund's performance (Class A shares) was in the 2nd quartile, 3rd quartile and 4th quartile, respectively, of the applicable Lipper universe (the 1st quartile being the best performers and the 4th quartile being the worst performers). The Board also observed that the Fund has underperformed its benchmark in the one-, three- and five-year periods ended December 31, 2009.

On the basis of this evaluation and the ongoing review of investment results by the Board, the Board concluded that the nature, quality and extent of services provided by DWS historically have been and continue to be satisfactory.

**Fees and Expenses.** The Board considered the Fund's investment management fee schedule, operating expenses, and total expense ratios, and comparative information provided by Lipper and the independent fee consultant regarding investment management fee rates paid to other investment advisors by similar funds (1st quartile being the most favorable and 4th quartile being the least favorable). With respect to management fees paid to other investment advisors by similar funds, the Board noted that the contractual fee rates paid by the Fund, which include the 0.10% fee paid to DWS under the Fund's administrative services agreement, were at the median (2nd quartile) of the applicable Lipper peer group (based on Lipper data provided as of December 31, 2009). The Board noted that the Fund's Class A shares total (net) operating expenses were expected to be lower than the median (1st quartile) of the applicable Lipper expense universe (based on Lipper data provided as of December 31, 2009, and analyzing Lipper expense universe Class A expenses less any applicable 12b-1 fees) ("Lipper Universe Expenses"). The Board also reviewed data comparing the each share class's total (net) operating expenses to the applicable Lipper Universe Expenses. The Board considered the Fund's management fee rate as compared to fees charged by DWS and certain of its affiliates for comparable mutual funds and considered differences in fund and fee structures between the DWS Funds. The Board also considered how the Fund's total (net) operating expenses compared to the total (net) operating expenses of a more customized peer group selected by Lipper (based on such factors as asset size).

The information considered by the Board as part of its review of management fees included information regarding fees charged by DWS and its affiliates to similar institutional accounts and to similar funds offered primarily to European investors ("DWS Europe funds"), in each case as applicable. The Board observed that advisory fee rates for institutional accounts generally were lower than the management fees charged by similarly managed DWS US mutual funds ("DWS Funds"), but also took note of the differences in services provided to DWS Funds as compared to institutional accounts. In the case of DWS Europe funds, the Board observed that fee rates for DWS Europe funds generally were higher than for similarly managed DWS Funds, but noted that differences in the types of services provided to DWS Funds relative to DWS Europe funds made it difficult to compare such fees.

On the basis of the information provided, the Board concluded that management fees were reasonable and appropriate in light of the nature, quality and extent of services provided by DWS.

**Profitability.** The Board reviewed detailed information regarding revenues received by DWS under the Agreement. The Board considered the estimated costs and pre-tax profits realized by DWS from advising the DWS Funds, as well as estimates of the pre-tax profits attributable to managing the Fund in particular. The Board also received information regarding the estimated enterprise-wide profitability of DWS and its affiliates with respect to all fund services in totality and by fund. The Board reviewed DWS's methodology in allocating its costs to the management of the Fund. Based on the information provided, the Board concluded that the pre-tax profits realized by DWS in connection with the management of the Fund were not unreasonable. The Board also reviewed information regarding the profitability of certain similar investment management firms. The Board noted that while information regarding the profitability of such firms is limited (and in some cases is not necessarily prepared on a comparable basis), DWS and its affiliates' overall profitability with respect to the DWS fund complex (after taking into account distribution and other services provided to the funds by DWS and its affiliates) was lower than the overall profitability levels of many comparable firms for which such data was available.

**Economies of Scale.** The Board considered whether there are economies of scale with respect to the management of the Fund and whether the Fund benefits from any economies of scale. The Board noted that the Fund's management fee schedule includes fee breakpoints. The Board concluded that the Fund's fee schedule represents an appropriate sharing between the Fund and DWS of such economies of scale as may exist in the management of the Fund at current asset levels.

**Other Benefits to DWS and Its Affiliates.** The Board also considered the character and amount of other incidental benefits received by DWS and its affiliates, including any fees received by DWS for administrative services provided to the Fund and any fees received by an affiliate of DWS for distribution services. The Board also considered benefits to DWS related to brokerage and soft-dollar allocations, including allocating brokerage to pay for research generated by parties other than the executing broker dealers, which pertain primarily to funds investing in equity securities, along with the incidental public relations benefits to DWS related to DWS Funds advertising and cross-selling opportunities among DWS products and services. The Board concluded that management fees were reasonable in light of these fallout benefits.

**Compliance.** The Board considered the significant attention and resources dedicated by DWS to documenting and enhancing its compliance processes in recent years. The Board noted in particular (i) the experience and seniority of both DWS's chief compliance officer and the Fund's chief compliance officer; (ii) the large number of

DWS compliance personnel; and (iii) the substantial commitment of resources by DWS and its affiliates to compliance matters.

Based on all of the information considered and the conclusions reached, the Board unanimously (including the Independent Trustees) determined that the continuation of the Agreement is in the best interests of the Fund. In making this determination, the Board did not give particular weight to any single factor identified above. The Board considered these factors over the course of numerous meetings, certain of which were in executive session with only the Independent Trustees and their counsel present. It is possible that individual Trustees may have weighed these factors differently in reaching their individual decisions to approve the continuation of the Agreement.

# Summary of Management Fee Evaluation by Independent Fee Consultant

October 3, 2010

Pursuant to an Order entered into by Deutsche Investment Management Americas and affiliates (collectively, "DeAM") with the Attorney General of New York, I, Thomas H. Mack, have been appointed the Independent Fee Consultant for the DWS Funds (formerly the DWS Scudder Funds). My duties include preparing an annual written evaluation of the management fees DeAM charges the Funds, considering among other factors the management fees charged by other mutual fund companies for like services, management fees DeAM charges other clients for like services, DeAM's costs of supplying services under the management agreements and related profit margins, possible economies of scale if a Fund grows larger, and the nature and quality of DeAM's services, including fund performance. This report summarizes my evaluation for 2010, including my qualifications, the evaluation process for each of the DWS Funds, consideration of certain complex-level factors, and my conclusions. I served in substantially the same capacity in 2007, 2008, and 2009.

## Qualifications

For more than 35 years I have served in various professional capacities within the investment management business. I have held investment analysis and advisory positions, including securities analyst, portfolio strategist and director of investment policy with a large investment firm. I have also performed business management functions, including business development, financial management and marketing research and analysis.

Since 1991, I have been an independent consultant within the asset management industry. I have provided services to over 125 client organizations, including investment managers, mutual fund boards, product distributors and related organizations. Over the past ten years I have completed a number of assignments for mutual fund boards, specifically including assisting boards with management contract renewal.

I hold a Master of Business Administration degree, with highest honors, from Harvard University and Master of Science and Bachelor of Science (highest honors) degrees from the University of California at Berkeley. I am an independent director and audit committee financial expert for two closed-end mutual funds and have served in various leadership and financial oversight capacities with non-profit organizations.

## Evaluation of Fees for each DWS Fund

My work focused primarily on evaluating, fund-by-fund, the fees charged to each of the 118 publicly offered Fund portfolios in the DWS Fund family. For each Fund, I considered each of the key factors mentioned above, as well as any other relevant information. In doing so I worked closely with the Funds' Independent Directors in their annual contract renewal process, as well as in their approval of contracts for several new funds (documented separately).

In evaluating each Fund's fees, I reviewed comprehensive materials provided by or on behalf of DeAM, including expense information prepared by Lipper Analytical, comparative performance information, profitability data, manager histories, and other materials. I also accessed certain additional information from the Lipper and Morningstar databases and drew on my industry knowledge and experience.

To facilitate evaluating this considerable body of information, I prepared for each Fund a document summarizing the key data elements in each area as well as additional analytics discussed below. This made it possible to consider each key data element in the context of the others.

In the course of contract renewal, DeAM agreed to implement a number of fee and expense adjustments requested by the Independent Directors which will favorably impact future fees and expenses, and my evaluation includes the effects of these changes.

### Fees and Expenses Compared with Other Funds

The competitive fee and expense evaluation for each fund focused on two primary comparisons:

- The Fund's contractual management fee (the advisory fee plus the administration fee where applicable) compared with those of a group of typically 12–15 funds in the same Lipper investment category (e.g. Large Capitalization Growth) having similar distribution arrangements and being of similar size.
- The Fund's total expenses compared with a broader universe of funds from the same Lipper investment category and having similar distribution arrangements.

These two comparisons provide a view of not only the level of the fee compared with funds of similar scale but also the total expense the Fund bears for all the services it receives, in comparison with the investment choices available in the Fund's investment category and distribution channel. The principal figure-of-merit used in these comparisons was the subject Fund's percentile ranking against peers.

### DeAM's Fees for Similar Services to Others

DeAM provided management fee schedules for all of its US domiciled fund and non-fund investment management accounts in any of the investment categories where there is a DWS Fund. These similar products included the other DWS Funds, non-fund pooled accounts, institutional accounts and sub-advisory accounts. Using this information, I calculated for each Fund the fee that would be charged to each similar product, at the subject Fund's asset level.

Evaluating information regarding non-fund products is difficult because there are varying levels of services required for different types of accounts, with mutual funds generally requiring considerably more regulatory and administrative types of service as well as having more frequent cash flows than other types of accounts. Also, while mutual fund fees for similar fund products can be expected to be similar, there will be some differences due to different pricing conditions in different distribution channels (e.g. retail funds versus those used in variable insurance products), differences in underlying investment processes and other factors.

**Costs and Profit Margins**

DeAM provided a detailed profitability analysis for each Fund. After making some adjustments so that the presentation would be more comparable to the available industry figures, I reviewed profit margins from investment management alone, from investment management plus other fund services (excluding distribution) provided to the Funds by DeAM (principally shareholder services), and DeAM profits from all sources, including distribution. A later section comments on overall profitability.

**Economies of Scale**

Economies of scale — an expected decline in management cost per dollar of fund assets as fund assets grow — are very rarely quantified and documented because of inherent difficulties in collecting and analyzing relevant data. However, in virtually every investment category that I reviewed, larger funds tend to have lower fees and lower total expenses than smaller funds. To see how each DWS Fund compares with this industry observation, I reviewed:

- The trend in Fund assets over the last five years and the accompanying trend in total expenses. This shows if the Fund has grown and, if so, whether total expense (management fees as well as other expenses) have declined as a percent of assets.
- Whether the Fund has break-points in its management fee schedule, the extent of the fee reduction built into the schedule and the asset levels where the breaks take effect, and in the case of a sub-advised Fund how the Fund's break-points compare with those of the sub-advisory fee schedule.
- How the Fund's contractual fee schedule compares with trends in the industry data. To accomplish this, I constructed a chart showing how actual latest-fiscal-year contractual fees of the Fund and of other similar funds relate to average fund assets, with the subject Fund's contractual fee schedule superimposed.

**Quality of Service — Performance**

The quality-of-service evaluation focused on investment performance, which is the principal result of the investment management service. Each Fund's performance was reviewed over the past 1, 3, 5 and 10 years, as applicable, and compared with that of other funds in the same investment category and with a suitable market index.

In addition, I calculated and reviewed risk-adjusted returns relative to an index of similar mutual funds' returns and a suitable market index. The risk-adjusted returns analysis provides a way of determining the extent to which the Fund's return comparisons are mainly the product of investment value-added (or lack thereof) or alternatively taking considerably more or less risk than is typical in its investment category.

I also received and considered the history of portfolio manager changes for each Fund, as this provided an important context for evaluating the performance results.

## Complex-Level Considerations

While this evaluation was conducted mainly at the individual fund level, there are some issues relating to the reasonableness of fees that can alternatively be considered across the whole fund complex:

- I reviewed DeAM's profitability analysis for all DWS Funds, with a view toward determining if the allocation procedures used were reasonable and how profit levels compared with public data for other investment managers.
- I considered whether DeAM and affiliates receive any significant ancillary or "fall-out" benefits that should be considered in interpreting the direct profitability results. These would be situations where serving as the investment manager of the Funds is beneficial to another part of the Deutsche Bank organization.
- I considered how aggregated DWS Fund expenses had varied over the years, by asset class and in the context of trends in asset levels.
- I reviewed the structure of the DeAM organization, trends in staffing levels, and information on compensation of investment management and other professionals compared with industry data.

## Findings

Based on the process and analysis discussed above, which included reviewing a wide range of information from management and external data sources and considering among other factors the fees DeAM charges other clients, the fees charged by other fund managers, DeAM's costs and profits associated with managing the Funds, economies of scale, possible fall-out benefits, and the nature and quality of services provided, in my opinion the management fees charged the DWS Funds are reasonable.

Thomas H. Mack

Thomas H. Mack

# Board Members and Officers

The following table presents certain information regarding the Board Members and Officers of the Trust as of December 31, 2010. Each Board Member's year of birth is set forth in parentheses after his or her name. Unless otherwise noted, (i) each Board Member has engaged in the principal occupation(s) noted in the table for at least the most recent five years, although not necessarily in the same capacity; and (ii) the address of each Independent Board Member is c/o Paul K. Freeman, Independent Chairman, DWS Funds, PO Box 101833, Denver, CO 80250-1833. Except as otherwise noted below, the term of office for each Board Member is until the election and qualification of a successor, or until such Board Member sooner dies, resigns, is removed or as otherwise provided in the governing documents of the fund. Because the fund does not hold an annual meeting of shareholders, each Board Member will hold office for an indeterminate period. The Board Members may also serve in similar capacities with other funds in the fund complex. The Length of Time Served represents the year in which the Board Member joined the board of one or more DWS funds now overseen by the Board.

### Independent Board Members

| Name, Year of Birth, Position with the Fund and Length of Time Served[1] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Paul K. Freeman (1950)<br>Chairperson since 2009<br>Board Member since 1993 | Consultant, World Bank/Inter-American Development Bank; Executive and Governing Council of the Independent Directors Council (education committees); formerly, Project Leader, International Institute for Applied Systems Analysis (1998–2001); Chief Executive Officer, The Eric Group, Inc. (environmental insurance) (1986–1998) | 122 |
| John W. Ballantine (1946)<br>Board Member since 1999 | Retired; formerly, Executive Vice President and Chief Risk Management Officer, First Chicago NBD Corporation/The First National Bank of Chicago (1996–1998); Executive Vice President and Head of International Banking (1995–1996). Directorships: Healthways, Inc. (provider of disease and care management services); Portland General Electric (utility company); Stockwell Capital Investments PLC (private equity). Former Directorships: First Oak Brook Bancshares, Inc. and Oak Brook Bank; Prisma Energy International | 122 |
| Henry P. Becton, Jr. (1943)<br>Board Member since 1990 | Vice Chair and former President, WGBH Educational Foundation. Directorships: Association of Public Television Stations; Lead Director, Becton Dickinson and Company[3] (medical technology company); Lead Director, Belo Corporation[3] (media company); Public Radio International; Public Radio Exchange (PRX); The PBS Foundation. Former Directorships: Boston Museum of Science; American Public Television; Concord Academy; New England Aquarium; Mass. Corporation for Educational Telecommunications; Committee for Economic Development; Public Broadcasting Service | 122 |
| Dawn-Marie Driscoll (1946)<br>Board Member since 1987 | President, Driscoll Associates (consulting firm); Executive Fellow, Center for Business Ethics, Bentley University; formerly, Partner, Palmer & Dodge (1988–1990); Vice President of Corporate Affairs and General Counsel, Filene's (1978–1988). Directorships: Trustee of 22 open-end mutual funds managed by Sun Capital Advisers, Inc. (since 2007); Director of ICI Mutual Insurance Company (since 2007); Advisory Board, Center for Business Ethics, Bentley University; Trustee, Southwest Florida Community Foundation (charitable organization). Former Directorships: Investment Company Institute (audit, executive, nominating committees) and Independent Directors Council (governance, executive committees) | 122 |
| Keith R. Fox (1954)<br>Board Member since 1996 | Managing General Partner, Exeter Capital Partners (a series of private investment funds). Directorships: Progressive International Corporation (kitchen goods importer and distributor); BoxTop Media Inc. (advertising); The Kennel Shop (retailer); former Chairman, National Association of Small Business Investment Companies | 122 |
| Kenneth C. Froewiss (1945)<br>Board Member since 2001 | Adjunct Professor of Finance, NYU Stern School of Business (September 2009–present; Clinical Professor from 1997–September 2009); Member, Finance Committee, Association for Asian Studies (2002–present); Director, Mitsui Sumitomo Insurance Group (US) (2004–present); prior thereto, Managing Director, J.P. Morgan (investment banking firm) (until 1996) | 122 |
| Richard J. Herring (1946)<br>Board Member since 1990 | Jacob Safra Professor of International Banking and Professor, Finance Department, The Wharton School, University of Pennsylvania (since July 1972); Co-Director, Wharton Financial Institutions Center (since July 2000); Co-Chair, U.S. Shadow Financial Regulatory Committee; Executive Director, Financial Economists Roundtable; Director, Japan Equity Fund, Inc. (since September 2007), Thai Capital Fund, Inc. (since September 2007), Singapore Fund, Inc. (since September 2007); Independent Director of Barclays Bank Delaware (since September 2010). Formerly, Vice Dean and Director, Wharton Undergraduate Division (July 1995–June 2000); Director, Lauder Institute of International Management Studies (July 2000–June 2006) | 122 |
| William McClayton (1944)<br>Board Member since 2004+ | Private equity investor (since October 2009); previously, Managing Director, Diamond Management & Technology Consultants, Inc. (global consulting firm) (2001–2009); Directorship: Board of Managers, YMCA of Metropolitan Chicago; formerly: Senior Partner, Arthur Andersen LLP (accounting) (1966–2001); Trustee, Ravinia Festival | 122 |

| Name, Year of Birth, Position with the Fund and Length of Time Served[1] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Rebecca W. Rimel (1951)<br>Board Member since 1995 | President and Chief Executive Officer, The Pew Charitable Trusts (charitable organization) (1994 to present); Trustee, Thomas Jefferson Foundation (charitable organization) (1994 to present); Trustee, Executive Committee, Philadelphia Chamber of Commerce (2001–2007); Director, CardioNet, Inc.[2] (2009–present) (health care). Formerly, Executive Vice President, The Glenmede Trust Company (investment trust and wealth management) (1983–2004); Board Member, Investor Education (charitable organization) (2004–2005); Director, Viasys Health Care[2] (January 2007–June 2007); Trustee, Pro Publica (charitable organization) (2007–2010) | 122 |
| William N. Searcy, Jr. (1946)<br>Board Member since 1993 | Private investor since October 2003; Trustee of 22 open-end mutual funds managed by Sun Capital Advisers, Inc. (since October 1998). Formerly, Pension & Savings Trust Officer, Sprint Corporation[2] (telecommunications) (November 1989–September 2003) | 122 |
| Jean Gleason Stromberg (1943)<br>Board Member since 1997 | Retired. Formerly, Consultant (1997–2001); Director, Financial Markets US Government Accountability Office (1996–1997); Partner, Fulbright & Jaworski, L.L.P. (law firm) (1978–1996). Directorships: The William and Flora Hewlett Foundation. Former Directorships: Service Source, Inc., Mutual Fund Directors Forum (2002–2004), American Bar Retirement Association (funding vehicle for retirement plans) (1987–1990 and 1994–1996) | 122 |
| Robert H. Wadsworth (1940)<br>Board Member since 1999 | President, Robert H. Wadsworth & Associates, Inc. (consulting firm) (1983 to present); Director, The Phoenix Boys Choir Association | 125 |

## Interested Board Member and Officer[4]

| Name, Year of Birth, Position with the Trust/ Corporation and Length of Time Served[1,5] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Ingo Gefeke[7] (1967)<br>Board Member since 2010<br>Executive Vice President since 2010 | Managing Director[3], Deutsche Asset Management; Global Head of Distribution and Product Management, DWS Global Head of Trading and Securities Lending. Member of the Board of Directors of DWS Investment GmbH Frankfurt (since July 2009) and DWS Holding & Service GmbH Frankfurt (since January 2010); formerly, Global Chief Administrative Officer, Deutsche Asset Management (2004–2009); Global Chief Operating Officer, Global Transaction Banking, Deutsche Bank AG, New York (2001–2004); Chief Operating Officer, Global Banking Division Americas, Deutsche Bank AG, New York (1999–2001); Central Management, Global Banking Services, Deutsche Bank AG, Frankfurt (1998–1999); Relationship Management, Deutsche Bank AG, Tokyo, Japan (1997–1998) | 55 |

## Officers[4]

| Name, Year of Birth, Position with the Fund and Length of Time Served[5] | Principal Occupation(s) During Past 5 Years and Other Directorships Held |
|---|---|
| Michael G. Clark[6] (1965)<br>President, 2006–present | Managing Director[3], Deutsche Asset Management (2006–present); President of DWS family of funds; Director, ICI Mutual Insurance Company (since October 2007); formerly, Director of Fund Board Relations (2004–2006) and Director of Product Development (2000–2004), Merrill Lynch Investment Managers; Senior Vice President Operations, Merrill Lynch Asset Management (1999–2000) |
| John Millette[8] (1962)<br>Vice President and Secretary, 1999–present | Director[3], Deutsche Asset Management |
| Paul H. Schubert[6] (1963)<br>Chief Financial Officer, 2004–present<br>Treasurer, 2005–present | Managing Director[3], Deutsche Asset Management (since July 2004); formerly, Executive Director, Head of Mutual Fund Services and Treasurer for UBS Family of Funds (1998–2004); Vice President and Director of Mutual Fund Finance at UBS Global Asset Management (1994–1998) |
| Caroline Pearson[8] (1962)<br>Chief Legal Officer, April 2010–present | Managing Director[3], Deutsche Asset Management; formerly, Assistant Secretary for DWS family of funds (1997–2010) |
| Rita Rubin[9] (1970)<br>Assistant Secretary, 2009–present | Vice President and Counsel, Deutsche Asset Management (since October 2007); formerly, Vice President, Morgan Stanley Investment Management (2004–2007) |
| Paul Antosca[8] (1957)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management (since 2006); Vice President, The Manufacturers Life Insurance Company (U.S.A.) (1990–2006) |
| Jack Clark[8] (1967)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management (since 2007); formerly, Vice President, State Street Corporation (2002–2007) |

| Name, Year of Birth, Position with the Fund and Length of Time Served[5] | Principal Occupation(s) During Past 5 Years and Other Directorships Held |
|---|---|
| Diane Kenneally[8] (1966)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management |
| John Caruso[9] (1965)<br>Anti-Money Laundering Compliance Officer, 2010–present | Managing Director[3], Deutsche Asset Management |
| Robert Kloby[9] (1962)<br>Chief Compliance Officer, 2006–present | Managing Director[3], Deutsche Asset Management |

1 *The length of time served represents the year in which the Board Member joined the board of one or more DWS funds currently overseen by the Board.*

2 *A publicly held company with securities registered pursuant to Section 12 of the Securities Exchange Act of 1934.*

3 *Executive title, not a board directorship.*

4 *As a result of their respective positions held with the Advisor, these individuals are considered "interested persons" of the Advisor within the meaning of the 1940 Act. Interested persons receive no compensation from the fund.*

5 *The length of time served represents the year in which the officer was first elected in such capacity for one or more DWS funds.*

6 *Address: 100 Plaza One, Jersey City, NJ 07311.*

7 *Effective January 11, 2011, Mr. Gefeke, an interested Board Member and Executive Vice President, resigned from the fund's Board and as an officer.*

*The mailing address of Mr. Gefeke is 345 Park Avenue, New York, New York 10154. Mr. Gefeke was an interested Board Member of certain DWS funds by virtue of his positions with Deutsche Asset Management. As an interested person, Mr. Gefeke received no compensation from the fund.*

8 *Address: One Beacon Street, Boston, MA 02108.*

9 *Address: 60 Wall Street, New York, New York 10005.*

*The fund's Statement of Additional Information ("SAI") includes additional information about the Board Members. The SAI is available, without charge, upon request. If you would like to request a copy of the SAI, you may do so by calling the following toll-free number: (800) 728-3337.*

DWS Investments is part of Deutsche Bank's Asset Management division and, within the US, represents the retail asset management activities of Deutsche Bank AG, Deutsche Bank Trust Company Americas, Deutsche Investment Management Americas Inc. and DWS Trust Company.

The views expressed in this report reflect those of the portfolio managers only through the end of the period of the report as stated on the cover. The managers' views are subject to change at any time based on market and other conditions and should not be construed as a recommendation.

This information must be preceded or accompanied by a current prospectus.

Portfolio changes should not be considered recommendations for action by individual investors.

DWS Investments Distributors, Inc.
222 South Riverside Plaza
Chicago, IL 60606
(800) 621-1148

VS2TEC-2 (2/11)

DWS INVESTMENTS
Deutsche Bank Group

DECEMBER 31, 2010

# ANNUAL REPORT

## DWS VARIABLE SERIES II

## DWS Turner Mid Cap Growth VIP

**This report must be preceded or accompanied by a prospectus. To obtain an additional prospectus or summary prospectus, if available, call (800) 728-3337 or your financial representative. We advise you to consider the Fund's objectives, risks, charges and expenses carefully before investing. The summary prospectus and prospectus contain this and other important information about the Fund. Please read the prospectus carefully before you invest.**

*Investments in variable insurance portfolios (VIPs) involve risk. Stocks may decline in value. Bond investments are subject to interest-rate and credit risks. When interest rates rise, bond prices generally fall. Credit risk refers to the ability of an issuer to make timely payments of principal and interest. Investing in derivatives entails special risks relating to liquidity, leverage and credit that may reduce returns and/or increased volatility. Investing in foreign securities, particularly those of emerging markets, presents certain risks, such as currency fluctuations, political and economic changes, and market risks. There are additional risks associated with investing in commodities, high-yield bonds, aggressive growth stocks, non-diversified/ concentrated funds and small- and mid-cap stocks which are more fully explained in the prospectuses. Please read the prospectus for more information.*

*DWS Investments is part of Deutsche Bank's Asset Management division and, within the US, represents the retail asset management activities of Deutsche Bank AG, Deutsche Bank Trust Company Americas, Deutsche Investment Management Americas Inc. and DWS Trust Company.*



DWS INVESTMENTS
Deutsche Bank Group

# Performance Summary

**December 31, 2010**

## DWS Turner Mid Cap Growth VIP

**All performance shown is historical, assumes reinvestment of all dividend and capital gain distributions and does not guarantee future results. Investment return and principal value fluctuate with changing market conditions so that, when redeemed, shares may be worth more or less than their original cost. Current performance may be lower or higher than the performance data quoted. Please contact your participating insurance company for the Fund's most recent month-end performance. Performance doesn't reflect charges and fees ("contract charges") associated with the separate account that invests in the Fund or any variable life insurance policy or variable annuity contract for which the Fund is an investment option. These charges and fees will reduce returns.**

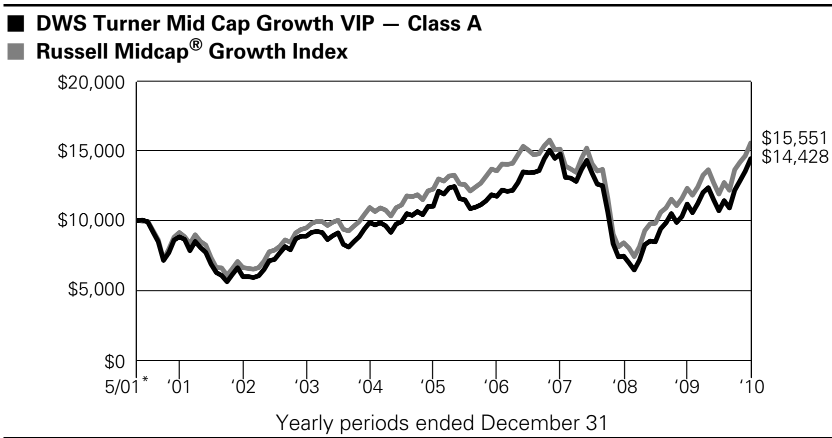
**The gross expense ratio of the Fund, as stated in the fee table of the prospectus dated May 1, 2010 is 0.89% for Class A shares and may differ from the expense ratio disclosed in the Financial Highlights table in this report.**

### Risk Considerations

Stocks of medium-sized companies involve greater risk than securities of larger, more-established companies. Stocks may decline in value. See the prospectus for details.

Fund returns for all periods shown reflect a fee waiver and/or expense reimbursement. Without this waiver/reimbursement, returns would have been lower.

**Growth of an Assumed $10,000 Investment in DWS Turner Mid Cap Growth VIP from 5/1/2001 to 12/31/2010**




*The Russell Midcap® Growth Index is an unmanaged index that measures the performance of those Russell Midcap companies with higher price-to-book ratios and higher forecasted growth values. The stocks are also members of the Russell 1000 Growth Index.*

*Index returns assume reinvestment of dividends and, unlike fund returns, do not reflect any fees or expenses. It is not possible to invest directly in an index.*

### Comparative Results

| DWS Turner Mid Cap Growth VIP | | 1-Year | 3-Year | 5-Year | Life of Fund* |
|---|---|---|---|---|---|
| **Class A** | Growth of $10,000 | $12,900 | $9,774 | $13,092 | $14,428 |
| | Average annual total return | 29.00% | –0.76% | 5.54% | 3.86% |
| Russell Midcap Growth Index | Growth of $10,000 | $12,638 | $10,294 | $12,692 | $15,551 |
| | Average annual total return | 26.38% | 0.97% | 4.88% | 4.67% |

*The growth of $10,000 is cumulative.*

* *The Fund commenced operations on May 1, 2001. Index returns began on April 30, 2001.*

# Information About Your Fund's Expenses

## DWS Turner Mid Cap Growth VIP

As an investor of the Fund, you incur two types of costs: ongoing expenses and transaction costs. Ongoing expenses include management fees and other Fund expenses. Examples of transaction costs include contract charges, redemption fees and account maintenance fees, which are not shown in this section. The following tables are intended to help you understand your ongoing expenses (in dollars) of investing in the Fund and to help you compare these expenses with the ongoing expenses of investing in other mutual funds. In the most recent six-month period, the Fund limited these expenses; had it not done so, expenses would have been higher. The example in the table is based on an investment of $1,000 invested at the beginning of the six-month period and held for the entire period (July 1, 2010 to December 31, 2010).

The tables illustrate your Fund's expenses in two ways:

- **Actual Fund Return.** This helps you estimate the actual dollar amount of ongoing expenses (but not transaction costs) paid on a $1,000 investment in the Fund using the Fund's actual return during the period. To estimate the expenses you paid over the period, simply divide your account value by $1,000 (for example, an $8,600 account value divided by $1,000 = 8.6), then multiply the result by the number in the "Expenses Paid per $1,000" line under the share class you hold.
- **Hypothetical 5% Fund Return.** This helps you to compare your Fund's ongoing expenses (but not transaction costs) with those of other mutual funds using the Fund's actual expense ratio and a hypothetical rate of return of 5% per year before expenses. Examples using a 5% hypothetical Fund return may be found in the shareholder reports of other mutual funds. The hypothetical account values and expenses may not be used to estimate the actual ending account balance or expenses you paid for the period.

Please note that the expenses shown in these tables are meant to highlight your ongoing expenses only and do not reflect any transaction costs. The "Expenses Paid per $1,000" line of the tables is useful in comparing ongoing expenses only and will not help you determine the relative total expense of owning different funds. If these transaction costs had been included, your costs would have been higher.

**Expenses and Value of a $1,000 Investment** for the six months ended December 31, 2010

| Actual Fund Return | Class A |
|---|---|
| Beginning Account Value 7/1/10 | $1,000.00 |
| Ending Account Value 12/31/10 | $1,348.50 |
| Expenses Paid per $1,000* | $ 5.68 |

| Hypothetical 5% Fund Return | Class A |
|---|---|
| Beginning Account Value 7/1/10 | $1,000.00 |
| Ending Account Value 12/31/10 | $1,020.37 |
| Expenses Paid per $1,000* | $ 4.89 |

* *Expenses are equal to the Fund's annualized expense ratio, multiplied by the average account value over the period, multiplied by the number of days in the most recent six-month period, then divided by 365.*

| Annualized Expense Ratio | Class A |
|---|---|
| DWS Variable Series II — DWS Turner Mid Cap Growth VIP | .96% |

For more information, please refer to the Fund's prospectus.

These tables do not reflect charges and fees ("contract charges") associated with the separate account that invests in the Fund or any variable life insurance policy or variable annuity contract for which the Fund is an investment option.

## DWS Turner Mid Cap Growth VIP

Both DWS Turner Mid Cap Growth VIP and the stock market capped 2010 with a strong finish, propelled by a strengthening global economy, robust earnings and a growing bullish sentiment among investors. The Standard & Poor's 500® (S&P 500) Index finished the year with a healthy gain of 15.06%. This is the index's second yearly gain in a row and its fourth over the past five years. The year, although strong, was not without its challenges as investors had to deal with the May 6th "flash crash", financial reform and continued concerns over the health of many European economies. On the other hand, the US Federal Reserve Board (the Fed) continued to be active in the market, with round two of the quantitative easing effort initiated later in the year, and corporate earnings continued to post strong gains.

For 2010, small-cap stocks outpaced both mid- and large-cap stocks. The Russell 2000® Index posted a gain of 26.85% versus 16.10% for the Russell 1000® Index. Growth stocks outperformed value stocks across the market-cap spectrum for the year as investors became more optimistic over the economic rebound and sought out companies with stronger earnings prospects.

With improving economic conditions and a favorable backdrop for companies looking to grow their earnings, the performance of the Fund was strong, with Class A shares returning 29.00%, outpacing the 26.38% return for the Fund's benchmark, the Russell Midcap® Growth Index, as of December 31, 2010 (unadjusted for contract charges). Seven of the nine portfolio sectors outperformed the benchmark, with outperformance largely attributed to strength in the technology sector due to good stock selection.

The technology and financial services sectors contributed the most to relative gains, while the health care sector and producer durables, a Turner Custom Sector, were the lead detractors. A sustained pickup in corporate spending aided the technology sector as our holdings in F5 Networks, Inc., Salesforce.com, Inc. and Cypress Semiconductor Corp. generated strong double-digit returns. Within financial services, the life/health insurance and real estate development industries led the way. Health care was among the worst-performing sectors as unanswered health care reform questions continued to linger over the industry. Electronic production equipment, electrical products and industrial machinery companies detracted.

As before, the Fund emphasizes three types of growth stocks. One, it holds classic growth stocks in industries such as biotechnology and wireless communications that we think have high-return potential for fundamental reasons. Two, it holds stocks of companies gaining market share in their businesses. And three, it holds cyclical stocks in industries such as metals, heavy equipment, bioagriculture, retailing and chemicals that historically have tended to do well as the economy improves.

Christopher K. McHugh

*Lead Manager, Turner Investment Partners, Inc.*
*Subadvisor to the Fund*

Tara Hedlund, CFA

Jason Schrotberger, CFA

*Portfolio Managers*

*The Standard & Poor's 500 (S&P 500) Index is an unmanaged, capitalization-weighted index of 500 stocks. The index is designed to measure performance of the broad domestic economy through changes in the aggregate market value of 500 stocks representing all major industries.*

*The Russell 1000 Index is an unmanaged index that measures the performance of the 1,000 largest companies in the Russell 3000® Index, which represents approximately 92% of the total market capitalization of the Russell 3000 Index.*

*The Russell Midcap Growth Index is an unmanaged index that measures the performance of those Russell Midcap companies with higher price-to-book ratios and higher forecasted growth values.*

*Index returns assume reinvestment of dividends and, unlike fund returns, do not reflect any fees or expenses. It is not possible to invest directly in an index.*

*Portfolio management market commentary is as of December 31, 2010, and may not come to pass. This information is subject to change at any time based on market and other conditions. Past performance does not guarantee future results. Current and future portfolio holdings are subject to risk.*

# Portfolio Summary

## DWS Turner Mid Cap Growth VIP

| **Asset Allocation** (As a % of Investment Portfolio excluding Securities Lending Collateral) | **12/31/10** | **12/31/09** |
|---|---|---|
| Common Stocks | 99% | 99% |
| Cash Equivalents | 1% | 1% |
| | 100% | 100% |

| **Sector Diversification** (As a % of Common Stocks) | **12/31/10** | **12/31/09** |
|---|---|---|
| Information Technology | 28% | 27% |
| Consumer Discretionary | 18% | 16% |
| Health Care | 12% | 15% |
| Industrials | 11% | 10% |
| Financials | 10% | 10% |
| Materials | 8% | 6% |
| Energy | 6% | 7% |
| Consumer Staples | 4% | 7% |
| Telecommunication Services | 2% | 1% |
| Utilities | 1% | 1% |
| | 100% | 100% |

*Asset allocation and sector diversification are subject to change.*

*For more complete details about the Fund's investment portfolio, see page 6.*

Following the Fund's fiscal first and third quarter-end, a complete portfolio holdings listing is filed with the SEC on Form N-Q. The form will be available on the SEC's Web site at www.sec.gov, and it also may be reviewed and copied at the SEC's Public Reference Room in Washington, D.C. Information on the operation of the SEC's Public Reference Room may be obtained by calling (800) SEC-0330. The Fund's portfolio holdings are also posted on www.dws-investments.com from time to time. Please see the Fund's current prospectus for more information.

# Investment Portfolio

December 31, 2010

## DWS Turner Mid Cap Growth VIP

| | Shares | Value ($) |
|---|---|---|
| **Common Stocks 98.8%** | | |
| **Consumer Discretionary 17.6%** | | |
| **Auto Components 1.2%** | | |
| BorgWarner, Inc.* (a) | 10,260 | **742,414** |
| **Hotels Restaurants & Leisure 6.5%** | | |
| Darden Restaurants, Inc. | 7,510 | 348,764 |
| Royal Caribbean Cruises Ltd.* | 12,510 | 587,970 |
| Starwood Hotels & Resorts Worldwide, Inc. (a) | 23,700 | 1,440,486 |
| WMS Industries, Inc.* | 16,775 | 758,901 |
| Wynn Resorts Ltd. | 6,660 | 691,575 |
| | | **3,827,696** |
| **Internet & Catalog Retail 1.2%** | | |
| Priceline.com, Inc.* | 1,770 | **707,203** |
| **Media 1.3%** | | |
| Interpublic Group of Companies, Inc.* | 75,190 | **798,518** |
| **Multiline Retail 1.5%** | | |
| Nordstrom, Inc. (a) | 20,850 | **883,623** |
| **Specialty Retail 3.7%** | | |
| Abercrombie & Fitch Co. "A" (a) | 13,290 | 765,903 |
| Dick's Sporting Goods, Inc.* | 14,010 | 525,375 |
| Guess?, Inc. | 18,850 | 891,982 |
| | | **2,183,260** |
| **Textiles, Apparel & Luxury Goods 2.2%** | | |
| Coach, Inc. | 23,230 | **1,284,851** |
| **Consumer Staples 3.8%** | | |
| **Beverages 0.5%** | | |
| Hansen Natural Corp.* | 6,020 | **314,726** |
| **Food & Staples Retailing 1.2%** | | |
| Whole Foods Market, Inc.* | 13,890 | **702,695** |
| **Food Products 2.1%** | | |
| Green Mountain Coffee Roasters, Inc.* | 15,560 | 511,302 |
| Mead Johnson Nutrition Co. | 11,210 | 697,822 |
| | | **1,209,124** |
| **Energy 6.3%** | | |
| **Energy Equipment & Services 1.0%** | | |
| Cameron International Corp.* | 11,800 | **598,614** |
| **Oil, Gas & Consumable Fuels 5.3%** | | |
| Alpha Natural Resources, Inc.* | 10,860 | 651,926 |
| Cimarex Energy Co. | 7,810 | 691,419 |
| Concho Resources, Inc.* | 9,200 | 806,564 |
| QEP Resources, Inc. | 12,800 | 464,768 |
| Whiting Petroleum Corp.* | 4,190 | 491,026 |
| | | **3,105,703** |
| **Financials 9.5%** | | |
| **Capital Markets 3.4%** | | |
| Invesco Ltd. | 27,690 | 666,221 |
| T. Rowe Price Group, Inc. (a) | 20,340 | 1,312,744 |
| | | **1,978,965** |
| **Commercial Banks 0.9%** | | |
| M&T Bank Corp. | 6,290 | **547,545** |
| **Consumer Finance 0.7%** | | |
| Discover Financial Services | 23,040 | **426,931** |
| **Diversified Financial Services 2.1%** | | |
| IntercontinentalExchange, Inc.* | 6,140 | 731,581 |
| MSCI, Inc. "A"* | 12,530 | 488,169 |
| | | **1,219,750** |
| **Insurance 1.3%** | | |
| Aon Corp. | 8,820 | 405,808 |
| Unum Group | 16,060 | 388,973 |
| | | **794,781** |
| **Real Estate Management & Development 1.1%** | | |
| CB Richard Ellis Group, Inc. "A"* | 32,550 | **666,624** |
| **Health Care 11.7%** | | |
| **Biotechnology 2.7%** | | |
| Alexion Pharmaceuticals, Inc.* (a) | 9,880 | 795,834 |
| Onyx Pharmaceuticals, Inc.* | 7,680 | 283,161 |
| United Therapeutics Corp.* | 8,340 | 527,255 |
| | | **1,606,250** |
| **Health Care Equipment & Supplies 1.8%** | | |
| Intuitive Surgical, Inc.* | 1,790 | 461,372 |
| Varian Medical Systems, Inc.* | 8,400 | 581,952 |
| | | **1,043,324** |
| **Health Care Providers & Services 4.2%** | | |
| AMERIGROUP Corp.* | 8,610 | 378,151 |
| AmerisourceBergen Corp. | 19,480 | 664,658 |
| Emergency Medical Services Corp. "A"* | 5,550 | 358,586 |
| Laboratory Corp. of America Holdings* | 3,960 | 348,163 |
| Universal Health Services, Inc. "B" | 17,110 | 742,916 |
| | | **2,492,474** |
| **Life Sciences Tools & Services 0.9%** | | |
| Charles River Laboratories International, Inc.* | 6,550 | 232,787 |
| Illumina, Inc.* | 4,670 | 295,798 |
| | | **528,585** |
| **Pharmaceuticals 2.1%** | | |
| Hospira, Inc.* | 9,020 | 502,324 |
| Valeant Pharmaceuticals International, Inc. | 12,560 | 355,322 |
| Watson Pharmaceuticals, Inc.* | 7,620 | 393,573 |
| | | **1,251,219** |
| **Industrials 10.6%** | | |
| **Aerospace & Defense 1.2%** | | |
| Goodrich Corp. | 8,480 | **746,834** |
| **Airlines 1.4%** | | |
| United Continental Holdings, Inc.* | 33,936 | **808,355** |
| **Machinery 4.5%** | | |
| Cummins, Inc. | 10,330 | 1,136,403 |
| Joy Global, Inc. | 11,890 | 1,031,458 |
| Parker Hannifin Corp. | 5,810 | 501,403 |
| | | **2,669,264** |
| **Professional Services 0.8%** | | |
| Manpower, Inc. | 7,200 | **451,872** |
| **Road & Rail 0.8%** | | |
| Canadian Pacific Railway Ltd. | 7,240 | **469,224** |

*The accompanying notes are an integral part of the financial statements.*

| | Shares | Value ($) |
|---|---|---|
| **Trading Companies & Distributors 1.9%** | | |
| Fastenal Co. (a) | 13,390 | 802,195 |
| WESCO International, Inc.* | 5,760 | 304,128 |
| | | **1,106,323** |
| **Information Technology 28.1%** | | |
| **Communications Equipment 6.3%** | | |
| Acme Packet, Inc.* | 8,270 | 439,633 |
| Aruba Networks, Inc.* | 28,110 | 586,937 |
| F5 Networks, Inc.* | 12,600 | 1,640,016 |
| Finisar Corp.* | 13,120 | 389,533 |
| Juniper Networks, Inc.* | 11,990 | 442,671 |
| Riverbed Technology, Inc.* | 5,950 | 209,261 |
| | | **3,708,051** |
| **Computers & Peripherals 3.4%** | | |
| NetApp, Inc.* (a) | 18,210 | 1,000,821 |
| SanDisk Corp.* | 20,230 | 1,008,668 |
| | | **2,009,489** |
| **Electronic Equipment, Instruments & Components 0.6%** | | |
| Aeroflex Holding Corp.* | 20,500 | **337,225** |
| **Internet Software & Services 2.7%** | | |
| Akamai Technologies, Inc.* | 7,620 | 358,521 |
| LogMeIn, Inc.* | 9,350 | 414,579 |
| MercadoLibre, Inc.* (a) | 4,270 | 284,596 |
| OpenTable, Inc.* | 1,650 | 116,292 |
| VeriSign, Inc. | 12,300 | 401,841 |
| | | **1,575,829** |
| **IT Services 0.9%** | | |
| VeriFone Systems, Inc.* | 13,290 | **512,462** |
| **Semiconductors & Semiconductor Equipment 10.5%** | | |
| ASML Holding NV (NY Registered Shares) (a) | 20,810 | 797,855 |
| Atheros Communications* | 22,530 | 809,278 |
| Broadcom Corp. "A" | 17,150 | 746,883 |
| Cree, Inc.* | 4,730 | 311,660 |
| Cypress Semiconductor Corp.* | 50,140 | 931,601 |
| First Solar, Inc.* (a) | 1,550 | 201,717 |
| Lam Research Corp.* | 15,670 | 811,393 |
| Netlogic Microsystems, Inc.* | 22,230 | 698,244 |
| Varian Semiconductor Equipment Associates, Inc.* | 24,730 | 914,268 |
| | | **6,222,899** |
| **Software 3.7%** | | |
| Fortinet, Inc.* | 11,110 | 359,408 |
| Salesforce.com, Inc.* | 9,790 | 1,292,280 |
| SuccessFactors, Inc.* | 19,030 | 551,109 |
| | | **2,202,797** |
| **Materials 8.3%** | | |
| **Chemicals 2.7%** | | |
| CF Industries Holdings, Inc. | 7,300 | 986,595 |
| LyondellBasell Industries NV* | 17,390 | 598,216 |
| | | **1,584,811** |
| **Metals & Mining 5.6%** | | |
| Cliffs Natural Resources, Inc. (a) | 10,920 | 851,869 |
| Silver Wheaton Corp.* | 10,820 | 422,413 |
| United States Steel Corp. (a) | 13,690 | 799,770 |
| Walter Energy, Inc. | 9,770 | 1,248,997 |
| | | **3,323,049** |
| **Telecommunication Services 2.3%** | | |
| **Wireless Telecommunication Services** | | |
| Crown Castle International Corp.* | 19,260 | 844,166 |
| NII Holdings, Inc.* | 11,200 | 500,192 |
| | | **1,344,358** |
| **Utilities 0.6%** | | |
| **Gas Utilities** | | |
| Questar Corp. | 21,780 | **379,190** |
| **Total Common Stocks** (Cost $36,798,115) | | **58,366,907** |

## Securities Lending Collateral 16.1%

| | Shares | Value ($) |
|---|---|---|
| Daily Assets Fund Institutional, 0.27% (b) (c) (Cost $9,501,633) | 9,501,633 | **9,501,633** |

## Cash Equivalents 1.2%

| | Shares | Value ($) |
|---|---|---|
| Central Cash Management Fund, 0.19% (b) (Cost $682,786) | 682,786 | **682,786** |

| | % of Net Assets | Value ($) |
|---|---|---|
| **Total Investment Portfolio** (Cost $46,982,534)† | 116.1 | **68,551,326** |
| **Other Assets and Liabilities, Net** | (16.1) | **(9,506,407)** |
| **Net Assets** | 100.0 | **59,044,919** |

* *Non-income producing security.*

† *The cost for federal income tax purposes was $47,461,113. At December 31, 2010, net unrealized appreciation for all securities based on tax cost was $21,090,213. This consisted of aggregate gross unrealized appreciation for all securities in which there was an excess of value over tax cost of $21,587,307 and aggregate gross unrealized depreciation for all securities in which there was an excess of tax cost over value of $497,094.*

(a) *All or a portion of these securities were on loan (see Notes to Financial Statements). The value of all securities loaned at December 31, 2010 amounted to $9,276,096, which is 15.7% of net assets.*

(b) *Affiliated fund managed by Deutsche Investment Management Americas Inc. The rate shown is the annualized seven-day yield at period end.*

(c) *Represents collateral held in connection with securities lending. Income earned by the Fund is net of borrower rebates.*

*The accompanying notes are an integral part of the financial statements.*

## Fair Value Measurements

*Various inputs are used in determining the value of the Fund's investments. These inputs are summarized in three broad levels. Level 1 includes quoted prices in active markets for identical securities. Level 2 includes other significant observable inputs (including quoted prices for similar securities, interest rates, prepayment speeds, and credit risk). Level 3 includes significant unobservable inputs (including the Fund's own assumptions in determining the fair value of investments). The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities.*

*The following is a summary of the inputs used as of December 31, 2010 in valuing the Fund's investments. For information on the Fund's policy regarding the valuation of investments, please refer to the Security Valuation section of Note A in the accompanying Notes to Financial Statements.*

| **Assets** | **Level 1** | **Level 2** | **Level 3** | **Total** |
|---|---|---|---|---|
| Common Stocks (d) | $ 58,366,907 | $ — | $ — | $ 58,366,907 |
| Short-Term Investments (d) | 10,184,419 | — | — | 10,184,419 |
| **Total** | **$ 68,551,326** | **$ —** | **$ —** | **$ 68,551,326** |

*There have been no significant transfers between Level 1 and Level 2 fair value measurements during the year ended December 31, 2010.*

(d) *See Investment Portfolio for additional detailed categorizations.*

*The accompanying notes are an integral part of the financial statements.*

# Statement of Assets and Liabilities

as of December 31, 2010

| | | |
|---|---|---|
| **Assets** | | |
| Investments: | | |
| Investments in unaffiliated securities, at value (cost $36,798,115) — including $9,276,096 of securities loaned | $ | 58,366,907 |
| Investment in Daily Assets Fund Institutional (cost $9,501,633)* | | 9,501,633 |
| Investment in Central Cash Management Fund (cost $682,786) | | 682,786 |
| Total investments, at value (cost $46,982,534) | | 68,551,326 |
| Cash | | 10,000 |
| Receivable for investments sold | | 312,238 |
| Dividends receivable | | 12,654 |
| Interest receivable | | 740 |
| Other assets | | 286 |
| Total assets | | 68,887,244 |
| **Liabilities** | | |
| Payable upon return of securities loaned | | 9,501,633 |
| Payable for investments purchased | | 155,357 |
| Payable for Fund shares redeemed | | 83,068 |
| Accrued management fee | | 40,161 |
| Other accrued expenses and payables | | 62,106 |
| Total liabilities | | 9,842,325 |
| **Net assets, at value** | **$** | **59,044,919** |
| **Net Assets Consist of** | | |
| Net unrealized appreciation (depreciation) on: | | |
| Investments | | 21,568,792 |
| Foreign currency | | 10 |
| Accumulated net realized gain (loss) | | (16,197,182) |
| Paid-in capital | | 53,673,299 |
| **Net assets, at value** | **$** | **59,044,919** |
| **Class A** | | |
| **Net Asset Value,** offering and redemption price per share ($59,044,919 ÷ 6,033,131 outstanding shares of beneficial interest, no par value, unlimited number of shares authorized) | **$** | **9.79** |

* *Represents collateral on securities loaned.*

# Statement of Operations

for the year ended December 31, 2010

| | | |
|---|---|---|
| **Investment Income** | | |
| Income: | | |
| Dividends (net of foreign taxes withheld of $3,538) | $ | 408,183 |
| Income distributions — Central Cash Management Fund | | 2,018 |
| Securities lending income, including income from Daily Assets Fund Institutional, net of borrower rebates | | 1,716 |
| Total income | | 411,917 |
| Expenses: | | |
| Management fee | | 368,747 |
| Administration fee | | 51,573 |
| Services to shareholders | | 1,911 |
| Custodian fee | | 12,628 |
| Legal fees | | 7,226 |
| Audit and tax fees | | 46,905 |
| Trustees' fees and expenses | | 3,784 |
| Reports to shareholders | | 13,380 |
| Other | | 3,465 |
| Total expenses before expense reductions | | 509,619 |
| Expense reductions | | (679) |
| Total expenses after expense reductions | | 508,940 |
| **Net investment income (loss)** | | **(97,023)** |
| **Realized and Unrealized Gain (Loss)** | | |
| Net realized gain (loss) from investments: | | |
| Investments | | 6,420,921 |
| Foreign currency | | 35 |
| | | 6,420,956 |
| Change in net unrealized appreciation (depreciation) on: | | |
| Investments | | 7,106,878 |
| Foreign currency | | 10 |
| | | 7,106,888 |
| **Net gain (loss)** | | **13,527,844** |
| **Net increase (decrease) in net assets resulting from operations** | **$** | **13,430,821** |

*The accompanying notes are an integral part of the financial statements.*

# Statement of Changes in Net Assets

| Increase (Decrease) in Net Assets | Years Ended December 31, 2010 | 2009 |
|---|---|---|
| Operations: | | |
| Net investment income (loss) | $ (97,023) | $ 10,140 |
| Net realized gain (loss) | 6,420,956 | (5,079,785) |
| Change in net unrealized appreciation (depreciation) | 7,106,888 | 23,095,058 |
| Net increase (decrease) in net assets resulting from operations | 13,430,821 | 18,025,413 |
| Distributions to shareholders from: | | |
| Net investment income: | | |
| Class A | (7,813) | — |
| Total distributions | (7,813) | — |
| Fund share transactions: | | |
| **Class A** | | |
| Proceeds from shares sold | 4,327,117 | 3,565,715 |
| Shares issued to shareholders in reinvestment of distributions | 7,813 | — |
| Payments for shares redeemed | (9,376,315) | (19,620,216) |
| Shares converted* | — | 5,097 |
| Net increase (decrease) in net assets from Class A share transactions | (5,041,385) | (16,049,404) |
| **Class B** | | |
| Payments for shares redeemed | — | (21) |
| Shares converted* | — | (5,097) |
| Net increase (decrease) in net assets from Class B share transactions | — | (5,118) |
| **Increase (decrease) in net assets** | 8,381,623 | 1,970,891 |
| Net assets at beginning of period | 50,663,296 | 48,692,405 |
| Net assets at end of period (including undistributed net investment income of $0 and $4,590, respectively) | **$ 59,044,919** | **$ 50,663,296** |

| **Other Information** | | |
|---|---|---|
| **Class A** | | |
| Shares outstanding at beginning of period | 6,675,631 | 9,629,198 |
| Shares sold | 522,352 | 533,210 |
| Shares issued to shareholders in reinvestment of distributions | 906 | — |
| Shares redeemed | (1,165,758) | (3,488,014) |
| Shares converted* | — | 1,237 |
| Net increase (decrease) in Class A shares | (642,500) | (2,953,567) |
| Shares outstanding at end of period | **6,033,131** | **6,675,631** |
| **Class B** | | |
| Shares outstanding at beginning of period | — | 1,306 |
| Shares redeemed | — | (5) |
| Shares converted* | — | (1,301) |
| Net increase (decrease) in Class B shares | — | (1,306) |
| Shares outstanding at end of period | **—** | **—** |

* *On March 6, 2009, Class B shares converted into Class A shares.*

*The accompanying notes are an integral part of the financial statements.*

# Financial Highlights

## Class A

| Years Ended December 31, | 2010 | 2009 | 2008 | 2007 | 2006 |
|---|---|---|---|---|---|
| **Selected Per Share Data** | | | | | |
| **Net asset value, beginning of period** | **$ 7.59** | **$ 5.06** | **$12.55** | **$10.92** | **$11.02** |
| *Income (loss) from investment operations:* | | | | | |
| Net investment income (loss)[a] | (.02) | .00* | (.01) | (.04) | (.01) |
| Net realized and unrealized gain (loss) | 2.22 | 2.53 | (5.28) | 2.64 | .77 |
| **Total from investment operations** | 2.20 | 2.53 | (5.29) | 2.60 | .76 |
| *Less distributions from:* | | | | | |
| Net investment income | (.00)* | — | — | — | — |
| Net realized gains | — | — | (2.20) | (.97) | (.86) |
| Tax return of capital | — | — | (.00)* | — | — |
| **Total distributions** | (.00)* | — | (2.20) | (.97) | (.86) |
| **Net asset value, end of period** | **$ 9.79** | **$ 7.59** | **$ 5.06** | **$12.55** | **$10.92** |
| Total Return (%) | 29.00[b] | 50.00 | (49.49)[b] | 25.75 | 6.52 |
| **Ratios to Average Net Assets and Supplemental Data** | | | | | |
| Net assets, end of period ($ millions) | 59 | 51 | 49 | 129 | 117 |
| Ratio of expenses before expense reductions (%) | .99 | .89 | 1.03 | .95 | .97 |
| Ratio of expenses after expense reductions (%) | .99 | .89 | 1.00 | .95 | .97 |
| Ratio of net investment income (loss) (%) | (.19) | .02 | (.14) | (.36) | (.06) |
| Portfolio turnover rate (%) | 96 | 86 | 156 | 133 | 148 |

[a] *Based on average shares outstanding during the period.*

[b] *Total return would have been lower had certain expenses not been reduced.*

* *Amount is less than $.005.*

# Notes to Financial Statements

## A. Organization and Significant Accounting Policies

DWS Variable Series II (the "Trust") is registered under the Investment Company Act of 1940, as amended (the "1940 Act"), as an open-end management investment company organized as a Massachusetts business trust. The Trust offers seventeen funds (hereinafter referred to individually as "Fund" or collectively as "Funds"). The Fund is classified as a diversified open-end management investment company.

The Trust's financial statements are prepared in accordance with accounting principles generally accepted in the United States of America which require the use of management estimates. Actual results could differ from those estimates. The policies described below are followed consistently by the Trust in the preparation of its financial statements.

**Security Valuation.** Investments are stated at value determined as of the close of regular trading on the New York Stock Exchange on each day the exchange is open for trading.

Various inputs are used in determining the value of the Fund's investments. These inputs are summarized in three broad levels. Level 1 includes quoted prices in active markets for identical securities. Level 2 includes other significant observable inputs (including quoted prices for similar securities, interest rates, prepayment speeds, and credit risk). Level 3 includes significant unobservable inputs (including the Fund's own assumptions in determining the fair value of investments). The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities.

Equity securities are valued at the most recent sale price or official closing price reported on the exchange (US or foreign) or over-the-counter market on which they trade and are categorized as Level 1 securities. Securities for which no sales are reported are valued at the calculated mean between the most recent bid and asked quotations on the relevant market or, if a mean cannot be determined, at the most recent bid quotation.

Money market instruments purchased with an original or remaining maturity of sixty days or less, maturing at par, are valued at amortized cost, which approximates value, and are categorized as Level 2. Investments in open-end investment companies are valued at their net asset value each business day and are categorized as Level 1.

Securities and other assets for which market quotations are not readily available or for which the above valuation procedures are deemed not to reflect fair value are valued in a manner that is intended to reflect their fair value as determined in accordance with procedures approved by the Board and are generally categorized as Level 3. In accordance with the Fund's valuation procedures, factors used in determining value may include, but are not limited to, the type of the security; the size of the holding; the initial cost of the security; the existence of any contractual restrictions on the security's disposition; the price and extent of public trading in similar securities of the issuer or of comparable companies; quotations or evaluated prices from broker-dealers and/or pricing services; information obtained from the issuer, analysts, and/or the appropriate stock exchange (for exchange-traded securities); an analysis of the company's or issuer's financial statements; an evaluation of the forces that influence the issuer and the market(s) in which the security is purchased and sold and with respect to debt securities; the maturity, coupon, creditworthiness, currency denomination and the movement of the market in which the security is normally traded. The value determined under these procedures may differ from published values for the same securities.

Disclosure about the classification of fair value measurements is included in a table following the Fund's Investment Portfolio.

**Securities Lending.** The Fund lends securities to certain financial institutions. The Fund retains beneficial ownership of the securities it has loaned and continues to receive interest and dividends paid by the issuer of securities and to participate in any changes in their market value. The Fund requires the borrowers of the securities to maintain collateral with the Fund consisting of either cash or liquid, unencumbered assets having a value at least equal to the value of the securities loaned. When the collateral falls below specified amounts, the lending agent will use its best effort to obtain additional collateral on the next business day to meet required amounts under the security lending agreement. The Fund may invest the cash collateral into a joint trading account in an affiliated money market fund pursuant to Exemptive Orders issued by the SEC. The Fund receives compensation for lending its securities either in the form of fees or by earning interest on invested cash collateral net of borrower rebates and fees paid to a lending agent. Either the Fund or the borrower may terminate the loan. There may be risks of delay and costs in recovery of securities or even loss of rights in the collateral should the borrower of the securities fail financially. The Fund is also subject to all investment risks associated with the reinvestment of any cash collateral received, including, but not limited to, interest rate, credit and liquidity risk associated with such investments.

**Taxes.** The Fund's policy is to comply with the requirements of the Internal Revenue Code, as amended, which are applicable to regulated investment companies and to distribute all of its taxable income to its shareholders.

At December 31, 2010, the Fund had an approximate net tax basis capital loss carryforward which may be applied against any realized net taxable capital gains of each succeeding year until fully utilized or until the following expiration dates, whichever occurs first:

| Fund | Capital Loss Carryforward ($) | Expiration Date | Capital Loss Carryforward Utilized ($) |
|---|---|---|---|
| DWS Turner Mid Cap Growth VIP | 800,000 | 12/31/2016 | 5,953,000 |
| | 14,919,000 | 12/31/2017 | |

The Fund has reviewed the tax positions for the open tax years as of December 31, 2010 and has determined that no provision for income tax is required in the Fund's financial statements. The Fund's federal tax returns for the prior three fiscal years remain open subject to examination by the Internal Revenue Service.

**Distribution of Income and Gains.** Distributions of net investment income of the Fund, if any, are made annually. Net realized gains from investment transactions, in excess of available capital loss carryforwards, would be taxable to the Fund if not distributed and, therefore, will be distributed to shareholders at least annually. The Fund may also make additional distributions for tax purposes if necessary.

The timing and characterization of certain income and capital gains distributions are determined annually in accordance with federal tax regulations which may differ from accounting principles generally accepted in the United States of America. These differences primarily relate to certain securities sold at a loss. As a result, net investment income (loss) and net realized gain (loss) on investment transactions for a reporting period may differ significantly from distributions during such period. Accordingly, the Fund may periodically make reclassifications among certain of its capital accounts without impacting the net asset value of the Fund.

At December 31, 2010, the Fund's components of distributable earnings on a tax basis were as follows:

| Fund | Capital Loss Carryforwards ($) | Unrealized Appreciation (Depreciation) on Investments ($) |
|---|---|---|
| DWS Turner Mid Cap Growth VIP | (15,719,000) | 21,090,213 |

In addition, the tax character of distributions paid by the Fund is summarized as follows:

| | Distributions from Ordinary Income ($)* | |
|---|---|---|
| | Years Ended December 31, | |
| Fund | 2010 | 2009 |
| DWS Turner Mid Cap Growth VIP | 7,813 | — |

* *For tax purposes, short-term capital gain distributions are considered ordinary income distributions.*

**Expenses.** Expenses of the Trust arising in connection with a specific fund are allocated to that fund. Other Trust expenses which cannot be directly attributed to a fund are apportioned among the funds in the Trust.

**Contingencies.** In the normal course of business, the Fund may enter into contracts with service providers that contain general indemnification clauses. The Fund's maximum exposure under these arrangements is unknown as this would involve future claims that may be made against the Fund that have not yet been made. However, based on experience, the Fund expects the risk of loss to be remote.

**Other.** Investment transactions are accounted for on a trade date plus one basis for daily net asset value calculations. However, for financial reporting purposes, investment transactions are reported on trade date. Interest income is recorded on the accrual basis. Dividend income is recorded on the ex-dividend date net of foreign withholding taxes. Realized gains and losses from investment transactions are recorded on an identified cost basis.

## B. Purchases and Sales of Securities

During the year ended December 31, 2010, purchases and sales of investment transactions (excluding short-term investments) were as follows:

| Fund | Purchases ($) | Sales ($) |
|---|---|---|
| DWS Turner Mid Cap Growth VIP | 48,107,657 | 53,568,971 |

## C. Related Parties

**Management Agreement.** Under the Investment Management Agreement with Deutsche Investment Management Americas Inc. ("DIMA" or the "Advisor"), an indirect, wholly owned subsidiary of Deutsche Bank AG, the Advisor directs the investments of the Fund in accordance with its investment objectives, policies and restrictions. The Advisor determines the securities, instruments and other contracts relating to investments to be purchased, sold or entered into by the Fund or delegates such responsibility to the Fund's subadvisor.

Turner Investment Partners, Inc. serves as subadvisor to the Fund and is paid by the Advisor for its services.

Under the Investment Management Agreement with the Advisor, the fee is equivalent to the annual rates shown below of the Fund's average daily net assets, computed and accrued daily and payable monthly:

| Fund | Annual Management Fee Rate |
|---|---|
| DWS Turner Mid Cap Growth VIP | |
| $0–$250 million | .715% |
| next $250 million | .700% |
| next $500 million | .685% |
| over $1 billion | .670% |

For the period from January 1, 2010 through September 30, 2010, the Advisor had contractually agreed to waive its fee and/or reimburse certain operating expenses to the extent necessary to maintain the operating expenses (excluding certain expenses such as extraordinary expenses, taxes, brokerage and interest expense) of the class as follows:

| Fund | Annual Rate |
|---|---|
| DWS Turner Mid Cap Growth VIP | |
| Class A | 1.01% |

For the period from October 1, 2010 through September 30, 2011, the Advisor has contractually agreed to waive its fee and/or reimburse certain operating expenses to the extent necessary to maintain the operating expenses (excluding certain expenses such as extraordinary expenses, taxes, brokerage and interest expense) of the class as follows:

| Fund | Annual Rate |
|---|---|
| DWS Turner Mid Cap Growth VIP | |
| Class A | .97% |

Accordingly, for the year ended December 31, 2010, the total management fee, management fee waived and effective management fee rate were as follows:

| Fund | Total Aggregated ($) | Waived ($) | Annual Effective Rate |
|---|---|---|---|
| DWS Turner Mid Cap Growth VIP | 368,747 | 559 | .71% |

**Administration Fee.** Pursuant to an Administrative Services Agreement, DIMA provides most administrative services to the Fund. For all services provided under the Administrative Services Agreement, the Fund pays DIMA an annual fee ("Administration Fee") of 0.10% of the Fund's average daily net assets, computed and accrued daily and payable monthly. For the year ended December 31, 2010, the Administration Fee was as follows:

| Fund | Total Aggregated ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS Turner Mid Cap Growth VIP | 51,573 | 4,967 |

**Service Provider Fees.** DWS Investments Service Company ("DISC"), an affiliate of the Advisor, is the transfer agent, dividend-paying agent and shareholder service agent for the Fund. Pursuant to a sub-transfer agency agreement between DISC and DST Systems, Inc. ("DST"), DISC has delegated certain transfer agent, dividend-paying agent and shareholder service agent functions to DST. DISC compensates DST out of the shareholder servicing fee it receives from the Fund. For the year ended December 31, 2010, the amounts charged to the Fund by DISC were as follows:

| Fund | Total Aggregated ($) | Waived ($) |
|---|---|---|
| DWS Turner Mid Cap Growth VIP Class A | 120 | 120 |

**Typesetting and Filing Service Fees.** Under an agreement with DIMA, DIMA is compensated for providing typesetting and certain regulatory filing services to the Fund. For the year ended December 31, 2010, the amount charged to the Fund by DIMA included in the Statement of Operations under "reports to shareholders" was as follows:

| Fund | Amount ($) | Unpaid at December 31, 2010 ($) |
|---|---|---|
| DWS Turner Mid Cap Growth VIP | 11,771 | 3,031 |

**Trustees' Fees and Expenses.** The Fund paid each Trustee not affiliated with the Advisor retainer fees plus specified amounts for various committee services and for the Board Chairperson.

**Affiliated Cash Management Vehicles.** The Fund may invest uninvested cash balances in Central Cash Management Fund, which is managed by the Advisor. The Fund indirectly bears their proportionate share of the expenses of the underlying money market funds. Central Cash Management Fund does not pay the Advisor an investment management fee. Central Cash Management Fund seeks a high level of current income consistent with liquidity and the preservation of capital.

## D. Ownership of the Fund

At December 31, 2010, the beneficial ownership in the Fund was as follows:

**DWS Turner Mid Cap Growth VIP:** Two Participating Insurance Companies were owners of record of 10% or more of the total outstanding Class A shares of the Fund, each owning 75% and 25%.

## E. Line of Credit

The Trust and other affiliated fund (the "Participants") share in a $450 million revolving credit facility provided by a syndication of banks. The Fund may borrow for temporary or emergency purposes, including the meeting of redemption requests that otherwise might require the untimely disposition of securities. The Participants are charged an annual commitment fee which is allocated based on net assets, among each of the Participants. Interest is calculated at a rate per annum equal to the sum of the Federal Funds Rate plus 1.25 percent plus if LIBOR exceeds the Federal Funds Rate the amount of such excess. The Fund may borrow up to a maximum of 33 percent of its net assets under the agreement.

## F. Subsequent Event

On January 12, 2011, the Board of the following Acquired Fund approved, in principle, the merger of the Acquired Fund into the Acquiring Fund. Completion of the merger is subject to a number of conditions. The merger is expected to be completed on or about May 1, 2011.

| Acquired Fund | Acquiring Fund |
|---|---|
| DWS Variable Series II — DWS Turner Mid Cap Growth VIP | DWS Variable Series II — DWS Small Cap Growth VIP |

In addition, on January 12, 2011, the Board approved changes to the name and strategy of DWS Small Cap Growth VIP. Effective on or about May 1, 2011, DWS Small Cap Growth VIP's investment objective will change from maximum appreciation of investors capital to long-term capital appreciation. In connection with the implementation of the new investment objective, the name will change from DWS Small Cap Growth VIP to DWS Small Mid Cap Growth VIP. In addition, the Russell 2500 Growth Index will replace the Russell 2000 Growth Index as the benchmark index because the Advisor believes that it better reflects the new investment strategy. For a description of the new investment objective, please see the supplement dated January 19, 2011 to the Fund's current prospectus posted on www.dws-investments.com.

# Report of Independent Registered Public Accounting Firm

**To the Board of Trustees and Shareholders of DWS Variable Series II:**

We have audited the accompanying statement of assets and liabilities of DWS Turner Mid Cap Growth VIP, one of the funds constituting the DWS Variable Series II (the "Trust"), including the investment portfolio, as of December 31, 2010, and the related statement of operations, the statement of changes in net assets and the financial highlights for each of the periods indicated therein. These financial statements and financial highlights are the responsibility of the Trust's management. Our responsibility is to express an opinion on these financial statements and financial highlights based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements and financial highlights are free of material misstatement. We were not engaged to perform an audit of the Trust's internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Trust's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements and financial highlights, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our procedures included confirmation of securities owned as of December 31, 2010, by correspondence with the custodian and brokers or by other appropriate auditing procedures where replies from brokers were not received. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements and financial highlights referred to above present fairly, in all material respects, the financial position of the aforementioned fund of the DWS Variable Series II at December 31, 2010, the results of its operations, the changes in its net assets and the financial highlights for each of the periods indicated therein, in conformity with U.S. generally accepted accounting principles.

Ernst + Young LLP

Boston, Massachusetts
February 14, 2011

## Tax Information

**(Unaudited)**

For corporate shareholders, the following percentage of income dividends paid during the Fund's fiscal year ended December 31, 2010 qualified for the dividends received deduction:

| Fund | Dividends Received % |
|---|---|
| DWS Turner Mid Cap Growth VIP | 100 |

Please consult a tax advisor if you have questions about federal or state income tax laws, or on how to prepare your tax returns. If you have specific questions about your account, please contact your insurance provider.

## Proxy Voting

The Trust's policies and procedures for voting proxies for portfolio securities and information about how the Trust voted proxies related to its portfolio securities during the 12-month period ended June 30 are available on our Web site — www.dws-investments.com (click on "proxy voting" at the bottom of the page) — or on the SEC's Web site — www.sec.gov. To obtain a written copy of the Trust's policies and procedures without charge, upon request, call us toll free at (800) 728-3337.

# Investment Management Agreement Approval

## DWS Turner Mid Cap Growth VIP

The Board of Trustees, including the Independent Trustees, approved the renewal of your Fund's investment management agreement (the "Agreement") with Deutsche Investment Management Americas Inc. ("DWS") and sub-advisory agreement (the "Sub-Advisory Agreement" and together with the Agreement, the "Agreements") between DWS and Turner Investment Partners, Inc. ("Turner") in September 2010.

In terms of the process that the Board followed prior to approving the Agreements, shareholders should know that:

- In September 2010, all but one of the Fund's Trustees were independent of DWS and its affiliates.
- The Trustees meet frequently to discuss fund matters. Each year, the Trustees dedicate substantial time to contract review matters. Over the course of several months, the Board's Contract Committee, in coordination with the Board's Equity Oversight Committee, reviewed comprehensive materials received from DWS, independent third parties and independent counsel. These materials included an analysis of the Fund's performance, fees and expenses, and profitability compiled by the Fund's independent fee consultant. The Board also received extensive information throughout the year regarding performance of the Fund.
- The Independent Trustees regularly meet privately with their independent counsel to discuss contract review and other matters. In addition, the Independent Trustees were also advised by the Fund's independent fee consultant in the course of their review of the Fund's contractual arrangements and considered a comprehensive report prepared by the independent fee consultant in connection with their deliberations (the "IFC Report").
- In connection with reviewing the Agreements, the Board also reviewed the terms of the Fund's distribution agreement, administrative services agreement, transfer agency agreement and other material service agreements.
- Based on its evaluation of the information provided, the Contract Committee presented its findings and recommendations to the Independent Trustees as a group. The Independent Trustees reviewed the Contract Committee's findings and recommendations and presented their recommendations to the full Board.

In connection with the contract review process, the Contract Committee and the Board considered the factors discussed below, among others. The Board also considered that DWS and its predecessors have managed the Fund since its inception, and the Board believes that a long-term relationship with a capable, conscientious advisor is in the best interests of the Fund. The Board considered, generally, that shareholders chose to invest or remain invested in the Fund knowing that DWS managed the Fund, and that the Agreement was approved by the Fund's shareholders. DWS is part of Deutsche Bank, a major global banking institution that is engaged in a wide range of financial services. The Board believes that there are significant advantages to being part of a global asset management business that offers a wide range of investing expertise and resources, including hundreds of portfolio managers and analysts with research capabilities in many countries throughout the world.

While shareholders may focus primarily on fund performance and fees, the Fund's Board considers these and many other factors, including the quality and integrity of DWS's and Turner's personnel and such other issues as back-office operations, fund valuations, and compliance policies and procedures.

**Nature, Quality and Extent of Services.** The Board considered the terms of the Agreements, including the scope of advisory services provided under the Agreements. The Board noted that, under the Agreements, DWS and Turner provide portfolio management services to the Fund and that, pursuant to a separate administrative services agreement, DWS provides administrative services to the Fund. The Board considered the experience and skills of senior management and investment personnel, the resources made available to such personnel, the ability of DWS to attract and retain high-quality personnel, and the organizational depth and stability of DWS. The Board reviewed the Fund's performance over short-term and long-term periods and compared those returns to various agreed-upon performance measures, including market indices and a peer universe compiled by the independent fee consultant using information supplied by Lipper Inc. ("Lipper"). The Board also noted that it has put into place a process of identifying "Focus Funds" (e.g., funds performing poorly relative to their benchmark or a peer universe compiled by Lipper), and receives more frequent reporting and information from DWS regarding such funds, along with DWS's remedial plans to address underperformance. The Board believes this process is an effective manner of identifying and addressing underperforming funds. Based on the information provided, the Board noted that for the one-, three- and five-year periods ended December 31, 2009, the Fund's performance (Class A shares) was in the 1st quartile, 2nd quartile and 3rd quartile, respectively, of the applicable Lipper universe (the 1st quartile being the best performers and the 4th quartile being the worst performers). The Board also observed that the Fund has outperformed its benchmark in the one-, three- and five-year periods ended December 31, 2009.

On the basis of this evaluation and the ongoing review of investment results by the Board, the Board concluded that the nature, quality and extent of services provided by DWS and Turner historically have been and continue to be satisfactory.

**Fees and Expenses.** The Board considered the Fund's investment management fee schedule, sub-advisory fee schedule, operating expenses, and total expense ratios, and comparative information provided by Lipper and the independent fee consultant regarding investment management fee rates paid to other investment advisors by similar funds (1st quartile being the most favorable and 4th quartile being the least favorable). With respect to management fees paid to other investment advisors by similar funds, the Board noted that the contractual fee rates paid by the Fund, which include the 0.10% fee paid to DWS under the Fund's administrative services agreement, were higher than the median (3rd quartile) of the applicable Lipper peer group (based on Lipper data provided as of December 31, 2009). With respect to the sub-advisory fee paid to Turner, the Board noted that the fee is paid by DWS out of its fee and not directly by the Fund. The Board noted that the Fund's Class A shares total (net) operating expenses were expected to be higher than the median (3rd quartile) of the applicable Lipper expense universe (based on Lipper data provided as of December 31, 2009, and analyzing Lipper expense universe Class A expenses less any applicable 12b-1 fees) ("Lipper Universe Expenses"). The Board considered the Fund's management fee rate as compared to fees charged by DWS and certain of its affiliates for comparable mutual funds and considered differences in fund and fee structures between the DWS Funds. The Board also considered how the Fund's total (net) operating expenses compared to the total (net) operating expenses of a more customized peer group selected by Lipper (based on such factors as asset size). The Board also noted that the expense limitation agreed to by DWS helped to ensure that the Fund's total (net) operating expenses would remain competitive.

The information considered by the Board as part of its review of management fees included information regarding fees charged by DWS and its affiliates to similar institutional accounts and to similar funds offered primarily to European investors ("DWS Europe funds"), in each case as applicable. The Board observed that advisory fee rates for institutional accounts generally were lower than the management fees charged by similarly managed DWS US mutual funds ("DWS Funds"), but also took note of the differences in services provided to DWS Funds as compared to institutional accounts. In the case of DWS Europe funds, the Board observed that fee rates for DWS Europe funds generally were higher than for similarly managed DWS Funds, but noted that differences in the types of services provided to DWS Funds relative to DWS Europe funds made it difficult to compare such fees.

On the basis of the information provided, the Board concluded that management fees were reasonable and appropriate in light of the nature, quality and extent of services provided by DWS and Turner.

**Profitability.** The Board reviewed detailed information regarding revenues received by DWS under the Agreement. The Board considered the estimated costs and pre-tax profits realized by DWS from advising the DWS Funds, as well as estimates of the pre-tax profits attributable to managing the Fund in particular. The Board also received information regarding the estimated enterprise-wide profitability of DWS and its affiliates with respect to all fund services in totality and by fund. The Board reviewed DWS's methodology in allocating its costs to the management of the Fund. Based on the information provided, the Board concluded that the pre-tax profits realized by DWS in connection with the management of the Fund were not unreasonable. The Board also reviewed information regarding the profitability of certain similar investment management firms. The Board noted that while information regarding the profitability of such firms is limited (and in some cases is not necessarily prepared on a comparable basis), DWS and its affiliates' overall profitability with respect to the DWS fund complex (after taking into account distribution and other services provided to the funds by DWS and its affiliates) was lower than the overall profitability levels of many comparable firms for which such data was available. The Board did not consider the profitability of Turner with respect to the Fund. The Board noted that DWS pays Turner's fee out of its management fee, and its understanding that the Fund's sub-advisory fee schedule was the product of an arm's length negotiation with DWS.

**Economies of Scale.** The Board considered whether there are economies of scale with respect to the management of the Fund and whether the Fund benefits from any economies of scale. The Board noted that the Fund's management fee schedule includes fee breakpoints. The Board concluded that the Fund's fee schedule represents an appropriate sharing between the Fund and DWS of such economies of scale as may exist in the management of the Fund at current asset levels.

**Other Benefits to DWS and Turner and Their Affiliates.** The Board also considered the character and amount of other incidental benefits received by DWS and Turner and their affiliates, including any fees received by DWS for administrative services provided to the Fund and any fees received by an affiliate of DWS for distribution services. The Board also considered benefits to DWS and Turner related to brokerage and soft-dollar allocations, including allocating brokerage to pay for research generated by parties other than the executing broker dealers, which pertain primarily to funds investing in equity securities, along with the incidental public relations benefits to DWS and Turner related to DWS Funds advertising and cross-selling opportunities among DWS products and services. The Board concluded that management fees were reasonable in light of these fallout benefits.

**Compliance.** The Board considered the significant attention and resources dedicated by DWS to documenting and enhancing its compliance processes in recent years. The Board noted in particular (i) the experience and seniority of both DWS's chief compliance officer and the Fund's chief compliance officer; (ii) the large number of DWS compliance personnel; and (iii) the substantial commitment of resources by DWS and its affiliates to compliance matters. The Board also considered the attention and resources dedicated by DWS to the oversight of the investment sub-advisor's compliance program and compliance with the applicable fund policies and procedures.

Based on all of the information considered and the conclusions reached, the Board unanimously (including the Independent Trustees) determined that the continuation of the Agreements is in the best interests of the Fund. In making this determination, the Board did not give particular weight to any single factor identified above. The Board considered these factors over the course of numerous meetings, certain of which were in executive session with only the Independent Trustees and their counsel present. It is possible that individual Trustees may have weighed these factors differently in reaching their individual decisions to approve the continuation of the Agreements.

# Summary of Management Fee Evaluation by Independent Fee Consultant

October 3, 2010

Pursuant to an Order entered into by Deutsche Investment Management Americas and affiliates (collectively, "DeAM") with the Attorney General of New York, I, Thomas H. Mack, have been appointed the Independent Fee Consultant for the DWS Funds (formerly the DWS Scudder Funds). My duties include preparing an annual written evaluation of the management fees DeAM charges the Funds, considering among other factors the management fees charged by other mutual fund companies for like services, management fees DeAM charges other clients for like services, DeAM's costs of supplying services under the management agreements and related profit margins, possible economies of scale if a Fund grows larger, and the nature and quality of DeAM's services, including fund performance. This report summarizes my evaluation for 2010, including my qualifications, the evaluation process for each of the DWS Funds, consideration of certain complex-level factors, and my conclusions. I served in substantially the same capacity in 2007, 2008, and 2009.

## Qualifications

For more than 35 years I have served in various professional capacities within the investment management business. I have held investment analysis and advisory positions, including securities analyst, portfolio strategist and director of investment policy with a large investment firm. I have also performed business management functions, including business development, financial management and marketing research and analysis.

Since 1991, I have been an independent consultant within the asset management industry. I have provided services to over 125 client organizations, including investment managers, mutual fund boards, product distributors and related organizations. Over the past ten years I have completed a number of assignments for mutual fund boards, specifically including assisting boards with management contract renewal.

I hold a Master of Business Administration degree, with highest honors, from Harvard University and Master of Science and Bachelor of Science (highest honors) degrees from the University of California at Berkeley. I am an independent director and audit committee financial expert for two closed-end mutual funds and have served in various leadership and financial oversight capacities with non-profit organizations.

## Evaluation of Fees for each DWS Fund

My work focused primarily on evaluating, fund-by-fund, the fees charged to each of the 118 publicly offered Fund portfolios in the DWS Fund family. For each Fund, I considered each of the key factors mentioned above, as well as any other relevant information. In doing so I worked closely with the Funds' Independent Directors in their annual contract renewal process, as well as in their approval of contracts for several new funds (documented separately).

In evaluating each Fund's fees, I reviewed comprehensive materials provided by or on behalf of DeAM, including expense information prepared by Lipper Analytical, comparative performance information, profitability data, manager histories, and other materials. I also accessed certain additional information from the Lipper and Morningstar databases and drew on my industry knowledge and experience.

To facilitate evaluating this considerable body of information, I prepared for each Fund a document summarizing the key data elements in each area as well as additional analytics discussed below. This made it possible to consider each key data element in the context of the others.

In the course of contract renewal, DeAM agreed to implement a number of fee and expense adjustments requested by the Independent Directors which will favorably impact future fees and expenses, and my evaluation includes the effects of these changes.

### Fees and Expenses Compared with Other Funds

The competitive fee and expense evaluation for each fund focused on two primary comparisons:

- The Fund's contractual management fee (the advisory fee plus the administration fee where applicable) compared with those of a group of typically 12–15 funds in the same Lipper investment category (e.g. Large Capitalization Growth) having similar distribution arrangements and being of similar size.
- The Fund's total expenses compared with a broader universe of funds from the same Lipper investment category and having similar distribution arrangements.

These two comparisons provide a view of not only the level of the fee compared with funds of similar scale but also the total expense the Fund bears for all the services it receives, in comparison with the investment choices available in the Fund's investment category and distribution channel. The principal figure-of-merit used in these comparisons was the subject Fund's percentile ranking against peers.

### DeAM's Fees for Similar Services to Others

DeAM provided management fee schedules for all of its US domiciled fund and non-fund investment management accounts in any of the investment categories where there is a DWS Fund. These similar products included the other DWS Funds, non-fund pooled accounts, institutional accounts and sub-advisory accounts. Using this information, I calculated for each Fund the fee that would be charged to each similar product, at the subject Fund's asset level.

Evaluating information regarding non-fund products is difficult because there are varying levels of services required for different types of accounts, with mutual funds generally requiring considerably more regulatory and administrative types of service as well as having more frequent cash flows than other types of accounts. Also, while mutual fund fees for similar fund products can be expected to be similar, there will be some differences due to different pricing conditions in different distribution channels (e.g. retail funds versus those used in variable insurance products), differences in underlying investment processes and other factors.

**Costs and Profit Margins**

DeAM provided a detailed profitability analysis for each Fund. After making some adjustments so that the presentation would be more comparable to the available industry figures, I reviewed profit margins from investment management alone, from investment management plus other fund services (excluding distribution) provided to the Funds by DeAM (principally shareholder services), and DeAM profits from all sources, including distribution. A later section comments on overall profitability.

**Economies of Scale**

Economies of scale — an expected decline in management cost per dollar of fund assets as fund assets grow — are very rarely quantified and documented because of inherent difficulties in collecting and analyzing relevant data. However, in virtually every investment category that I reviewed, larger funds tend to have lower fees and lower total expenses than smaller funds. To see how each DWS Fund compares with this industry observation, I reviewed:

- The trend in Fund assets over the last five years and the accompanying trend in total expenses. This shows if the Fund has grown and, if so, whether total expense (management fees as well as other expenses) have declined as a percent of assets.
- Whether the Fund has break-points in its management fee schedule, the extent of the fee reduction built into the schedule and the asset levels where the breaks take effect, and in the case of a sub-advised Fund how the Fund's break-points compare with those of the sub-advisory fee schedule.
- How the Fund's contractual fee schedule compares with trends in the industry data. To accomplish this, I constructed a chart showing how actual latest-fiscal-year contractual fees of the Fund and of other similar funds relate to average fund assets, with the subject Fund's contractual fee schedule superimposed.

**Quality of Service — Performance**

The quality-of-service evaluation focused on investment performance, which is the principal result of the investment management service. Each Fund's performance was reviewed over the past 1, 3, 5 and 10 years, as applicable, and compared with that of other funds in the same investment category and with a suitable market index.

In addition, I calculated and reviewed risk-adjusted returns relative to an index of similar mutual funds' returns and a suitable market index. The risk-adjusted returns analysis provides a way of determining the extent to which the Fund's return comparisons are mainly the product of investment value-added (or lack thereof) or alternatively taking considerably more or less risk than is typical in its investment category.

I also received and considered the history of portfolio manager changes for each Fund, as this provided an important context for evaluating the performance results.

## Complex-Level Considerations

While this evaluation was conducted mainly at the individual fund level, there are some issues relating to the reasonableness of fees that can alternatively be considered across the whole fund complex:

- I reviewed DeAM's profitability analysis for all DWS Funds, with a view toward determining if the allocation procedures used were reasonable and how profit levels compared with public data for other investment managers.
- I considered whether DeAM and affiliates receive any significant ancillary or "fall-out" benefits that should be considered in interpreting the direct profitability results. These would be situations where serving as the investment manager of the Funds is beneficial to another part of the Deutsche Bank organization.
- I considered how aggregated DWS Fund expenses had varied over the years, by asset class and in the context of trends in asset levels.
- I reviewed the structure of the DeAM organization, trends in staffing levels, and information on compensation of investment management and other professionals compared with industry data.

## Findings

Based on the process and analysis discussed above, which included reviewing a wide range of information from management and external data sources and considering among other factors the fees DeAM charges other clients, the fees charged by other fund managers, DeAM's costs and profits associated with managing the Funds, economies of scale, possible fall-out benefits, and the nature and quality of services provided, in my opinion the management fees charged the DWS Funds are reasonable.

Thomas H. Mack

Thomas H. Mack

# Board Members and Officers

The following table presents certain information regarding the Board Members and Officers of the Trust as of December 31, 2010. Each Board Member's year of birth is set forth in parentheses after his or her name. Unless otherwise noted, (i) each Board Member has engaged in the principal occupation(s) noted in the table for at least the most recent five years, although not necessarily in the same capacity; and (ii) the address of each Independent Board Member is c/o Paul K. Freeman, Independent Chairman, DWS Funds, PO Box 101833, Denver, CO 80250-1833. Except as otherwise noted below, the term of office for each Board Member is until the election and qualification of a successor, or until such Board Member sooner dies, resigns, is removed or as otherwise provided in the governing documents of the fund. Because the fund does not hold an annual meeting of shareholders, each Board Member will hold office for an indeterminate period. The Board Members may also serve in similar capacities with other funds in the fund complex. The Length of Time Served represents the year in which the Board Member joined the board of one or more DWS funds now overseen by the Board.

### Independent Board Members

| Name, Year of Birth, Position with the Fund and Length of Time Served[1] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Paul K. Freeman (1950)<br>Chairperson since 2009<br>Board Member since 1993 | Consultant, World Bank/Inter-American Development Bank; Executive and Governing Council of the Independent Directors Council (education committees); formerly, Project Leader, International Institute for Applied Systems Analysis (1998–2001); Chief Executive Officer, The Eric Group, Inc. (environmental insurance) (1986–1998) | 122 |
| John W. Ballantine (1946)<br>Board Member since 1999 | Retired; formerly, Executive Vice President and Chief Risk Management Officer, First Chicago NBD Corporation/The First National Bank of Chicago (1996–1998); Executive Vice President and Head of International Banking (1995–1996). Directorships: Healthways, Inc. (provider of disease and care management services); Portland General Electric (utility company); Stockwell Capital Investments PLC (private equity). Former Directorships: First Oak Brook Bancshares, Inc. and Oak Brook Bank; Prisma Energy International | 122 |
| Henry P. Becton, Jr. (1943)<br>Board Member since 1990 | Vice Chair and former President, WGBH Educational Foundation. Directorships: Association of Public Television Stations; Lead Director, Becton Dickinson and Company[3] (medical technology company); Lead Director, Belo Corporation[3] (media company); Public Radio International; Public Radio Exchange (PRX); The PBS Foundation. Former Directorships: Boston Museum of Science; American Public Television; Concord Academy; New England Aquarium; Mass. Corporation for Educational Telecommunications; Committee for Economic Development; Public Broadcasting Service | 122 |
| Dawn-Marie Driscoll (1946)<br>Board Member since 1987 | President, Driscoll Associates (consulting firm); Executive Fellow, Center for Business Ethics, Bentley University; formerly, Partner, Palmer & Dodge (1988–1990); Vice President of Corporate Affairs and General Counsel, Filene's (1978–1988). Directorships: Trustee of 22 open-end mutual funds managed by Sun Capital Advisers, Inc. (since 2007); Director of ICI Mutual Insurance Company (since 2007); Advisory Board, Center for Business Ethics, Bentley University; Trustee, Southwest Florida Community Foundation (charitable organization). Former Directorships: Investment Company Institute (audit, executive, nominating committees) and Independent Directors Council (governance, executive committees) | 122 |
| Keith R. Fox (1954)<br>Board Member since 1996 | Managing General Partner, Exeter Capital Partners (a series of private investment funds). Directorships: Progressive International Corporation (kitchen goods importer and distributor); BoxTop Media Inc. (advertising); The Kennel Shop (retailer); former Chairman, National Association of Small Business Investment Companies | 122 |
| Kenneth C. Froewiss (1945)<br>Board Member since 2001 | Adjunct Professor of Finance, NYU Stern School of Business (September 2009–present; Clinical Professor from 1997–September 2009); Member, Finance Committee, Association for Asian Studies (2002–present); Director, Mitsui Sumitomo Insurance Group (US) (2004–present); prior thereto, Managing Director, J.P. Morgan (investment banking firm) (until 1996) | 122 |
| Richard J. Herring (1946)<br>Board Member since 1990 | Jacob Safra Professor of International Banking and Professor, Finance Department, The Wharton School, University of Pennsylvania (since July 1972); Co-Director, Wharton Financial Institutions Center (since July 2000); Co-Chair, U.S. Shadow Financial Regulatory Committee; Executive Director, Financial Economists Roundtable; Director, Japan Equity Fund, Inc. (since September 2007), Thai Capital Fund, Inc. (since September 2007), Singapore Fund, Inc. (since September 2007); Independent Director of Barclays Bank Delaware (since September 2010). Formerly, Vice Dean and Director, Wharton Undergraduate Division (July 1995–June 2000); Director, Lauder Institute of International Management Studies (July 2000–June 2006) | 122 |
| William McClayton (1944)<br>Board Member since 2004+ | Private equity investor (since October 2009); previously, Managing Director, Diamond Management & Technology Consultants, Inc. (global consulting firm) (2001–2009); Directorship: Board of Managers, YMCA of Metropolitan Chicago; formerly: Senior Partner, Arthur Andersen LLP (accounting) (1966–2001); Trustee, Ravinia Festival | 122 |

| Name, Year of Birth, Position with the Fund and Length of Time Served[1] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Rebecca W. Rimel (1951)<br>Board Member since 1995 | President and Chief Executive Officer, The Pew Charitable Trusts (charitable organization) (1994 to present); Trustee, Thomas Jefferson Foundation (charitable organization) (1994 to present); Trustee, Executive Committee, Philadelphia Chamber of Commerce (2001–2007); Director, CardioNet, Inc.[2] (2009–present) (health care). Formerly, Executive Vice President, The Glenmede Trust Company (investment trust and wealth management) (1983–2004); Board Member, Investor Education (charitable organization) (2004–2005); Director, Viasys Health Care[2] (January 2007–June 2007); Trustee, Pro Publica (charitable organization) (2007–2010) | 122 |
| William N. Searcy, Jr. (1946)<br>Board Member since 1993 | Private investor since October 2003; Trustee of 22 open-end mutual funds managed by Sun Capital Advisers, Inc. (since October 1998). Formerly, Pension & Savings Trust Officer, Sprint Corporation[2] (telecommunications) (November 1989–September 2003) | 122 |
| Jean Gleason Stromberg (1943)<br>Board Member since 1997 | Retired. Formerly, Consultant (1997–2001); Director, Financial Markets US Government Accountability Office (1996–1997); Partner, Fulbright & Jaworski, L.L.P. (law firm) (1978–1996). Directorships: The William and Flora Hewlett Foundation. Former Directorships: Service Source, Inc., Mutual Fund Directors Forum (2002–2004), American Bar Retirement Association (funding vehicle for retirement plans) (1987–1990 and 1994–1996) | 122 |
| Robert H. Wadsworth (1940)<br>Board Member since 1999 | President, Robert H. Wadsworth & Associates, Inc. (consulting firm) (1983 to present); Director, The Phoenix Boys Choir Association | 125 |

## Interested Board Member and Officer[4]

| Name, Year of Birth, Position with the Trust/ Corporation and Length of Time Served[1,5] | Business Experience and Directorships During the Past Five Years | Number of Funds in DWS Fund Complex Overseen |
|---|---|---|
| Ingo Gefeke[7] (1967)<br>Board Member since 2010<br>Executive Vice President since 2010 | Managing Director[3], Deutsche Asset Management; Global Head of Distribution and Product Management, DWS Global Head of Trading and Securities Lending. Member of the Board of Directors of DWS Investment GmbH Frankfurt (since July 2009) and DWS Holding & Service GmbH Frankfurt (since January 2010); formerly, Global Chief Administrative Officer, Deutsche Asset Management (2004–2009); Global Chief Operating Officer, Global Transaction Banking, Deutsche Bank AG, New York (2001–2004); Chief Operating Officer, Global Banking Division Americas, Deutsche Bank AG, New York (1999–2001); Central Management, Global Banking Services, Deutsche Bank AG, Frankfurt (1998–1999); Relationship Management, Deutsche Bank AG, Tokyo, Japan (1997–1998) | 55 |

## Officers[4]

| Name, Year of Birth, Position with the Fund and Length of Time Served[5] | Principal Occupation(s) During Past 5 Years and Other Directorships Held |
|---|---|
| Michael G. Clark[6] (1965)<br>President, 2006–present | Managing Director[3], Deutsche Asset Management (2006–present); President of DWS family of funds; Director, ICI Mutual Insurance Company (since October 2007); formerly, Director of Fund Board Relations (2004–2006) and Director of Product Development (2000–2004), Merrill Lynch Investment Managers; Senior Vice President Operations, Merrill Lynch Asset Management (1999–2000) |
| John Millette[8] (1962)<br>Vice President and Secretary, 1999–present | Director[3], Deutsche Asset Management |
| Paul H. Schubert[6] (1963)<br>Chief Financial Officer, 2004–present<br>Treasurer, 2005–present | Managing Director[3], Deutsche Asset Management (since July 2004); formerly, Executive Director, Head of Mutual Fund Services and Treasurer for UBS Family of Funds (1998–2004); Vice President and Director of Mutual Fund Finance at UBS Global Asset Management (1994–1998) |
| Caroline Pearson[8] (1962)<br>Chief Legal Officer, April 2010–present | Managing Director[3], Deutsche Asset Management; formerly, Assistant Secretary for DWS family of funds (1997–2010) |
| Rita Rubin[9] (1970)<br>Assistant Secretary, 2009–present | Vice President and Counsel, Deutsche Asset Management (since October 2007); formerly, Vice President, Morgan Stanley Investment Management (2004–2007) |
| Paul Antosca[8] (1957)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management (since 2006); Vice President, The Manufacturers Life Insurance Company (U.S.A.) (1990–2006) |
| Jack Clark[8] (1967)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management (since 2007); formerly, Vice President, State Street Corporation (2002–2007) |

| Name, Year of Birth, Position with the Fund and Length of Time Served[5] | Principal Occupation(s) During Past 5 Years and Other Directorships Held |
|---|---|
| Diane Kenneally[8] (1966)<br>Assistant Treasurer, 2007–present | Director[3], Deutsche Asset Management |
| John Caruso[9] (1965)<br>Anti-Money Laundering Compliance Officer, 2010–present | Managing Director[3], Deutsche Asset Management |
| Robert Kloby[9] (1962)<br>Chief Compliance Officer, 2006–present | Managing Director[3], Deutsche Asset Management |

1 *The length of time served represents the year in which the Board Member joined the board of one or more DWS funds currently overseen by the Board.*

2 *A publicly held company with securities registered pursuant to Section 12 of the Securities Exchange Act of 1934.*

3 *Executive title, not a board directorship.*

4 *As a result of their respective positions held with the Advisor, these individuals are considered "interested persons" of the Advisor within the meaning of the 1940 Act. Interested persons receive no compensation from the fund.*

5 *The length of time served represents the year in which the officer was first elected in such capacity for one or more DWS funds.*

6 *Address: 100 Plaza One, Jersey City, NJ 07311.*

7 *Effective January 11, 2011, Mr. Gefeke, an interested Board Member and Executive Vice President, resigned from the fund's Board and as an officer.*

*The mailing address of Mr. Gefeke is 345 Park Avenue, New York, New York 10154. Mr. Gefeke was an interested Board Member of certain DWS funds by virtue of his positions with Deutsche Asset Management. As an interested person, Mr. Gefeke received no compensation from the fund.*

8 *Address: One Beacon Street, Boston, MA 02108.*

9 *Address: 60 Wall Street, New York, New York 10005.*

*The fund's Statement of Additional Information ("SAI") includes additional information about the Board Members. The SAI is available, without charge, upon request. If you would like to request a copy of the SAI, you may do so by calling the following toll-free number: (800) 728-3337.*

DWS Investments Distributors, Inc.
222 South Riverside Plaza
Chicago, IL 60606
(800) 621-1148

VS2TMCG-2 (2/11)

DWS INVESTMENTS
Deutsche Bank Group

**Zurich American Life Insurance Company (formerly known as Kemper Investors Life Insurance Company)**

Administrative office:
2000 Wade Hampton Blvd.
Greenville, SC 29615-1064



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